

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION

Before Commissioners:

Dan G. Blair, Chairman;
Dawn A. Tisdale, Vice Chairman;
Mark Acton; Ruth Y. Goldway;
and Tony Hammond

Regulations Establishing a System of
Ratemaking

Docket No. RM2007-1

ORDER PROPOSING REGULATIONS TO ESTABLISH
A SYSTEM OF RATEMAKING



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Attachment A—Comments to Regulations Establishing a System of Ratemaking

I. INTRODUCTION

[1001] This is the third in a series of orders designed to establish regulations implementing a modern system for regulating rates and classes for market dominant and competitive products.¹ In response to those earlier orders, the Commission received more than 100 comments from interested parties.² The Commission has reviewed these comments carefully. They have been useful in clarifying the Commission's analysis, and the parties' contributions are appreciated.

[1002] In this order, the Commission outlines how it intends to administer various provisions of the Postal Accountability and Enhancement Act (PAEA), Pub. L. No. 109-435, 120 Stat. 3198 (December 20, 2006). The proposed regulations are set forth in section V. Comments are due by September 14, 2007. Reply comments are due by September 28, 2007.

[1003] Although afforded 18 months, until June 19, 2008, to promulgate the new regulations under the PAEA, the Commission has made a concerted effort to accelerate that schedule considerably. The Commission views early implementation as beneficial to all stakeholders. Early implementation of a ratemaking framework prior to the statutory deadline will enable the Postal Service to use new, streamlined procedures to initiate rate (and class) changes as needed to respond to its financial needs and market conditions. The regulations may serve as a safety valve, providing an immediate means to address challenges faced by the Postal Service and perhaps obviate the necessity for rate relief through an omnibus rate case under existing procedures. The commenters urge that such a filing should be avoided, thereby allowing the Postal Service and the Commission to dedicate more resources to thoughtfully implementing other aspects of the reform legislation. It would be unfortunate if, in this reformed environment, rate changes had to be litigated under the old cost of service system. Having this new

¹ PRC Order No. 2, January 30, 2007 and PRC Order No. 15, May 17, 2007.

² Attachment A to this order contains a list of the parties filing comments.

framework in place, and the Postal Service operating under the new framework as early as practical, would provide the Postal Service flexibility to respond quickly to changed conditions.

[1004] The Commission's goal is to make this new system of rate adjustment advantageous for all stakeholders, enabling the Postal Service to price its own products, ensuring the lawfulness of competitive rates, providing increased transparency, and maintaining universal service at affordable rates. Fulfilling these objectives requires that competing interests be carefully balanced.

[1005] The Commission, among other things, identifies the mail matter that comprises each type of mail listed in section 3631(a) and the products within the competitive category of mail. It also discusses generally the mail matter that comprises each type of mail listed in section 3621(a). However, in lieu of identifying specific market dominant products, the Commission has determined that for reasons of accuracy and expedition, it would be preferable to accept the Postal Service offer to prepare and submit a draft mail classification schedule, which, *inter alia*, identifies the market dominant products it believes should be contained therein. This will enable the Postal Service to categorize its market dominant services into products that best serve its business needs. In addition, it will permit the Postal Service to fashion a draft mail classification schedule with what it believes is an appropriate level of detail. The Commission then will be able to evaluate this draft for consistency with the principles discussed in this order. The draft mail classification schedule is due September 14, 2007. Comments on the draft mail classification schedule are due September 28, 2007.

[1006] The proposed regulations represent the Commission's initial effort to establish a functional framework for regulating rates and classes for market dominant and competitive products. The proposed regulations do not seek to address every issue that might arise under the PAEA. The intent is that these regulations provide a reasonable starting point and that will they evolve over time.

[1007] In the sections that follow, the Commission discusses proposed regulations governing:

- Rules Applicable to Rate Adjustments for Market Dominant Products (part 3100);
- Regulation of Rates for Competitive Products (part 3110); and
- Product Lists (part 3200).

[1008] The Commission must also issue proposals amending the structure of its rules, and specific regulations applicable to complaints, reporting requirements, and commercially sensitive materials, as well as regulations to implement sections 404a and 504(f). Completing those tasks is complementary to the proposed regulations, which, once implemented, will be sufficient to enable the Postal Service to begin to operate as contemplated by the PAEA.

II. MARKET DOMINANT PRODUCTS

A. Introduction

[2001] *Background.* This segment of the rulemaking focuses on rate changes (referred to as “rate adjustments” in the PAEA for market dominant products). The emphasis is on proposing regulations that will provide the Postal Service with the option of pursuing its next general round of price changes under the new law’s ratesetting provisions, which feature a price cap mechanism and a streamlined advance notice and review, and on providing a comprehensive framework.

[2002] Much of the discussion on this topic since the enactment of the PAEA has occurred in the context of a joint Postal Regulatory Commission–Postal Service summit, regional field hearings,³ comments filed in response to Commission orders,⁴ and Congressional hearings. The Commission’s preliminary conclusions about the direction of this regulatory effort reflect considered review of the comments and testimony presented in these forums.

[2003] Commenters identify two main tasks for the Commission at this stage of implementation. One is reaching consensus on conceptual and practical aspects of the scope, depth and timeframe of Commission review of planned rate changes. The other is transforming numerous statutory requirements, objectives and factors into a new “road map” for navigating the regulatory calendar, expedited procedures, and price cap mechanism that are core components of the new system. Most commenters observe that these tasks involve balancing policy considerations, pragmatic concerns, and a revamped PRC/Postal Service partnership.⁵ They agree that the statute provides

³ See PRC Order No. 19, Notice and Order on Field Hearings to Receive Testimony on Implementation of Modern System of Ratemaking, Docket No. RM2007-1, June 8, 2007.

⁴ The parties have submitted several rounds of comments in response to the two advance notices of proposed rulemaking. As a matter of convenience, citations to these comments will identify the party’s comments by filing date; reply comments will be so denoted. For example, the referenced Postal Service initial comments are cited as Postal Service Comments, June 18, 2007, at xx; reply comments are cited similarly, e.g., PSA Reply Comments, July 3, 2007, at xx.

certainty on some key points, but point to numerous instances where other important issues are open to interpretation. Some urge the Commission to adopt a light-handed approach to the new notice-and-review process, with the price cap calculation being the sole focus.⁶ Others caution that implementation will allow price changes to occur more often than annually, the cap to be applied unequally to products within a class of mail, and the cap to be exceeded (within a certain range) under an exception referred to as “unused rate adjustment authority” or the banking exception. They suggest that these possibilities may have significant implications with respect to mailers’ expectations that the modern system will provide predictability, certainty and stability.

[2004] The Commission appreciates the responses to its request for assistance in developing new regulations, and finds that the commenters’ observations provide useful guidance. It also appreciates the Postal Service’s efforts, outside of this rulemaking, to work with mailers on developing a viable regulatory calendar and on addressing rate implementation issues. See Postal Service Reply Comments, May 7, 2007, at 3-4 and Appendix B. The Commission proposes basic rules regarding the regulatory calendar in proposed rule 3100.7.

⁵ See, for example, Advo Comments, April 6, 2007, at 2-3; MOAA Reply Comments, May 7, 2007, at 1-2; PSA Comments, April 6, 2007, at 1-4; Time Warner Comments, April 6, 2007, at 1-3; and Postal Service Comments, April 6, 2007, at 2-4.

⁶ Jon Mulford, for example, states: “[the] PAEA has given the Commission extraordinary power to regulate the USPS. The Commission, in devising its system for setting rates ... should at all costs avoid unnecessarily tying USPS management’s hands as they attempt to cope with an impending financial crisis.” Mulford Comments, March 9, 2007, at 5.

B. Statutory Framework for Rate Changes

[2005] Section 3622(d) of the PAEA, captioned “Requirements,” addresses some of the mandatory features the Commission must include in the modern regulatory system.⁷ It provides, in pertinent part:

(1) In General.—The system for regulating rates and classes for market-dominant products shall—

(A) include an annual limitation on the percentage changes in rates to be set by the Postal Regulatory Commission that will be equal to change in the Consumer Price Index for All Urban Consumers unadjusted for seasonal variation over the most recent available 12-month period preceding the date the Postal Service files notice of its intention to increase rates;

(B) establish a schedule whereby rates, when necessary and appropriate, would change at regular intervals by predictable amounts;

(C) not later than 45 days before the implementation of any adjustment in rates under this section, including adjustments made under subsection (c)(10) —

(i) require the Postal Service to provide public notice of the adjustment;

(ii) provide an opportunity for review by the Postal Regulatory Commission;

(iii) provide for the Postal Regulatory Commission to notify the Postal Service of any noncompliance of the adjustment with the limitation under subparagraph (A); and

(iv) require the Postal Service to respond to the notice provided under clause (iii) and describe the actions to be taken to comply with the limitation under subparagraph (A);

(D) establish procedures whereby the Postal Service may adjust rates not in excess of the annual limitations under subparagraph (A).

....

⁷ These requirements are not “stand alone” elements of the new system, but must be given effect in concert with certain statutory factors and objectives. However, unlike the “requirements,” most of which are new postal ratemaking features, many of the factors and objectives are identical to those employed in the Postal Reorganization Act of 1970 (PRA) ratemaking.

[2006] However, the “price cap” in subsection 3622(d)(1)(A) is not an absolute limit; other provisions expressly require that the new system:

(E) notwithstanding any limitation set under subparagraphs (A) and (C), and provided there is not sufficient unused rate authority under paragraph (2)(C), establish procedures whereby rates may be adjusted on an expedited basis due to either extraordinary or exceptional circumstances, provided that the Commission determines, after notice and opportunity for a public hearing and comment, and within 90 days after any request by the Postal Service, that such adjustment is reasonable and equitable and necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.

....

[2007] Further, the following provisions in subsection 3622(d)(2) authorize the annual cap to be exceeded under certain conditions:

...

(C) Use of Unused Rate Authority.—

(i) Definition.—In this subparagraph, the term “unused rate adjustment authority” means the difference between—

(I) the maximum amount of a rate adjustment that the Postal Service is authorized to make in any year subject to the annual limitation under paragraph (1); and

(II) the amount of the rate adjustment the Postal Service actually makes in that year.

(ii) Authority. Subject to clause (iii), the Postal Service may use any unused rate adjustment authority for any of the 5 years following the year such authority occurred.

[2008] Finally, the exercise of “banking authority” is itself subject to the following limitations:

(iii) Limitations.—In exercising the authority under clause (ii) in any year, the Postal Service—

(I) may use unused rate adjustment authority from more than 1 year;

(II) may use any part of the unused rate adjustment authority from any year;

(III) shall use the unused rate adjustment authority from the earliest year such authority first occurred and then each following year; and

(IV) for any class or service, may not exceed the annual limitation under paragraph (1) by more than 2 percentage points.

....

[2009] These comprehensive provisions unequivocally establish subsection 3622(d) as the administrative cornerstone of the new rate setting system for market dominant products. Collectively, streamlined advance review procedures, the price cap mechanism, the banking exception, and the exigency clause are designed to foster pricing flexibility, reduce burden, and facilitate quick implementation of rate changes. The Commission's proposed regulations are intended to fill in many of the details of price cap administration, content of rate change filings, and due process.

C. Summary of Main Issues

[2010] The PAEA specifies use of the Bureau of Labor Statistics' widely-known CPI-U, but does not address some related aspects of administration, such as how to calculate the index adjustment and how to calculate the base to which the adjustment applies. It also does not address the extent of documentation of worksharing discounts. The Commission sought comments on these matters in its Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking, May 17, 2007.

[2011] Additional implementation issues raised in the comments include:

- Whether the phrase “not later than 45 days” used in section 3622(d)(1)(C) limits Commission review to this number of days, or allows a longer period;
- Whether price change filings, other than exigent requests, involve “barebones” notice and documentation or more comprehensive support;
- Whether the Commission’s advance review is limited to assessing compliance with the price cap provisions or extends to other matters, such as an evaluation of worksharing discounts;
- Whether the Commission should solicit public comment in routine rate change filings;
- Whether the authority to “bank” unused rate adjustment authority for up to 5 years carries with it the ability to apply the banked pricing credit to a class other than the one in which it was accumulated; and
- Whether the rules should define “exigent circumstances” and whether trial-type proceedings must or should be held.

D. Structure of New Proceedings and Rules

[2012] Review of the comments points to interest in a new road map for rate changes. William Berkley usefully highlights this by observing:

We need to keep in mind that we have to keep proceedings simple and rules of practice simple to avoid a system that only postal attorneys and economists can use. We ask when you establish these new rules that you remember to keep it as simple as you can. Proceedings before every regulator are always difficult, but let us also insure that we make it easy to navigate and understand the proceedings in this evolving system.

Berkley Testimony at 5.⁸

[2013] United Parcel Service (UPS), addressing implementation in general, asserts: “To the extent possible, the Commission should interpret PAEA in a way that recognizes the value of administrative simplicity and practicality, and that minimizes the Postal Service’s burden, while remaining consistent with the statutory requirements.” UPS Reply Comments, July 3, 2007, at 10.

[2014] Accordingly, the Commission proposes to:

- Organize most of the rules directly affecting market dominant products into a largely self-contained unit;
- Standardize terms, definitions and methods to the extent feasible; and
- Establish streamlined proceedings to facilitate all types of price changes.

[2015] The Commission proposes to establish a separate part, designated part 3100, Rules Applicable to Rate Adjustments for Market Dominant Products, in 39 CFR. This part is divided into five subparts:

⁸ Testimony of William S. Berkley, President and CEO, Tension Envelope Corporation, Before the United States Postal Regulatory Commission Field Hearing, Kansas City, June 22, 2007.

- Subpart A General Provisions
- Subpart B Rules for Rate Adjustments for Rates of General Applicability (Type 1 Rate Adjustments)
- Subpart C Rules for Applying the Price Cap
- Subpart D Rules for Rate Adjustments for Negotiated Service Agreements (Type 2 Rate Adjustments)
- Subpart E Rules for Rate Adjustments in Exigent Circumstances (Type 3 Rate Adjustments)

E. Overview of Proposed Subpart A—General Provisions

[2016] This subpart consists of seven proposed rules. The first provision, proposed § 3100.1, captioned “Applicability,” is a general representation that the rules in subpart A implement the ratesetting policies and procedures of the PAEA for market dominant products. It also notes a distinction between “notice” filings and “request” filings.

[2017] Proposed § 3100.2(a) codifies the following basic scenarios in which rate changes for market dominant products may be addressed: under price cap authority or a variation thereon, often referred to by commenters as the banking exception or banking authority; under a special contractual, or negotiated service agreement; and under an exigent circumstance. For ease of reference and reporting, this rule reflects the Commission’s proposal to refer to each of these scenarios as “types” of filings, similar to the approach that has been used successfully for six categories of library references since Docket No. RM98-2. The Commission notes, for example, that for purposes of conducting the 10-year assessment of the new ratesetting approach, it may prove useful to have a ready tool for determining how many different types of notices and requests have been filed. The Commission incorporates these definitions into the regulations and the accompanying discussion. The following table summarizes this approach.

Table II-1

Summary of Alternative Filing Terms		
Statutory Source	Filing Basis	Proposed Alternative(s)
39 U.S.C. § 3622(d)(1)(A)	“annual limitation on the percentage changes in rates”	Type 1–A Rate Adjustment
39 U.S.C. § 3622(d)(2)(C)(i)	“unused rate adjustment authority”	Type 1–B Rate Adjustment
39 U.S.C. § 3622(c)(10)	“the desirability of special classifications ... including agreements between the Postal Service and postal users”	Type 2 Rate Adjustment
39 U.S.C. § 3622(d)(1)(E)	“due to either extraordinary or exceptional circumstances”	Type 3 Rate Adjustment

F. Overview of Proposed Subpart B—Rules for Rate Adjustments for Rates of General Applicability (Type 1 Rate Adjustments)

[2018] This subpart consists of five rules. These rules lay out basic procedures and certain fundamental Commission positions. Some of the debate among commenters centered on the timeframe for Commission action in a price change proceeding and on public input. The timeframe issue stems from the highlighted wording in the following passage from the PAEA:

(C) *not later than 45 days before the implementation of any adjustment in rates under this section, including adjustments made under subsection (c)(10)—*

(i) require the Postal Service to provide public notice of the adjustment;

(ii) provide an opportunity for review by the Postal Regulatory Commission.

39 U.S.C. § 3622(d)(1)(C)(i)-(ii).

[2019] The crux of the issue is whether the statute intends 45 days as the maximum or minimum period for advance notice and review. The Postal Service appears to read this language as establishing a statutory maximum, but acknowledges that some changes, as a matter of good business practice, such as those involving new worksharing discounts, will create more implementation issues. It indicates that it intends to provide additional notice in these instances. Postal Service Comments, June 18, 2007, at 14-15. The Mail Order Association of America (MOAA) shares the Postal Service's view. MOAA Reply Comments, May 7, 2007, at 14-15. Many commenters, however, see the wording in the statute as establishing a minimum, and therefore clearly authorizing the Commission to require the Postal Service to provide more notice. Time Warner suggests 90 days. Time Warner Comments, April 6, 2007, at 15.

[2020] The Commission concludes that as a matter of statutory interpretation, the Postal Service's position reads the qualifier "at least" completely out of the statute. The conclusion more consistent with the statute's overall theme of transparency is that 45

days is the minimum period required by the statute, and the Commission may require a longer period in certain circumstances.⁹ At the same time, it seems that any extension should be in keeping with the notion of streamlined review; thus, the four months the OCA suggests as the routine approach appears excessive for the Commission's task of assessing the planned rate changes in terms of the price cap and/or the use of banking authority.

[2021] The Commission concludes that for purposes of drafting an initial set of regulations, the language from the statute requiring notice and review "not later than 45 days" can be carried over directly into proposed rules 3100.10(a)(1) and (2). A provision in proposed rule 3100.10(b) encouraging more time for review recognizes the Postal Service's representations on this record that it intends to provide additional time for review when price changes are more complicated. Postal Service Comments, June 18 2007, at 9-10. Proposed rule 3100.10(a) does not require the Postal Service to publish a *Federal Register* notice concerning a planned adjustment, but does contemplate broad dissemination of its intent to the mailing community and to the general public. This typically provides more effective notice than a *Federal Register* notice, in keeping with a modern rate setting system, and reduces administrative burden by freeing the Postal Service from the production details necessarily associated with *Federal Register* publication. The Commission notes that it imposes on itself, in proposed rule 3100.13(a), an obligation to publish notice of a rate adjustment filing in the *Federal Register*.

[2022] Commenters are divided on the question of public input during the review period. Some, including the Postal Service, argue against it on grounds that the logic of the PAEA suggests that if public input is not expressly provided for in the statute, it is not authorized. On the other hand, the OCA and several others think it would be helpful. Newspaper Association of America (NAA), for example, asserts that allowing public

⁹ Based on the Postal Service's comments, it anticipates filing 90 days in advance of implementation with the first 45 days constituting the statutory period for Commission review and the second half for implementation.

comment would promote transparency. NAA Comments, March 30, 2007, at 2. NAA acknowledges that the new statute expressly provides for public participation when rate adjustments are based on exigent circumstances, but asserts:

Nothing in the PAEA, however, prohibits the Commission from inviting such comment also when the Postal Service purports to notice rate adjustments consistent with the CPI limitation. Public comment — which necessarily would have to be expedited and would be submitted in writing — would promote transparency and could provide information helpful to the Commission's review.

Id. at 7.

It adds:

Where the Postal Service's notice is straightforward, there likely will be relatively few comments. However, in instances when the Postal Service notices a more complicated set of rate changes, the Commission may benefit from the insights that the mailing community and broader public may be able to offer. The stakes of this review are important because the rates that will take effect from this process will be in effect for a substantial period of time before they are later reviewed by the Commission either in an annual review or in a complaint.

Id. at 7-8.

[2023] The Commission agrees that the statute does not expressly provide for public participation during the review period as it does in the exigency clause (in subsection 3622(d)(1)(E)). At the same time, the statute gives the Commission broad discretion in deciding on how to conduct its review. It follows that if the Commission believes public input might be helpful in determining the compliance of the anticipated rate changes with the statutory pricing provisions, there is no statutory bar to incorporating this into its review proceedings/procedures. The Commission believes this will be the case, and provides, in proposed rule 3100.13(a) for 20 days (from the date of filing of a rate adjustment notice) for the public to file written comments.

[2024] Proposed rule 3100.11 addresses several “housekeeping” details. It notes the limitation on rate increases in any 12-month period, the existence of CPI-U as a limitation, the exception allowing annual recapture of unused rate authority, and the allocation of unused rate authority to each class of mail. The latter provision directly addresses some commenters’ concerns about “cross-class” banking.

[2025] Proposed rule 3100.12 adopts the PAEA’s stated inflation measure (CPI-U) and describes the source as the Bureau of Labor Statistics. The clarity of the PAEA on this point meant that there was no debate among the commenters on the benchmark that is to be used.

[2026] Proposed rules 3100.13 and 14 address the nature of proceedings and the content of rate adjustment filings, and are the most extensive rules in this subpart. The flagship proceedings under the former statutory structure were 10-month trial-type “omnibus” rate and classification proceedings, bookended between considerable advance preparation on the part of the Postal Service (and many mailers) and a post-decision phase encompassing review by the Governors and the potential for reconsideration. Commenters agree that, barring a final omnibus rate case under 39 U.S.C. § 3622(f), the PAEA casts that apparatus aside and replaces it with a simpler process. In keeping with the new statutory emphasis on simpler proceedings, the Commission does not propose formal discovery, Notices of Inquiry, Presiding Officer’s Information Requests, testimony, and hearings. It anticipates handling resolution of discrepancies or other matters through direct communication with the Postal Service.

[2027] There also has been considerable discussion of the statutory scope of the Commission’s review. The main positions are that it extends to:

- Only, or primarily, the price cap;
- The price cap, plus some evaluation of worksharing; and
- The price cap, worksharing evaluation, plus consistency with statutory factors and objectives, *plus* identification of certain features, such as differential intra-class treatment exceeding a certain percentage.

[2028] Some commenters, such as the Postal Service and MOAA, advocate “light-handed” review, the OCA seeks extensive review, and some, such as the NAA take a middle ground. NAA suggests that during the review period, the Commission has, at a minimum, legal authority:

- To review the notices of rate adjustments for compliance with the CPI cap;
- To review the noticed change to ensure at least facial compliance with the provisions of section 3622(e) regarding workshare discounts;
- To prohibit rates that are unlawful on their face from taking effect; and
- To review the justification for changes in rate categories within a class that exceed CPI by an amount set by the Commission, such as the CPI plus 2 percent proposed by NAA.

NAA Reply Comments, May 7, 2007, at 25-26.

[2029] The Commission agrees that the PAEA ushers in a fundamentally different approach to rate regulation for market dominant products, and that its implementing regulations should honor the spirit and letter of the new law. Proposed rule 3100.13(b) limits the appropriate scope of public comments to compliance with the price cap formula and consistency with certain statutory policies; thus, they represent a marked shift away from PRA-style in-depth examination. The proposed scope of public comment is no longer open-ended. The Commission does not invite, and will not entertain, public comment during the 45-day review period on matters such as costing methods. Moreover, in proposed rule 3100.13(e), the Commission expedites review to determine the consistency of an amended notice of rate adjustment with filing requirements.

[2030] *Filing contents.* Proposed rule 3100.14 describes the contents of the Postal Service’s rate adjustment filings. The notice is to include a schedule of proposed rates, identification of the effective date(s), and a representation or evidence that public notice of the planned changes has been issued or will be issued at least 45 days before the effective date(s) of the proposed rates.

[2031] In addition, proposed rule 3100.14(b)(1)-(8) identifies explanatory material that is to be provided. This includes the amount of the applicable change in CPI-U calculated under Commission rules and the percentage change in rates for each class, calculated as required by Commission rules along with supporting workpapers. It also includes the amount of new unused rate authority that will be generated by the instant notice of rate adjustment and a 5-year schedule showing unused rate authority for each class of mail, along with supporting calculations. For Type 1-B filings, which draw on recaptured pricing authority, the Postal Service is to identify for each affected class how much existing unused rate authority is used in the proposed rates calculated as required by Commission rules. See proposed rule 3100.14(d). An explanation must be provided if new unused rate authority will be generated for a class of mail that is not expected to cover its attributable costs.

[2032] Several commenters express concern about the potential for intra-class increases to exceed the cap. NAA asserts that the Postal Service's authority to exceed the annual cap for a rate category is not unlimited, as the phrase "predictable amounts" is not limited to the aggregate change for a class, but "on its face requires that the specific rate changes themselves within the class should be reasonably predictable." NAA Comments, March 30, 2007, at 9. It contends that Objective 8, which requires that the rate schedule be "just and reasonable" supports this interpretation. *Id.* NAA suggests that the Commission impose a standard whereby, absent special justification, increases for a rate category beyond a pre-established range (such as CPI plus 2 percent) would not be considered "predictable" or "just and reasonable." *Id.* at 9-10. It asserts that this approach, which it refers to as a "soft band," would satisfy the statutory objective of providing the Postal Service with pricing flexibility, while honoring the provision in Objective 8 allowing changes of unequal magnitude within, between or among class of mail. *Id.* at 9; NAA Reply Comments, May 7, 2007, at 8. In terms of proposed rules, NAA suggests that the Postal Service could be required to certify that no rate would change by more than the permitted range (when this is the case) or bring changes exceeding the range to the Commission's attention and provide additional

justification. NAA Comments, March 30, 2007, at 10. It contends that over time, as the Commission reviews these explanations on a case-by-case basis, it will become evident which explanations are adequate to allow the rates to become effective, and which are not. NAA Reply Comments, May 7, 2007, at 8.

[2033] The Parcel Shippers Association (PSA) does not suggest prohibiting adjustments beyond a certain level, but suggests that the Commission require the Postal Service to provide a written, on the record, justification for any market dominant rate increases that *substantially* exceed inflation. PSA Comments, April 6, 2007, at 4-5, 22-23. (Emphasis in original.)

[2034] In a similar vein, OCA suggests, given the potential for large percentage increases in rates for individual subclasses, that subclass increases be capped at 50 percent above the overall class increase. OCA Comments, June 18, 2007, at 2, 15-19. It notes:

Some of the principles of rate setting include continuity of expectations, implementation of rates that are understandable, and perceived and/or actual fairness. Accordingly, some level of subclass protection appears to be appropriate. We suggest 50 percent as reasonable: that is, if rates for a class of service increase by an overall maximum of two percent, no subclass rate would increase by more than three percent.

Id. at 15.

[2035] Discover Financial Services, LLC (DFS) asserts that the OCA's recommendation is "at odds with the legislation, which nowhere indicates that such a cap would be permissible. Indeed, notions that rates should be capped in any fashion other than at the class level were much debated in Congress and specifically rejected as not giving the Postal Service sufficient rate flexibility." DFS Further Comments, July 16, 2007, at 4.

[2036] NAA, PSA and OCA identify a clear example of where statutory objectives may conflict. The Commission does not view capping subclass increases as sanctioned by the PAEA. Requiring a separate certification or justification is not statutorily suspect

in the same sense; however, adopting a rule of this sort makes the process cumbersome. It is to be expected that rate adjustments within a class will be both above and below average. Requiring written justification for individual rates is contrary to the goals of a simpler, more flexible, process. The Commission finds that the Postal Service should be given an opportunity to exercise its pricing flexibility by making changes of unequal magnitude without having to file separate justification for what some might consider “excessive” above-cap increases within a class. Should the Postal Service abuse this discretion, and regularly fail to develop rate adjustments consistent with the statutory objective of maintenance of just and reasonable rate schedules, additional regulations in this area can be developed.

[2037] *Information supporting proposed workshare discounts.* The PAEA charges the Commission with establishing a modern system of ratemaking that is designed to achieve nine specific objectives including to maximize incentives to reduce costs and increase efficiency. The PAEA also enumerates several factors which must be considered by the Commission in establishing this system. Two of these factors — 3622(c)(5), the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service; and 3622(c)(12), the need for the Postal Service to increase its efficiency and reduce its costs — can be linked directly to workshare discounts. Section 3622(e)(2) directs the Commission to ensure that [workshare] discounts do not exceed the cost that the Postal Service avoids as a result of workshare activity.¹⁰

[2038] The PAEA defines workshare discounts as rate discounts provided to mailers for the presorting, pre-barcoding, handling, or transportation of mail. Both the Commission and the Postal Service have long held the view that setting workshare

¹⁰ There are four limited exceptions to this mandate: (1) when the discount is new and mailers must be encouraged to use it; (2) when the discount is already in place and reducing it will cause rate shock; (3) when the discount is provided in connection with subclasses consisting exclusively of mail matter of educational, cultural, scientific, or informational value; and (4) when reducing or eliminating the discount would cause a shift in mail mix that would lead to operational inefficiencies for the Postal Service. For the first two exceptions, the Postal Service must eventually phase out the excess discount.

discounts in line with the Efficient Component Pricing Rule (ECPR) is an effective method for encouraging efficient mailing practices. The ECPR is the principle that workshare discounts should be set equal, on a per-unit basis, to the costs avoided by the Postal Service when the mailer performs the workshare activity.

[2039] Several parties reiterated the importance of ECPR in encouraging efficiency and satisfying the objectives of the PAEA. Pitney Bowes states “regulations should require the Postal Service to establish discounts that reflect the full measure of workshare-related costs avoided to the extent practicable.” Pitney Bowes Comments, April 6, 2007, at 36. In addition, Pitney Bowes sponsored the comments of John Panzar which focus exclusively on the merits of continued use of ECPR in ratemaking. The Alliance of Nonprofit Mailers, National Association of Presort Mailers, and National Postal Policy Council (ANM/NAPM/NPPC) believe that the Postal Service’s rates should be presumed reasonable as long as the discounts satisfy the ECPR. ANM/NAPM/NPPC Comments, April 6, 2007, at 16-19.

[2040] Support for efficient component pricing is also found in testimony received during the Commission’s field hearings. Don Hall, Jr., President and CEO of Hallmark Cards, seeks assurance that the workshare discounts will reflect the true savings to the Postal Service. Transcript of Kansas City Field Hearing, June 22, 2007, at 29. John Campo, Vice President of Postal Relations for Pitney Bowes, said the “regulations should encourage the Postal Service to adopt pricing incentives or work sharing discounts to fully reward mailer activity that reduces total postal system costs.” Transcript of Wilmington Field Hearing, July 9, 2007, at 10. John Carper, Director of Mail and Receiving Services, Pepperdine University, claims that “[worksharing] can flourish fully only if the discounts offered by the Postal Service ... fully reflect the costs that the Postal Service saves.” Transcript of Los Angeles Field Hearing, June 28, 2007, at 39.

[2041] In contrast, Advo, Inc. presents three reasons why ECPR should not be followed in setting rates under the PAEA:

First, the statute does not permit consideration of factors other than compliance with price caps in the review process. Second,

ECP, although useful in theory as a pricing tool, is not the only appropriate consideration in setting discounts and is susceptible to being misapplied. Third, adoption of ECP as the 'gold standard' will inevitably and unnecessarily impinge on the Postal Service's pricing flexibility — a flexibility that is imperative to its ability to remain viable under the price cap regime.

Advo Reply Comments, July 3, 2007, at 6.

[2042] MOAA, NAA, and the Postal Service recognize the importance of the ECPR, but contend that other, perhaps competing, factors are also important. Therefore, they believe that ECPR should not be a requirement for workshare discounts.

[2043] The Commission strongly believes that efficient component pricing should be used as a guiding principle in establishing and maintaining workshare discounts. In both sections 3622(b) and 3622(c) the statute stresses the need for efficient rates and efficient component pricing is an established method of measuring efficient ratemaking. Nonetheless, the Commission recognizes that other factors must also be considered, and that the PAEA grants the Postal Service substantial flexibility in setting rates. However, in the interest of transparency and accountability, the Postal Service has a burden to explain how its rates, including workshare discounts, meet the objectives and factors of the PAEA.

[2044] The Postal Service has proposed that when it files its notice of price adjustment, it will also file, for pre-existing workshare discounts, a comparison of the new (or unchanged) discount price with the historical, Commission reviewed cost avoidances of the last Annual Compliance Review, and will provide appropriate justification for any discount that exceeds those cost avoidances. Postal Service Comments, June 18, 2007, at 11. The proposed rules reflect this undertaking. To meet its burden of ensuring that the rates are in compliance with the objectives and factors of the PAEA, the Postal Service must also identify and explain any discounts that are substantially below the cost avoidances.

[2045] The Postal Service is to provide with each notice of rate adjustment a schedule of the workshare discounts included in the proposed rates, together with a

companion schedule listing underlying avoided costs, along with supporting workpapers. The avoided cost figures must be developed from the most recent PRC Annual Compliance Report. The Postal Service is to provide a separate justification for all proposed workshare discounts that exceed avoided costs. The Postal Service shall also identify and explain discounts that are set substantially below avoided costs, and explain any relationship between discounts that are above and those that are below avoided costs.

[2046] In addition, when new workshare discounts are established, the Postal Service is to include with its filing a statement explaining its reasons for establishing the discount; provide all data, economic analyses, and other information believed to justify the discount; and certify, based on comprehensive, competent analyses that the discount will not adversely affect either the rates or the service levels of users of postal services who do not take advantage of the discount.

[2047] Lastly, the Postal Service is to provide a discussion of how the proposed rates will help achieve the objectives listed in 39 U.S.C. § 3622(b) and properly take into account the factors listed in § 3622(c).

G. Overview of Subpart C—Rules for Applying the Price Cap

[2048] This subpart consists of nine rules related primarily to administration of the price cap mechanism. Proposed rule 3100.21 addresses how to calculate the statutory annual inflation-based limitation. A question has arisen over the practical import of the highlighted words in the following statutory language:

... an annual limitation ... equal to the change in the Consumer Price Index for All Urban Consumers unadjusted for seasonal variation *over the most recent available 12-month period preceding the date the Postal Service files notice of its intention to increase rates.*

39 U.S.C. § 3622(d)(1)(A). (Emphasis added.)

[2049] Two suggestions have emerged on this record, but commenters generally agree that both approaches are consistent with the statute. One is referred to as the “point-to-point” method and was initially suggested by the Postal Service and the OCA. The other is the “running average” or “weighted average” method which is incorporated in the proposed rules.

[2050] JPMorgan Chase & Company (Chase) comments are representative. Chase urges the Commission to calculate the index adjustment based on a 12-month average of CPI levels, rather than on a “snapshot” of year-over-year changes to the CPI between a single pair of beginning and end dates. It reasons:

While the two approaches should achieve similar results over the long run, the use of the twelve-month average is likely to produce a much less bumpy and volatile path along the way by damping the short-term oscillations in the CPI index. For Chase and other mailers that operate on an annual budget cycle-i.e., for the mailers that generate most of the Postal Service's

volume, reducing the short-term unpredictability of cost increases is extremely important.

Emens Testimony at 5.¹¹

[2051] Many parties commented that they prefer the moving average method because it provides more predictability and stability in rates. NAA states, the average method “better advance[s] the statutory objective of creating ‘predictability and stability in rates’ while promoting transparency in rates and assuring that the Postal Service is financially sound.” NAA Comments, June 18, 2007, at 2. *See also* Advo Comments, June 18, 2007, at 2; Advo Reply Comments, July 3, 2007, at 1; GCA Reply Comments, July 3, 2007, at 1-2; Pitney Bowes Reply Comments, July 3, 2007, at 3; and PostCom Reply Comments, July 3, 2007, at 2.

[2052] Contrary to these views, OCA states that the point method “does not result in significantly less rate stability and predictability.” OCA Reply Comments, July 3, 2007, at 6. It contends that the moving average method “would have substantial lags in the updating of rates.” OCA Initial Comments, June 18, 2007, at 7. *See also* Valpak Comments, June 18, 2007, at 5; and OCA Reply Comments, July 3, 2007, at 2-4.

[2053] The Postal Service expressed concern that using the moving average method includes 24 months of data rather than 12. USPS states, “It is arguable that calculating the price cap by reference to CPI-U data over a 24-month period is counter to the statutory requirement that the CPI calculation be “equal to” the change in CPI-U “over the most recent available 12-month period.” Postal Service Comments, June 18, 2007, at 3-4. APWU also believes that the point method better adheres to the plain language of the PAEA. APWU Comments, June 18, 2007, at 2-3. APWU and Valpak advocate the point method as providing more transparency and less administrative burden. APWU Comments, June 18, 2007, at 2; and Valpak Comments, June 18, 2007, at 4-5.

¹¹ Testimony of Daniel C. Emens on Behalf of JPMorgan Chase & Co., July 9, 2007 (Emens Testimony).

[2054] The majority of commenters are satisfied that both the moving average method and point method meet the statutory requirements of the PAEA. MOAA states, “The provisions of [the] PAEA are sufficiently broad that either the [moving average method] or the [point method] could be used for the purpose of calculating the CPI cap limitation as set forth in §3622 (b), (c) and (d).” MOAA Comments, June 18, 2007, at 1. See also GCA Comments, June 18, 2007, at 2; Advo Comments, June 18, 2007, at 2; PostCom Comments, June 18, 2007, at 2; and Pitney Bowes Comments, June 18, 2007, at 2.

[2055] The Commission proposes to use the moving average method of calculating the CPI-U limitation. This method provides mailers with stable and predictable rates, and also grants the Postal Service the same benefits. The moving average method does not impose any undue administrative burden on the Postal Service and does not inhibit transparency. The Commission finds the increased predictability and stability resulting from use of the moving average method are quite valuable, and directly further the specific objectives of the PAEA. The Commission derives the moving average method from Bureau of Labor Statistics (BLS) monthly CPI-U values. At the end of each calendar year, BLS calculates the annual percentage change between two years as the percentage change between the two years’ annual averages. The only difference in methodology is that BLS applies this methodology to calendar years, and the Commission will apply it to 12-month periods.

[2056] Calculation of the annual limitation in this method involves three steps. First, a simple average CPI-U index (Recent Average) is calculated by summing the most recently available 12 monthly CPI-U values from the date the Postal Service files notice of its intentions to increase rates, and dividing the sum by 12. Then, a second simple average CPI-U index (Base Average) is similarly calculated by summing the 12 monthly CPI-U values preceding those used in the Recent Average calculation and dividing the sum by 12. Finally, the percentage change between the Recent Average and the Base Average is computed, using the following formula:

Annual Limitation (Moving Average Method) = (Recent Average/ Base Average) – 1.

[2057] Example 1 illustrates the annual limitation calculation, using the moving average method, assuming that the Postal Service had filed a hypothetical notice of its intentions to increase rates during the third week of April 2006.¹²

Example 1

(A)			(B)		
<u>April 2006 Notice Recent Average</u>			<u>April 2006 Notice Base Average</u>		
<u>YEAR</u>	<u>MONTH</u>	<u>CPI-U MONTHLY INDEX</u>	<u>YEAR</u>	<u>MONTH</u>	<u>CPI-U MONTHLY INDEX</u>
2005	April	194.6	2004	April	188.0
2005	May	194.4	2004	May	189.1
2005	June	194.5	2004	June	189.7
2005	July	195.4	2004	July	189.4
2005	August	196.4	2004	August	189.5
2005	September	198.8	2004	September	189.9
2005	October	199.2	2004	October	190.9
2005	November	197.6	2004	November	191.0
2005	December	196.8	2004	December	190.3
2006	January	198.3	2005	January	190.7
2006	February	198.7	2005	February	191.8
2006	March	199.8	2005	March	193.3
12-Month Average		197.0	12-Month Average		190.3

ANNUAL LIMITATION =

April 2006 Notice Recent Average (A)	-1	=	197.0	-1	=	3.5%
April 2006 Notice Base Average (B)			190.3			

[2058] Example 1 assumes that rate filings are 12 months apart; that is, that the Postal Service filed its most recent previous notice for a rate increase in April 2006. This

¹² All CPI-U data is obtained from the BLS website at: <http://data.bls.gov/cpi-bin/surveymost>.

assumption can be adjusted in two ways depending on when the Postal Service files a notice of rate adjustment.

[2059] The first adjustment occurs when the Postal Service files a notice of rate adjustment less than one year after the previous adjustment. In this instance, if the calculation were to use 12 months of data, the Postal Service would benefit from double counting months of CPI data. This would violate the statutory limitation. To remedy this problem, a partial year limitation is calculated.

[2060] Example 2 calculates a partial year limitation. First, a simple 12-month average must be calculated using the most recently available 12 months of CPI-U data from the BLS website (Recent Average). Then the partial year limitation is calculated by dividing the Recent Average by the Recent Average from the most recent previous notice and subtracting 1. The formula is as follows:

$$\text{Partial Year Limitation} = (\text{Recent Average} / \text{Recent Average from most recent previous notice}) - 1.$$

[2061] Still assuming that the Postal Service filed its first notice of rate adjustment in April of 2006 (Example 1), assume now that the Postal Service files its second hypothetical notice of rate adjustment in October 2006 (six months later). Example 2 shows how the partial year limitation will be calculated for the October 2006 rate adjustment.

Example 2

(C)		
<u>October 2006 Notice Recent Average</u>		
<u>YEAR</u>	<u>MONTH</u>	<u>CPI-U MONTHLY INDEX</u>
2005	October	199.2
2005	November	197.6
2005	December	196.8
2006	January	198.3
2006	February	198.7
2006	March	199.8
2006	April	201.5
2006	May	202.5
2006	June	202.9
2006	July	203.5
2006	August	203.9
2006	September	202.9
12-Month Average		200.6

(D)		
<u>October 2006 Notice Base Average = April 2006 Notice Recent Average</u>		
<u>YEAR</u>	<u>MONTH</u>	<u>CPI-U MONTHLY INDEX</u>
2005	April	194.6
2005	May	194.4
2005	June	194.5
2005	July	195.4
2005	August	196.4
2005	September	198.8
2005	October	199.2
2005	November	197.6
2005	December	196.8
2006	January	198.3
2006	February	198.7
2006	March	199.8
12-Month Average		197.0

PARTIAL YEAR LIMITATION =

October 2006 Notice Recent Average (C)	-1	=	200.6	-1	=	1.8%
October 2006 Notice Base Average (D)			197.0			

[2062] A corresponding adjustment can be made should the Postal Service file a notice of rate adjustment more than 12 months after the last adjustment. This scenario provides no reason to alter the calculation of the annual inflation-based limitation, but does present a different concern; there are several months of CPI-U changes that the Postal Service may lose. The clear intent of the statutory provision allowing for recapture of unused rate authority is to encourage the Postal Service to whenever possible refrain from imposing the maximum permissible rate increases. If the Postal Service can delay imposing increases on the public, it should not be penalized. See proposed rule

3100.26(c). To address this concern, the interim unused rate authority will be added to the cumulative unused rate authority.

[2063] Still assuming that the Postal Service filed its first notice of rate adjustment in April 2006 (Example 1), assume now that the Postal Service files its second hypothetical notice of rate adjustment in July 2007 (15 months later). Example 3 illustrates how the price cap will be calculated for the July 2007 notice of rate adjustment, along with the calculation of the three months of interim unused rate authority. To calculate interim unused rate authority, divide the Base Average of the current notice by the Recent Average of the last notice and subtract 1. The formula to calculate the amount of interim unused rate authority is as follows:

$$\text{Interim Unused Rate Authority} = (\text{Base Average for Current Notice} / \text{Recent Average for Last Notice}) - 1.$$

Example 3

(F)

July 2007 Notice Base Average		
<u>YEAR</u>	<u>MONTH</u>	<u>CPI-U MONTHLY INDEX</u>
2005	July	195.4
2005	August	196.4
2005	September	198.8
2005	October	199.2
2005	November	197.6
2005	December	196.8
2006	January	198.3
2006	February	198.7
2006	March	199.8
2006	April	201.5
2006	May	202.5
2006	June	202.9
12-Month Average		199.0

(E)

July 2007 Notice Recent Average		
<u>YEAR</u>	<u>MONTH</u>	<u>CPI-U MONTHLY INDEX</u>
2006	July	203.5
2006	August	203.9
2006	September	202.9
2006	October	201.8
2006	November	201.5
2006	December	201.8
2007	January	202.4
2007	February	203.5
2007	March	205.4
2007	April	206.7
2007	May	207.9
2007	June	208.4
12-Month Average		204.1

ANNUAL LIMITATION =

$$\frac{\boxed{\text{July 2007 Notice Recent Average (E)}}}{\boxed{\text{July 2007 Notice Base Average (F)}}}^{-1} = \frac{\boxed{204.1}}{\boxed{199.0}}^{-1} = \boxed{2.6\%}$$

INTERIM UNUSED RATE AUTHORITY =

$$\frac{\boxed{\text{July 2007 Notice Base Average (F)}}}{\boxed{\text{April 2006 Notice Recent Average (C)}}}^{-1} = \frac{\boxed{199.0}}{\boxed{197.0}}^{-1} = \boxed{1.0\%}$$

[2064] APWU argues for cross-class application of unused rate authority and recommends a method of weighting the revenue. This cross-class application of unused rate authority would grant the Postal Service the ability to use unused rate authority from one class, and apply it to other classes of mail in later years. APWU Comments, April 6, 2007, at 9-10. Several parties assert that this would (1) be at odds with section 3622(d)(2)(C), which states that the annual limitations shall apply to a class of mail and defines unused rate authority in terms of an individual class of mail; (2) be inconsistent with the legislative history; and (3) merge multiple class-specific baskets into a single basket. See ANM/MPA Reply Comments, May 7, 2007, at 3-6; ANM/NAPM/NPPC Reply Comments, May 7, 2007, at 9-11; MOAA Reply Comments, May 7, 2007, at 11; Pitney Bowes Comments, April 6, 2007, at 9; and USPS Reply Comments, May 7, 2007, at 16.

[2065] The Commission agrees that unused rate authority for a given class of mail may only be applied to the class where it originated.

[2066] Finally, The McGraw-Hill Companies, Inc. (McGraw-Hill) suggests that the rules should include a method to reduce the price cap if the Postal Service performance levels deteriorate, or if the Postal Service places costly mail preparation requirements on mailers. See McGraw-Hill Reply Comments, July 30, 2007, at 6-7. During the Kansas

City field hearings, witness Stumbo of Meredith Corporation expressed a similar concern:

We would submit that the critical issues regarding cost shifting and service reduction are [sic] the rate-setting process must contain a mechanism to adjust rates to reflect the shift in cost from the Postal Service to private industry. In addition, the rules should contain methodology to adjust rates to reflect the diminished level of service the imposition of preparation rule changes or other means.

Transcript of Kansas City Field Hearing, June 22, 2007, at 40.

[2067] No commenter has suggested a method for applying such adjustments. The Commission is sympathetic to these concerns, yet finds the better course is to defer such considerations. The statute establishes a system of accountability through increased transparency. The Commission is developing separate rules providing for annual Postal Service reports that will include data on service achievement. Additionally, proposed rule 3200.91 requires the Postal Service to inform the Commission of changes that would alter the nature of a product through the imposition of preparation rule changes.

[2068] The Commission expects that the Postal Service will operate within both the letter and the spirit of the PAEA. For now, it is best to presume that the Postal Service will do so. If experience shows that additional regulations in this area are necessary to achieve the objectives of the legislation, the Commission is obligated to develop such regulations, or recommend to Congress appropriate additional legislation.

[2069] *Test for compliance with the annual limitation.* Proposed rule 3100.20 states that the appropriate annual limitation shall be applied to a measure of the rates paid by mail sent in each class for which rate adjustments are to be made to determine whether planned rates are consistent with the annual limitation.

[2070] 39 U.S.C. § 3622(d) requires that the system for regulating rates and classes for market dominant products include a limitation on the percentage increase in rates. To calculate the percentage change in an individual rate is a simple matter, but section 3622(d)(2)(A) stipulates that the restriction be applied at the class level.

Therefore, to determine compliance in the context of a pre-implementation compliance review of a notice of rate adjustment, it is necessary to develop rules that provide a means of calculating the aggregate percentage change in rates for each class. To accomplish this, weights (in the form of billing determinants) must be applied to the set of rates that comprise a class.

[2071] *Postal Service proposal.* The Postal Service proposes to apply the most recent available billing determinants to the current rates, then apply the same billing determinants to the new rates and compare the resulting revenues to determine the change in rates for a class. As acknowledged by the Postal Service, this is not ideal because an annual rate cycle combined with the need for advance notice dictates that the billing determinants will not correspond to a single set of rates, but will reflect mailer behavior for part of a year at the current rates and part at the previous rates. Postal Service Reply Comments, May 7, 2007, Appendix C. Rather than debating the rates (current or new) to which the *ideal* billing determinants would correspond, the parties' comments have focused on more practical considerations regarding the use of historical billing determinants instead of forecast billing determinants.

[2072] *Parties' positions.* On this, there is near universal support for the Postal Service's proposed approach, or some slight variation thereof. Pitney Bowes, OCA, MOAA, ANM/MPA, APWU, PostCom, Advo, and JPMorgan/Chase all support the use of historical billing determinants as weights in their comments. The primary rationale for this position is that historical data are far less likely to be controversial than forecasts, and given the limited time and public participation for the review of notices of rate adjustment, simplicity and speed of analysis should take precedence.

[2073] There is some disagreement regarding the treatment of classification changes and negotiated service agreements. The Postal Service proposes to make adjustments to the historical billing determinants to incorporate the effects of classification changes, such as the creation or elimination of rates. It proposes to use known mail characteristics and reasonable judgments to make the necessary adjustments. See Postal Service Comments, June 18, 2007, at 7-10, *inter alia*. This

proposal is supported by MOAA. See MOAA Comments, April 6, 2007 at 4-5; ANM/MPA Comments, May 7, 2007, at 1-2; and APWU Comments, June 18, 2007, at 3-4.

[2074] PostCom takes the position that the effects of classification changes are outside the scope of the Commission's pre-implementation review of a notice of rate adjustment. It argues that the effects of such changes on compliance with the price cap may only be determined in a *post hoc* review of the new rates. PostCom concludes that, "any attempt by the Commission to assess the effects of a change in rate design at the time that the change is proposed will entail a re-introduction of the old cost of service methods that the Commission has used under the Postal Reorganization Act, including the attempt to establish a test year, the reintroduction of roll-forwards and volume and revenue forecasts, and all of the uncertainty, controversy and confusion that these methods entail." PostCom Comments, June 18, 2007, at 4-5.

[2075] *Commission analysis.* The Commission's proposed rules calculate the percentage change in rates using the most recent available billing determinant as weights. As many parties point out, any attempt to develop a forecast of billing determinants would likely be controversial and complex, and a worthwhile analysis and resolution cannot realistically be achieved in the context of a pre-implementation review under section 3622(d)(1)(C).

[2076] The rules also instruct the Postal Service to make reasonable adjustments to the billing determinants to account for the effects of classification changes. The Postal Service has stated that such adjustments will typically be straightforward and based on known mail characteristics. Any adjustments are to be fully explained by the Postal Service at the time of the notice.

[2077] The Commission recognizes that the pre-implementation method of calculating the percentage change in rates in the proposed rules is not a perfect measure of what the actual change in rates will be. The billing determinants to be used will likely not correspond to a single set of rates, and adjustments for classification changes will be imperfect. Some commenters suggest that the after-the-fact review will be the most effective means of ensuring compliance with the rate cap. *Id.* at 4-6; see also Transcript

of Wilmington Field Hearing, July 9, 2007, at 47. (Emens).¹³ The statute requires the Commission to monitor the effectiveness of these rules and consider modifications to improve their effectiveness as events warrant.

[2078] Proposed rule 3100.23, captioned “Calculation of percentage change in rates,” explains in paragraph (b) that for each class of mail, the percentage change in rates is calculated in three steps. The first step involves multiplying the volume of each rate cell in the class by the current rate for that cell and summing the resulting products. (In the case of seasonal or temporary rates, the most recently applied rate shall be considered the current rate.) The second step involves multiplying the same set of rate cell volumes by the corresponding planned rate for each cell and summing the resulting products. The third step involves calculating the percentage change in rates by dividing the results of the first step by the results of the second step and subtracting 1 from the quotient. The result is expressed as a percentage. Paragraph (c) sets out the formula.

[2079] *Treatment of volume associated with negotiated service agreements.* Advo and Pitney Bowes advocate the exclusion of negotiated service agreements from the determination of percentage changes in rates. They assert that including the lower rates offered to negotiated service agreement partners will allow for offsetting larger increases for non-negotiated service agreement mail, thus undermining the price cap protection afforded to non-participating mailers. See Advo Comments, June 18, 2007, at 4; Pitney Bowes Comments, June 18, 2007, at 4. The Postal Service disagrees, arguing that in certain situations, some negotiated service agreement mailers may pay prices higher than list prices. If this occurs, excluding negotiated service agreements from the calculation of change in revenue would deny non-negotiated service agreement mailers the opportunity for potentially lower increases. Postal Service Reply Comments, July 3, 2007, at 6-7.

¹³ See also Campbell, James, *An Analysis of Provisions of the Postal Accountability and Enhancement Act Relating to the Regulation of Postal Rates and Services*, August 3, 2007, at 52-55.

[2080] The proposed rules exclude the effects of negotiated service agreements from the calculation of percentage change in rates. The foundational argument in support of negotiated service agreements is that they can be structured to benefit the participating mailer and the Postal Service, while not harming (and hopefully, benefiting) non-participating mailers. Pitney Bowes and Advo are correct in their conclusion that including negotiated service agreements in the test for compliance with the rate cap may lead to rates for non-participating mailers that exceed the rate cap. This would undermine the rationale for permitting negotiated service agreements.

[2081] Proposed section 3100.24 addresses volume associated with negotiated service agreements. Paragraph (a) provides that mail volumes sent at non-tariff rates under negotiated service agreements are to be included in the calculation of percentage change in rates as though they paid the appropriate rates of general applicability. Where it is impractical to identify the rates of general applicability, the volumes associated with the mail sent under the terms of the negotiated service agreement shall be excluded from the calculation of percentage change in rates. Paragraph (b) requires related support in the form of identification and explanation of all assumptions made with respect to the treatment of negotiated service agreements in the calculation of the percentage change in rates and the rationale for assumptions.

[2082] *Limit on application of banking exception.* Proposed rule 3100.25 addresses certain limits on unused rate adjustment authority. It provides that these adjustments may only be applied together with inflation-based limitation rate adjustments or when inflation-based limitation rate adjustments are not possible. It further provides that unused rate adjustment authority may not be used in lieu of an inflation-based limitation rate adjustment.

H. Overview of Subpart D—Rules for Rate Adjustments for Negotiated Service Agreements (Type 2 Rate Adjustments)

[2083] Section 3622(c)(10) of the PAEA requires consideration of the desirability of special classifications for both postal users and the Postal Service. Subsections 3622(c)(10)(A) and (B) mandate that such agreements must improve the net finances of the Postal Service or enhance operational performance while not causing unreasonable harm to the marketplace. Section 3622(d)(1)(C) further details the review period that will begin “not later than 45 days before the implementation” of any agreement made under subsection (c)(10). These subsections of the PAEA provide the basis and criteria for evaluating and approving negotiated service agreements.

[2084] In their comments, parties have expressed a range of views on how the Commission should implement the legislative framework for negotiated service agreement regulation. The level of review described in these diverse comments can be summarized into two groups: parties who consider the current negotiated service agreement process amenable with the PAEA, and parties who assert that the PAEA calls for a significantly streamlined process.

[2085] Parties who support a continuation of the current process, and in some instances, the regulations as currently written, include Valpak, NAA, Jon Mulford Associates, and APWU. This viewpoint was summarized by NAA, stating

[t]he Commission should continue to adhere to its established, balanced approach to considering special classifications in the form of negotiated services agreements or niche classifications. This includes conducting a thorough public and prior review, which results in a determination that the proposed mailer-specific agreement may or may not take effect. In keeping with the new statutory approach giving the Commission the final say, that determination should be subject to judicial review.

NAA Reply Comments, May 7, 2007, at 13.

[2086] Parties supporting a simplified and minimal review of negotiated service agreements include Advo, Discover Financial Services, LLC (DFS), MOAA, Pitney Bowes, and Time Warner. This viewpoint was summarized by Pitney Bowes stating, “The elimination of advance, on-the-record Commission review of NSAs should significantly enhance the Postal Service’s ability to meet the needs of mailers... .” Pitney Bowes Reply Comments, May 7, 2007, at 13.

[2087] The Commission finds that the statute requires a regulatory approach that combines elements of the divergent views among parties. The legislation seeks to provide the Postal Service with added flexibility to enhance producer and consumer surplus through negotiated service agreements. The proposed rules will decrease the administrative and economic burden in implementing such agreements. However, arguments such as those presented in the comments of Jon Mulford, stating “[t]he Commission should insure that periodic audits verify that claimed benefits persist through the duration of the NSA” also reflect the policies of the PAEA. See Jon Mulford Associates Comments, March 14, 2007, at 4. Combining flexibility and accountability is the essence of the new legislation, and the Commission attempts to achieve the proper balance in the subpart D rules.

[2088] This subpart consists of four rules. Proposed rule 3100.40 expresses the Commission’s objective in administering the implementation of negotiated service agreements. It clarifies that this objective is directly tied to statutory requirements in 39 U.S.C. § 3622(c)(10) mandating that special classifications either improve the net financial position of the Postal Service or enhance the performance of operational functions and do not cause unreasonable harm to the marketplace.

[2089] *Timing of notice and review.* Proposed rule 3100.41 addresses procedures. Paragraphs (a)(1) and (2) reflect the requirements for Type 2 changes that public notice and notice to the Commission occur not later than 45 days prior to the intended rate implementation date.

[2090] *Contents of filing.* Proposed rule 3100.42 addresses the contents of a notice in support of a negotiated settlement agreement. It indicates that this should include, at

a minimum, a copy of the negotiated service agreement and a statement identifying all parties and a description explaining the operative components. It is also to include the estimated mailer-specific costs, volumes and revenues of the Postal Service absent the implementation of the agreement; the estimated mailer-specific costs, volumes and revenues of the Postal Service which result from implementation; and an analysis of the effects of the agreement on the contribution to institutional costs from mailers not party to the agreement. If mailer-specific costs are not available, the source and derivation of the costs that are used shall be provided, together with a discussion of the currency and reliability of those costs, and their suitability as a proxy for the mailer-specific costs.

[2091] The Postal Service is also to identify each component of the agreement expected to enhance the performance of mail preparation, processing, transportation or other functions in each year of the agreement, and a discussion of the nature and expected impact of each such agreement. Furthermore, it is to provide details regarding any and all actions to assure that the agreement will not result in unreasonable harm to the marketplace.

[2092] Finally, the Postal Service is to collect and provide annual data that are intended to enable the Commission and interested persons to evaluate whether each negotiated service agreement has met, and is likely to meet in the future, the expectations that caused the Postal Service to enter the agreement. It is understood that not every agreement will meet Postal Service expectations. Nonetheless, continuing periodic review is the best way to assure that flaws in Postal Service projection techniques are recognized and remedied.

I. Overview of Subpart E—Rules for Rate Adjustments in Exigent Circumstances (Type 3 Rate Adjustments)

[2093] The PAEA also requires that the Commission establish procedures to allow rate adjustments in excess of the annual limitation on an expedited basis due to either extraordinary or exceptional circumstances, provided:

[T]here is not sufficient unused rate authority as defined in 39 U.S.C. §3622(d)(2)(C); and

[T]he Commission determines, after notice and opportunity for a public hearing and comment, and within 90 days after any request by the Postal Service, that such adjustment is reasonable and equitable and necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.

See 39 U.S.C. § 3622(d)(1)(E).

[2094] There are several significant differences between a Type 3 change and the other three types. First, based on the legislative history, a Type 3 change is expected to be an atypical occurrence, while the other types are considered more routine. Types 1-A, 1-B and two changes follow the streamlined 45-day notice-and-review process, while a Type 3 filing occurs pursuant to a request and a hearing, with up to 90 days for consideration.

[2095] Commenters addressing implementation of the exigency clause in 39 U.S.C. § 3622(d)(1)(E) focus mainly on the extent to which Commission rules should define “exigent circumstances” for purposes of rate adjustments; the related possibility, if the definition is too broad, that frequent requests for exigent increases could undermine the intended discipline of the price cap mechanism; and the nature and extent of public participation in exigent request filings.

[2096] The Postal Service describes the PAEA’s exigency clause as a safety valve for those “extraordinary or exceptional situations in which the [price] cap cannot be met

even through honest, efficient, and economical management.” Postal Service Comments, April 6, 2007, at 16. It does not address the content of an exigent rate filing or the role of the public, but asserts, with respect to defining exigent circumstances, that it is not necessary or prudent for the Commission to attempt to specify in this rulemaking the situations that might be covered in advance of an actual need to do so. Postal Service Reply Comments, May 7, 2007, at 15.

[2097] Pitney Bowes and Time Warner share the Postal Service’s view that the Commission should not attempt to define qualifying circumstances at this time. Pitney Bowes suggests addressing the question on a case-by-case basis as circumstances arise. Pitney Bowes Comments, April 6, 2007, at 10. Similarly, Time Warner says:

... the Commission need not and should not attempt to determine a substantive standard for granting Postal Service requests under the exigent circumstances provision (other than the standard set out in § 3622(d)(1)(E) itself) until presented with the concrete circumstances attending an actual Postal Service request under that provision; the kind of judgment that the Commission is called on to make in deciding whether to grant such a request cannot be exercised well in the abstract or upon hypotheticals; moreover, to the extent that such a standard might err on the side of leniency, it would undermine the discipline that the price caps are intended to instill, and to the extent that it might err on the side of stringency, it could create perverse incentives to find alternative ways of circumventing the caps.

Time Warner Comments, April 6, 2007, at 22-23.

[2098] Several other commenters echo Time Warner’s concern about the relationship between the exigency clause and the price cap mechanism. The Alliance of Nonprofit Mailers, National Association of Presort Mailers, and National Postal Policy Council jointly state: “... the exigency provision for ‘extraordinary or exceptional’ services must be drawn very narrowly; otherwise the availability of this mechanism will undermine the index as a constraint on costs and efficiency.” ANM/NAPM/NPPC Comments, April 6, 2007, at 2 and 11; *see also* ANM/NAPM/NPPC Reply Comments, May 7, 2007, at 8. They urge the Commission to make it clear that exigent financial

consequences should have to be large enough to threaten the Postal Service's financial integrity, and must not be due to an unreasonable failure to hedge and insure against risk or any other form of inefficient or uneconomical management. ANM/NAPM/NPPC Comments, April 6, 2007, at 11. Randy Stumbo, representing Meredith Corporation, says: "An easy out provided by a liberal exigency provision would seriously damage the cost control incentive created by a rate cap." Stumbo Testimony at 3.¹⁴

[2099] Don Hall, Jr., representing Hallmark, also cautions: "... [I]f the exigency provision is over-used, mail users in all classes will have to conclude that the price cap scheme is not going to succeed — and, as the Act also provides, after 10 years this Commission will have to devise something better." Hall Testimony at 7.¹⁵

[2100] Mr. Hall also asserts that it is imperative that the Commission clarify what circumstances warrant the rate cap to be pierced and to make certain that the Postal Service exhaust all other resources provided by its ability to retain earnings before seeking rate increases above the cap. *Id.* at 12.

[2101] Mr. Stumbo seeks more specific direction, as he suggests:

While it seems premature and imprudent to explicitly define in the abstract the events under which exigency may be exercised, it is necessary to define what it is not. Attributable cost shortfalls at the class or subclass level do not constitute exigent circumstances. Nor should the exigency clause be used to re-apportion rates in any way.

Stumbo Testimony at 3.

[2102] The Magazine Publishers Association (MPA) and the Alliance of Nonprofit Mailers (ANM) agree that the failure of a class to cover its attributable costs should be affirmatively identified as not qualifying as an exigent circumstances. ANM/MPA Comments, April 6, 2007, at 11-12. Time Warner, however, claims that the Commission

¹⁴ Testimony of Randy Stumbo, Director of Distribution and Postal Affairs for Meredith Corporation, Postal Regulatory Commission Field Hearing, Kansas City, June 22, 2007 (Stumbo Testimony).

¹⁵ Testimony of Don Hall, Jr., President and CEO, Hallmark Cards, Inc., June 22, 2007 (Hall Testimony).

need not and should not decide that failure of a class to recover attributable costs could *never* constitute exigent circumstances justifying above-cap increases. Time Warner Reply Comments, May 2, 2007, at 33.

[2103] The Greeting Card Association (GCA) suggests that the Commission could clarify the scope of the exigency clause by defining “extraordinary or exceptional circumstances” to exclude matters that, under the Postal Reorganization Act of 1970, would have been dealt with under the provision for contingencies. GCA Comments, April 6, 2007, at 9. It says the Commission should provide guidance on how the nature of the “extraordinary or exceptional” circumstances motivating the adjustment relates to the allocation of burdens among mail users. *Id.* at 11-12. GCA also concludes, after addressing the potential impact of external and internal events, that the Commission

... should make clear in setting up the subparagraph (E) [exigency clause] procedures that the Postal Service, in first presenting its proposed adjustment, must explain fully (i) the nature of the extraordinary or exceptional circumstances claimed to justify the rate change, and (ii) the theory on which it considers its proposed rate changes appropriate to reflect (i).

Id. at 13. Moreover, it asserts that this explanation should be required to be part of the initial filing, as the Commission must make its required findings in 90 days or less. *Id.*

[2104] Commenters differ on the nature and extent of public comment. Advo, for example, simply notes, in contrasting the types of public input called for in the PAEA, that the statute requires that the Commission provide “notice and opportunity for public hearing and comment,” but does not address the nature and scope of the public hearing. Advo Comments, April 6, 2007, at 5. GCA and Time Warner note that the PAEA provides an opportunity for public participation when the Postal Service files an exigent request, but do not contend that this mandates formal trial-type hearings. GCA, instead, asserts that the procedures must provide “some opportunity” for parties to raise challenges to the bases of the proposed increase, and that the Postal Service must overcome such challenges to meet the burden of justifying exigent increases. GCA Comments, April 6, 2007, at 14-15. Others suggest that the PAEA’s reference to an

“opportunity for public participation and comment” means that the Commission must establish trial-type proceedings for exigent requests. *See, for example,* ANM/NAPM/NPPC Comments, May 7, 2007, at 11.

[2105] *Discussion.* The Commission appreciates commenters’ concerns that the exigency clause, if invoked too frequently, could undermine the statutory price cap mechanism. At this point, it should be assumed that the Postal Service’s intent is to honor the clear import of the PAEA’s overarching ratesetting philosophy that exigent requests are meant to be a safety net for dealing with unforeseeable emergencies. The Commission believes that the commenters’ concerns can largely be addressed by requiring, as proposed rule 3100.61 does, that the Postal Service provide focused explanation in support of any exigent request. This includes a full discussion of the circumstances giving rise to the filing, the reasons why the requested increases are necessary, and why the specific proposed increases are reasonable and equitable as between the types of users of market dominant products. The Postal Service will be required to provide considerable additional context, such as an explanation of how long the exigent increases are intended to be in effect, the circumstances under which rescission of the increases might occur, a justification addressing the foreseeability or avoidability of the circumstances giving rise to the request, and other information that would assist the Commission in reaching a decision. The Commission reserves the right, in proposed rule 3100.62, to require the Postal Service to clarify or further supplement its request. These provisions do not explicitly define “exigent circumstances,” and unmistakably convey the message that exigent requests are indeed “extraordinary or exceptional.”

[2106] The proposed rules provide that upon receipt of an exigent request, the Commission will conduct an expedited review, including a public hearing, that allows for resolution within 90 days. The rulemaking record is relatively slim on this aspect of PAEA implementation, perhaps due to the focus on filings considered more routine. The Commission has carefully considered the nature and extent of public input for exigent requests, and preliminarily has concluded that while the PAEA would not preclude

reviving the trial-type proceedings that held sway in the past, it also does not require them. The fact that the statute does not explicitly refer to a hearing “on the record,” which is universally associated with trial-type hearings under the Administrative Procedure Act (APA), provides support for this conclusion. The drafters were well aware that the system they were replacing had included APA-style formal proceedings, and could have mandated equivalent proceedings for exigent requests by including an unmistakable reference to “on the record” proceedings, but did not. Additional support is drawn from the period of time (90 days) allowed for review, which is inconsistent with overly-elaborate hearings; and as the Postal Service and some joint commenters suggest, the likelihood that issues will not simply require adjudication of facts, but also may involve significant policy considerations. Given these considerations, the Commission proposes a written process, without cross-examination, to facilitate public participation, coupled with public hearings at which one or more responsible Postal Service official would appear for questioning by the Commission. This mechanism strikes an appropriate balance between assuring transparency and accountability in keeping with the statute, while facilitating completion of review within 90 days. These provisions appear in proposed subpart E.

III. COMPETITIVE PRODUCTS

[3001] Subchapter II of chapter 36 of title 39, 39 U.S.C. §§ 3631-34, sets forth the provisions applicable to competitive products, which, pursuant to section 3631(a), initially include priority mail, expedited mail, bulk parcel post, bulk international mail, and mailgrams.¹⁶ Section 3631(c) provides that “[m]ail matter referred to in [§ 3631(a)] shall, for purposes of this subchapter, be considered to have the meaning given to such mail matter under the mail classification schedule.” In Order No. 15, the Commission solicited the parties’ views on “mail matter” comprising each of the foregoing types of mail and on the meaning of the phrase “mail classification schedule.” PRC Order No. 15, May 17, 2007, at 6. Several parties addressed these issues. See, e.g., Postal Service Comments, June 18, 2007, at 11-16; UPS Comments, June 18, 2007, at 2-4; OCA Comments, June 18, 2007 at 22-27; and PSA Comments, June 18, 2007, at 1-3.

A. Mail Classification Schedule

[3002] OCA and UPS contend that “mail classification schedule” as used in section 3631(c) refers to the Domestic Mail Classification Schedule (DMCS).¹⁷ For several reasons, the Commission is not persuaded by this construction. First, section 3631(a) includes mail matter not subject to the DMCS, i.e., bulk international mail. Second, when Congress intended that the DMCS be used, it was specific. See section 3622(d)(2)(A), applying the price cap limit to “a class of mail, as defined in the Domestic Mail Classification Schedule as in effect on the date of enactment of the [PAEA].” Thus, the failure to specify the DMCS in section 3631(c) suggests that something else is intended. Third, while the DMCS may be useful in initially determining mail matter comprising the

¹⁶ Pursuant to section 3642, the Commission may change the lists of competitive products under section 3631 and market dominant products under section 3621 by adding new products to or removing products from the lists, or transferring products between the lists.

¹⁷ OCA Comments, June 18, 2007, at 23; UPS Comments, June 18, 2007, at 2.

competitive products, the mail classification schedule has a continuing, if somewhat new, role under the statute. Among other things, the mail classification schedule incorporates international mail (both single-piece and bulk) and is subject to section 3642, which authorizes the Commission to modify the makeup of competitive and market dominant products.

[3003] The Postal Service recognizes that the PAEA contemplates a mail classification schedule, suggesting that it would contain “a level of detail equivalent to the current DMCS,” with additional language added to account for international mail. Postal Service Comments, June 18, 2007, at 16. The Postal Service advocates that separate classification schedules be established for market dominant and competitive products. *Id.*

[3004] In supplemental comments, the Postal Service offers its views on what it calls the classification process.¹⁸ Regarding competitive products, it argues that the Commission has no role in developing or overseeing the mail classification schedule other than determining, pursuant to section 3642, what products are in the competitive category of mail. *Id.* at 14. The Postal Service asserts that “the Governors will maintain the ‘Competitive Products Classification Schedule,’” with changes made pursuant to section 3632(b). *Id.* The Commission interprets its responsibilities under the PAEA differently, concluding that the mail classification schedule falls within its purview.

[3005] The Postal Service states that “the PAEA clearly vests classification authority with the Governors[.]” *Id.* To a point, this statement is unobjectionable. Notably, however, it overlooks limitations on the Governors’ authority, namely, that it is subject to subchapter II (of chapter 36 of title 39) and regulations promulgated by the Commission under section 3633. Moreover, the Governors’ authority to change rates or classes (pursuant to section 3632) cannot reasonably be read to encompass the wholly separate power to develop and maintain a mail classification schedule for competitive

¹⁸ Postal Service Supplemental Comments, June 19, 2007. The bulk of these comments relate to market dominant products, with the Postal Service suggesting a framework for classification changes and development of a mail classification schedule. *Id.* at 1-14.

products. If the Governors were intended to have such authority, there would be no reason for the process mandated by section 3631 or for subjecting the Governors' authority to change rates or classes to the Commission's regulations. Nor would there be any reason for the separate provision, section 3642, for establishing new products.

[3006] Section 3631(a) identifies the initial list of competitive mail matter, including priority mail, expedited mail, bulk parcel post, and bulk international mail.¹⁹ None of these terms is defined in the statute. To establish what each of the foregoing means section 3631(c) instructs that the “[m]ail matter referred to in subsection (a) shall, for purposes of this subchapter, be considered to have the meaning given to such mail matter under the mail classification schedule.” Pursuant to this rulemaking, the Commission will identify the mail matter, including the products, in the (competitive) mail classification schedule that initially comprise each type of mail listed in section 3631(a). This process is integral to the Commission fulfilling its responsibilities under the PAEA, which requires, among other things, that each competitive product cover its attributable costs.

[3007] Commission maintenance of the mail classification schedule does not deprive the Governors of any flexibility to change rates or classes or offer new products. It does, however, assure non-discriminatory service and transparency in a manner contemplated by the statute.²⁰ The mail classification schedule identifies the products subject to the Commission's oversight, a task which does not fall to the Governors.²¹

¹⁹ The list also includes “mailgrams,” a service which was terminated on August 17, 2006. See *Postal Bulletin* 22192, October 26, 2006, at 5; see also letter from Daniel J. Foucheaux, Jr. to Steven W. Williams, Secretary, Postal Rate Commission, filed November 2, 2006.

²⁰ The Commission concurs with the Postal Service's position that the mail classification schedule should provide a level of detail similar to the DMCS. The Commission also agrees with the Postal Service that maintaining separate classification schedules for market dominant products and competitive products is reasonable. Nonetheless, for administrative convenience and clarity, the Commission intends to initially combine the separate lists for market dominant and competitive products in a single mail classification schedule.

²¹ The mail classification schedule also serves as the source of the list of competitive products maintained by the Commission pursuant to section 3642.

B. Competitive Mail Matter

[3008] Not unreasonably, parties addressing the issue define mail matter, in the first instance, by reference to the existing materials, namely, the DMCS and International Mail Manual (IMM). This works reasonably well for “priority mail” and “expedited mail,” both of which appear in the DMCS. Thus, for example, the Postal Service suggests that “priority mail” consists of mail within the “Priority Mail” subclass (DMCS § 223) and “expedited mail” consists of Express Mail entered under the “Expedited Mail Classification Schedule” (DMCS § 110 *et seq.*). Postal Service Comments, June 18, 2007, at 11-12.²²

[3009] For purposes of promulgating the initial regulations applicable to competitive products, the Commission agrees that, at a minimum, mail matter qualifying as priority mail and expedited mail is that described in the DMCS. There are three features to this initial classification: each represents only domestic mail; each is a separate product; and the rates for each product are rates of general applicability.

[3010] OCA notes that the listing of priority mail and expedited mail in section 3631(a) does not distinguish between domestic and international mail or between single-piece and bulk. OCA Comments, June 18, 2007, at 23. Thus, it asserts that priority mail and expedited mail should include both domestic and international in the competitive mail classification schedule.²³ This position is not unreasonable and the Commission proposes to include outbound international priority mail (Priority Mail International) and expedited mail (Global Express Guaranteed and Express Mail International) as separate products within the priority mail and expedited mail classifications respectively. As discussed below, inbound shipments would be classified as market dominant.

²² See also OCA Comments, June 18, 2007, at 22; PSA Comments, April 6, 2007, at 8, n.8; PSA Comments, June 18, 2007, at 2; and UPS Comments, June 18, 2007, at 2.

²³ *Id.* Elsewhere, however, OCA appears to suggest that other than two “bulk international mail” services all remaining international mail should be categorized as market dominant. *Id.* at 26.

[3011] Reference to the DMCS and IMM works less well for “bulk parcel post” and “bulk international mail” since neither is clearly delineated.²⁴ The parties addressing the issue agree generally that “bulk parcel post” consists of the following mail matter: Parcel Select (DMCS §§ 521.23-26); Parcel Select Return Service (DMCS §§ 521.27-28); Inter-BMC qualifying for OBMC and BMC discounts (DMCS §§ 521.41-42); and Inter-BMC and Intra-BMC qualifying for a barcode discount (DMCS § 521.5). See Postal Service Comments, June 18, 2007, at 12-13; PSA Comments, June 18, 2007, at 3; OCA Comments, June 18, 2007, at 24; and UPS Comments, June 18, 2007, at 2-3.

[3012] The Commission agrees with the consensus view that “bulk parcel post” consists of the following mail matter: Parcel Select, Parcel Return Service, and Parcel Post mail qualifying for OBMC, BMC, and barcode discounts. Initially, therefore, bulk parcel post would be comprised of these three products.

[3013] UPS and the Postal Service also suggest that bulk parcel post include additional mail matter. UPS would include mail entered as Inter-BMC or Intra-BMC Parcel Post by commercial mailers in quantities greater than one. UPS Comments, June 18, 2007, at 3; see *also* UPS Reply Comments, July 3, 2007, at 1. PSA opposes UPS’s proposal as contrary to the commonly accepted use of the terms “bulk” and “single-piece” in the DMCS. PSA Reply Comments, July 3, 2007, at 2-3.

[3014] To qualify for various current Parcel Post discounts, mailers must deposit at least 50 properly prepared pieces. See, *e.g.*, DMCS §§ 521.23-26 and 521.41-42. This minimum quantity is a prerequisite for mailing at discounted (or non-single-piece) rates. UPS offers no justification for reducing that minimum volume threshold to two. Accordingly, the Commission will not adopt that suggestion.²⁵

[3015] The Postal Service suggests that “bulk parcel post” include Inter- and Intra-BMC Parcel Post pieces if postage is paid using a Merchandise Return Service

²⁴ As PSA points out, the listing of “Bulk Parcel Post” among the rate categories of the Parcel Post subclass (DMCS § 521.3) is an anachronism since there is no current rate associated with that rate category which preceded the Parcel Select rate categories. PSA Comments, June 18, 2007, at 2.

²⁵ Should experience prove otherwise, mail matter defined as single-piece parcel post may, if appropriate, be transferred to the competitive products classification pursuant to section 3642.

permit. Postal Service Comments, June 18, 2007, at 12-13. Merchandise Return Service is a special service enabling the permit holder to authorize a mailer to mail parcels, including Parcel Post mail, with the postage and fees paid by the permit holder. Merchandise Return Service is also available for sending First-Class Mail parcels. No party commented on this proposal specifically.²⁶

[3016] Although the proposal has some appeal, the Commission will not adopt it at this juncture. Under the PAEA, special services are classified as market dominant as are First-Class Mail parcels. The availability of Merchandise Return Service as both a market dominant and competitive service raises practical difficulties that are unexplored in this docket. Moreover, there may well be other special services that would be better categorized as competitive. Thus, to consider one in isolation may lead to results with unintended consequences. The better practice is to utilize the procedures for transferring items between the market dominant and competitive product lists once these lists have been established as specified by Congress in the PAEA.

[3017] The parties' attempts to define the term "bulk international mail" are handicapped by the lack of a long-standing mail classification schedule. Instead, they turn to the IMM for guidance. It is a useful tool, but does not eliminate uncertainty surrounding the meaning of the term "bulk international mail." Based on the parties' comments, there appears to be little dispute that, at a minimum, bulk international mail consists of the following:²⁷ International Priority Airmail Service (IPA), which is available to bulk mailers of all international letter items (IMM § 292); International Surface Airlift Service (ISAL), which is a bulk mailing system for the delivery of letter items (IMM § 293); and International Customized Mailing Agreements (ICMs), which are mailer-specific

²⁶ In its reply comments, UPS notes that it agrees generally with the Postal Service's definition of bulk parcel post. UPS Reply Comments, July 3, 2007, at 1.

²⁷ See Postal Service Reply Comments, May 7, 2007, at 32-33; Postal Service Comments, June 18, 2007, at 13-14; UPS Comments, June 18, 2007, at 4; OCA Comments, June 18, 2007, at 26; and PSA Comments, April 6, 2007, at 8, n.8; see *also* Pitney Bowes Comments, June 18, 2007, at 12-13.

agreements subject to minimum revenue or quantity requirements (IMM § 297).²⁸ There is, however, some controversy over the characterization of the remaining international mail services.

[3018] The Postal Service suggests that bulk international mail should be interpreted to include “multi-item mailings tendered by a single mailer.”²⁹ The Postal Service indicates that multiple quantities may be satisfied by volume commitments or other types of annual guarantees. *Id.* at 13. Thus, in addition to the foregoing international services, the Postal Service proposes that the following be characterized as bulk international mail: Global Bulk Economy, which it indicates provides for surface transportation of bulk First-Class Mail international items; Global Direct, which it indicates provides for direct entry of bulk mailings sent through the Postal Service bearing the indicia, postal markings, and return address of the destination country; and direct sacks of printed matter sent to a single foreign addressee, also known as M-bags. *Id.* at 14.³⁰

²⁸ OCA contends that ICMs involving single-piece international mail should be characterized as a market dominant product. OCA Comments, June 18, 2007, at 56-57.

²⁹ Postal Service Comments, June 18, 2007, at 13. In an earlier round of comments, the Postal Service endorsed the views of PSA and the International Mailers’ Advisory Group (IMAG) that certain single-piece international mail should be categorized as competitive products, but on different grounds, namely, that the products, *e.g.*, Global Express Guaranteed, Priority Mail International, and Express Mail International, are “subject to fierce competition[.]” Postal Service Reply Comments, May 7, 2007, at 32. In its more recent comments, the Postal Service’s position on what constitutes bulk international mail appears to be limited to multi-item mailings tendered by a single mailer. See Postal Service Reply Comments, July 3, 2007, at 38-39. As an exception to this, the Postal Service indicates that because costs and revenues associated with Global Package Discount service are not separately collected, Express International Mail would need to be categorized as a competitive product. Postal Service Comments, June 18, 2007, at 15, n.17.

³⁰ In its discussion of ICMs, the Postal Service refers to Global Shipping Solutions and Global Package Discounts. Postal Service Comments, June 18, 2007, at 15, *see also id.* at n.17. Whether these are separate services or marketing programs in the form of ICMs is unclear. In its comments, the Postal Service should clarify their status.

[3019] No party filed comments opposing the Postal Service's view of bulk international mail.³¹ UPS agrees with it. UPS Reply Comments, July 3, 2007, at 1. For purposes of promulgating these initial regulations, the Commission proposes to define bulk international mail by reference to bulk commercial services, which may be satisfied by volume commitments or other types of annual guarantees. This would include IPA, ISAL, ICMs, and M-bags.³² The Commission proposes to define IPA, ISAL, and M-bags as separate products and, at least initially, each ICM as a product.

[3020] Regarding international mail determined by the Commission to be a competitive product, the PAEA amends title 39 by adding section 407(e)(2) as follows:³³

With respect to shipments of international mail that are competitive products within the meaning of section 3631 that are exported or imported by the Postal Service, the Customs Service and other appropriate Federal agencies shall apply the customs laws of the United States and all other laws relating to the importation or exportation of such shipments in the same manner to both shipments by the Postal Service and similar shipments by private companies.

Section 407(e)(1) defines the term "private company" as one "substantially owned or controlled by persons who are citizens of the United States." Thus, the Commission's findings regarding international mail classified as competitive products are relevant to the application of customs and related laws to the importation and exportation of such

³¹ As noted above, in earlier comments OCA contends that an ICM involving single-piece international mail, such as Priority Mail International, should be categorized as a market dominant product. OCA Comments, June 18, 2007, at 56-57.

³² The Postal Service identifies Global Bulk Economy and Global Direct as candidates for inclusion in the bulk international mail category. Postal Service Comments, June 18, 2007, at 15. It indicates that these services are available through an ICM. Whether these services are available only as an ICM or if they represent a separate category of international mail similar to IPA and ISAL is unclear. In its comments, the Postal Service should clarify their status.

³³ The Express Delivery & Logistics Association filed a white paper concerning section 407(e) taking issue with the Postal Service position on inbound mail. White Paper by Express Delivery & Logistics Association Regarding Implementation of Section 405 of the Postal Accountability and Enhancement Act of 2006, July 20, 2007, at 2. See also FedEx Comments, April 6, 2007, at 4-5.

shipments, requiring that such laws be applied “in the same manner to both shipments by the Postal Service and similar shipments by private companies.” Regarding outbound international mail classified as competitive products, e.g., IPA, ISAL, and ICMs, section 407(e)(2) would apply to shipments by the Postal Service and similar shipments by private companies.³⁴

[3021] Regarding inbound international mail, there are two issues. First, the demarcation between bulk and single-piece international mail is less clear. The Universal Postal Union (UPU) identifies three types of mail: Letter Post, Express, and Parcel Post. The issues of inbound international mail have not been addressed sufficiently to enable the Commission to determine what inbound international mail qualifies as “bulk international mail.” Given the UPU’s designations, one possibility would be to classify Letter Post as market dominant with the other types of mail classified as competitive products. The Commission, however, has no data indicating that either Express or Parcel Post is properly considered to be “bulk international mail.”

[3022] Second, it is not apparent that classifying any inbound international mail as a competitive product has the same significance it does for outbound mail. To be sure, section 407(e) applies to the importation of shipments deemed competitive. More specifically, however, it applies to such shipments by the Postal Service and private companies owned by U.S. citizens. The Postal Service does not operate ETOEs (extra-territorial offices of exchange). Thus, there are no foreign-originating mail shipments by the Postal Service. Currently, shipments of inbound mail are handled by foreign posts and by private carriers. Foreign posts are not defined as private companies for purposes of section 407(e). In addition, although the Postal Service receives inbound mail from foreign posts at various customs locations, whether such mail is, within the meaning of section 407(e), “imported by the Postal Service” is unclear. Finally, even if *shipments received by* the Postal Service from foreign posts are

³⁴ The Commission’s interpretation of section 407(e) concerns only its role as the arbiter of international mail to be classified as a competitive product. It is not intended to suggest how other federal agencies may apply the customs laws and other laws relating to the importation and exportation of mail.

construed as *shipments by* the Postal Service, there may be good reason to view such inbound mail as market dominant. The record is not sufficiently developed to enable the Commission to determine what inbound international mail is appropriately classified as “bulk international” and, therefore, a competitive product. The parties commenting on the foregoing discussion should thoroughly address the law and facts supporting their position and, in particular, the application of section 407(e) to inbound mail.

[3023] Lastly, regarding competitive products, section 3632(b)(3) permits rate (or class) changes not of general applicability for competitive products. In recognition of this, the Commission is initially of the view that negotiated service agreements for mail classified as competitive are within the competitive products category and that each such agreement should be classified as a separate product.

C. General Applicability of Rates and Classes

[3024] Section 3632(b) identifies two types of rates or classes — those of general applicability and those not of general applicability. Each is qualified by the phrase “in the Nation as a whole or in any substantial region of the Nation[.]” Sections 3632(b)(2) and (b)(3). Section 3632(b)(4) provides that the Commission shall establish by regulation the criteria for determining whether a rate or class is or is not of general applicability in the nation or any substantial part of the nation.

[3025] Three parties address the “general applicability” of rates or classes largely by reference to their availability. The Postal Service suggests that a rate (or class) is of general applicability if it is “publicly available throughout the nation[.]” Postal Service Comments, June 18, 2007, at 19. UPS advocates a generally similar standard, contending that a rate or class is of general applicability “if it is available to all mailers equally,” even if not all mailers satisfy the conditions for the rate or class. UPS Comments, June 18, 2007, at 7. At the other end of the spectrum, the parties suggest that rates or classes negotiated between the Postal Service and individual mailers are not of general applicability. See Postal Service Comments, June 18, 2007, at 19; UPS Comments, June 18, 2007, at 7; and PSA Comments, June 18, 2007, at 4.

[3026] Defining whether a rate or class is “of general applicability” by reference to its availability is a reasonable means for establishing the outer bounds of the term. The Commission will adopt that standard. Thus, a rate (or class) of general applicability is one that is available nationwide to all mailers equally, i.e., on the same terms. That some mailers may not be able to qualify for the rate, e.g., for failure to satisfy the preparation requirements, or because it is not available in all geographic areas, does not alter the nature of the rate as one of general applicability.³⁵

[3027] On the other hand, a contract rate (negotiated service agreement) negotiated between the Postal Service and an individual mailer would not be of general

³⁵ Express Mail is not available to or from certain difficult-to-access locations. Nonetheless, it is available in the nation as a whole.

applicability.³⁶ Between these parameters, however, determining whether a rate or class is or is not of general applicability throughout the nation or in any substantial region of the nation is less exact and, in all likelihood, would turn on the facts. In those situations, availability will continue to serve as a reasonable touchstone for determining the general applicability of the rate or class.

[3028] Only the Postal Service addresses the meaning of the term “substantial region,” suggesting that it be defined by the size of the population of the relevant region. Postal Service Comments, June 18, 2007, at 19-20. That standard is one of several that might be appropriate.³⁷ Rather than address the issue in the abstract, the Commission concludes that whether a rate or class is or is not of general applicability in any substantial region of the country is, at least at the outset, best determined on a case-by-case basis based on the facts presented. Currently, with the possible exception of Alaska bypass, the Postal Service does not provide any non-nationwide service.³⁸ Among other things, section 3642 concerns the establishment of new products. Thus, to the extent the Postal Service chooses to offer a product on a less-than-nationwide basis, there will be an opportunity to consider the phrase “substantial region of the nation” in the context of a specific proposal.

³⁶ A “negotiated service agreement” is a contract negotiated between the Postal Service and another entity, most likely the mailer, for service and rates different from those of general applicability.

³⁷ The Census Bureau, for example, divides the country into four regions, which are further subdivided into divisions. The geographic area of the nine states that comprise the West Region’s Mountain Division is more than three times greater than that occupied by the South Region’s South Atlantic Division, which is comprised of eight states and the District of Columbia stretching from Delaware to Florida (856.1 thousand square miles versus 266.1 thousand square miles). However, the population in the South Atlantic Division is more than 2.5 times greater than that of the Mountain Division (57.1 million versus 20.8 million based on July 2006 estimates).

³⁸ Although Express Mail service is not available at every post office, unquestionably the service would be fairly characterized as being of general applicability throughout the nation.

D. Information Supporting Rate and Class Decisions

[3029] The Governors' authority to establish rates and classes for competitive products is subject to subchapter II of chapter 36 of title 39 and the regulations promulgated by the Commission under section 3633 to: (a) prohibit cross-subsidies of competitive products by market dominant products, (b) require each competitive product to cover its attributable costs, and (c) ensure that collectively competitive products cover an appropriate share of the institutional costs of the Postal Service. In Order No. 15, the Commission solicited the parties' views on what information is needed to support changes in rates or classes whether of general applicability or not. PRC Order No. 15, May 17, 2007, at 6-7. In addition, the Commission asked whether the information needed to support a rate decrease differed from that for a rate increase. *Id.* at 6.

[3030] The parties offer starkly contrasting views on the information needed to support changes in rates. Advo, PSA, and the Postal Service contend that nothing need be filed with the Commission, other than the notice required under section 3632(b)(3), at the time rate changes are announced.³⁹ These parties assert that competitive products' compliance with section 3633 should be considered only in the annual compliance review under section 3653. *Id.* UPS, on the other hand, contends that rate changes should be accompanied by the following information: volumes, revenues, billing determinants, attributable costs, including an explanation of substantial cost changes; prior fiscal year audited data; projected data for the period when the rates are in effect; and unaudited data for the current fiscal year.⁴⁰ UPS concludes that pre-implementation review is a prerequisite for determining competitive products' compliance with section 3633. *Id.*

³⁹ Advo Comments, June 18, 2007, at 10-11; PSA Comments, June 18, 2007, at 4; and Postal Service Comments, June 18, 2007, at 18-19.

⁴⁰ UPS Comments, June 18, 2007, at 4-5. In its reply comments, UPS appears to modify its position, indicating, among other things, that it is not suggesting the Postal Service be required to file test year projections and that fiscal year data included in the annual report may be sufficient for rate changes noticed relatively shortly after the filing of the annual report. UPS Reply Comments, July 3, 2007, at 3-4.

[3031] The Postal Service asserts that the “structure of the statute, including, the nature of the data required to show compliance with § 3633, suggests that there is no prior review by the Commission.” Postal Service Comments, June 18, 2007, at 18. In support, it points to the different notice requirements associated with rate changes of general applicability (*Federal Register* notice no less than 30 days prior to the effective date) and rate changes of less than general applicability (filing with the Commission not less than 15 days prior to the effective date). *Id.* at 18-19. It argues that the former suggests that any substantive review is limited to the annual compliance review, whereas the latter seemingly is intended to protect the confidentiality of customized agreements. *Id.* at 19. This argument is not persuasive.

[3032] The statutory provisions governing competitive products, 39 U.S.C. §§ 3631-34, neither explicitly provide for nor prohibit pre-implementation review of rate changes by the Commission. Section 3633 directs the Commission to promulgate regulations to: (a) prohibit cross-subsidies of competitive products by market dominant products; (b) ensure that each competitive product covers its attributable costs; and (c) that collectively competitive products make an appropriate contribution to the Postal Service’s overhead. To fulfill these responsibilities, the Commission cannot turn a blind eye to changes which may not be in compliance with those requirements. The different notice/filing requirements prescribed by section 3632 suggest the need for closer scrutiny of certain types of rate changes.

[3033] Section 3632(b)(2) requires that, for rate (or class) changes of general applicability, the Governors publish each rate (or class) decision and the record of the Governors’ proceeding in the *Federal Register* at least 30 days before the effective date of any new rates or classes.⁴¹ Rates (or classes) of general applicability are available to all mailers equally, i.e., those satisfying the eligibility standards for the rate (or class). So, for example, Parcel Select rates would be available to all mailers meeting the eligibility

⁴¹ Pursuant to the proposed regulations, the Postal Service will also be required to file the notice of all proposed rate (and class) changes of general applicability with the Commission no later than the date such notice is published in the *Federal Register*.

requirements for such service. In essence, rates of general applicability are the published (or tariff) rates for the particular service. When a carrier's published rates (those of general applicability) are changed, experience suggests that they are likely to be increased.⁴² As a general rule, anytime competitive prices are increased concern over unfair competition is diminished. Likewise, increases in postal rates of general applicability above those found in compliance with section 3633 can, for purposes of these implementing regulations, be deemed to be presumptively reasonable. In that situation, the annual review would appear to be adequate to assure compliance with section 3633. The complaint process would be available as well.

[3034] An identical presumption of reasonableness cannot fairly be presumed for rate decreases of general applicability, which, at a minimum, intensify concerns about potentially unfair competition. This is not to suggest any limitation on the Governors' authority to change rates. Unlike its private enterprise counterparts, however, the Postal Service has no residual claimants, i.e., stockholders, to shoulder the consequences of an improvident decision to change rates. The Commission's role is to ensure that rates and classes comply with section 3633. By doing so, the Commission preserves fair competition. The change in circumstances giving rise to the decrease, resulting in a reduction from the pre-existing presumptively lawful rates, justifies the pre-implementation review to ensure continued compliance with section 3633. Thus, the Commission proposes that for decreases in rates of general applicability the Postal Service will be required to demonstrate the change is in compliance with section 3633. See section 3110.3(c) of the proposed regulations. The Commission does not anticipate that the regulations will either unduly burden the Postal Service or delay the effectiveness of changes satisfying the minimal standards of lawfulness.

[3035] Section 3632(b)(3) authorizes the Governors to establish rates (or classes) not of general applicability, i.e., to execute negotiated service agreements with mailers

⁴² See, e.g., FedEx Corporation's press releases of December 4, 2006, announcing a 4.9 percent increase in certain "standard list rates;" and of November 3, 2006, announcing a 3.5 percent increase in the net average shipping rate for FedEx Express, both of which may be accessed at: <http://www.fedex.com/us/about/news/pressreleases/?link=4>.

providing for rates different from the published rates (of general applicability). Notably, negotiated service agreements are subject to different filing requirements than are rate changes of general applicability. Specifically, each such negotiated service agreement (rate or class decision not of general applicability) and the record of proceedings in connection with such decision must be filed with the Commission not less than 15 days prior to the effective date of any new rate or class. There is good reason for the different filing requirements depending upon the type of rate change involved.⁴³

[3036] Changes not of general applicability will invariably involve discounts compared to published rates and perhaps involve combinations of services. Thus, such arrangements will inevitably raise concerns about the potential for unfair competition. The Commission would be remiss if it did not review these filings prior to their implementation to ensure compliance with section 3633. The Governors' rate (or class) changes must be in writing and include a statement of explanation and justification. Section 3632(b)(1). The information to demonstrate compliance with section 3633 will presumably have been reviewed by the Postal Service and be readily available. Thus, the Commission proposes to require the Postal Service to file with all competitive negotiated service agreements, i.e., rate (or class) changes not of general applicability, sufficient cost and revenue information to enable the Commission to assess, as a preliminary screen, whether the agreement satisfies the requirements of section 3633. In particular, the Commission proposes that the Postal Service be required to show that each negotiated service agreement covers its attributable costs and to represent that the agreement is otherwise in compliance with section 3633.

[3037] The Commission does not anticipate that this review process will delay the effective date of any negotiated service agreement found to be in compliance with section 3633. Nor will the review process impinge on the Governors' authority to change

⁴³ The Postal Service's suggestion that customized agreements are required to be filed with the Commission, as opposed to simply being noticed in the *Federal Register*, to protect the confidentiality of such agreements (Postal Service Comments, June 18, 2007, at 19), is only one aspect of this issue. The Postal Service is aware that certain information should be public. See 72 FR 37454 (July 10, 2007), concerning recent revisions to the IMM regarding the notifications of ICMs.

rates or execute negotiated service agreements. The limited review is intended to provide some assurance that, at least preliminarily, the arrangement is not unlawful. As these arrangements will undoubtedly contain commercially sensitive information, it is understood that the Postal Service may exercise its prerogative to seek appropriate protective conditions.

E. Section 3633 Standards

[3038] Section 3633 contains three provisions by which the lawfulness of competitive products' rates are judged. These provisions, prohibiting cross-subsidies, establishing an attributable cost floor, and requiring an appropriate institutional cost contribution, are designed to act in concert to ensure that competitive rates are lawful. Each provision, along with the parties' suggestions for its implementation, is discussed in turn.

1. Prohibition Against Cross-subsidies

[3039] Section 3633(a)(1) prohibits the subsidization of competitive products by market dominant products. In response to Order No. 15, the parties suggest a wide range of standards to be used to test for cross-subsidies.

- OCA suggests that the standard requires competitive products to cover both their attributable costs plus an appropriate share of institutional costs. OCA Comments, June 18, 2007, at 33.
- APWU contends that there is no cross-subsidy if competitive products cover their attributable costs. APWU Comments, June 18, 2007, at 5.
- PSA advocates use of the incremental cost test, whereby "revenues for each competitive product cover its incremental cost." PSA Comments, April 6, 2007, at 5. It suggests that the Commission's attributable costs serve as a proxy for incremental costs. *Id.*⁴⁴
- Advo endorses the incremental cost test applied to competitive products collectively, i.e., revenues from competitive products "cover their combined incremental costs." Advo Comments, June 18, 2007, at 11.⁴⁵
- UPS contends that subsection (a)(1) redefines the term "subsidy" to require that competitive products collectively cover their attributable costs, their

⁴⁴ PostCom supports PSA's position. PostCom Reply Comments, July 3, 2007, at 5.

⁴⁵ Advo notes the possibility that implementation of section 2011(h) may cause an increase in competitive products' costs, "resulting in a rate floor that is well in excess of the 'cross subsidy' threshold." *Id.*

appropriate share of institutional costs, plus an additional amount representing “a fair share of the unattributable network costs from which competitive products benefit.” UPS Comments, June 18, 2007, at 9.⁴⁶

- The Postal Service advocates a standard requiring competitive products’ total revenues to be at least equal to the sum of each product’s attributable costs “plus the group-specific costs caused by the competitive products as a group.” Postal Service Comments, June 18, 2007, at 24.⁴⁷

[3040] To test for cross-subsidies, the Commission will initially apply the incremental cost test, a standard that Advo and PSA suggest.⁴⁸ Incremental costs are the variable and fixed costs that would be eliminated if a product (or products) was (were) (hypothetically) discontinued.⁴⁹ In prior rate cases, the Commission has discussed the issue and adopted a definition offered by Postal Service witness Panzar: “The revenues collected from any service (or group of services) must be at least as large as the additional (or incremental) cost of adding that service (or group of services) to the enterprise’s other offerings.” PRC Op. R97-1, ¶ 4022, quoting USPS-T-11 at 8. While acknowledging that this is the test it should endeavor to apply (*id.*, ¶ 4026), the Commission’s attempts to do so have been thwarted by concerns about the underlying assumptions used, *e.g.*, constant variability and the stability of the operating plan. See, *e.g.*, PRC Op. R2000-1, ¶ 4055 (“the results of the test may still be unreliable where deleting a subclass or combination of subclasses causes a large reduction in an important cost driver.”)

[3041] The Commission recognizes that presently it lacks the data that would enable it to employ rigorously the incremental costs to test for cross-subsidies of

⁴⁶ UPS asserts that the Federal Trade Commission’s report, pursuant to section 703(d) of the PAEA, will aid the Commission in determining the “net economic benefit realized by the Postal Service due to preferential legal treatment[.]” *Id.*

⁴⁷ The Postal Service indicates that an analysis will be required to identify group-specific costs. *Id.* at 21.

⁴⁸ PSA’s endorsement of the incremental cost test appears to be designed to satisfy both the proscription against cross-subsidies and the requirement that each product cover its attributable costs. See PSA Comments, April 6, 2007, at 5.

⁴⁹ See Docket No. R87-1, USPS-T-3 at 11.

competitive products. Shortly, the Department of the Treasury will provide its analysis of Postal Service costs, and the Commission will initiate a public proceeding to evaluate this information.⁵⁰ Previously, to test for cross-subsidies the Commission has used each product's attributable cost as a reasonable proxy for the costs associated with that product.⁵¹ Endorsing this standard as an appropriate surrogate, the Commission remarked that "nonnegative markups are good evidence against the presence of the most elementary cross subsidies." PRC Op. R97-1, ¶ 4024.⁵²

[3042] The Postal Service's suggested test, competitive products' revenues at least equal to the sum of the products' attributable costs plus the products' causally related group-specific costs, appears to be similar to the incremental cost test. To test for cross-subsidies, the incremental cost test should consider all possible combinations of products (services). It is not clear whether this is different from what the inclusion of "group-specific costs" contemplates. See Postal Service Reply Comments, July 3, 2007, at 40. In any event, the Postal Service does agree that "analysis will be required" to quantify the additional, causally related, non-variable group-specific costs. Postal Service Comments, June 18, 2007, at 21.

[3043] To test for cross-subsidies, the inclusion of such group-specific costs is appropriate. Thus, until reliable incremental cost data are available, the Commission will continue to use its current cross-subsidy test, supplemented to include causally related,

⁵⁰ UPS and NAA urge the Commission to commence a separate proceeding to address cost issues. UPS Comments, June 18, 2007, at 15; NAA Comments, June 18, 2007, at 11-12.

⁵¹ PSA suggests this as well. PSA Comments, April 6, 2007, at 5.

⁵² APWU does not elaborate on its suggestion there is no cross-subsidy provided that competitive products cover their attributable costs. APWU Comments, June 18, 2007, at 5-6. Without more, however, that standard appears merely to restate subsection (a)(2)'s requirement of an attributable cost floor. OCA's suggested test, on the other hand, does take into account non-negative markups, but also includes "an appropriate share of institutional costs[.]" OCA Comments, June 18, 2007, at 33. The test for cross-subsidies is independent from the issue of what the appropriate share should be for competitive products as a whole. Revenues in excess of incremental costs (or attributable costs in the interim) demonstrate no cross-subsidy exists, but are not necessarily an indication that the contribution to institutional costs (the share) is appropriate.

group-specific costs. If and when incremental costs can be accurately determined, the Commission may adjust its existing practice.

[3044] UPS asserts that the PAEA redefines cross-subsidy to require that competitive products collectively bear costs in excess of their attributable costs “and a fair share of the unattributable network costs from which competitive products benefit.” UPS Comments, June 18, 2007, at 9. The Postal Service, Advo, and PSA take issue with UPS’s contention that the PAEA redefines the term “subsidy.”⁵³ The Commission will not adopt UPS’s construction. The relevant PAEA provisions, sections 3633(a)(1) and 2011(h)(1)(A)(i)(II), prohibit the cross-subsidy of competitive products by market dominant products. Apart from any consideration of the public policies that might be furthered by the UPS test, an issue not developed on this record,⁵⁴ the Commission does not interpret the foregoing provisions as redefining the concept of cross-subsidy.

2. Attributable Cost Floor

[3045] Section 3633(a)(2) requires that each competitive product cover its attributable costs, which, in section 3631(b), are defined as “the direct and indirect postal costs attributable to such product through reliably identified causal relationships.” This standard codifies the Commission’s long-standing method of attribution under the Postal Reorganization Act. See, e.g., PRC Op. R97-1, ¶ 4017 (“The Commission is not prepared to depart from the position that attributable cost means costs which can be said to be reliably caused by a subclass of mail or service.”)⁵⁵ For purposes of initially implementing regulations pursuant to section 3633, the Commission intends to employ

⁵³ Postal Service Reply Comments, July 3, 2007, at 24-27; Advo Reply Comments, July 3, 2007, at 5-7; and PSA Reply Comments, July 3, 2007, at 3-5.

⁵⁴ See Advo Reply Comments, July 3, 2007, at 7.

⁵⁵ Elaborating on the point, the Commission noted that in addition to specific fixed costs it also found other nonvariable costs to be attributable, e.g., the fixed portion of special delivery messengers. *Id.* at ¶ 4016. See also PSA Comments, April 6, 2007, at 9.

this long-established attribution method to determine compliance with section 3633(a)(2).

[3046] UPS advocates that long-run incremental costs be used as the benchmark for each competitive product's attributable costs. UPS Comments, June 18, 2007, at 12. It views this approach as preferable to the existing method because it includes "shared fixed costs," i.e., fixed costs incurred over the long run by more than one product. *Id.* In reply comments, UPS appears to endorse this standard to test for cross-subsidies as well, at least with respect to calculating group-specific costs. UPS Reply Comments, July 3, 2007, at 5. The Commission does not adopt UPS's suggestion.

[3047] Section 3633(a)(2) specifies attributable costs as a term that has an accepted meaning in the context of Postal Service costing. Employing long-run incremental costs as a measure of attributable costs renders all costs variable in theory.⁵⁶ Furthermore, although the notion of shared fixed costs may be relevant to the issue of cross-subsidies, as discussed in the previous subsection, UPS has not demonstrated any reasonable nexus between those costs, which by definition are fixed regardless of the number of products, and a product's attributable costs, including those reliably identified based on causal relationships.

[3048] In its response to Order No. 15, the Postal Service does not appear to comment specifically on the standard to be used to measure compliance with section 3633(a)(2). Rather, it includes that subsection in its interpretation of what section 3633 requires as a whole, namely, that competitive products' revenues "be sufficient to cover the sum of attributable costs and group specific costs, plus any mark-up on attributable costs that the Commission determines is 'appropriate.'" Postal Service Comments, June 18, 2007, at 23. In its reply comments, the Postal Service recognizes that the statutory definition, section 3631(b), codifies the long-standing attribution method. Postal Service Reply Comments, July 3, 2007, at 29. The Postal Service goes on, however, to note its apparent agreement with UPS "that, for purposes of § 3633(a)(2), the cost floor for each

⁵⁶ See Postal Service Reply Comments, July 3, 2007, at 29-30, remarking on the period deemed sufficient to allow the Postal Service to adjust fully to the impact the provision of the product creates.

competitive product should be the costs the Postal Service would avoid if it did not offer that competitive product.” *Id.* This statement appears to suggest agreement with UPS’s position regarding the use of long-run incremental costs for purposes other than testing for cross-subsidies, although the Postal Service does raise the issue of how one would define the period sufficient to allow the Postal Service to adjust fully to the impact the provision of the service creates. *See id.* at 30. This appears to be an area where future analysis may be warranted.

3. Appropriate Share of Institutional Costs

[3049] Section 3633(a)(3) requires that competitive products collectively cover an “appropriate share” of the Postal Service’s institutional costs. The term “appropriate share” is not defined; its meaning is left for the Commission to determine based on consideration of all relevant factors. The parties addressing this issue suggest a variety of approaches, the most concrete of which is that the Commission begin with the markups from Docket No. R2006-1.⁵⁷ Several parties urge that the contribution be set at a low level, arguing, among other things, that it represents a floor not a ceiling, that the Postal Service has incentive to exceed that floor, and that if set too high the Postal Service will be unable to compete and, as a result, contribution will be lost to the detriment of market dominant mailers.⁵⁸ One party contends that contributions from market dominant and competitive products must be compared, suggesting various ways in which this might be accomplished, e.g., on a per-piece (unit contribution) or

⁵⁷ See OCA Comments, June 18, 2007, at 34-35; PSA Comments, April 6, 2007, at 11-13; Pitney Bowes Comments, April, 6, 2007, at 38; and UPS Reply Comments, July 3, 2007, at 6. Initially, UPS suggested that the contribution from competitive products should be maximized. UPS Comments, April 6, 2007, at 5-7.

⁵⁸ Advo Reply Comments, May 7, 2007, at 15-19; MOAA Comments, June 18, 2007, at 2; and APMU Comments, April 6, 2007, at 3-5.

percentage (markup) basis.⁵⁹ The Postal Service advocates that the contribution be set at a relatively low level,⁶⁰ suggesting that it be “calculated as a mark-up on the sum of the competitive products’ attributable cost.” *Id.* at 23. UPS agrees with this method of calculating the contribution. UPS Reply Comments, July 3, 2007, at 6.

[3050] The Commission considered various options, including all of those suggested in the comments, in evaluating how best to quantify, at least initially, appropriate share. Among the options considered and rejected were: equal unit contribution, equal percentage markup, markup of competitive products’ attributable costs, and percentage of revenues. None of these was deemed preferable to the alternative of basing competitive products’ contribution on a percentage of total institutional costs. To be sure, the various other methods could all be expressed mathematically in terms of percentage of total institutional costs, but each implies a pricing technique, e.g., a particular coverage level, absent from simply basing appropriate share on a percentage of total institutional costs. The latter better reflects the section 3633(a)(3) directive and is more easily understood than the various alternatives. Moreover, this approach is a fitting starting point, recognizing that by year’s end the Department of the Treasury will submit recommendations to the Commission relating to treatment of Postal Service costs. Interested persons will have an opportunity to comment on those recommendations. See section 2011(h)(2)(A).

[3051] In attempting to quantify appropriate share, the Commission begins its analysis with the competitive products’ contribution resulting from rates recommended in Docket No. R2006-1. Based on the recommended rates, the Commission estimates that in TY 2008 competitive products will contribute approximately \$2.4 billion to the Postal

⁵⁹ Valpak Comments, June 18, 2007, at 13-14. Valpak states that such comparisons “would enable the Commission to ensure that competitive products are not subsidizing market-dominant products[.]” *Id.* at 14.

⁶⁰ Postal Service Comments, June 18, 2007, at 24-26.

Service's institutional costs.⁶¹ Expressed as a percentage, this figure represents approximately 6.9 percent of the total contribution to institutional costs.

[3052] For purposes of implementing these regulations initially, the Commission is persuaded that the competitive products' contribution should be modified from Docket No. R2006-1 levels. The Commission proposes to set the initial contribution at 5.5 percent of the Postal Service's institutional costs. Illustratively, based on Docket No. R2006-1 TY 2008 figures, this percentage yields a contribution of approximately \$1.9 billion.

[3053] Several factors influence the Commission's proposal to establish an appropriate share below the contribution level derived from rates recommended in Docket No. R2006-1. The PAEA so thoroughly overhauls the ratemaking process that the Commission would be remiss if it failed to consider the differences in the rate setting process. Under the pre-PAEA Postal Reorganization Act (PRA), postal rates were constrained by a break-even requirement and systemwide pricing scheme under which institutional costs were assigned based on non-cost factors.⁶² Given these constraints, pricing was a "zero-sum game," i.e., an increase (or decrease) in the assignment to one subclass (or service) must be offset by a decrease (or increase) to one or more other subclasses (or services).

[3054] In lieu of that system, the PAEA bifurcates Postal Service products into market dominant and competitive categories with a principal objective being to reduce costs and increase efficiency. Under the PAEA, the Postal Service has an incentive to

⁶¹ Necessarily, the results are estimated since data are not reported for bulk parcel post and bulk international mail separately from their single-piece counterparts. For purposes of this exercise, bulk parcel post consists of Parcel Select, Parcel Return Service, and Parcel Post eligible for a BMC, OBMC, or barcode discount. The foregoing estimate includes a TY 2008 contribution for bulk international mail of approximately \$176 million (out of \$376 million), calculated using the average percentage contribution for competitive international mail in FY 2005 and FY 2006 as a proxy.

⁶² Among the non-cost factors the Commission used to assign institutional costs are: value of service, impact on mailers and competitors, availability of alternatives, and simplicity of rate structure. See 39 U.S.C. §3622(b) (2002). For purposes of this discussion, reference to the PRA is shorthand for the Act prior to its amendment by the PAEA.

reduce both attributable and institutional costs due to limitations on market dominant rates and because it is authorized to retain earnings.

[3055] Under the PRA, the assignment of institutional costs was designed to ensure that each subclass or type of mail made a reasonable contribution to the Postal Service's overhead, yielding rates that were fair and equitable and subsidy-free. The PAEA addresses the issues of rate levels and subsidies differently. Market dominant rates are limited by a price cap, not by policy considerations. Thus, market dominant mailers are insulated from the consequences of any failure by the Postal Service to compete successfully. Rates for competitive products are subject to market conditions and, by statute, must satisfy criteria which preclude the possibility of subsidization by market dominant products.

[3056] The "appropriate share" required by the PAEA is not synonymous with "reasonably assignable" required by PRA section 3622(b)(3). No longer are rates for competitive products predicated on explicit consideration of specific non-cost factors. Moreover, the resulting rate levels represent significantly different things. Under the PRA, rate levels equate with maximum rates for the subclass or type of mail, as rates are not designed to generate a surplus. In contrast, under the PAEA, the concept of rate levels for competitive products largely disappears, with the Postal Service given the flexibility to price competitive products however it wishes, provided its rates satisfy the statutory standards of lawfulness. Appropriate share is a floor for all competitive products, but the hope (and expectation) is that competitive products will generate contributions in excess of the floor. Thus, it is unlike reasonably assignable in two other respects: it applies to competitive products collectively, not to subclasses or services individually; and it represents a minimum (not maximum) contribution level, serving as a threshold for compliance with section 3633(a)(3). Because it may retain earnings, the Postal Service has incentives to exceed this threshold, including reducing rate pressure on market dominant rates, continuation of universal service, and the possibility of bonuses.

[3057] Section 3633 requires that each competitive product cover its attributable costs and prohibits competitive products from being subsidized by market dominant products. Thus, they must be self-sustaining since any shortfall cannot be recovered by increasing market dominant rates.

[3058] In attempting to quantify an appropriate contribution, the Commission is mindful of the risks of setting it too high, particularly at the outset of the new system of regulation. The market is competitive; the Postal Service's market share is relatively small; and the Postal Service needs some flexibility to compete. On the other hand, the Commission has an obligation to preserve competition by not establishing a markup so low as to give the Postal Service an artificial competitive advantage. The task, as Advo noted, "calls for a delicate balance." Advo Reply Comments, May 7, 2007, at 16.

[3059] The Commission's proposal to set the minimum contribution level at 5.5 percent of total institutional costs is influenced by historic results. A review of the Cost and Revenue Analysis (CRA) for domestic and international postal operations supports a best estimate of competitive products' contribution to institutional costs at 5.4 percent in FY 2005 and 5.7 percent in FY 2006. These figures were developed based on the reported FY 2005 and FY 2006 data for Priority Mail, Express Mail, and international mail.⁶³ The CRA reports Parcel Post data in the aggregate. Thus, to develop an estimate for bulk Parcel Post, consisting of Parcel Select, Parcel Return Service, and Parcel Post mail eligible for a BMC, OBMC, or barcode discount, the Commission calculated an estimated bulk parcel post unit contribution for FY 2005 based on actual FY 2005 data. Comparable data are not available for FY 2006. Thus, the estimated

⁶³ The figures for international mail were developed based on the contribution associated with that mail included within the competitive category in this order. The international CRA for FY2006 does not separately identify data for Global Bulk Economy (GBE) mail. However, since GBE had no reported volume in FY 2005, its contribution in FY 2006, if any, would likely have no measurable affect on the total international mail contribution.

FY 2006 bulk parcel post contribution is based on the same proportional relationship between bulk parcel post and parcel post as a whole used for FY 2005.⁶⁴

[3060] Setting the initial competitive products' contribution at historic levels is a reasonable means to quantify appropriate share, particularly at the outset of the new form of competitive rate regulation. Since it is no longer subject to the pricing constraints of the PRA, the Postal Service should perform at least as well as it has historically.

[3061] This order represents the initial effort to implement the competitive products' regulations. The Commission emphasizes that its initial quantification of appropriate share is not written in stone. The statute specifically authorizes the Commission to revise this share as needed and, in any event, requires that the regulations be reviewed every five years to determine whether they be retained, modified, or eliminated. The Commission anticipates that that need may arise for any number of reasons, *e.g.*, additions or deletions to the competitive product lists and market conditions.⁶⁵

4. Application of the Term "Product"

[3062] The PAEA defines the term "product" to mean "a postal service with a distinct cost or market characteristic for which a rate or rates are, or may reasonably be, applied." 39 U.S.C. § 102(6). The parties offer widely differing suggestions as to how this definition should be applied. The Postal Service recognizes that the term could be interpreted to mean individual rate categories are products. Postal Service

⁶⁴ The contribution from bulk parcel post is, in any event, relatively minor. For the convenience of the parties, workpapers showing the development of these estimates will be made available on the Commission's website (<http://www.prc.gov>) in Docket No. RM2007-1. The Commission is providing this level of detail so that parties have an opportunity to review the underlying data and, if appropriate, suggest revisions which may more accurately portray historic results.

⁶⁵ Pursuant to section 2011(h)(1)(A)(ii), the Secretary of the Treasury will recommend substantive and procedural rules that should be followed in determining the assumed Federal income tax on competitive products income. Those recommendations are due on or before December 19, 2007. Interested persons will have an opportunity to comment on those recommendations. For purposes of this order, it is sufficient to note that the assumed Federal income tax on competitive products income is an issue that may affect future efforts to develop an appropriate share.

Supplemental Comments, June 19, 2007, at 6. It dismisses that construction, however, contending that product should be “interpreted at a high level of aggregation” and proposing that it be interpreted “as generally equivalent to the current ‘subclasses’ under the PRA.” *Id.* Several parties echo the Postal Service’s view that product should be equated with subclass.⁶⁶ OCA, on the other hand, takes the position that, for competitive products, the term “product” be interpreted “at the rate-cell level.” OCA Comments, April 6, 2007, at 36. NAA asserts that product is not synonymous with subclass or rate category, but instead should be construed “more consistent with everyday understandings[.]”⁶⁷ Other parties assert that various specific arrangements, *e.g.*, special classifications, customized agreements, and negotiated service agreements, either are or are not products.⁶⁸

[3063] Suggestions that the term “product” be applied in a blanket fashion are neither practical nor justified. Instead, as discussed below, a more nuanced approach, based on balancing the objectives of the PAEA and practical considerations, is required.

[3064] Plainly, product cannot reasonably be read as equivalent to subclass since product is defined as having either “a distinct cost *or* market characteristic”⁶⁹ whereas, under the Commission’s long-established practice, subclass requires both cost *and* demand differences. The Commission has clearly expressed the relevant standard: “To identify groupings of mail, which should be accorded subclass rather than rate category

⁶⁶ See, *e.g.*, PSA Comments, June 18, 2007, at 11; MOAA Reply Comments, July 3, 2007, at 4; Advo Reply Comments, July 3, 2007, at 12; and Pitney Bowes Comments, June 18, 2007, at 11.

⁶⁷ NAA Comments, June 18, 2007, at 14. NAA observes, correctly, that product is defined in a manner that “resembles the Commission’s traditional test for a rate category.” *Id.* at 14-15.

⁶⁸ See, *e.g.*, NPPC Comments, June 18, 2007, at 10 (negotiated service agreements are products); PostCom Reply Comments, July 3, 2007, at 7-8 (each market dominant negotiated service agreement should be viewed as a distinct product); GCA Comments, June 18, 2007, at 9-10 (special classifications and class not of general applicability containing one service would be a product, but a negotiated service agreement may or may not be); and NAA Comments, June 18, 2007, at 16 (status of negotiated service agreements should be decided on a case-by-case basis). See *also* UPS Comments, June 18, 2007, at 19 (rates for a given type of mail may vary only if there is “a distinct and significant cost or market characteristic for [that] type of mail ...”).

⁶⁹ 39 U.S.C. § 102(6) (emphasis added).

treatment, the Commission traditionally has sought to identify differences in both cost *and* market, or demand.”⁷⁰

[3065] The PAEA overhauls postal ratemaking, bifurcating the mailstream into market dominant and competitive mail categories, and prescribing different rate setting mechanisms for each. Market dominant rates are subject to an annual price cap. Section 3622(d)(1)(A). This foremost ratemaking requirement is, by statute, applicable to classes of mail as defined in the DMCS in effect on the date of enactment of the PAEA. Section 3622(d)(2)(A). In contrast, competitive rates are not tied to a cap; instead, they cannot be set below certain cost thresholds, including, among other things, the requirement that each competitive product covers its attributable costs. Section 3633(a)(2). When drafting the PAEA, Congress was well aware of the Commission’s long-established definitions, as it showed when defining “costs attributable” in section 3631(b). It can be assumed to have intentionally chosen the term “product” in preference to “subclass,” a term that is not defined by the PAEA and, under the new rate setting procedures, is largely an irrelevant artifact.

[3066] Nor is the Commission persuaded by the Postal Service’s attempts to buttress its suggestion that product be defined as a subclass by reference to other provisions of the PAEA. For example, it compares section 3622(c)(2) with former section 3622(b)(3) and notes that attribution “is expressly linked ‘to each competitive product.’” Postal Service Supplemental Comments, June 19, 2007, at 7. Based on this, it concludes “there is nothing to suggest that attribution be done differently under the PAEA than it was done under the PRA: at the subclass level.” *Id.* The focus on attribution does not support the Postal Service’s argument. The PAEA reaffirms the Commission’s attribution method and specifically applies it to each competitive product, which is given a different meaning than subclass. Moreover, concerning market dominant products, the

⁷⁰ See PRC Op. MC95-1, ¶ 3022 (emphasis added); see also *id.* ¶ 3023 (“The Commission has consistently expected proponents of separate subclass treatment to show differences in both costs and demand.”).

price cap regulation supersedes attribution.⁷¹ As discussed below, the rejection of the contention that product should, in all instances, be equated with subclass does not foreclose a finding that a specific subclass is a product.

[3067] OCA's proposal is the polar opposite of the Postal Service's. Instead of "a high level of aggregation,"⁷² OCA would apply the term "product" at the most disaggregated level. Specifically, OCA proposes that, for competitive products, product be applied at the rate cell level, a result it contends is suggested by the phrase "distinct cost ... characteristic." OCA Comments, April 6, 2007, at 36. Thus, under its reading, every competitive rate cell must cover its attributable costs. The Commission does not construe section 102(6) so narrowly.

[3068] Rate cells generally reflect cost differences, but that is not the same as having separate distinct cost characteristics. There are myriad cost driving factors, e.g., degree of preparation, density, weight, shape, distance, and type of delivery, that may be characterized as cost characteristics. Rate cells identify variations within characteristics such as zoned rates, or levels of presortation. OCA's system would be impractical to implement and impossible to administer. Aside from these practical difficulties, OCA's proposal is flawed in another respect. It contends that rate cell satisfies the requirement that "a rate or rates" be applied because a rate cell may have more than one rate, e.g., the same weight/zone Express Mail Post Office-to-Post Office has different rates than Post Office-to-Addressee. This hardly proves that a rate cell may have more than one rate; rather, the example involves separate rate categories with separate rate cells.

⁷¹ The Postal Service also contends that language in section 3652(b), which concerns annual reports to the Commission, supports its interpretation of product as being equivalent to subclass. Specifically, it contends that the phrase "with respect to each market-dominant product for which a workshare discount was in effect" suggests that a market dominant product is not equivalent to workshare discount, "such that an individual workshare discount (which is a rate category) is not itself an individual 'product.'" *Id.* at 8. This supposition is not persuasive. First, as the Postal Service concedes, the term "product" could be interpreted as a rate category; thus a workshare discount could be a product. Second, the Commission reads the phrase "each market-dominant product for which a workshare discount was in effect" as reflecting the possibility that mail matter for which a workshare discount is in effect, e.g., First-Class automation letters, could be found to be a separate product.

⁷² *Id.* at 6.

[3069] To qualify as a product, a postal service must exhibit either a distinct cost or market characteristic for which a rate or rates are, or may reasonably be, applied. But the existence of a separate rate, implying a cost difference, does not require that the particular postal service, *e.g.*, rate cell, be deemed a product. A rule of reason must be applied.

[3070] The revamped ratemaking under the PAEA is designed to achieve various goals, principal among them are to afford the Postal Service enhanced pricing flexibility, while at the same time providing accountability through greater transparency. These joint goals will best be achieved if they are balanced with one another. Transparency cannot be achieved if the term “product” is applied too broadly, *e.g.*, solely at the subclass level. Aggregating postal services into only a few products, a result urged by several parties, forfeits transparency and serves no legitimate business or regulatory need. Stated differently, it will not provide for accountability, a bedrock principle underlying the PAEA. By the same token, pricing flexibility is illusory if the term “product” is applied too narrowly, *e.g.*, at the rate cell level. Disaggregating postal services into too many products would impose unwarranted administrative burdens on the Postal Service, thwart pricing flexibility, and serve no legitimate business or regulatory need. It would not, in short, lead to any enhancement in postal service, which, too, is a central principle underlying the PAEA.

[3071] In applying the term “product” to the competitive and market dominant categories of mail, the Commission has been guided by these principles and has tried to strike an appropriate balance between these competing goals. In doing so, the Commission has also considered other factors, including the type of mail involved, the pre-existing classifications, and the potential for other reasonable groupings of postal services.

[3072] The term “product” has greater significance for competitive products than for market dominant products. Section 3633(a)(2) requires each competitive product to cover its attributable costs. Each competitive product is identified following the process outlined in section 3631, which first, in section 3631(a), lists four types of mail (“priority

mail, expedited mail, bulk parcel post, and bulk international mail”) as being within the competitive category of mail;⁷³ and second, in section 3631(c), instructs that the “mail matter” comprising each of these types of mail has “the meaning given to such mail matter under the mail classification schedule.” The Commission is charged with the responsibility of determining what mail matter comprises each of these types of mail, and that mail matter is what initially becomes the competitive products.⁷⁴

[3073] In the discussion above, the Commission identified 11 products that initially comprise the competitive products’ category. These are as follows:

- Priority mail, consisting of Domestic Priority Mail and International Priority Mail;
- Expedited mail, consisting of Domestic Express Mail and International Express Mail,
- Bulk parcel post, consisting of Parcel Select, Parcel Return Service, and parcel post qualifying for BMC, OBMC, and barcode discounts;
- Bulk international mail, consisting of IPA, ISAL, and M-bags; and
- Negotiated service agreements, which includes ICMs.⁷⁵

These products not only form the basis for the mail classification schedule, but also comprise the initial competitive product list required by section 3642.

[3074] In developing the initial list of competitive products, the Commission balanced the Postal Service’s business needs for pricing flexibility with the public’s need for accountability. The results demonstrate that the term “product” can be applied in a judicious manner, based on a consideration of the law and facts. This process results in

⁷³ Mailgrams have been discontinued and, thus, are not discussed.

⁷⁴ A few parties suggest that competitive products are defined as the types of mail listed in section 3631(a). See, e.g., NAA Comments, June 18, 2007, at 14-15; PSA Reply Comments, May 8, 2007, at 6; see also Postal Service Supplemental Comments, June 19, 2007, at 8-9. These contentions lack merit. Competitive products are not “define[d]” in section 3631(a). PSA Comments, May 8, 2007, at 6. That section merely lists the types of mail designated as competitive. It does not define, i.e., identify, what each competitive product is. That process requires the Commission to identify the mail matter that comprises each type of mail listed in section 3631(a) and, as appropriate, to identify the product (or products) within each.

⁷⁵ Each negotiated service agreement is a separate product.

products based on classes of mail (Express Mail), subclasses of mail (Priority), rate categories (Parcel Select), and negotiated service agreements. While these products could, in theory, be further disaggregated or, in the case of negotiated service agreements, further aggregated, the Commission concludes that doing so at this time is unwarranted. This effort represents the initial listing of competitive products. In fashioning this list, the Commission has endeavored to balance goals of the PAEA, while also taking into account the parties' competing concerns. The PAEA contemplates that the implementing regulations and the product lists may be changed. See sections 3622(a), 3633(a), and 3642(a). Once experience is gained, the list of products may be changed as warranted.

[3075] The application of the term "product" to the types of mail listed in section 3621(a) is of lesser significance because, as noted above, the price cap is applied at the class level, not at a product (or any other) level. Nonetheless, the same rule of construction applies. *Compare* sections 3621(b) and 3631(c). The process begins with section 3621(a) which lists the following 10 types of mail as being within the market dominant category of mail:

- (1) First-Class Mail letters and sealed parcels;
- (2) First-Class Mail cards;
- (3) Periodicals;
- (4) Standard Mail;
- (5) Single-piece parcel post;
- (6) Media Mail;
- (7) Bound Printed Matter;
- (8) Library Mail;
- (9) Special services; and
- (10) Single-piece international mail.

[3076] As with competitive products, section 3621(b) instructs that the "mail matter" comprising each of the foregoing types of mail "have the meaning given to such mail matter under the mail classification schedule." Moreover, the foregoing list (and thus the

mail matter represented therein) are “subject to any changes the Postal Regulatory Commission may make under section 3642.” Section 3621(a). The Commission is charged with the responsibility of determining what mail matter comprises each type of mail, and that mail matter is what initially becomes the market dominant products. These products, in turn, form the basis for the mail classification schedule and also serve as the source of the market dominant product list required by section 3642.

[3077] The types of market dominant mail listed in section 3621(a) represent a medley of current postal services. Five are classes of mail, i.e., Periodicals; Standard Mail; Bound Printed Matter; and Media and Library Mail; two are subclasses, i.e., First-Class letters and sealed parcels, and First-Class cards; and one, single-piece parcel post, is a rate category. The remaining two include special services, i.e., ancillary services, and single-piece international mail. An additional consideration is that three of these types of mail, First-Class letters and sealed parcels, First-Class cards, and Standard Mail, are covered by the postal monopoly.⁷⁶

[3078] In considering how best to identify the mail matter comprising each type of mail, the Commission turns initially to the existing reference materials, an approach suggested by numerous parties. With respect to domestic mail, identifying the relevant mail matter may be accomplished by reference to the DMCS, a relatively straightforward proposition, except for single-piece parcel post. However, since the Commission has identified the competitive products associated with bulk parcel post, the latter simply represents the remaining parcel post mail matter. With respect to single-piece international mail, the relevant mail matter may be gleaned from the IMM. In an earlier filing, the Postal Service suggested specific types of mail matter that might be considered single-piece international mail. Postal Service Reply Comments, May 7, 2007, at 33. Since the Commission has identified the competitive products associated

⁷⁶ As a result, these types of mail are distinguishable from other market dominant products. See section 3642(b)(2). At first blush, this distinction may suggest a lesser need to disaggregate these types of mail matter into more than one product. Other considerations, e.g., transparency and the business and/or regulatory needs, may outweigh that initial inclination.

with bulk international mail, the single-piece counterpart would logically consist of the remaining international mail matter.

[3079] In addition to the foregoing, the Commission proposes to add negotiated service agreements, i.e., special classifications pursuant to section 3622(c)(10), as separate market dominant product. Initially, each agreement (special classification) will be treated as a separate product.⁷⁷ This treatment affords the Postal Service flexibility to enter into any special classification it wishes, but provides the necessary transparency to satisfy relevant business and regulatory needs. Absent the discipline that such accountability imposes, both the Postal Service and the Commission roles under the PAEA may be compromised. For example, the Postal Service may lack agreement-specific details on profitability of the agreement, while the Commission would be unable to assess whether the agreement complied with the statute.

[3080] In lieu of identifying at this time the market dominant products associated with the foregoing mail, the Commission concludes, for reasons of accuracy and expedition, that a preferable alternative exists. In commenting on the mail classification process, the Postal Service volunteered to compile a mail classification schedule. Postal Service Supplemental Comments, June 19, 2007, at 11, n.34. The Commission appreciates that offer. Doing so will be a useful exercise as it will enable the Postal Service to draft a mail classification schedule, consistent with this order, that best suits its needs. Previously, the Postal Service indicated the mail classification schedule would contain a level of detail similar to the DMCS. *Id.* at 10-11. The Commission finds that prospect acceptable.

[3081] In its submission, the Postal Service should identify the market dominant products it believes should be in the mail classification schedule. This will enable the Postal Service to categorize its services into products so that it can make appropriate business decisions. The draft mail classification schedule should incorporate the competitive products discussed above.

⁷⁷ In some instances, it may be appropriate to group as a single product negotiated service agreements that are functionally equivalent and thus take on the characteristics of a niche classification.

[3082] The draft mail classification schedule is due September 14, 2007. Responses to this schedule may be filed by no later than September 28, 2007.

[3083] Lastly, section 3642 provides the Commission with authority to add or remove products from the market dominant and competitive product lists, and to transfer products between the lists. This proceeding represents the initial attempt to establish these lists. The Commission anticipates that changes to these lists will be necessary. Once the initial lists are established, the Postal Service may wish to modify them to better serve its and its customers' needs.

IV. PART 3200—PRODUCT LISTS

[4001] Rule 3200.1 explains the purpose of all rules that follow in part 3200. The rules establish a Mail Classification Schedule, which categorizes products as either market dominant or competitive. The categorizations must initially be consistent with the types of mail specified by 39 U.S.C. § 3621(a) and 39 U.S.C. § 3631(a). Once the Mail Classification Schedule is established, the rules specify the procedures to modify the market dominant and competitive product lists and to update the explanatory information contained therein. Authority for this rule flows directly from the general requirements specified in 39 U.S.C. § 3642, which allows the Commission to consider modifications to the market dominant and competitive product lists.

[4002] Experimental products offered as market tests are specifically excluded from the requirements of part 3200 by 39 U.S.C. § 3641(a)(2). The Commission intends to develop separate rules allowing recognition of experimental products in the Mail Classification Schedule during the market tests to facilitate transparency.

A. Subpart A—Mail Classification Schedule

[4003] The Commission is charged with maintaining accurate product lists. 39 U.S.C. § 3642. The Commission views the Mail Classification Schedule as the vehicle for presenting the product lists with necessary descriptive content. The explanatory information included with the product lists will inform participants in Commission proceedings of the nature and scope of Postal Service products and must be sufficiently detailed to allow the Commission to verify that the rates and categorization of products are in compliance with the PAEA. Thus, the Mail Classification Schedule is important in that it will provide for the transparent and accurate maintenance of the product lists.

[4004] The Postal Service suggests two mail classification schedules: one for market dominant products and one for competitive products. Postal Service Supplemental Comments, June 19, 2007, at 11. The Postal Service believes this is

appropriate because different regulatory regimes apply to each side of the business. Postal Service Comments, June 18, 2007, at 16. Additionally, the Postal Service views the product lists as an entity separate from the mail classification schedules.

[4005] The Commission, as a matter of preference and administrative ease, proposes a single Mail Classification Schedule subdivided into two parts. A single schedule will be less likely to cause confusion, simpler to administer when modifying product lists, and will facilitate the process of providing adequate public notice when modifications to the product lists occur.

[4006] Rule 3200.10 describes the Mail Classification Schedule as a single document containing two parts. The first part contains the list of market dominant products with related explanatory information, and the second part contains the list of competitive products with related explanatory information.

[4007] The Postal Service has expressed the view that it should maintain the physical Mail Classification Schedule. Postal Service Supplemental Comments, June 19, 2007, at 14. The Commission finds the Mail Classification Schedule to be the appropriate vehicle for maintaining the market dominant and competitive product lists that the Commission is charged with overseeing. This does not impose constraints on the Postal Service's flexibility to develop new products or modify products consistent with the policies of title 39. The Commission's primary role under 39 U.S.C. § 3642, as evident from the proposed rules, is the proper categorization of Postal Service products. The rules proposed for updating product descriptions and features in the Mail Classification Schedule will not inhibit Postal Service flexibility.

[4008] The Postal Service has indicated that it may be appropriate for the Mail Classification Schedule to be at a similar level of detail as the previous Domestic Mail Classification Schedule (DMCS). Postal Service Comments, June 18, 2007, at 16. Elements of the International Mail Manual (IMM) also will have to be incorporated into the Mail Classification Schedule. *Id.* The Commission concludes that the Postal Service is in the best position to describe its own products and propose descriptive language to be included in the Mail Classification Schedule. Whether the type of mail is categorized as

market dominant or competitive is already determined by statute as specified in 39 U.S.C. § 3621(a) and 39 U.S.C. § 3631(a). The portion of this notice of proposed rulemaking describing the regulation of competitive products clarifies the proper categorization where potential questions of interpretation might arise. Rule 3200.11 directs the Postal Service to initially propose the contents of a Mail Classification Schedule consistent with the categorization specified by statute.

[4009] A short 30-day period from the enactment of this rule is provided for the Postal Service to formulate its Mail Classification Schedule proposal. This should provide sufficient time because it is expected that the Postal Service will draw heavily from existing material provided in the DMCS and the IMM. The Postal Service also has considerable time to plan and undertake preliminary preparation for this activity prior to this rule becoming final.

[4010] Several comments suggest that the product categorizations specified in the statute did not fully reflect the distinctions between market dominant and competitive products. Some time after the initial rounds of rulemakings are complete, the Commission expects the Postal Service to propose comprehensive modifications to the product lists to more accurately reflect market dominant and competitive products.⁷⁸

[4011] The Commission will file notice of the Postal Service's Mail Classification Schedule proposal in the *Federal Register*, with initial commentary by the Commission, and solicit public comment. This process will allow the Commission to develop a Mail Classification Schedule that can become part of the Commission's rules.

[4012] The Commission currently publishes the Domestic Mail Classification Schedule in the *Code of Federal Regulations*. However, extensive portions of this document are abridged to facilitate the Office of the Federal Register's publication requirements. Redacting portions of this document is labor intensive, and the portions of the document eventually published do not provide a complete description of Postal

⁷⁸ This may include incorporating some ancillary services, which currently are considered special services, into host products.

Service products to interested parties. The Postal Service incorporates by reference the Mailing Standards of the United States Postal Service, Domestic Mail Manual (DMM) and the IMM into its rules, which avoids many of the publication problems now experienced by the Commission. Incorporating a document by reference into the *Code of Federal Regulations* requires permission from the Office of the Federal Register. The Commission has initiated discussions with the Office of the Federal Register to obtain the permission necessary to incorporate by reference the Mail Classification Schedule. Thus, rule 3200.12 adopts the Postal Service's approach and pending Office of the Federal Register approval incorporates the Mail Classification Schedule by reference into the Commission's rules of practice.

[4013] Rule 3200.13 specifies the content of the Mail Classification Schedule. Unlike the current DMCS which is organized by classes and subclasses, the Mail Classification Schedule will be organized by Postal Service products with market dominant and competitive products each appearing in separate sections of the document. This is intended to satisfy the requirement to maintain separate market dominant and competitive product lists.

[4014] Unique to the market dominant section of the Mail Classification Schedule is the requirement to specify the class of each product. See rule 3200.13(a)(1). A single product might be a class in and of itself, or a group of products such as single-piece Parcel Post, Media Mail, Bound Printed Matter, and Library Mail might make up a class. Identification of class is necessary to implement the system of regulating rates and classes required under 39 U.S.C. § 3622(d)(2)(A).

[4015] Rules 3200.13(a)(2) and (b)(1) require presentation of product descriptions, and rules 3200.13(a)(3) and (b)(2) require presentation of the current rates and fees. The Commission invites comment on whether the rate and fee schedules should be integrated with each product description, or whether rate and fee schedules should be collected and appear at the end of the market dominant section or the competitive section as applicable, similar to how they now appear in the DMCS.

[4016] For competitive products, the rules only require disclosure of rates and fees for products of general applicability. For products not of general applicability, the rates and fees of negotiated agreements still may be disclosed, but disclosure is not required because of the probability that these rates and fees may be subject to confidentiality requirements.

[4017] Several products may be subject to unique regulatory treatment under the PAEA, such as products of special classification, products not of general applicability, experimental products undergoing market tests, and non-postal products. Rules 3200.13(a)(4)-(6) and (b)(3)-(5) simply require that these products be identified as such.

[4018] The Commission is required to provide notice in the *Federal Register* whenever modifications are approved for the market dominant and competitive product lists. Rule 3200.14(e) implements these notice requirements specified by 39 U.S.C. § 3642(d)(2).

B. Subpart B—Requests Initiated by the Postal Service to Modify the Product Lists Described Within the Mail Classification Schedule

[4019] Rule 3200.30 provides the procedure for the Postal Service to propose modifications to the market dominant and competitive product lists as specified by 39 U.S.C. § 3642(a). Proposals to modify the lists shall be initiated by filing a request with the Commission. The modifications that may be proposed are to add a product to a list, remove a product from a list, or to transfer a product between lists. Multiple modifications may be included in one request.

[4020] The Commission requires specific information to properly determine the correct categorization of a product as either market dominant or competitive. It also needs information to assure the accuracy of the product lists in the Mail Classification Schedule. The Postal Service is to provide this information in its request.

[4021] Rule 3200.31 specifies the content of the Postal Service's request. It requires the Postal Service to identify the product and class of the product, if applicable, (rule 3200.31(a)), and any special characteristics of the product such as: whether it is a special classification, whether it is a product not of general applicability, or whether it is a non-postal product (rule 3200.31(d)). Rule 3200.31(c) requires the Postal Service to indicate the nature of the request, i.e., whether it is a request to add, remove or transfer a product. Rule 3200.31(f) requires the Postal Service to propose modifications to the Mail Classification Schedule necessary to implement its request. Finally, rules 3200.31(b) and (e) require the Postal Service to provide supporting justification for its request. The supporting justification includes a copy of the Governors' decision supporting the request if one has been issued, and the material specified in rule 3200.32 described below.

[4022] Rule 3200.32 directs the Postal Service to provide supporting justification to demonstrate that the modification it requests is in accordance with the policies and applicable criteria of title 39. The supporting justification shall be in the form of a statement from a sponsor(s) of the request who attests to the accuracy of the information

provided. Given a presumption that a hearing on the record will not be provided unless a need is demonstrated, the statement need not be in the form of testimony.

[4023] Paragraphs (b) through (h) of rule 3200.32 focus attention on specific provisions of title 39. For market dominant products, paragraph (b) requires the Postal Service to demonstrate that its proposal is not inconsistent with the objectives, factors, and requirements of modern rate regulation for market dominant products specified in 39 U.S.C. § 3622. For competitive products, paragraph (c) requires the Postal Service to demonstrate that its proposal is not inconsistent with the requirements for rates of competitive products specified in 39 U.S.C. § 3633.

[4024] The primary criteria upon which the Commission is to review the Postal Service's request are provided in 39 U.S.C. § 3642(b). These criteria require consideration of the product's market power, monopoly status, private sector provision of similar products, the opinions of users of the product, and the impact on small business concerns. Paragraphs (d) through (h) of the proposed rule require the Postal Service to provide specific information necessary for the Commission to analyze the request in light of these criteria. Finally, paragraph (i) requires the Postal Service to provide other information as is necessary to fully inform the Commission of its proposal.

[4025] Rule 3200.33 institutes a docket for each Postal Service request. Assigning a docket allows the Commission to organize and track all material related to a request within its docketing, i.e., filing online, system. Notice of each docket shall be published in the *Federal Register*. The notice will provide information regarding the opportunity for written comment from the public. Written comment will be the primary avenue for public input as to whether or not the proposed product modification complies with applicable statutory provisions and Commission rules.

[4026] The PAEA anticipates a different form of review than what was provided for classification changes under previous legislation. The primary focus of the review will be on compliance with the statutory requirements for proper categorization of the Postal Service product as either market dominant or competitive. Review of the operational parameters of the product and the financial basis of the product typically will be minimal.

The Postal Service's request will be reviewed as presented. Participant input into the review process will be through notice and comment. The Commission will review each request for compliance with applicable statutory provisions and Commission rules with consideration of the views expressed in public comments.

[4027] Rule 3200.34 outlines the review procedures. If the requested modification appears to be in compliance with applicable statutory provisions and Commission rules, the Commission may approve the modification without further proceedings. This is consistent with providing the Postal Service flexibility and with the after-the-fact review anticipated by the PAEA. If the request does not appear to be in compliance, the Commission will provide an explanation to the Postal Service and, if appropriate, institute a proceeding to further consider the request. Where minor problems are discovered, the Commission may provide the Postal Service with the opportunity to modify its request to bring the request into compliance.

[4028] Rule 3200.35 provides options for further consideration of a request where there is an indication that the request is not in compliance. Consideration will begin with the Commission convening a conference to identify issues and discuss appropriate approaches for exploring relevant issues. In preparation for the conference, the Commission will request written statements of positions that identify the issues and solicit proposals for further review procedures. Shortly after the conclusion of the conference, the Commission will issue a procedural ruling on how to proceed with the request. The Commission preserves options ranging from immediately approving the request, to providing an opportunity for a hearing, to instituting any other action appropriate to the nature of issues involved.

C. Subpart C—Requests Initiated by Users of the Mail to Modify the Product Lists Described Within the Mail Classification Schedule

[4029] Rule 3200.50 provides the procedure for users of the mail to propose modifications to the market dominant and competitive product lists as specified by 39 U.S.C. § 3642(a). To allow the Postal Service to be the first to initiate proposals to modify product lists, rules in subpart C will not become effective until 6 months after the rules in subpart B become effective.

[4030] In general, the rules in subpart C parallel the rules discussed above in subpart B applicable to Postal Service requests. The notable exceptions are discussed below.

[4031] In many instances, a Postal Service request will be supported by a Governors' decision. Typically, a Governors' decision will not be available for modification requests initiated by users of the mail. Thus, a user of the mail does not have a requirement to provide a Governors' decision in support of its request. Rule 3220.5, *cf.* rule 3200.31(b).

[4032] A user of the mail may or may not have informed the Postal Service of its intent to file a request. Thus, rule 3200.54 directs the Secretary of the Commission to provide a copy of the request to the Postal Service. At the same time, the Postal Service is given an opportunity to provide its initial views, within 28 days, as to the request and to suggest appropriate Commission action. The initial views provided by the Postal Service play an important part in the review process. With a request initiated by the Postal Service, it is presumed that the request is feasible to implement and consistent with the operational plans and goals of the Postal Service. This may or may not be the case for requests initiated by users of the mail.

[4033] The review of a request under rule 3200.55 is more complex than a review of a Postal Service request under rule 3200.34 because the initial views of the Postal Service must be considered. It would be impractical to proceed with a request that was operationally not feasible for the Postal Service to implement, or inconsistent with Postal

Service policies and goals. With this in mind, if the proposed modification is in compliance with statutory provisions and Commission rules, the Commission may approve the modification without further proceedings, but only to the extent that the request is consistent with the Postal Service's views. If the request does not appear in compliance with applicable statutory provisions, Commission rules, or is not consistent with the views of the Postal Service, the Commission will either reject the request, or if appropriate, institute proceedings to further consider the request under rule 3200.56.

D. Subpart D—Proposal of the Commission to Modify the Product Lists Described Within the Mail Classification Schedule

[4034] Rule 3200.70 provides the procedure for the Commission to propose modifications to the market dominant and competitive product lists as specified by 39 U.S.C. § 3642(a). To allow the Postal Service to be the first to initiate proposals to modify product lists, rules in subpart C will not become effective until 6 months after the rules in subpart B become effective.

[4035] In general, the rules in subpart D parallel the rules discussed above in subpart B applicable to Postal Service requests. The notable exceptions are discussed below.

[4036] As with a request initiated by a user of the mail, a Governors' decision will not be available for modification proposals initiated by the Commission. Thus, the Commission does not have a requirement to provide a Governors' decision in support of its request. The Commission will, however, provide its explanation for initiating the docket. Rule 3220.71, *cf.* rule 3200.31(b).

[4037] To formally start the review process, rule 3200.74 directs the Secretary of the Commission to provide a copy of the Commission proposal to the Postal Service. As with a request initiated by a user of the mail, the Postal Service is given an opportunity to provide its initial views as to the proposal and to suggest appropriate Commission action, within 28 days. The initial views provided by the Postal Service play an equally important role in the review process, whether the request was initiated by a user of the mails or proposed by the Commission.

[4038] The review of a request under rule 3200.75 is similar to a request initiated by a user of the mail under rule 3200.55 in that the initial views of the Postal Service must be considered. With this in mind, if the proposed modification is in compliance with statutory provisions and Commission rules, the Commission may approve the modification without further proceedings, but only to the extent that the request is consistent with the Postal Service's views. If the request does not appear in compliance

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with applicable statutory provisions, Commission rules, or is not consistent with the views of the Postal Service, the Commission will either withdraw the proposal, or if appropriate, institute proceedings to further consider the proposal under rule 3200.76.

E. Subpart E—Requests Initiated by the Postal Service to Update the Mail Classification Schedule

[4039] The accuracy and timeliness of the Mail Classification Schedule are important as the Commission will rely on the Mail Classification Schedule when undertaking its regulatory responsibilities. Users of the mail also may rely on the Mail Classification Schedule to form the basis for understanding and utilizing Postal Service products and services and presenting their positions before the Commission. This subpart provides a simplified path for the Postal Service to provide necessary updates to the Mail Classification Schedule.

[4040] The Postal Service is in the best position to provide timely and accurate descriptions of its products. Rule 3200.90 requires the Postal Service to assure that the product descriptions (i.e., all information about a product appearing in the Mail Classification Schedule) accurately reflect the current offerings of Postal Service products and services.

[4041] There are inherent limits on the scope or magnitude of any update allowable under subpart E. Specifically excluded are updates that would modify the market dominant or the competitive product lists. Implicitly excluded are updates that might be governed by other rules such as changes to rates and fees. A proposed update may not change the nature of a service to such an extent that it effectively creates a new product or eliminates an existing product. This subpart is not intended for such changes.

[4042] Within these limitations, however, this subpart allows the Postal Service the flexibility to update provisions of the Mail Classification Schedule with minimal review. To prevent abuse, other checks and balances always are available such as the compliant process. This is consistent with both allowing the Postal Service flexibility and providing after-the-fact review where appropriate.

[4043] The simplified path provided by rule 3200.91 to make changes to the descriptions of the products and services described within the Mail Classification Schedule only requires the Postal Service to provide notice to the Commission prior to

the effective date of a proposed change. While preserving the Commission's editorial rights in the Mail Classification Schedule, rule 3200.92 indicates that the Commission intends to implement requested appropriate updates to the Mail Classification Schedule. There is no provision requiring review of the substance of such changes. The document will be updated to coincide with the effective date of the change determined by the Postal Service.

F. Subpart F—Size and Weight Limitations for Mail Matter

[4044] The Postal Service may establish size and weight limitations for mail matter pursuant to 39 U.S.C. § 3682. Subpart F requires the Postal Service to include size and weight limitations for mail matter in the Mail Classification Schedule to provide visibility to users of the mail and provide information necessary for the Commission to fulfill its statutory role. For market dominant mail matter, the Commission will provide notice of the proposed update in the *Federal Register* and allow public comment. If the Commission finds the proposed update in accordance with the policies and the applicable criteria of title 39, the Mail Classification Schedule will be updated to coincide with the effective date of the proposed change. If the Commission finds the proposed update not in accordance with the policies and the applicable criteria of title 39, the Commission will take such action as it deems appropriate. For competitive mail matter, the Postal Service simply provides notice of an update to the Mail Classification Schedule pursuant to Subpart E. The Commission does not review proposed updates to weight and size limitations of competitive mail matter.

IT IS ORDERED:

1. The Commission proposes to amend its rules of practice and procedure as shown chapter V below. The proposed amendments involve revising rule 5, 39 CFR section 3001.5, by amending rules 5(r) and (s) and adding new rules 5(t) and (u); and adding new parts 3100, Rules Applicable to Rate Adjustments for Market Dominant Products; 3110, Regulation of Rates for Competitive Products; and 3200, Product Lists.
2. Interested persons may submit comments by September 14, 2007.
3. Interested persons may submit reply comments by September 28, 2007.
4. The United States Postal Service shall submit, by September 14, 2007, a draft mail classification schedule containing a market dominant product list and a competitive product list consistent with the discussion in chapter III, section E.4.
5. Interested persons may submit comments concerning the draft mail classification schedule by September 28, 2007.
6. The Secretary shall arrange for publication of this order in the *Federal Register*.

By the Commission.

Steven W. Williams
Secretary

V. PROPOSED RULES

PART 3001—RULES OF PRACTICE AND PROCEDURE

1. Revise § 3001.5 to read as follows:

§ 3001.5 Definitions

* * * * *

(r) *Negotiated service agreement* means a written contract, to be in effect for a defined period of time, between the Postal Service and a mailer, that provides for customer-specific rates or fees and/or terms of service in accordance with the terms and conditions of the contract. A rate associated with a negotiated service agreement is not a rate of general applicability.

(s) *Postal service* refers to the delivery of letters, printed matter, or mailable packages, including acceptance, collection, sorting, transportation, or other functions ancillary thereto.

(t) *Product* means a postal service with a distinct cost or market characteristic for which a rate or rates are, or may reasonably be, applied.

(u) *Rate or class of general applicability* means a rate or class that is available to all mailers equally on the same terms and conditions.

2. Add new parts to read as follows:

Subpart A—General Provisions

§ 3100.1 Applicability.

The rules in this part implement provisions in the Postal Accountability and Enhancement Act (PAEA) establishing ratesetting policies and procedures for market dominant products. With the exception of exigency-based rate adjustments, these procedures allow a minimum of 45 days for advance public notice of the Postal Service's planned rate adjustments and the Commission's assessment of their compliance with provisions establishing an annual limitation, unused rate adjustment authority, or standards for negotiated service agreements, as applicable. Exigency-based rate adjustments require the Postal Service to file a formal request with the Commission and are subject to special procedures.

§ 3100.2 Types of rate adjustments for market dominant products.

(a) There are four types of rate adjustments for market dominant products. A Type 1–A rate adjustment, authorized under 39 U.S.C. § 3622(d)(1)(D), is based on the statutory annual limitation. A Type 1–B rate adjustment, authorized under 39 U.S.C. § 3622(d)(2)(C), is based on an exception to the annual limitation, and is referred to as unused rate adjustment authority. A Type 2 rate adjustment, authorized under 39 U.S.C. § 3622(c)(10), is based on a negotiated service agreement. A Type 3 rate adjustment, authorized under 39 U.S.C. § 3622(d)(1)(E), is based on exigent circumstances.

(b) Upon the establishment of unused rate adjustment authority in any class, the Postal Service shall devise and maintain a schedule that tracks the establishment and subsequent use of unused rate adjustment authority.

(c) The Postal Service may combine Types 1–A, 1–B and 2 rate adjustments for purposes of filing with the Commission.

§ 3100.3 Type 1–A rate adjustment—in general.

(a) A Type 1–A rate adjustment represents the usual type of adjustment to rates of general applicability.

(b) A Type 1–A rate adjustment may result in a rate adjustment that is less than or equal to the annual limitation, but may not exceed the annual limitation.

(c) A Type 1–A rate adjustment for any class that is less than the applicable change in CPI–U results in unused rate adjustment authority associated with that class. Part or all of the unused rate adjustment authority may be used in a subsequent adjustment for that class, subject to the expiration terms in rule 3100.26(d).

§ 3100.4 Type 1–B rate adjustment—in general.

(a) A Type 1–B rate adjustment is a rate adjustment which uses unused rate adjustment authority in whole or in part. A rate adjustment using unused rate adjustment authority may not result in a rate that exceeds the applicable annual limitation plus 2 percentage points.

(b) Unused rate adjustment authority in each class may be applied to rate adjustments in the same class for up to 5 years.

§ 3100.5 Type 2 rate adjustment—in general.

A negotiated service agreement rate adjustment entails a rate adjustment negotiated between the Postal Service and a customer or group of customers.

§ 3100.6 Type 3 adjustment—in general.

(a) A Type 3 rate adjustment is a request for an exigency-based rate adjustment. It is authorized only when justified by exceptional or extraordinary circumstances.

(b) An exigency-based rate adjustment is not subject to the inflation-based limitation or the restrictions on the use of unused rate adjustment authority, and does not implement a negotiated service agreement.

(c) A Postal Service request for a Type 3 rate adjustment is subject to public participation and Commission review within 90 days.

§ 3100.7 Schedule of regular rate changes.

(a) The Postal Service shall maintain on file with the Commission a Schedule for Regular and Predictable Rate Changes. The Commission shall display the Schedule for Regular and Predictable Rate Changes on the Commission website, *http://www.prc.gov*.

(b) The Schedule for Regular and Predictable Rate Changes shall provide mailers with estimated implementation dates for future Type 1–A rate changes for each separate class of mail, should such changes be necessary and appropriate. Rate changes will be scheduled at specified regular intervals.

(c) The Schedule for Regular and Predictable Rate Changes shall provide an explanation that will allow mailers to predict with reasonable accuracy the amounts of future scheduled rate changes.

(d) The initial Schedule for Regular and Predictable Rate Changes must be filed within 90 days of the effective date of this rule. The Postal Service should balance its financial and operational needs with the convenience of mailers of each class of mail in developing the schedule.

(e) Whenever the Postal Service deems it appropriate to change the Schedule for Regular and Predictable Rate Changes, it shall file a revised schedule and explanation with the Commission.

(f) The Postal Service may, for good cause shown, vary rate adjustments from those estimated by the Schedule for Regular and Predictable Rate Changes. In such case, the Postal Service should provide a succinct explanation for such variation with its Type 1–A filing. No explanation is required for changes involving smaller than predicted rate adjustments.

Subpart B—Rules for Rate Adjustments for Rates of General Applicability (Type 1 Rate Adjustments)

§ 3100.10 Procedures.

(a) The Postal Service, in every instance in which it determines to exercise its statutory authority to make a Type 1–A or Type 1–B rate adjustment for a market dominant postal product shall:

(1) Provide public notice in a manner reasonably designed to inform the mailing community and the general public that it intends to change rates not later than 45 days prior to the intended implementation date; and

(2) Transmit a notice of rate adjustment to the Commission no later than 45 days prior to the intended rate implementation date.

(b) The Postal Service is encouraged to provide public notice and to submit its notice of rate adjustment as far in advance of the 45-day minimum as practicable, especially in instances where the intended price changes include classification changes or operations changes likely to have material impact on mailers.

§ 3100.11 Limit on size of rate increases.

Rate increases for each class of market dominant products in any 12-month period are limited.

(a) Rates of general applicability are subject to an inflation-based limitation computed using CPI-U values as detailed in rule 3100.12.

(b) An exception to the inflation-based limitation allows a limited annual recapture of unused rate authority. The amount of unused rate authority is measured separately for each class of mail.

(c) In any 12-month period the inflation-based limitation combined with the allowable recapture of unused rate authority equals the price cap applicable to each class of mail.

§ 3100.12 Source of CPI-U data for purposes of annual limitation.

The monthly CPI-U values needed for the calculation of the annual limitation under this part shall be obtained from the Bureau of Labor Statistics (BLS) Consumer Price Index—All Urban Consumers, U.S. All Items, Not Seasonally Adjusted, Base Period 1982-84=100. The current Series ID for the index is “CUUR0000SA0.”

§ 3100.13 Proceedings for Type 1-A and Type 1-B rate adjustment filings.

(a) The Commission will establish a docket for each rate adjustment filing, promptly publish notice of the filing in the *Federal Register*, post the filing on its website, and allow 20 days from the date of the filing for public comment.

(b) Public comments should address:

(1) Whether the planned rate adjustments measured using the formula established in rule 3100.21(b) are at or below the annual limitation established in rule 3100.11; and

(2) Whether the planned rate adjustments are consistent with the policies of 39 U.S.C. § 3622 and any subsequent amendments thereto.

(c) Within 14 days of the conclusion of the public comment period the Commission will determine whether the planned rate adjustments are consistent with the test for compliance with the annual limitation and issue a notice and order announcing its findings.

(1) If the planned rate adjustments are in compliance with the annual limitation and, if applicable, with the exception for unused rate adjustment authority, they may take effect; or

(2) If the planned rate adjustments are not in compliance with the annual limitation or with the exception for unused rate adjustment authority, the Commission shall explain the basis of its determination.

(d) If planned rate adjustments are not in compliance with the annual limitation or with the exception for unused rate adjustment authority, the Postal Service will submit an amended notice of rate adjustment and describe the modifications to its planned rate adjustments that will bring its rate adjustments into compliance. An amended notice of rate adjustment shall be accompanied by sufficient explanatory information to show that all deficiencies identified by the Commission have been corrected.

(e) The Commission will review any amended notice of rate adjustment for compliance with the annual limitation and the exception for unused rate adjustment authority and within 14 days issue a notice and order announcing its findings.

(1) If the planned rate adjustments are in compliance with the annual limitation or, if applicable, with the exception for unused rate adjustment authority, they may take effect. However, no rate shall take effect until 45 days after the Postal Service files a notice of rate adjustment specifying that rate.

(2) If the planned rate adjustments in an amended notice of rate adjustment are found to be not in compliance with the annual limitation or, if applicable, with the

exception for unused rate adjustment authority, the Commission shall explain the basis of its determination and suggest an appropriate remedy.

§ 3100.14 Contents of notice of rate adjustment.

(a) *General.* The Postal Service notice of rate adjustment must include the following information:

- (1) A schedule of the proposed rates;
- (2) The planned effective date(s) of the proposed rates;
- (3) A representation or evidence that public notice of the planned changes has been issued or will be issued at least 45 days before the effective date(s) for the proposed new rates; and
- (4) The identity of a responsible Postal Service official who will be available to provide prompt responses to requests for clarification from the Commission.

(b) *Supporting technical information and justifications.* The notice of rate adjustment shall be accompanied by:

- (1) The amount of the applicable change in CPI-U calculated as required by rule 3100.21 or 3100.22, as appropriate. This information must be supported by workpapers in which all calculations are shown, and all input values including all relevant CPI-U values are listed with citations to the original sources.
- (2) A schedule showing unused rate authority available for each class of mail displayed by class and available amount for each of the preceding 5 years. This information must be supported by workpapers in which all calculations are shown.
- (3) The percentage change in rates for each class of mail calculated as required by rule 3100.23. This information must be supported by workpapers in which all

calculations are shown, and all input values including current rates, new rates, and billing determinants are listed with citations to the original sources.

(4) The amount of new unused rate authority, if any, that will be generated by the rate adjustment calculated as required by rule 3100.26. All calculations are to be shown with citations to the original sources. If new unused rate authority will be generated for a class of mail that is not expected to cover its attributable costs, the Postal Service should explain the rationale underlying this rate adjustment.

(5) A schedule of the workshare discounts included in the proposed rates, and a companion schedule listing the avoided costs that underlie each such discount. The avoided cost figures must be developed from the most recent PRC Annual Compliance Report. This information must be supported by workpapers in which all calculations are shown, and all input values are listed with citations to the original sources.

(6) Separate justification for all proposed workshare discounts that exceed avoided costs. Each such justification shall reference applicable reasons identified in 39 U.S.C. § 3622(e)(2) or (3). The Postal Service shall also identify and explain discounts that are set substantially below avoided costs and explain any relationship between discounts that are above and those that are below avoided costs.

(7) A discussion of how the proposed rates will help achieve the objectives listed in 39 U.S.C. § 3622(b) and properly take into account the factors listed in § 3622(c).

(8) Such other information as the Postal Service believes will assist the Commission to issue a timely determination of whether the requested increases are consistent with applicable statutory policies.

(c) *New workshare discounts.* Whenever the Postal Service establishes a new workshare discount rate, it must include with its filing:

- (1) A statement explaining its reasons for establishing the discount;
 - (2) All data, economic analyses, and other information believed to justify the discount; and
 - (3) A certification based on comprehensive, competent analyses that the discount will not adversely affect either the rates or the service levels of users of postal services who do not take advantage of the discount.
- (d) *Information required only when Type 1–B rate adjustments are proposed.* The notice of rate adjustment shall identify for each affected class how much existing unused rate authority is used in the proposed rates calculated as required by rule 3100.27. All calculations are to be shown, including citations to the original sources.

Subpart C—Rules for Applying the Price Cap

§ 3100.20 Test for compliance with the annual limitation.

The appropriate annual limitation shall be applied to a measure of the rates paid by mail sent in each class for which rate adjustments are to be made to determine whether planned rates are consistent with the annual limitation.

§ 3100.21 Calculation of annual limitation.

(a) The calculation of an annual limitation involves three steps. First, a simple average CPI–U index is calculated by summing the most recently available 12 monthly CPI–U values from the date the Postal Service files its notice of rate adjustment and dividing the sum by 12 (Recent Average). Then, a second simple average CPI–U index is similarly calculated by summing the 12 monthly CPI–U values immediately preceding the Recent Average and dividing the sum by 12 (Base Average). Finally, the annual limitation is calculated by dividing the Recent Average by the Base Average and subtracting 1 from the quotient. The result is expressed as a percentage.

(b) The formula for calculating an annual limitation is as follows: Annual Limitation = (Recent Average/Base Average) – 1.

§ 3100.22 Calculation of less than annual limitation.

(a) If a notice of rate adjustment is filed less than 1 year after the last Type 1–A or Type 1–B notice of rate adjustment applicable to an affected class of mail, then the annual limitation will recognize the rate increases that have occurred during the preceding 12 months. When the effects of those increases are removed, the remaining partial year limitation is the applicable restriction on rate increases.

(b) The applicable partial year limitation is calculated in two steps. First, a simple average CPI–U index is calculated by summing the 12 most recently available monthly CPI–U values from the date the Postal Service files its notice of rate adjustment and dividing the sum by 12 (Recent Average). The partial year limitation is then calculated by dividing the Recent Average by the Recent Average from the most recent previous notice of rate adjustment (Previous Recent Average) applicable to each affected class of mail and subtracting 1 from the quotient. The result is expressed as a percentage.

(c) The formula for calculating the partial year limitation for a notice of rate adjustment filed less than 1 year after the last notice is as follows: Partial Year Limitation = (Recent Average/Previous Recent Average) – 1.

§ 3100.23 Calculation of percentage change in rates.

(a) The term “rate cell” as applied in the test for compliance with the annual limitation shall apply to each and every separate rate identified in any applicable notice of rate adjustment for rates of general applicability. Thus, seasonal or temporary rates, for example, shall be identified and treated as rate cells separate and distinct from the corresponding non-seasonal or permanent rates.

(b) For each class of mail, the percentage change in rates is calculated in three steps. First, the volume of each rate cell in the class is multiplied by the current rate for the respective cell and the resulting products are summed. In the case of seasonal or temporary rates, the most recently applied rate shall be considered the current rate. Then, the same set of rate cell volumes are multiplied by the corresponding planned rate for each cell and the resulting products are summed. Finally, the percentage change in rates is calculated by dividing the results of the first step by the results of the second step and subtracting 1 from the quotient. The result is expressed as a percentage.

(c) The formula for calculating the percentage change in rates for a class described in subsection (b) is as follows:

$$\text{Percentage change in rates} = \left(\frac{\sum_{i=1}^N (R_{i,n})(V_i)}{\sum_{i=1}^N (R_{i,c})(V_i)} \right) - 1$$

- N = number of rate cells in the class
- i = denotes a rate cell (i = 1, 2, ..., N)
- R_{i,n} = planned rate of rate cell i
- R_{i,c} = current rate of rate cell i
- V_i = volume of rate cell i

§ 3100.24 Treatment of volume associated with negotiated service agreements.

(a) Mail volumes sent at non-tariff rates under negotiated service agreements are to be included in the calculation of percentage change in rates as though they paid the appropriate rates of general applicability. Where it is impractical to identify the rates of general applicability (e.g., because unique rate categories are created for a mailer), the

volumes associated with the mail sent under the terms of the negotiated service agreement shall be excluded from the calculation of percentage change in rates.

(b) The Postal Service shall identify and explain all assumptions it makes with respect to the treatment of negotiated service agreements in the calculation of the percentage change in rates and provide the rationale for its assumptions.

§ 3100.25 Limitation on unused rate adjustment authority rate adjustments.

Unused rate adjustment authority rate adjustments may only be applied together with inflation-based limitation rate adjustments or when inflation-based limitation rate adjustments are not possible. Unused rate adjustment authority rate adjustments may not be used in lieu of an inflation-based limitation rate adjustment.

§ 3100.26 Calculation of unused rate adjustment authority.

(a) Unused rate adjustment authority accrues during the entire period between Type 1 rate adjustments.

(b) When notices of rate adjustments are filed 12 months apart or less, either the annual or partial year limitation (developed pursuant to rule 3100.21(a) or .22(b) respectively) is used to measure the accrued unused rate authority. In either circumstance, the new unused rate authority for each class is equal to the difference between the maximum allowable percentage change in rates under the applicable rate limitation and the actual percentage change in rates for that class.

(c) When a notice of rate adjustment is filed more than 12 months after the previous notice of rate adjustment, unused rate authority is computed in three steps.

(1) The unused rate authority for the 12 months represented by the annual limitation is computed as described in subsection (b).

(2) The additional unused rate authority accrued is measured by dividing the Base Average applicable to the instant notice of rate adjustment (as developed pursuant to rule 3100.21(a)) by the Recent Average utilized in the previous notice of rate adjustment (as developed pursuant to rule 3100.21(a)) and subtracting 1 from the quotient. The result is expressed as a percentage.

(3) The results from step one and step two are added together.

(d) Unused rate adjustment authority lapses 5 years after the date of filing of the notice of rate adjustment leading to its computation.

§ 3100.27 Application of unused rate adjustment authority.

When the percentage change in rates for a class is greater than the applicable annual limitation, then the difference between the percentage change in rates for the class and the price cap shall be subtracted from the existing unused rate authority for the class, using a first-in, first-out (FIFO) method, beginning 5 years before the instant notice.

§ 3100.28 Maximum size of unused rate adjustment authority rate adjustments.

Unused rate adjustment authority rate adjustments for any class may not exceed the applicable annual limitation described in rule 3001.21 plus the lesser of:

(a) 2 percent; or

(b) The sum of any unused rate adjustment authority for that class.

**Subpart D—Rules for Rate Adjustments for Negotiated Service Agreements
(Type 2 Rate Adjustments)**

§ 3100.40 Negotiated service agreements.

(a) In administering this subpart, it shall be the objective of the Commission to allow implementation of negotiated service agreements that satisfy the statutory requirements of 39 U.S.C. § 3622(c)(10). Negotiated service agreements must either:

- (1) Improve the net financial position of the Postal Service (§ 3622(c)(10)(A)(i)), or
- (2) Enhance the performance of operational functions (§ 3622(c)(10)(A)(ii)).

(b) Negotiated service agreements may not cause unreasonable harm to the marketplace (§ 3622(c)(10)(B)).

§ 3100.41 Procedures.

The Postal Service, in every instance in which it determines to exercise its statutory authority to make a Type 2 rate adjustment for a market dominant postal product shall provide public notice in a manner reasonably designed to inform the mailing community and the general public that it intends to change rates not later than 45 days prior to the intended implementation date; and transmit a notice of agreement to the Commission no later than 45 days prior to the intended rate implementation date.

§ 3100.42 Contents of notice of agreement in support of a negotiated service agreement.

(a) Whenever the Postal Service proposes to establish or change rates or fees and/or the Mail Classification Schedule based on a negotiated service agreement, the Postal Service shall file with the Commission a notice of agreement. This shall include at a minimum:

- (b) *General.* Each notice of agreement will include:

- (1) A copy of the negotiated service agreement;
 - (2) The planned effective date(s) of the proposed rates;
 - (3) A representation or evidence that public notice of the planned changes has been issued or will be issued at least 45 days before the effective date(s) for the proposed new rates; and
 - (4) The identity of a responsible Postal Service official who will be available to provide prompt responses to requests for clarification from the Commission.
- (c) A statement identifying all parties to the agreement and a description clearly explaining the operative components of the agreement.
- (d) Details regarding the expected improvements in the net financial position or operations of the Postal Service. The projection of change in net financial position as a result of the agreement shall include for each year of the agreement:
- (1) The estimated mailer-specific costs, volumes, and revenues of the Postal Service absent the implementation of the negotiated service agreement;
 - (2) The estimated mailer-specific costs, volumes, and revenues of the Postal Service which result from implementation of the negotiated service agreement; and
 - (3) An analysis of the effects of the negotiated service agreement on the contribution to institutional costs from mailers not party to the agreement.
 - (4) If mailer-specific costs are not available, the source and derivation of the costs that are used shall be provided, together with a discussion of the currency and reliability of those costs and their suitability as a proxy for the mailer-specific costs.

(e) An identification of each component of the agreement expected to enhance the performance of mail preparation, processing, transportation or other functions in each year of the agreement, and a discussion of the nature and expected impact of each such enhancement.

(f) Details regarding any and all actions (performed or to be performed) to assure that the agreement will not result in unreasonable harm to the marketplace.

(g) Such other information as the Postal Service believes will assist the Commission to issue a timely determination of whether the requested increases are consistent with applicable statutory policies.

§ 3100.43 Data collection plan.

The Postal Service shall include with any notice of agreement a detailed plan for providing data or information on actual experience under the agreement sufficient to allow evaluation of whether the negotiated service agreement operates in compliance with § 3622(c)(10). This shall include, at a minimum, a plan for providing the following annualized information on a yearly basis within 60 days of the date of implementation of a proposed agreement:

(a) The change in net financial position as a result of the agreement. This calculation shall include for each year of the agreement:

(1) The actual mailer-specific costs, volumes, and revenues of the Postal Service;
and

(2) An analysis of the effects of the negotiated service agreement on the net overall contribution to the institutional costs of the Postal Service.

(3) If mailer-specific costs are not available, the source and derivation of the costs that are used shall be provided, including a discussion of the currency and reliability of those costs, and their suitability as a proxy for the mailer-specific costs.

(b) A discussion of the changes in operations of the Postal Service that have resulted from the agreement. This shall include, for each year of the agreement, identification of each component of the agreement known to enhance the performance of mail preparation, processing, transportation, or other functions in each year of the agreement.

(c) An analysis of the impact of the negotiated service agreement on the marketplace, including a discussion of any and all actions taken to protect the marketplace from unreasonable harm.

Subpart E Rules for Rate Adjustments in Exigent Circumstances (Type 3 Rate Adjustments)

§ 3100.60 Applicability.

The Postal Service may request to increase rates for market dominant products in excess of the annual limitation on the percentage changes in rates described in rule 3100.11(c) due to extraordinary or exceptional circumstances. Such requests will be known as exigent requests.

§ 3100.61 Contents of exigent requests.

- (a) Each exigent request shall include the following:
 - (1) A schedule of the proposed rates;
 - (2) Calculations quantifying the increase for each affected product and class;

(3) A full discussion of the extraordinary or exceptional circumstance(s) giving rise to the request, and a complete explanation of how both the requested overall increase, and the specific rate increases requested, relate to those circumstances;

(4) A full discussion of why the requested increases are necessary to enable the Postal Service, under best practices of honest, efficient and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States;

(5) A full discussion of why the requested increases are reasonable and equitable as between types of users of market dominant products;

(6) An explanation of when, or under what circumstances, the Postal Service expects to be able to rescind the exigent increases in whole or in part;

(7) A justification for exigent treatment which analyzes why the circumstance giving rise to the request was neither foreseeable nor avoidable by reasonable prior action; and

(8) Such other information as the Postal Service believes will assist the Commission to issue a timely determination of whether the requested increases are consistent with applicable statutory policies.

(b) The Postal Service shall identify one or more knowledgeable Postal Service official(s) who will be available to provide prompt responses to Commission requests for clarification related to each topic specified in rule 3100.61(a).

§ 3100.62 Supplemental information.

The Commission may require the Postal Service to provide clarification of its request or to provide information in addition to that called for by rule 3100.61 in order to gain a

better understanding of the circumstances leading to the request or the justification for the specific rate increases requested.

§ 3100.63 Treatment of unused rate adjustment authority.

(a) Each exigent request will identify the unused rate authority for each class of mail as of the date of the request.

(b) Pursuant to an exigent request, increases may use accumulated unused rate adjustment authority in amounts greater than the limitation described in rule 3100.28.

(c) Exigent increases will exhaust all unused rate adjustment authority for each class of mail before imposing additional rate increases in excess of the price cap for any class of mail.

§ 3100.64 Expeditious treatment of exigent requests.

Requests under this subpart seek rate relief required by extraordinary or exceptional circumstances and will be treated with expedition at every stage. It is Commission policy to provide appropriate relief as quickly as possible consistent with statutory requirements and procedural fairness.

§ 3100.65 Special procedures applicable to exigent requests.

(a) When the Commission receives a request for exigent rate increases, it will publish a notice in the *Federal Register* describing the request and inviting public participation.

(b) The Commission will hold a public hearing on the Postal Service request. During the public hearing, responsible Postal Service officials will appear and respond under oath to questions from the Commissioners or their designees addressing previously identified aspects of the Postal Service's request and the supporting information provided in response to the topics specified in rule 3100.61(a).

(c) Interested persons will be given an opportunity to submit to the Commission suggested relevant questions that might be posed during the public hearing. Such questions, and any explanatory materials submitted to clarify the purpose of the questions, should be filed in accordance with rule 3001.9, and will become part of the administrative record of the proceeding.

(d) The timing and length of the public hearing will depend on the nature of the circumstances giving rise to the request and the clarity and completeness of the supporting materials provided with the request.

(e) If the Postal Service is unable to provide adequate explanations during the public hearing, supplementary written or oral responses may be required.

(f) Following the conclusion of the public hearings and submission of any supplementary materials interested persons will be given the opportunity to submit written comments on:

(1) The sufficiency of the justification for an exigent rate increase;

(2) The adequacy of the justification for increases in the amounts requested by the Postal Service; and

(3) Whether the specific rate adjustments requested are reasonable and equitable.

(g) An opportunity to submit written reply comments will be given to the Postal Service and other interested persons.

§ 3100.66 Deadline for Commission decision.

The Commission will act expeditiously on the Postal Service request, taking into account all written comments. In every instance a Commission decision will be issued within 90 days of a Postal Service request for an exigent rate increase.

PART 3110—REGULATION OF RATES FOR COMPETITIVE PRODUCTS

§ 3110.1 Scope.

Rules in this part are applicable to competitive products.

§ 3110.2 Increase in rates of general applicability.

(a) When the Postal Service determines to increase a rate or rates of general applicability, it shall file notice of the increase with the Commission no later than the date of publication of the decision in the *Federal Register* concerning such change, but at least 30 days before the effective date of the increase.

(b) The notice filed with the Commission shall include an explanation and justification for the change, the effective date, and a schedule of the changed rates.

§ 3110.3 Decrease in rates of general applicability.

(a) When the Postal Service determines to decrease a rate or rates of general applicability, it shall file notice of the decrease with the Commission no later than the date of publication of the decision in the *Federal Register* concerning such change, but at least 30 days before the effective date of the decrease.

(b) The notice filed with the Commission shall include an explanation and justification for the change, the effective date, and a schedule of the changed rates.

(c) In addition to the notice, the Postal Service shall file with the Commission:

(1) Sufficient annualized revenue and cost data to demonstrate that each affected competitive product will be in compliance with 39 U.S.C. § 3633(a)(2); and

(2) A certified statement by a representative of the Postal Service attesting to the accuracy of the data submitted, and explaining why, following the change, competitive products in total will be in compliance with 39 U.S.C. §§ 3633(a)(1) and (3).

§ 3110.4 Change in class of general applicability.

(a) In the case of a change in class of general applicability, the Postal Service shall file notice of the change with the Commission no later than the date of publication of the decision in the *Federal Register*, but at least 30 days before the effective date of the increase.

(b) The notice filed with the Commission shall include an explanation and justification for the change, the effective date, and the record of proceedings regarding such decision.

§ 3110.5 Rate or class not of general applicability.

(a) When the Postal Service determines to add or change a rate or class not of general applicability, it shall file notice of its decision with the Commission at least 15 days before the effective date of the change.

(b) The notice filed with the Commission shall include an explanation and justification for the change, the effective date, the rate and class decision, and the record of proceedings regarding such decision.

(c) In addition to the notice, the Postal Service shall file with the Commission:

(1) Sufficient annualized revenue and cost data to demonstrate that each affected competitive product will be in compliance with 39 U.S.C. § 3633(a)(2); and

(2) A certified statement by a representative of the Postal Service attesting to the accuracy of the data submitted, and explaining why, following the change, competitive products in total will be in compliance with 39 U.S.C. §§ 3633(a)(1) and (3).

§ 3110.6 Sufficiency of information.

If, after review of the information submitted pursuant to this part, the Commission determines additional information is necessary to enable it to evaluate whether competitive products will be in compliance with 39 U.S.C. § 3633(a), it may, in its discretion, require the Postal Service to provide additional information as deemed necessary.

§ 3110.7 Standards for compliance.

For purposes of determining competitive products' compliance with 39 U.S.C. § 3633, the Commission will apply the following standards:

(a) Incremental costs will be used to test for cross-subsidies by market dominant products of competitive products. To the extent that incremental cost data are unavailable, the Commission will use competitive products' attributable costs supplemented to include causally related, group-specific costs to test for cross-subsidies.

(b) Each competitive product must recover its attributable costs as defined in 39 U.S.C. § 3631(b).

(c) Annually, on a fiscal year basis, the appropriate share of institutional costs to be recovered from competitive products collectively is, at a minimum, 5.5 percent of the Postal Service's total institutional costs.

PART 3200—PRODUCT LISTS

§ 3200.1 Applicability.

(a) The rules in this part provide for establishing a Mail Classification Schedule. The Mail Classification Schedule shall categorize postal products as either market dominant or competitive. As established, the market dominant and competitive product lists specified in the Mail Classification Schedule shall be consistent with the market dominant product list specified in 39 U.S.C. § 3621(a) and the competitive product list specified in 39 U.S.C. § 3631(a).

(b) Once established, the Mail Classification Schedule may be modified subject to the procedures specified in this part. See part 3210 for rules applicable to Mail Classification Schedule modifications for market tests of experimental products.

Subpart A—Mail Classification Schedule

§ 3200.10 General.

The Mail Classification Schedule shall consist of two parts. Part One shall specify the list of market dominant products and include the explanatory information specified in § 3200.13(a). Part Two shall specify the list of competitive products and include the explanatory information specified in § 3200.13(b).

§ 3200.11 Initial Mail Classification Schedule.

The Postal Service shall file with the Commission a proposed Mail Classification Schedule within 30 days of enactment of this rule. The proposed Mail Classification Schedule shall reflect the market dominant and competitive product lists as specified in 39 U.S.C. § 3621(a) and 39 U.S.C. § 3631(a) respectively. The Commission shall cause notice of the Postal Service filing to be published in the *Federal Register*. The notice shall provide the opportunity for public comment. After consideration of the proposed Mail Classification Schedule and public comment, the Commission shall incorporate a

Mail Classification Schedule into the Commission's rules, and cause notice thereof to be published in the *Federal Register*. Thereafter, the Mail Classification Schedule may be modified as specified by Commission rule.

§ 3200.12 Publication of the Mail Classification Schedule.

(a) *Incorporation by reference.* Section 552(a) of title 5, U.S.C., relating to the public information requirements of the Administrative Procedure Act, provides in pertinent part that "...matter reasonably available to the class of persons affected thereby is deemed published in the Federal Register when incorporated by reference therein with the approval of the Director of the Federal Register." In conformity with that provision, and with 39 U.S.C. section 503, and as provided in this part, the Postal Regulatory Commission hereby incorporates by reference in this part, the Mail Classification Schedule, a looseleaf document published and maintained by the Postal Regulatory Commission.

(b) Availability of the Mail Classification Schedule.

(1) Copies of the Mail Classification Schedule, both current and previous issues, are available during regular business hours for reference and public inspection at the Postal Regulatory Commission's Reading Room located at 901 New York Avenue, NW, Suite 200, Washington, DC 20268-0001. The Mail Classification Schedule, both current and previous issues, also are available on the Internet at <http://www.prc.gov>. A copy of the Mail Classification Schedule may be obtained by contacting the Postal Regulatory Commission's Docket Section in Washington, DC.

(2) Interested persons may receive electronic notification of updates to the Mail Classification Schedule by contacting the Postal Regulatory Commission's Docket Section in Washington, DC.

(3) Interested persons may inspect a copy of the Mail Classification Schedule at the National Archives and Records Administration (NARA). For information on the availability of this material at NARA, call 202-741-6030, or go to: <http://www.archives.gov/federal-register/cfr/ibr-locations.html>.

(c) *Amendments to the Mail Classification Schedule.*

(1) Except final regulations published as provided in paragraph (2) of this section, only notices rather than complete text of changes made to the Mail Classification Schedule are published in the *Federal Register*. These notices are published in the form of one summary transmittal letter for each issue of the Mail Classification Schedule. A complete issue of the Mail Classification Schedule, including the text of all changes published to date, will be filed with the Director, Office of the Federal Register.

(2) When the Postal Regulatory Commission invites comments from the public on a proposed change to the Mail Classification Schedule, the proposed change and, if adopted, the full text of the final regulation is published in the *Federal Register*.

(3) For references to amendments to the Mail Classification Schedule adopted under paragraph (2) of this section after issuance of the most recent transmittal letter (termed Summary of Changes in the Mail Classification Schedule) listed below, see section 3200.12(c) in the List of CFR sections affecting title 39 of the *Code of Federal Regulations*.

Transmittal letter for issue	Dated	Federal Register publication
1	[TBD]	[TBD FR TBD]

(d) *Approval of the director of the Federal Register.* Incorporation by reference of the publication now titled the Mail Classification Schedule [was approved] by the Director of the Federal Register under 5 U.S.C. 552(a) and 1 CFR Part 51 is pending.

§ 3200.13 Contents of the Mail Classification Schedule.

The Mail Classification Schedule shall provide:

- (a) The list of market dominant products, including:
 - (1) The class of each market dominant product;
 - (2) The description of each market dominant product;
 - (3) A schedule listing for each market dominant product the current rates and fees;
 - (4) Where applicable, the identification of a product as a special classification within the meaning of 39 U.S.C. § 3622(c)(10) for market dominant products;
 - (5) Where applicable, the identification of a product as an experimental product undergoing a market test; and
 - (6) Where applicable, the identification of a product as a non-postal product.
- (b) The list of competitive products, including:
 - (1) The description of each competitive product;
 - (2) A schedule listing for each competitive product of general applicability the current rates and fees;
 - (3) The identification of each product not of general applicability within the meaning of 39 U.S.C. § 3632(b)(3) for competitive products;
 - (4) Where applicable, the identification of a product as an experimental product undergoing a market test; and

- (5) Where applicable, the identification of a product as a non-postal product.

§ 3200.14 Notice of change.

Whenever the Postal Regulatory Commission modifies the list of products in the market dominant category or the competitive category, it shall cause notice of such change to be published in the *Federal Register*. The notice shall:

- (a) Include the current list of market dominant products and the current list of competitive products appearing in the Mail Classification Schedule;
- (b) Indicate how and when the previous product lists have been modified; and
- (c) Describe other changes to the Mail Classification Schedule as necessary.

Subpart B—Requests initiated by the Postal Service to Modify the Product Lists Described Within the Mail Classification Schedule.

§ 3200.30 General.

The Postal Service, by filing a request with the Commission, may propose a modification to the market dominant product list or the competitive product list appearing in the Mail Classification Schedule. For purposes of this part, modification shall be defined as adding a product to a list, removing a product from a list, or moving a product from one list to the other list.

§ 3200.31 Contents of a request.

A request to modify the market dominant product list or the competitive product list shall:

- (a) Provide the name, and class if applicable, of each product that is the subject of the request;
- (b) Provide a copy of the Governor's decision supporting the request, if any;

(c) Indicate whether the request proposes to add a product to the market dominant list or the competitive list, remove a product from the market dominant list or the competitive list, or transfer a product from the market dominant list to the competitive list or from the competitive list to the market dominant list;

(d) Indicate whether each product that is the subject of the request is:

(1) A special classification within the meaning of 39 U.S.C. § 3622(c)(10) for market dominant products;

(2) A product not of general applicability within the meaning of 39 U.S.C. § 3632(b)(3) for competitive products; or

(3) A non-postal product.

(e) Provide all supporting justification upon which the Postal Service proposes to rely; and

(f) Include a copy of the applicable sections of the Mail Classification Schedule and the proposed changes therein in legislative format.

§ 3200.32 Supporting justification.

Supporting justification shall be in the form of a statement from one or more knowledgeable Postal Service official(s) who sponsors the request and attests to the accuracy of the information contained within the statement. The justification shall:

(a) Demonstrate why the change is in accordance with the policies and the applicable criteria of title 39;

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

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

(d) Verify that the change does not classify as competitive a product over which the Postal Service exercises sufficient market power that it can:

- (1) Set the price of such product substantially above costs;
- (2) Raise prices significantly;
- (3) Decrease quality; or
- (4) Decrease output

without risk of losing a significant level of business to other firms offering similar products. Provide available supporting documentation.

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

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

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

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

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

§ 3200.33 Docket and notice.

The Commission shall institute a docket for consideration of each request to modify the market dominant or the competitive product lists. The Commission shall cause notice of each docket to be published in the *Federal Register*, which includes:

- (a) A description of the request;
- (b) Direction to obtain further information in regard to the request, if any;
- (c) Direction for participation in the docket;
- (d) Designation of an officer of the Commission to represent the interests of the general public; and
- (e) Information regarding an opportunity for written comment addressing compliance with statutory provisions and applicable Commission rules in regard to the proposed modification.

§ 3200.34 Review.

The Commission shall review the request and responsive comments. The Commission shall either:

- (a) Approve the request to modify the market dominant and competitive product lists;
- (b) Institute further proceedings to consider all or part of the request if it finds that there is substantial likelihood that the modification is inconsistent with statutory policies

or Commission rules, and explain its reasons for not approving the request to modify the market dominant and competitive product lists;

- (c) Provide an opportunity for the Postal Service to modify its request; or
- (d) Direct other action as the Commission may consider appropriate.

§ 3200.35 Further proceedings.

If the Commission determines that further proceedings are necessary, a conference shall be scheduled to consider the concerns expressed by the Commission. Written statements commenting on the Commission's concerns shall be requested, to be filed 7 days prior to the conference. Upon conclusion of the conference, the Commission shall promptly issue a ruling to:

- (a) Provide for a period of discovery to obtain further information;
- (b) Schedule a hearing on the record for further consideration of the request;
- (c) Explain the reasons for not going forward with additional proceedings and approve the request to modify the market dominant and competitive product lists; or
- (d) Direct other action as the Commission may consider appropriate.

Subpart C—Requests Initiated by Users of the Mail to Modify the Product Lists Described Within the Mail Classification Schedule

§ 3200.50 General.

Users of the mail, by filing a request with the Commission, may propose a modification to the market dominant product list or the competitive product list appearing in the Mail Classification Schedule. For purposes of this part, modification shall be defined as adding a product to a list, removing a product from a list, or transferring a product from one list to the other list.

§ 3200.51 Contents of a request.

A request to modify the market dominant product list or the competitive product list shall:

(a) Provide the name, and class if applicable, of each product that is the subject of the request;

(b) Indicate whether the request proposes to add a product to the market dominant list or the competitive list, remove a product from the market dominant list or the competitive list, or move a product from the market dominant list to the competitive list or from the competitive list to the market dominant list;

(c) Indicate whether each product that is the subject of the request is:

(1) A special classification within the meaning of 39 U.S.C. § 3622(c)(10) for market dominant products

(2) A product not of general applicability within the meaning of 39 U.S.C. § 3632(b) for competitive products; or

(3) A non-postal product.

(d) Provide all supporting justification upon which the proponent of the request proposes to rely; and

(e) Include a copy of the applicable sections of the Mail Classification Schedule and the proposed changes therein in legislative format.

§ 3200.52 Supporting justification.

Supporting justification shall be in the form of a statement from a knowledgeable proponent of the request who attests to the accuracy of the information contained within the statement. The justification shall:

- (a) Demonstrate why the change is in accordance with the policies and the applicable criteria of title 39;
- (b) Explain why, as to market dominant products, the change is not inconsistent with each requirement of § 3622(d), and that it advances the objectives of § 3622(b), taking into account the factors of § 3622(c);
- (c) Explain why, as to competitive products, the addition, deletion, or transfer will not result in the violation of any of the standards of § 3633.
- (d) Verify that the change does not classify as competitive a product over which the Postal Service exercises sufficient market power that it can:
 - (1) Set the price of such product substantially above costs;
 - (2) Raise prices significantly;
 - (3) Decrease quality; or
 - (4) Decrease output

without risk of losing a significant level of business to other firms offering similar products.

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

- (f) Provide a description of the availability and nature of enterprises in the private sector engaged in the delivery of the product;
- (g) Provide any information available on the views of those who use the product on the appropriateness of the proposed modification;
- (h) Provide a description of the likely impact of the proposed modification on small business concerns; and
- (i) Include such information and data, and such statements of reasons and bases, as are necessary and appropriate to fully inform the Commission of the nature, scope, significance, and impact of the proposed modification.

§ 3200.53 Docket and notice.

The Commission shall institute a docket for consideration of each request to modify the market dominant or the competitive product lists. The Commission shall cause notice of each docket to be published in the *Federal Register*, which includes:

- (a) A description of the request;
- (b) Direction to obtain further information in regard to the request, if any;
- (c) Direction for participation in the docket;
- (d) Designation of an officer of the Commission to represent the interests of the general public; and
- (e) Information regarding an opportunity for written comment addressing compliance with statutory provisions and applicable Commission rules in regard to the proposed modification.

§ 3200.54 Postal Service notice and reply.

The Secretary of the Commission shall forward to the Postal Service a copy of the request. Within 28 days of the filing of the request, the Postal Service shall provide its preliminary views in regard to the request. The Postal Service may include suggestions for appropriate Commission action in response to the request.

§ 3200.55 Review.

The Commission shall review the request, Postal Service reply, and public comment to determine whether the proposed modification to the market dominant and competitive product lists complies with applicable statutory requirements and the Commission's rules, and whether the proposed modification is consistent with the position of the Postal Service as expressed in its reply. The Commission shall either:

- (a) Approve the request to modify the market dominant and competitive product lists, but only to the extent the modification is consistent with the position of the Postal Service;
- (b) Reject the request;
- (c) Institute further proceedings to consider the request to modify the market dominant and competitive product lists; or
- (d) Direct other action as the Commission may consider appropriate.

§ 3200.56 Further proceedings.

If the Commission determines that further proceedings are necessary, a conference shall be scheduled to consider the merits of going forward with the request. Upon conclusion of the conference, the Commission shall promptly issue a ruling to:

- (a) Provide for a period of discovery to obtain further information;

- (b) Schedule a hearing on the record for further consideration of the request;
- (c) Explain the reasons for not going forward with formal proceedings; or
- (d) Direct other action as the Commission may consider appropriate.

Subpart D—Proposal of the Commission to Modify the Product Lists Described Within the Mail Classification Schedule

§ 3200.70 General.

The Commission, of its own initiative, may propose a modification to the market dominant product list or the competitive product list provided within the Mail Classification Schedule. For purposes of this part, modification shall be defined as adding a product to a list, removing a product from a list, or transferring a product from one list to the other list.

§ 3200.71 Contents of a proposal.

A proposal to modify the market dominant product list or the competitive product list shall:

- (a) Provide the name, and class if applicable, of each product that is the subject of the proposal;
- (b) Indicate whether the proposal would add a product to the market dominant list or the competitive list, remove a product from the market dominant list or the competitive list, or move a product from the market dominant list to the competitive list or from the competitive list to the market dominant list;
- (c) Indicate whether each product that is the subject of the proposal is:
 - (1) A special classification within the meaning of 39 U.S.C. § 3622(c)(10) for market dominant products;

- (2) A product not of general applicability within the meaning of 39 U.S.C. § 3632(b) for competitive products, or
- (3) A non-postal product.
- (d) Provide justification supporting the proposal; and
- (e) Include a copy of the applicable sections of the Mail Classification Schedule and the proposed changes therein in legislative format.

§ 3200.72 Supporting justification.

Supporting justification shall:

- (a) Provide an explanation for initiating the docket;
- (b) Explain why, as to market dominant products, the change is not inconsistent with each requirement of § 3622(d), and that it advances the objectives of § 3622(b), taking into account the factors of § 3622(c);
- (c) Explain why, as to competitive products, the addition, subtraction, or transfer will not result in the violation of any of the standards of § 3633.
- (d) Verify that the change does not classify as competitive a product over which the Postal Service exercises sufficient market power that it can:
 - (1) Set the price of such product substantially above costs;
 - (2) Raise prices significantly;
 - (3) Decrease quality;
 - (4) Decrease output

without risk of losing a significant level of business to other firms offering similar products.

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

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

(g) Provide any information available on the views of those who use the product involved on the appropriateness of the proposed modification;

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

(i) Include such information and data, and such statements of reasons and bases, as are necessary and appropriate to fully inform the Postal Service and users of the mail of the nature, scope, significance, and impact of the proposed modification

§ 3200.73 Docket and notice.

The Commission shall institute a docket for consideration of each proposal to modify the market dominant or the competitive product lists. The Commission shall cause notice of each docket to be published in the *Federal Register*, which includes:

(a) A description of the proposal;

(b) Direction to obtain further information in regard to the proposal, if any;

(c) Direction for participation in the docket;

(d) Designation of an officer of the Commission to represent the interests of the general public; and

(e) Information regarding an opportunity for written comment addressing compliance with statutory provisions and applicable Commission rules in regard to the proposed modification.

§ 3200.74 Postal Service notice and reply.

The Secretary of the Commission shall forward to the Postal Service a copy of the notice of proposal. Within 28 days of the filing of the proposal, the Postal Service shall provide its preliminary views in regard to the proposal. The Postal Service may include suggestions for appropriate further procedural steps.

§ 3200.75 Review.

The Commission shall review the Postal Service reply and public comment. The Commission shall either:

- (a) Approve the proposal to modify the market dominant and competitive product lists, but only to the extent the modification is consistent with the position of the Postal Service;
- (b) Withdraw the proposal;
- (c) Institute further proceedings to consider the proposal, identifying relevant issues that may require further development; or
- (d) Direct other action as the Commission may consider appropriate.

§ 3200.76 Further proceedings.

If the Commission determines that further proceedings are appropriate, a conference shall be scheduled to consider the merits of going forward with the proposal. Upon conclusion of the conference, the Commission shall promptly issue a ruling to:

- (a) Provide for a period of discovery to obtain further information;

- (b) Schedule a hearing on the record for further consideration of the proposal;
- (c) Explain the reasons for not going forward with formal proceedings; or
- (d) Direct other action as the Commission may consider appropriate.

Subpart E—Requests Initiated by the Postal Service to Update the Mail Classification Schedule

§ 3200.90 General.

The Postal Service shall assure that product descriptions in the Mail Classification Schedule accurately represent the current offerings of Postal Service products and services.

§ 3200.91 Modifications.

The Postal Service shall submit corrections to product descriptions in the Mail Classification Schedule, that do not constitute a proposal to modify the market dominant product list or the competitive product list as defined in rule 3200.30, by filing notice of the proposed change with the Commission no later than 15 days prior to the effective date of the proposed change.

§ 3200.92 Implementation.

The Commission shall review the proposed corrections for formatting and conformance with the structure of the Mail Classification Schedule, and subject to editorial changes, shall update the Mail Classification Schedule to coincide with the effective date of the proposed change.

Subpart F—Size and Weight Limitations for Mail Matter

§ 3200.110 General.

Applicable size and weight limitations for mail matter shall appear in the Mail Classification Schedule as part of the description of each product.

§ 3200.111 Limitations applicable to market dominant mail matter.

(a) The Postal Service shall inform the Commission of updates to size and weight limitations for market dominant mail matter by filing notice with the Commission 45 days prior to the effective date of the proposed update. The notice shall include a copy of the applicable sections of the Mail Classification Schedule and the proposed updates therein in legislative format.

(b) The Commission shall provide notice of the proposed update in the *Federal Register* and seek public comment on whether the proposed update is in accordance with the policies and the applicable criteria of title 39.

(c) If the Commission finds the proposed update in accordance with the policies and the applicable criteria of title 39, the Commission shall review the proposed Mail Classification Schedule language for formatting and conformance with the structure of the Mail Classification Schedule, and subject to editorial changes, shall change the Mail Classification Schedule to coincide with the effective date of the proposed update.

(d) If the Commission finds the proposed update not in accordance with the policies and the applicable criteria of title 39, the Commission may direct other action as deemed appropriate.

§ 3200.112 Limitations applicable to competitive mail matter.

The Postal Service shall notify the Commission of updates to size and weight limitations for competitive mail matter pursuant to subpart E.

**COMMENTS TO REGULATIONS ESTABLISHING
A SYSTEM OF RATEMAKING**

PARTICIPANT	TITLE	FILING DATE
Advo, Inc. (Advo)	Comments of Advo, Inc. in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	April 6, 2007
	Reply Comments of Advo, Inc. in Response to Advance Notice of Proposed Rulemaking	May 7, 2007
	Comments of Advo, Inc. in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	June 18, 2007
	Reply Comments of Advo, Inc. in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	July 3, 2007
Akerman Senterfitt Wickwire Gavin	Submission of Comments	April 2, 2007
Alliance of Nonprofit Mailers, National Association of Presort Mailers and National Postal Policy Council (ANM-NAPM-NPPC)	Comments of Alliance of Nonprofit Mailers, National Association of Presort Mailers and National Postal Policy Council on Advance Notice of Proposed Rulemaking	April 6, 2007
	Reply Comments of Alliance of Nonprofit Mailers, National Association of Presort Mailers and National Postal Policy Council on Advance Notice of Proposed Rulemaking	May 7, 2007
Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. (ANM-MPA)	Comments of Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. on Advance Notice of Proposed Rulemaking	April 6, 2007
	Reply Comments of Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. on Advance Notice of Proposed Rulemaking	May 7, 2007

PARTICIPANT	TITLE	FILING DATE
<i>ANM-MPA cont'd.</i>	Initial Comments of Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. on Further Advance Notice of Proposed Rulemaking (Order No. 15)	June 18, 2007
	Reply Comments of Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. on Further Advance Notice of Proposed Rulemaking (Order No. 15)	July 3, 2007
Amazon.com	Statement of Paul Misener, Vice President for Global Public Policy on Behalf of Amazon.com at Wilmington, Delaware Field Hearing on July 9, 2007	July 9, 2007
American Business Media (ABM)	Initial Comments of American Business Media	April 6, 2007
American Business Media, Greeting Card Association, and Newspaper Association of America (ABM-GCA-NAA)	Joint Comments of American Business Media, Greeting Card Association, and Newspaper Association of America With Respect to the Complaint Process	April 6, 2007
American Business Media, Greeting Card Association, Newspaper Association of America, and National Newspaper Association (ABM-GCA-NAA-NNA)	Joint Reply Comments of American Business Media, Greeting Card Association, Newspaper Association of America, and National Newspaper Association With Respect to the Complaint Process	May 7, 2007
American Postal Workers Union, AFL-CIO (APWU)	Initial Comments of the American Postal Workers Union, AFL-CIO, in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	April 6, 2007
	Reply Comments of the American Postal Workers Union, AFL-CIO	May 7, 2007
	Initial Comments of the American Postal Workers Union, AFL-CIO, in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	June 18, 2007

PARTICIPANT	TITLE	FILING DATE
<i>APWU cont'd.</i>	Reply Comments of the American Postal Workers Union, AFL-CIO, in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	July 3, 2007
Association for Postal Commerce (PostCom)	Initial Comments of PostCom in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	April 6, 2007
	Reply Comments of the Association for Postal Commerce	May 7, 2007
	Comments of PostCom in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	June 18, 2007
	Joint Comments on OCA Positions	July 3, 2007
	Reply Comments of PostCom in Response to Second Advance Notice of Proposed Rulemaking	July 3, 2007
Association of Priority Mail Users, Inc. (APMU)	Association of Priority Mail Users, Inc. Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 2	April 6, 2007
	Association of Priority Mail Users, Inc. Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 15	June 18, 2007
	Association of Priority Mail Users, Inc. Reply Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 15	July 3, 2007
Senators Collins and Carper	PRC Comments from Senators Collins and Carper	April 11, 2007
DigiStamp, Inc.	Comments of DigiStamp	April 2, 2007

PARTICIPANT	TITLE	FILING DATE
Direct Marketing Association, Inc. (DMA)	Direct Marketing Association, Inc. Initial Comments Pursuant to PRC Order No. 2	April 6, 2007
	Direct Marketing Association, Inc. Reply Comments Pursuant to PRC Order No. 2	May 7, 2007
	Direct Marketing Association, Inc. Reply Comments Pursuant to PRC Order No. 15	July 3, 2007
Discover Financial Services LLC (DFS)	Reply Comments of Discover Financial Services LLC	May 7, 2007
	Further Comments of DFS Services LLC	July 16, 2007
DST Systems, Inc., DST Output, Inc. and DST Mailing Service, Inc.	Statement of Mury Salls on Behalf of DST Systems, Inc., DST Output, Inc. and DST Mailing Service, Inc., at Kansas City Field Hearing June 22, 2007	June 26, 2007
Federal Express Corporation (FedEx)	Comments of Federal Express Corporation	April 5, 2007
Greeting Card Association (GCA)	Comments of the Greeting Card Association in Response to Advance Notice of Proposed Rulemaking	April 6, 2007
	Reply Comments of the Greeting Card Association	May 7, 2007
	Comments of the Greeting Card Association in Response to Second Advance Notice of Proposed Rulemaking	June 18, 2007
	Reply Comments of the Greeting Card Association in Response to Second Advance Notice of Proposed Rulemaking	July 3, 2007
Hallmark Cards, Inc.	Statement of Don Hall, Jr., President and CEO, Hallmark Cards, Inc. at Kansas City, Missouri Field Hearing, June 22, 2007	June 26, 2007
International Mailers' Advisory Group	Comments on Behalf of the International Mailers' Advisory Group	April 6, 2007
JP Morgan Chase & Co.	Statement of Daniel C. Emens on Behalf of JP Morgan Chase & Co. at Wilmington, Delaware Field Hearing on July 9, 2007	July 9, 2007

PARTICIPANT	TITLE	FILING DATE
Jon Mulford Associates	Comments of Jonathan Mulford on Behalf of John Mulford Associates Regarding Docket No. RM2007-1	March 14, 2007
Los Angeles Times	Statement of David D. Hiller, Publisher, Los Angeles Times at Los Angeles Field Hearing on June 28, 2007	June 28, 2007
Mail Order Association of America (MOAA)	Comments of Mail Order Association of America	April 6, 2007
	Reply Comments of Mail Order Association of America	May 7, 2007
	Response of the Mail Order Association of America to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	June 18, 2007
	Reply Comments of Mail Order Association of America to Comments Filed in Response to Second Notice of Proposed Rulemaking	July 3, 2007
Major Mailers Association (MMA)	Initial Comments of Major Mailers Association	June 18, 2007
The McGraw-Hill Companies, Inc.	Reply Comments of The McGraw-Hill Companies, Inc. Pursuant to Order No. 2	May 7, 2007
McBride, Ken	Statement of Ken McBride at Los Angeles Field Hearing on June 28, 2007	June 28, 2007
	Reply Comments of The McGraw-Hill Companies, Inc. in Response to Supplemental Comments of the United States Postal Service on the Classification Process	July 6, 2007
Meredith Corporation	Statement of Randy Stumbo, Director of Distribution and Postal Affairs for Meredith Corporation, at Kansas City, Missouri Field Hearing on June 22, 2007	June 26, 2007
The Nation	Comments of The Nation on Docket RM2007-1	June 19, 2007

PARTICIPANT	TITLE	FILING DATE
National Association of Homebuilders	Comments of National Association of Home Builders	June 18, 2007
National Association of Letter Carriers (NALC)	National Association of Letter Carriers' Response to Other Parties' Comments on Proposed Rulemaking Concerning Exigency Clause and Future Complaint Procedures	May 7, 2007
National Association of Presort Mailers (NAPM)	Comments of the National Association of Presort Mailers	June 18, 2007
National Catholic Development Conference	Statement of Sr. Georgette Lehmuth, OSF on Behalf of National Catholic Development Conference at Wilmington, Delaware Field Hearing on July 9, 2007	July 9, 2007
National Newspaper Association (NNA)	Comments of the National Newspaper Association (NNA)	April 6, 2007
National Newspaper Association (NNA) and Missouri Press Association	Statement of Dave Berry, Vice President, Community Newspaper Publishers, Inc. and Publisher of the Bolivar Herald-Free Press, Bolivar, Missouri on Behalf of the NNA and Missouri Press Association, at Kansas City Field Hearing June 22, 2007	June 26, 2007
National Postal Policy Council (NPPC)	Comments of National Postal Policy Council in Response to Further Advance Notice of Proposed Rulemaking	June 18, 2007
National Postal Policy Council and National Association of Presort Mailers (NPPC-NAPM)	Reply Comments of National Postal Policy Council and National Association of Presort Mailers in Response to Further Advance Notice of Proposed Rulemaking	July 3, 2007
Newgistics, Inc.	Initial Comments of Newgistics, Inc.	April 6, 2007
Newspaper Association of America (NAA)	Comments of the Newspaper Association of America	March 30, 2007
	Reply Comments of the Newspaper Association of America	May 7, 2007

PARTICIPANT	TITLE	FILING DATE
<i>NAA cont'd.</i>	Comments of the Newspaper Association of America on Second Advance Notice of Proposed Rulemaking	June 18, 2007
	Reply Comments of the Newspaper Association of America on Second Advance Notice of Proposed Rulemaking	July 3, 2007
Office of the Consumer Advocate (OCA)	OCA Comments in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	April 6, 2007
	OCA Comments in Reply to Those Filed in Response to Order No. 2	May 7, 2007
	Office of the Consumer Advocate Comments in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	June 18, 2007
	Office of the Consumer Advocate Reply Comments in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	July 3, 2007
	Office of the Consumer Advocate Comments in Response to Supplemental Comments of the United States Postal Service on the Classification Process	July 3, 2007
Parcel Shippers Association (PSA)	Comments of the Parcel Shippers Association	April 6, 2007
	Reply Comments of Parcel Shippers Association to Comments of United Parcel Service	May 7, 2007
	Errata to Reply Comments of Parcel Shippers Association to Comments of United Parcel Service	May 8, 2007

PARTICIPANT	TITLE	FILING DATE
<i>PSA cont'd.</i>	Reply Comments of Parcel Shippers Association to Comments of United Parcel Service and Comments of the Office of the Consumer Advocate [Revised Filing]	May 8, 2007
	Response of the Parcel Shippers Association to Second Advance Notice of Proposed Rulemaking	June 18, 2007
	Reply of Parcel Shippers Association to Comments Filed in Response to Second Notice of Proposed Rulemaking	July 3, 2007
Pepperdine University	Statement of John Carper on Behalf of Pepperdine University at Los Angeles Field Hearing on June 28, 2007	June 28, 2007
Pitney Bowes Inc.	Initial Comments of John C. Panzar on Behalf of Pitney Bowes Inc. in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	April 6, 2007
	Initial Comments of Pitney Bowes Inc. in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	April 6, 2007
	Reply Comments of Pitney Bowes Inc. in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	May 7, 2007
	Initial Comments of Pitney Bowes Inc. in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	June 18, 2007
	Reply Comments of Pitney Bowes Inc. in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	July 3, 2007

PARTICIPANT	TITLE	FILING DATE
<i>Pitney Bowes cont'd.</i>	Statement of Michael Monahan, Executive Vice President and President, Mailing Solutions and Services, on Behalf of Pitney Bowes Inc. at Wilmington, Delaware Field Hearing on July 9, 2007	July 9, 2007
Sprint-Nextel	Initial Comments of Sprint-Nextel	April 6, 2007
Stamps.com	Submission of Comments of Stamps.com	April 6, 2007
	Reply Comments of Stamps.com	May 7, 2007
	Stamps.com Comments	June 18, 2007
Tension Envelope Corporation	Statement of William S. Berkley, President and CEO, Tension Envelope Corporation at the Kansas City, Missouri Field Hearings on June 22, 2007	June 26, 2007
Time Warner Inc.	Initial Comments of Time Warner Inc. in Response to Commission Order No. 2	April 6, 2007
	Reply Comments of Time Warner Inc. to Initial Comments in Response to Commission Order No. 2	May 7, 2007
	Comments of Time Warner Inc. In Response to Commission Order No. 15	June 18, 2007
United Parcel Service (UPS)	Comments of United Parcel Service in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	April 6, 2007
	Reply Comments of United Parcel Service in Response to Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	May 7, 2007
	Comments of United Parcel Service in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	June 18, 2007

PARTICIPANT	TITLE	FILING DATE
<i>UPS cont'd.</i>	Reply Comments of United Parcel Service in Response to Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking	July 3, 2007
United States Postal Service (USPS)	Initial Comments of the United States Postal Service	April 6, 2007
	Reply Comments of the United States Postal Service	May 7, 2007
	Initial Comments of the United States Postal Service on the Second Advance Notice of Proposed Rulemaking	June 18, 2007
	Supplemental Comments of the United States Postal Service on the Classification Process	June 19, 2007
	Reply Comments of the United States Postal Service on the Second Advance Notice of Proposed Rulemaking	July 3, 2007
Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. (Valpak)	Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 2	April 6, 2007
	Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. Reply Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 2	May 7, 2007
	Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 15	June 18, 2007

PARTICIPANT	TITLE	FILING DATE
<i>Valpak cont'd.</i>	Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. Reply Comments on Regulations Establishing a System of Ratemaking in Response to Commission Order No. 15	July 3, 2007
Williams-Sonoma Inc.	Statement of James West, Director, Postal and Government Affairs, on Behalf of Williams-Sonoma Inc. at Los Angeles Field Hearing on June 28, 2007	June 28, 2007
YourAuctionCompany.com	Statement of Adam and Wendy Leidhecker, Chief Executive Officers, on Behalf of YourAuctionCompany.com at Wilmington, Delaware Field Hearing on July 9, 2007	July 9, 2007

