

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

COMPETITIVE PRODUCT PRICES
GLOBAL PLUS
NEGOTIATED SERVICES AGREEMENTS

Docket Nos.
CP2008-8
CP2008-9
CP2008-10

**UNITED STATES POSTAL SERVICE RESPONSE TO ORDER NO. 81 AND NOTICE
OF FILING INFORMATION RESPONSIVE TO PART 3020 OF THE COMMISSION'S
RULES OF PRACTICE AND PROCEDURE**
(June 13, 2008)

On June 6, 2008, the Commission issued Order No. 81, giving notice of the following actions by the Postal Service: (i) the filing under seal of a Governors' Decision setting forth price ranges for Global Plus contracts and modifying previously proposed descriptive language about such contracts in the Mail Classification Schedule (MCS), and (ii) the filing under seal of two Global Plus contracts with customers.¹ The Commission directed the Postal Service to (i) identify and list any contracts currently in existence that would no longer qualify as Global Plus contracts under the changed classification language proposed by the Postal Service, along with those contracts' expiration dates; (ii) provide a detailed explanation as to why Global Plus contracts'

¹ While the Postal Service notice of the Governors' Global Plus Decision cited 39 C.F.R. §§ 3015.5 (Regulation of Rates for Competitive Products, Rate or class not of general applicability) and 3020.90 (Requests Initiated by the Postal Service to Change the Mail Classification Schedule), its notice of the Global Plus customer agreements cited only the former of these provisions. Order No. 81 concludes that the Global Plus customer agreements will be classified as new products. Order No. 81 determines that the Commission will consider the Global Plus contracts as if they had been filed pursuant to 39 C.F.R. 3020, Subpart B (Requests Initiated by the Postal Service to Modify Product Lists Described within the Mail Classification Schedule), making the Commission's review of the dockets pursuant to Rule 3020.34 (Review). Having exercised its discretion to construe the two proceedings collectively as supporting a request to modify product lists, the Commission invited the Postal Service to supplement the materials previously filed.

expiration dates, without disclosing the identity of the customer, should not be made publicly available; (iii) address the reasons why the entire Governors' Decision is considered to be highly confidential or otherwise entitled to be filed under seal; and (iv) address why, under the Global Plus contracts filed in CP2008-9 and CP2008-10, mailers would pay discounted rates prior to necessary regulatory approval for such rates, subject to subsequent collection of the full rate if regulatory approval is not obtained. In addition to responding to these points, the Postal Service hereby offers further detail about why the Global Plus contracts filed in CP2008-9 and CP2008-10 share similar cost and market characteristics and therefore should be placed within the shell classification as a single product.

I. Functional Equivalency of Global Plus Contracts

In Order No. 81, the Commission considered the Governors' Decision as establishing, in essence, a "shell classification" for functionally equivalent Global Plus contracts, but it declined to classify the specific Global Plus agreements filed in CP2008-9 and CP2008-10 within that product classification. In Order No. 43, the Commission acknowledged that it might be appropriate to group functionally equivalent negotiated service agreements (NSAs) as a single product.² In Order No. 81, the Commission repeated this acknowledgement insofar as functionally equivalent NSAs exhibit similar cost and market characteristics. With their Decision, the Governors have established a pricing formula and classification that ensures that each contract meets the criteria of 39 U.S.C. § 3633 and the regulations promulgated thereunder. Therefore, the costs of each contract meet a common description. In addition, the language proposed for Section 2610.5 of the MCS requires that each Global Plus contract must

² PRC Order No. 43, at 57-58, 64, 75.

cover its attributable costs. All Global Plus contracts meeting the Governors' criteria will necessarily exhibit similar cost and market characteristics; therefore, all Global Plus contracts will be functionally equivalent and may be classified according to the general product description.³ The Postal Service specifically requests that the contracts filed in Docket Nos. CP2008-9 and CP2008-10 be treated as complying with the terms of the shell classification set forth by the Governors' Decision and should be treated as modifications to the Global Plus product, not as individual products, for classification purposes.

In a concrete sense as well, Global Plus contracts share the same cost and market characteristics. First, both of the customers for the Global Plus contracts filed in CP2008-9 and CP2008-10 are large Postal Qualified Wholesalers (PQWs) with a common constituency of end users, which treats their service offerings as interchangeable.⁴ The Postal Service anticipates that many, if not all, customers for future Global Plus contracts will operate on similar terms. Further, these two Global Plus contracts cover the same underlying services. Any difference in the level of volume commitment between these or other Global Plus contracts does not alter this equivalency, because the total costs associated with Global Plus contracts are volume-variable. Both contracts further include a revenue commitment as a precondition for the prescribed discounts. The revenue commitment covers the same set of products, namely, International; Surface Airlift (ISAL), International Priority Airlift (IPA), Express Mail International (EMI), Priority Mail International (PMI), Global Bulk Economy (GBE)

³ The certification that accompanies the filing of the Global Plus contracts in these proceedings effectively fits those Global Plus contracts within the Governors' shell classification.

⁴ The supporting justification appended hereto as Attachment A expands further on the common market characteristics of Global Plus contracts in general and the particular Global Plus contracts filed in these proceedings.

and Global Direct (GD). Because both agreements incorporate the same cost attributes and methodology, the relevant characteristics are similar, if not the same, for these two Global Plus contracts and for all others that would fit within the proposed MCS description.

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

At the Commission's invitation, the Postal Service is providing additional supporting materials under Part 3020, subpart B of the Rules of Practice and Procedure.⁵ Attachment A is the supporting statement of Frank Cebello, Executive Director, Global Business Management, under Rule 3020.32. With this filing, the Postal Service provides further support for the addition of the shell classification of Global Plus contracts, as described in language proposed by the Postal Service for inclusion in section 2610.5 of the MCS, to the competitive products list for products not of general applicability. Mr. Cebello's statement further articulates the impact of adding the Global Plus contracts filed in this docket to the competitive products list. If the Global Plus shell classification is added to the competitive products list, then the Global Plus contracts filed in this docket would fit its criteria and would belong to the functionally equivalent grouping defined thereby.

The Postal Service did not understand that filing of the shell classification under Part 3020, Subpart B of the Commission's Procedure was necessary in view of the MCS language that the Postal Service submitted to the Commission in November

⁵ In conformance with Rule 3020.31(b) and (f) of the Commission's Rules of Practice and Procedure, the Postal Service has provided copies of the relevant Governors' Decision, under seal, and applicable MCS section, with proposed changes, in previous filings on this docket. Mr. Cebello's statement, appended hereto as Attachment A, serves as the supporting justification required by Rule 3020.31(e).

2007.⁶ The Postal Service believes that with this classification and the filing of the supplemental material, the classification review can be streamlined. Under 39 U.S.C. § 3642(b), the only criteria for such review are whether the product qualifies as market-dominant, whether it is excluded from the postal monopoly, and whether the proposed classification reflects certain market considerations. Each of these criteria has been addressed in this case. With its Order No. 43, the Commission has already assigned all NSAs concerning outbound international mail to the competitive category⁷, and all Global Plus contracts, regardless of whether they may be classified as a single product or individually, are NSAs concerning outbound international mail. Therefore, there is no further need to ponder whether Global Plus contracts are market dominant or, by dint thereof, covered within the postal monopoly. To the extent that the Commission believes the additional considerations listed in 39 U.S.C. § 3642(b)(3) have not yet been satisfied, the Postal Service is filing Mr. Cebello's statement in response to Order No. 81. Because all of 39 U.S.C. § 3642's criteria for classification have been met, the Postal Service respectfully urges the Commission to act promptly in fulfilling its statutory function by adding these products to the competitive product list as requested. It is in the Postal Service and the Commission's common interest to avoid the creation of uncertainty among customers as to the effective dates of instruments to which they have agreed, and to resolve the appropriate classification for these products.

III. Identification of Existing Global Plus Contracts

In Order No. 81, the Commission directed the Postal Service to identify and list any contracts currently in existence that would no longer qualify as Global Plus

⁶ United States Postal Service Submission of Additional Mail Classification Schedule Information in Response to Order No. 43 (Nov. 20, 2007).

⁷ PRC Order No. 43, App. A, at 9, 11.

contracts under the classification changes supplied by the Postal Service, along with those contracts' expiration dates. These changes simply reflect the recent addition of published price incentives for EMI and PMI⁸, which to some degree overtake the need for individualized agreements, and shape-based pricing criteria for First-Class Mail International.⁹ No existing Global Plus contracts fail to fit within the revised MCS language that the Postal Service has proposed.

IV. Confidentiality

In Order No. 81, the Commission directed the Postal Service to provide a detailed justification for why it believes that Global Plus contracts' expiration dates, without disclosing the customers' identities, should not be made publicly available. The Postal Service has no objection to the listing of expiration dates for Global Plus contracts, because it does not regard this information, considered in isolation, to be commercially sensitive. The Postal Service notes, however, that the expiration date for both of the new Global Plus contracts is July 1, 2009. Therefore, the Postal Service recommends use of docket numbers or some other unique identifier to distinguish individual Global Plus contracts.

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

⁸ See PRC Order No. 70, at 18-20.

⁹ See PRC Order No. 66, at 20.

The Commission also requests that the Postal Service address the reasons why the entire Governors' Decision should be treated as highly confidential and filed under seal. The Governors' Decisions for competitive, outbound international NSAs that have been issued to date¹⁰ contain sensitive commercial information that should not be publicly disclosed. These Decisions authorize management to execute instruments containing prices that fall within a range determined by a formula that the Governors have established as producing results that comply with the criteria of 39 U.S.C. § 3633(a)(1)-(3).¹¹ Public disclosure of these formulas and related information would seriously undermine postal management's leverage in negotiations with customers.¹² This pricing information is clearly of a commercial nature, and the Postal Service is aware of no competitor or private company of comparable size and scope that releases such information to the public. Hence, specifics about price calculation in the Governors' Decision continue to merit confidential treatment. To aid the Commission and to expedite this proceeding, the Postal Service will file under cover of a separate notice a redacted version of the Governors' Decision filed in Docket No. CP2008-8 that is suitable for public disclosure.

IV. Retroactivity

The Commission questions certain provisions in the two Global Plus contracts filed in CP2008-9 and CP2008-10. The Commission notes that under those agreements, customers would receive certain price incentives prior to regulatory approval for such rates, subject to subsequent collection of the difference in the full

¹⁰ That is, the Governors' Decisions filed in CP2008-4, CP2008-6, and CP2008-8.

¹¹ Under the approach taken by the Governors, any agreements executed by management would still require certification and filing with the Commission.

¹² Even disclosure of the price range's upper bound would give prospective customers tactical information about the range within which the Postal Service can negotiate.

price if regulatory approval is not obtained. The Commission questions these provisions on grounds that the Postal Accountability and Enhancement Act (PAEA) “does not appear to contemplate this arrangement for new products.”¹³

The provisions in question provide that until July 1, 2008, the customers may avail themselves of certain prices effective as of April 30, 2008. These prices happen to be the same as those in effect under instruments executed with the same customers under the Postal Service’s previous statutory authority. These prices were made available so that the customers could continue mailing while the Commission and the Postal Service continue their collaborative approach to navigating from the former Postal Reorganization Act to the PAEA. These new Global Plus contracts assume that new, higher prices will be in effect by July 1, 2008, if the contracts are approved before that time. If the contracts are not approved by July 1, 2008, the customers become liable for the difference in Postal Service revenue between the prices that took effect on May 1, 2008, and the applicable published prices. The product finance calculations in the work papers filed with each agreement take account of these potentialities, including in the cost coverage evaluation the lower prices in effect between May 1, 2008 and July 1, 2008.

The retroactivity provisions are not inconsistent with any statutory or regulatory authority. If anything, pragmatic factors weigh strongly against construing the statute to forestall the reimbursement provisions in the instant Global Plus contracts. The purpose of these provisions is to maintain stability in these customer relationships and avoid an interruption in service. They are intended to mitigate the risk to the Postal Service that the new Global Plus contracts might not become effective, since the mailer

¹³ PRC Order No. 81, at 4.

becomes liable for the difference between the prices initially paid and the analogous published prices currently in effect. In effect, this conditional deficiency requires the mailer to bear responsibility for payment of the published prices until such time as the agreement is approved. Neither applicable statutes, the Domestic Mail Classification Schedule (DMCS), nor the new MCS language proposed by the Postal Service requires prepayment of postage for international mail services. Therefore, the Postal Service is not barred from permitting or requiring international mail customers to assume conditional revenue deficiencies.

Neither has the Postal Service somehow bypassed any regulatory approval processes required under the Postal Accountability and Enhancement Act. Ultimately, the retroactivity provisions of these Global Plus contracts do not give effect to new rates before the Commission has had an opportunity to review the agreements. Since the mailer bears responsibility for payment of the published rates in the event of non-approval, the Postal Service has done nothing more than extend credit to the customer in the interim. The provisions thus provide for a reasonable and practical solution for mailers with existing agreements to continue their commercial relationship with the Postal Service while the Global Plus contracts undergo review. It would be contrary to sound business judgment to have let the agreements lapse without a practical solution to bridge the gap. The provisions are carefully crafted and limited in scope to existing Global Plus customers, both of which have a proven business relationship with the Postal Service and present little risk of default. Because these customers themselves serve a very substantial customer base, it would have been highly disruptive to the mailing industry if the Postal Service had been unable to offer a solution to maintain the

status quo during this period of uncertainty as to the new regulatory approval processes and the availability of new prices.

Respectfully submitted,

UNITED STATES POSTAL SERVICE
By its attorneys:

Anthony F. Alverno
Chief Counsel, Global Business

Jacob D. Howley

475 L'Enfant Plaza, S.W.
Washington, D.C. 20260-1137
(202) 268-8917; Fax -6187
jacob.d.howley@usps.gov
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Statement of Supporting Justification

I, Frank Cebello, Executive Director, Global Business Management, am sponsoring this request that the Commission add the shell classification for Global Plus contracts, filed in Docket No. CP2008-8, or the Global Plus Contracts filed in Docket Nos. CP2008-9 and CP2008-10 to the competitive products list for prices not of general applicability. This statement supports the Postal Service's request by providing the information required by each applicable subsection of 39 C.F.R. § 3020.32. I attest to the accuracy of the information contained herein.

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

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

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

Not applicable. The Postal Service is proposing that the shell classification for Global Plus Contracts be a competitive product or, alternatively, that the Global Plus Contracts filed in CP2008-9 and CP2008-10 and offered in accordance with that shell classification be added to the competitive products list.

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

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

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

When negotiating Global Plus Contracts, the Postal Service's bargaining position is constrained by the existence of other shippers who can provide services similar to the Postal Service's. As such, the market precludes the Postal Service from taking unilateral action to increase prices or decrease service. Global Plus Contracts concern volume-based incentives for the tendering of large volumes of International Priority Airmail (IPA), International Surface Air Lift (ISAL), Global Bulk Economy (GBE), Global Direct (GD), Express Mail International (EMI), and/or Priority Mail International (PMI), all of which have been classified as competitive by virtue of their exclusion from the letter

monopoly, as well as the significant level of competition in their respective markets. As with each of the respective underlying products in general, the Postal Service may not decrease quality or output without risking the loss of business to large competitors that offer international express and package delivery services. The relevant market also does not allow the Postal Service to raise prices or offer prices substantially above costs; rather, the contracts are premised on prices that provide sufficient incentive for customers to ship specified volumes with the Postal Service rather than a competitor. If the Postal Service were to raise these prices, it risks losing these customers to a private competitor in the international shipping industry.

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

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

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

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

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

The customers for these Global Plus Contracts are Postal Qualified Wholesalers (PQWs) and other large businesses offer mailing services to end users for shipping articles via IPA, ISAL, GBE, GD, EMI, and/or PMI. These customers have previously entered Global Plus Contracts with the Postal Service pursuant to the latter's former authority, and they find the arrangement sufficiently attractive to merit renewal. The Postal Service has concluded similar arrangements with other businesses of comparable size, which indicates that the relevant segment of postal customers in general, as well as their end users, finds this type of product to be advantageous as against similar products offered by the Postal Service's competitors. Customers are aware that competitive services are provided by such private enterprises. However, no specific data are available to the Postal Service on Global Plus Contract customer views regarding the regulatory classification of these Global Plus Contracts as market dominant or competitive.

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

The market for international express and package delivery services comparable to IPA, ISAL, GBE, GD, EMI, and PMI is highly competitive. Therefore, a shell classification for Global Plus Contracts will likely have little, if any, impact upon small business concerns. Large shipping companies serve this market, particularly with respect to the volume customers represented by this and other Global Plus Contracts; the Postal Service is unaware of any small business concerns that could offer comparable service for these volumes.

In addition, these Global Plus Contracts will form the basis for the PQW customers' service offerings to their own end users, which include small businesses. By offering the prices in these Global Plus Contracts, the Postal Service is giving small businesses an additional option for shipping articles internationally, beyond the services offered by private competitors. Thus, the net impact on small businesses is positive, because of the absence of negative impact on small business competitors and the positive impact on the small businesses who will use the services that the Global Plus customers can offer them under these contracts.

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

The customer eligibility criteria for Global Plus Contracts concluded under the Postal Service's previous authority included lower capacity thresholds for EMI and PMI, along the lines of the Postal Service's initially proposed Mail Classification Schedule (MCS) language. The Postal Service recently published EMI and PMI price incentives for smaller customers, some of whom might have met the previous Global Plus capacity thresholds. Because the capacity to meet the EMI and PMI threshold previously included in the proposed MCS language would now entitle a customer to published prices, the Postal Service proposes to modify the eligibility criteria for the Global Plus Contract product classification to include EMI and PMI with the other underlying products in the contract's overall capacity thresholds. In addition, the Postal Service is offering changes to the previously proposed MCS language that concern shape-based criteria for IPA

and ISAL, in accordance with the recent advent of shape-based pricing for First-Class Mail International.