

ORDER NO. 84

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

Before Commissioners:

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

Competitive Product Prices
Express Mail International
Bilateral/Multilateral Agreements

Docket No. CP2008-7

ORDER CONCERNING THE CHINA POST GROUP
INBOUND EMS AGREEMENT

(June 27, 2008)

On May 20, 2008, the Postal Service filed notice, pursuant to 39 U.S.C. 3632(b)(3) and 39 CFR 3015.5, of the Governors' decision establishing prices for competitive products not of general applicability for Inbound Express Mail International (EMS).¹ The Postal Service's filing, docketed as Docket No. CP2008-6, includes supporting material, including the Governors' decision, filed under seal. Concurrently, the Postal Service filed notice, pursuant to 39 CFR 3015.5, of a specific negotiated

¹ Notice of United States Postal Service of Governors' Decision on Inbound Prices Under Express Mail International (EMS) Bilateral/Multilateral Agreements, May 20, 2008 (Notice).

service agreement covering Inbound EMS prices.² This filing, docketed as Docket No. CP2008-7, includes the contract and supporting materials filed under seal.

On June 3, 2008, the Commission issued Order No. 79, which determined that Docket No. CP2008-6 establishes, in essence, a shell classification, while Docket No. CP2008-7 is a specific agreement negotiated pursuant to the conditions of the shell classification. Given this interrelationship, the Commission consolidated the proceedings for purposes of review under Docket No. CP2008-7.³

In Order No. 79, the Commission also reiterated its position that each negotiated service agreement will initially be classified as a separate product, while acknowledging the possibility of grouping functionally equivalent agreements as a single product if they exhibit similar cost and market characteristics. *Id.* at 2-3. This, in effect, invoked the filing and review requirements of 39 CFR part 3020, subpart B, along with the requirements of rule 3015.5 for competitive products.

On June 10, 2008, the Postal Service filed material responsive to questions posed in Order No. 79, and material responsive to 39 CFR part 3020, subpart B.⁴ The material responsive to 39 CFR part 3020, subpart B included a statement of supporting justification sponsored by Pranab Shah. See Postal Service Response, Attachment A.

The Commission previously proposed, at a minimum, identifying each international mail agreement with foreign posts involving competitive products (both in the Mail Classification Schedule and in other documents generated by the Commission) by the name(s) of the foreign post(s), the mail product(s) involved, and the agreement's expiration date. Order No. 79 at 3-4. In this instance, the Postal Service did not object to this proposal. Postal Service Response at 3.

² Notice of United States Postal Service of Filing an Agreement for Inbound Express Mail International (EMS) Prices, May 20, 2008 (Pricing Notice).

³ PRC Order No. 79, Notice and Order Concerning Prices Under Express Mail International Bilateral/Multilateral Agreements, June 3, 2008 at 2 (Order No. 79).

⁴ United States Postal Service Response to Order No. 79 and Notice of Filing Information Responsive to Part 3020 of the Commission's Rules of Practice and Procedure, June 10, 2008 (Postal Service Response).

The Commission also noted that it has made no determination as to whether the portions of the agreement in Docket No. CP2008-7 that relate to outbound mail are subject to its review. Order No. 79 at 3. The Postal Service reiterated its position that an “outbound EMS agreement with China Post Group would no more need to be classified as a product or otherwise subjected to Commission review than would an agreement to purchase trucking services from highway contractors or to purchase air transportation from air carriers.” Postal Service Response at 3.

Order No. 79 also provided an opportunity for public comment on the Postal Service’s proposals. Comments were received from the Public Representative (an employee of the Commission assigned to represent the interests of the general public) and United Parcel Service.⁵ Neither the Public Representative nor United Parcel Service expressed opposition to the China Post Group agreement.

The Public Representative concludes that the China Post Group agreement “complies with the legal requirements for cost coverage and contribution to the Postal Service’s institutional costs.” Public Representative Comments at 4. United Parcel Service supports the Commission’s conclusion that this initial agreement be treated as a new product. UPS Comments at 2. It also suggests that because private carriers face more onerous customs and brokerage requirements than the Postal Service, the market for international package delivery and expedited services is less competitive than is often assumed. *Id.* Both the Public Representative and United Parcel Service discuss issues encompassing the provision of materials under seal. Public Representative Comments at 2-3; UPS Comments at 1.

Commission analysis. The statutory responsibility of the Commission, in this instance, is to assign a new product to either the market dominant list or the competitive product list. 39 U.S.C. 3642. As part of this responsibility, the Commission also will

⁵ Public Representative Comments in Response to United States Postal Service Notice of Negotiated Service Agreement (NSA) for Inbound Express Mail International (EMS) with China Post (Public Representative Comments); Comments of United Parcel Service in Response to Order Concerning Prices Under Express Mail International Bilateral/Multilateral Agreements (UPS Comments); both filed June 16, 2008.

preliminarily review the proposal for compliance with the requirements of the Postal Accountability and Enhancement Act (PAEA) of 2006. For proposed competitive products, this includes review of the provisions applicable to rates for competitive products. 39 U.S.C. 3633.

The Postal Service contends that adding the shell classification as a product will improve the Postal Service's competitive posture. It argues that this can be accomplished while allowing verification that each agreement covers attributable costs, does not result in subsidization of competitive products by market dominant products, and increases contribution from competitive products. Alternatively, adding the individual agreement as a product also will improve the competitive posture of the Postal Service, but to a lesser degree. Postal Service Response, Attachment A, at 2.

The Commission has reviewed the financial analysis provided under seal that accompanies the agreement and finds that the China Post Group agreement should cover its attributable costs (39 U.S.C. 3633(a)(2)), should not lead to the subsidization of competitive products by market dominant products (39 U.S.C. 3633(a)(1)), and should have a positive effect on the collective competitive products ability to provide their appropriate share of institutional costs (39 U.S.C. 3633(a)(3)).⁶ Thus, a preliminary review of the agreement indicates that it comports with the provisions applicable to rates for competitive products.

In determining whether to assign the China Post Group agreement as a product to the market dominant product list or the competitive product list the Commission must consider whether:

...the Postal Service exercises sufficient market power that it can effectively set the price of such product substantially above costs, raise

⁶ The Commission notes that the Postal Service derived inflation adjustment factors from two point estimates for a 21-month period, September 2007 to May 2009, rather than June 2008 to May 2009, which coincides with the duration of the bilateral agreement. The Commission also notes that the estimate of the total unit cost of inbound Express Mail from China Post Group is based upon an estimate of the unit cost of domestic mail processing that represents an average of the domestic mail processing cost of inbound Express Mail from all countries rather than the average unit domestic mail processing cost for transition system countries. These observations did not have a significant impact on the overall analysis; however, the rationale for a 21-month period and the use of an average should be explained when filing future similar agreements.

prices significantly, decrease quality, or decrease output, without risk of losing a significant level of business to other firms offering similar products.

39 U.S.C. 3642(b)(1). If this is the case, the product will be categorized as market dominant. The competitive category of products shall consist of all other products.

The Commission is further required to consider the availability and nature of enterprises in the private sector engaged in the delivery of the product, the views of those that use the product, and the likely impact on small business concerns. 39 U.S.C. 3642(b)(3).

The Postal Service asserts that its bargaining position is constrained by the existence of other shippers who can provide similar services. Thus, the market precludes the Postal Service from taking unilateral action to increase prices or decrease service without the risk of losing volume to private companies in the international shipping industry. Postal Service Response, Appendix A at 2-3. The Postal Service contends that private consolidators and freight forwarders may offer international arrangements under similar conditions. *Id.* at 3. The Postal Service has no specific data on the views of those that use the products on the regulatory classification. *Id.* at 4. Finally, the Postal Service states that large shippers serve the market under consideration, and that there should be little impact upon small business other than adding an additional option for shipping articles to the United States. *Id.*

The Commission previously assigned Inbound International Expedited Services to the competitive product list.⁷ The Postal Service contends that the China Post Group agreement falls within the Inbound International Expedited Services heading. The Commission has not received public opposition to the proposed regulatory classification during the comment period. Having considered the statutory requirements, the argument put forth by the Postal Service, and the public comment, the Commission finds that the China Post Group agreement is appropriately categorized as a

⁷ PRC Order No. 43, Order Establishing Ratemaking Regulations for Market Dominant and Competitive Products, October 29, 2008, ¶ 3019.

competitive product and should be added to the competitive product list. The revisions to the competitive product list are shown below the signature of this Order, and shall become effective upon publication in the *Federal Register*.

Mail Classification Schedule. The Postal Service previously proposed applicable draft Mail Classification Schedule language governing Inbound Express Mail International Services (EMS).⁸ Attachment A to the Governors' decision filed in Docket No. CP2008-6 repeats this language. These proposals suggest assigning the China Post Group agreement to the Express Mail, Inbound Express Mail International category. In Docket Nos. CP2008-4, CP2008-5, CP2008-8, CP2008-9, and CP2008-10, the Postal Service's draft Mail Classification Schedule language proposes to assign the associated agreements to the Negotiated Service Agreements, Outbound International category. The intent of the overall Negotiated Service Agreements category is to organize all negotiated agreements. Thus, the categorization in the instant docket does not appear to be consistent with the other proposals. The Commission invites the Postal Service to share its thoughts and concerns on development of a consistent approach to organizing competitive product negotiated agreements within the Mail Classification Schedule.

The Postal Service's proposed Mail Classification Schedule language indicates that other negotiated agreements may exist within Inbound Express Mail International: Bilateral Express Mail Service (EMS); EMS Cooperative Pay for Performance; Kahala Posts Group; European Parcel Group; and China Post Group. The Commission does not have specific information on the negotiated agreements for these products. The Postal Service shall provide the Commission with a list of ongoing agreement names, and expiration dates separated by product, along with a copy of each agreement.⁹ Providing this information will aid the Commission in understanding the Postal Service's

⁸ See United States Postal Service Submission of Additional Mail Classification Schedule Information in Response to Order No. 43, November 20, 2007.

⁹ See 39 U.S.C. 407(d)(2). Agreements that fall outside of the defined product models also are to be provided.

product offerings, and enhance the transparency of the Postal Service to the mailing community.

Updating the Mail Classification Schedule. The China Post Group agreement contains provisions for early termination and automatic renewal of the agreement. The Postal Service shall notify the Commission of an early termination no later than the date of termination. The Commission then will remove the agreement from the Mail Classification Schedule at the earliest possible opportunity. The Postal Service also shall notify the Commission of an automatic renewal of the agreement 15 days prior its occurrence. Otherwise, the Commission will assume that the contract has lapsed and remove the agreement from the Mail Classification Schedule without notice.

Additional agreements. As of now, the China Post Group agreement represented by Inbound International Expedited Services 1 (CP2008-7) in the competitive product list may be considered the same entity. In the future, the Postal Service may enter into other agreements substantially similar to the China Post Group agreement. When this occurs, Inbound International Expedited Services 1 (CP2008-7) will be considered the product and the included individual agreements will be treated as price categories under the product.¹⁰

If the Postal Service determines that it has entered into an agreement substantially equivalent to the China Post Group agreement with another country, it may file such an agreement using the abbreviated requirements provided by rule 3015.5. In each case, the individual agreement must be filed with the Commission, and each agreement must meet the requirements of 39 U.S.C. 3633. The Postal Service shall identify all significant differences between the new agreement and the pre-existing product group. Such differences would include terms and conditions that impose new obligations or new requirements on any party to the agreement. The Commission will verify whether or not the second agreement is in fact substantially equivalent. Agreements that are not substantially equivalent will continue to have to meet the filing

¹⁰ This may require future modification of the China Post Group descriptive language.

requirements provided by 39 CFR part 3020, subpart B. If this approach proves too cumbersome, alternative approaches may be considered.

Confidentiality of information. The Commission is aware that the treatment of information as confidential is a sensitive issue. The Postal Service, the Public Representative, and United Parcel Service all express valid concerns that the Commission will address in the future on a broader level.

In this docket, the Commission will take a limited first step to add transparency and facilitate the process of reviewing future agreements of this style. The Commission has reviewed the Governor's decision supporting the request provided as required by rule 3020.31(b), and has determined that most of the document does not pose a risk of competitive harm if disclosed. In fact, the Postal Service disclosed similar information associated with Docket Nos. CP2008-8, CP2008-9, and CP2008-10. The Postal Service is directed to file a redacted version of the Governor's decision provided under seal in Docket No. CP2008-6.¹¹

It is Ordered:

1. The China Post Group agreement is added as a product not of general applicability to the competitive product list under Inbound International Expedited Services as Inbound International Expedited Services 1 (CP2008-7).
2. The Postal Service shall provide the Commission with suggestions regarding the development of a consistent approach to organizing competitive product negotiated agreements within the Mail Classification Schedule by July 23, 2008.

¹¹ The redacted version should be filed under Docket No. MC2008-7. The Commission anticipates the redacted version will be similar in nature to what the Postal Service provided associated with Docket Nos. CP2008-8, CP2008-9, and CP2008-10 on June 16, 2008.

3. The Postal Service shall file with the Commission a list of all ongoing Inbound International Expedited Services agreements and expiration dates separated by product, along with a copy of each agreement, by July 23, 2008.
4. The Postal Service shall file with the Commission a redacted version of the Governors' decision provided under seal in Docket No. CP2008-6 by July 23, 2008.
5. The Secretary shall arrange for publication of this Order in the *Federal Register*.

By the Commission.

Steven W. Williams
Secretary

CHANGE IN MAIL CLASSIFICATION SCHEDULE

The following material represents changes to the Product List codified at 39 CFR Appendix A to Subpart A of Part 3020—Mail Classification Schedule. These changes are in response to the Postal Service’s Docket No. CP2008-7 request. The bracketed text signifies that the text is new, and shall appear in addition to all other Mail Classification Schedule text.

PART B—COMPETITIVE PRODUCTS

2000 COMPETITIVE PRODUCT LIST

EXPRESS MAIL

Express Mail
Outbound International Expedited Services
Inbound International Expedited Services
[Inbound International Expedited Services 1 (CP2008-7)]

PRIORITY MAIL

Priority Mail
Outbound Priority Mail International
Inbound Air Parcel Post

PARCEL SELECT

PARCEL RETURN SERVICE

INTERNATIONAL

International Priority Airlift (IPA)
International Surface Airlift (ISAL)
International Direct Sacks—M-Bags
Global Customized Shipping Services
Inbound Surface Parcel Post (at non-UPU rates)
International Money Transfer Service
International Ancillary Services

NEGOTIATED SERVICE AGREEMENTS

Domestic
Outbound International