

BEFORE THE
POSTAL REGULATORY COMMISSION

COMPETITIVE PRODUCT PRICES
PRIORITY MAIL
PRIORITY MAIL CONTRACT GROUP

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Docket No. MC2009-25

COMMENTS OF UNITED PARCEL SERVICE
IN RESPONSE TO COMMISSION ORDER NO. 217
(June 8, 2009)

Pursuant to Order No. 217 (May 26, 2009), United Parcel Service comments on the Postal Service's request to add a Priority Mail Contract Group product to the Competitive Product List. UPS opposes the addition of this specific product to the Competitive Product List because it is defined too broadly. It does not meet PAEA's definition of a "product."

The Proposed Priority Mail Contract Group Does Not Meet PAEA's Definition of "Product" and Is Inconsistent with the Commission's Prior Determination.

PAEA defines "product" as 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) (emphasis added). The mail included in a single postal product must share distinct cost and market characteristics to be grouped together as one product. As a result, the Commission has already determined that, by and large, every negotiated service agreement ("NSA") is a separate product. Docket No. RM2007-1, Order No. 43 at ¶ 2177 (October 29, 2007). The only, very limited, exception is for NSAs that are

functionally equivalent to each other. As the Commission has stated, two (or more) NSAs may be grouped together as a single product only “if it can be shown that they have similar cost **and** market characteristics.” *Id.* (emphasis added). In other words, the agreements must be alike in all material respects.

Here, all future Priority Mail contracts would be grouped together as one product as long as the anticipated cost coverage of each contract falls within a certain (undisclosed) cost coverage range. Postal Service Request, Attachment 1 at 1-2 (May 19, 2009).¹ There are no other limitations or restrictions. Rather, “[e]ach individual contract [may] specify the applicable rates, any postage payment methods required, whether any volume minimums apply, whether packaging is provided by the Postal Service, the length of the contract and any price adjustment mechanism, and any other customized terms or conditions. . . .” *Id.*

The proposed product is not limited to agreements that share the same cost and market characteristics. Many of the customized terms in the initial five contracts have a significant effect on each individual contract’s costs. For example, the five proposed contracts range from 3 months (Contract 10) to 3 years (Contracts 6, 7, and 8) in length. A contract that will be in effect for only the summer of 2009 would not have the same market or cost characteristics as contracts that will be in effect for all seasons of the year from now through the first half of 2012.

1. Because the cost coverage range has been filed under seal, these comments do not address the appropriateness of the range itself. The breadth of the range as well as its upper and lower bounds may raise additional concerns about the proposed product.

Whether the Postal Service or the mailer provides packaging could also affect costs significantly, as would entry and preparation requirements. For example, a contract requiring the shipper to enter its mail at a downstream facility (as it appears Contract 10 does) would be grouped as part of the same product as contracts under which the mail would be picked up (as Contracts 6-9 appear to provide), even though these contracts have very different cost characteristics.

Moreover, shippers can qualify for contracts under the proposed product without regard to market similarities as long as the expected cost coverage falls within the specified range. This means that a contract covering only Priority Mail letter shipments in envelopes could be grouped with a contract covering only heavier weight packages.²

The Commission has correctly determined in a rulemaking proceeding that only functionally equivalent contracts, *i.e.*, ones that share both the same cost **and** the same market characteristics, can be classed as one product. Docket No. RM2007-1, Order No. 43 at ¶ 2177 (October 29, 2007). Here, the proposed product would improperly include contracts that do not share both the same cost and the same market characteristics. PAEA prohibits such a broad grouping.

The product proposed here would undermine the effectiveness of PAEA's most important safeguards. See, *e.g.*, Docket No. RM2007-1, Order No. 26 at ¶ 3070 (August 15, 2007) (“[a]ggregating postal services into only a few products . . . forfeits

2. That each contract's anticipated cost coverage would fall within a specified range is not the same as having similar cost and market characteristics. Two contracts with vastly different costs could have cost coverages that fall within the specified range. Otherwise, Single-Piece Parcel Post and In County Periodicals could be grouped together because they had similar cost coverages in FY2008, even though they have very distinct cost and market characteristics. See Docket No. ACR2008, LR-USPS-FY08-1, FY 2008 Public Cost and Revenue Analysis Report (December 29, 2008).

transparency and serves no legitimate business or regulatory need. Stated differently, it will not provide for accountability, a bedrock principle underlying the PAEA”).

The Commission’s annual compliance review is “[p]erhaps the most important tool[] provided by the PAEA for achieving the transparency on which the new statutory scheme relies. . . .” Docket No. RM2008-4, Order No. 104 at 2 (August 22, 2008). It is also the most important tool for ensuring that a number of PAEA’s substantive ratemaking requirements are met. The annual compliance process focuses on compliance **at the product level**. Section 3652(a)(1) requires costs, revenues, and rates to be reported “in sufficient detail to demonstrate that all **products** during such year complied with all applicable requirements of this title” (emphasis added). Likewise, PAEA requires the Commission to make its annual compliance determination “for **products** individually or collectively.” 39 U.S.C. § 3653(b)(1) (emphasis added).

The effectiveness of the annual compliance process therefore depends in large part on how products are defined. Grouping NSAs too broadly would not only greatly diminish the Annual Compliance Report’s value as a tool for achieving transparency, but it would also undermine substantive ratemaking requirements, such as the requirement that each competitive product must cover its attributable costs. 39 U.S.C. § 3633(a)(2). As the Commission has already recognized, “[a]bsent 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.” Docket No. RM2007-1, Order No. 26 at ¶ 3079 (August 15, 2007).

As proposed, it would be difficult if not impossible in the abbreviated compliance review process to identify and remedy any improper discrimination that may result, for example, from applying price adjustment mechanisms that differ from contract to contract.³ The reduced transparency would not be limited to the annual compliance review process: pre-implementation review would also be diminished, because PAEA imposes less public notice and Commission review requirements on new rates (including new functionally equivalent contracts) within an existing product than it does on new products. *Compare, e.g.,* 39 U.S.C. § 3632(b)(3) with 39 U.S.C. § 3642(d).

These difficulties would grow as contract rates continue to generate a greater share of overall revenues.

3. Even if each individual Priority Mail contract initially covers its costs, there is no guarantee that this would remain the case, since the price adjustment mechanism could vary from contract to contract.

Conclusion

Grouping together as one product all Priority Mail contracts that have estimated cost coverages within a certain range is contrary to PAEA's definition of product and the Commission's reasoned application of that definition to negotiated service agreements. It should not be approved.

Respectfully submitted,

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