

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

Before Commissioners:

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

Competitive Product Prices  
International Business Reply Service Competitive  
Contract 3 (MC2011-21)  
Negotiated Service Agreement

Docket No. CP2011-61

ORDER APPROVING AN ADDITIONAL  
INTERNATIONAL BUSINESS REPLY SERVICE COMPETITIVE CONTRACT 3  
NEGOTIATED SERVICE AGREEMENT

(Issued March 11, 2011)

I. INTRODUCTION

The Postal Service seeks to add a new International Business Reply Service contract to the International Business Reply Service Competitive Contract 3 product established in Docket No. MC2011-21. For the reasons discussed below, the Commission approves the request.

II. BACKGROUND

On February 18, 2011, the Postal Service filed a notice, pursuant to 39 CFR 3015.5, that it entered into an additional International Business Reply Service

(IBRS) contract.<sup>1</sup> The instant contract is the successor to the IBRS contract filed by the Postal Service and approved by the Commission in Docket No. CP2010-22 for the same mailer. *Id.* at 3. The Postal Service requests that the instant contract be included within the IBRS Competitive Contract 3 product. *Id.* at 6.<sup>2</sup>

In support of its Notice, the Postal Service filed the following attachments:

- Attachment 1—a redacted copy of the contract;
- Attachment 2—a redacted copy of the certified statement required by 39 CFR 3015.5(c)(2);
- Attachment 3—Governors’ Decision No. 08-24, which establishes prices and classifications for the IBRS contracts product, and includes Mail Classification Schedule language for IBRS contracts, formulas for pricing along with an analysis, certification of the Governors vote, and certification of compliance with 39 U.S.C. 3633(a); and
- Attachment 4—an application for non-public treatment of materials to maintain the redacted portions of the contract, customer identifying information, and related financial information under seal.

In Order No. 684, the Commission approved the addition of IBRS Competitive Contract 3 to the competitive product list and the designation of the contract filed in Docket No. CP2011-59 as the baseline contract for future functional equivalence analyses.<sup>3</sup>

The Postal Service asserts that the instant contract is functionally equivalent to the IBRS contract filed in Docket No. CP2011-59. Notice at 4. It also asserts that the

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<sup>1</sup> Notice of the United States Postal Service Filing of a Functionally Equivalent International Business Reply Service Competitive Contract 3 Negotiated Service Agreement, February 18, 2011 (Notice).

<sup>2</sup> The Postal Service will notify the mailer of the effective date within 30 days of receiving all necessary regulatory approvals. The contract will remain in effect for 1 year unless terminated earlier by either party. *Id.* Attachment 1 at 4.

<sup>3</sup> See Docket Nos. MC2011-21 and CP2011-59, Request of the United States Postal Service to Add International Business Reply Service Competitive Contract 3 to the Competitive Products List and Notice of Filing of Contract (Under Seal), February 11, 2011.

“functional terms” of the instant contract and the “functional terms” of the baseline IBRS Competitive Contract 3 “are the same, although other terms that do not directly change the nature of the agreements’ basic obligations may vary.” *Id.* To that end, the Postal Service indicates that prices under IBRS contracts may differ based on volume or postage commitments and when the agreement is signed. It identifies certain customer-specific information that distinguishes the instant contract from the proposed baseline agreement. *Id.* at 5.

In Order No. 680, the Commission gave notice of the docket, appointed a Public Representative, and provided the public with an opportunity to comment.<sup>4</sup>

### III. COMMENTS

Comments were filed by the Public Representative.<sup>5</sup> No other interested person submitted comments. The Public Representative states that the instant contract adds to the total competitive product contribution. *Id.* at 2. He asserts that IBRS contracts result in higher revenues, broader shipping options for such merchandise, reduced internal business costs, and improved rates to final customers from use of recycled parts. *Id.*

The Public Representative reviewed the Postal Service’s estimation of attributable costs based on its calculation of average unit attributable costs for mail processing, delivery, and transportation functions. In his analysis of the Postal Service’s method of determining attributable costs for transportation expenses, he finds that the procedure for calculating transportation costs relies on the assumption that inbound transportation costs for contract volume uses the same average mix of

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<sup>4</sup> Notice and Order Concerning Filing of an Additional International Business Reply Service Competitive Contract 3 Negotiated Service Agreement, February 24, 2011 (Order No. 680).

<sup>5</sup> Public Representative Comments in Response to United States Postal Service Filing of a Functionally Equivalent International Business Reply Services Competitive Contract 3 Negotiated Service Agreement, March 4, 2011 (PR Comments); see *also* Public Representative Motion for Acceptance of Late-Filed Comments, March 4, 2011. This motion is granted.

transportation reflected at the system level.<sup>6</sup> *Id.* at 3. The Public Representative contends that this approach raises an inherent bias in the analysis of transportation costs. *Id.* He recommends a more accurate cost estimation method which reflects the specific mix of transportation modes and average length of haul (distance) per mode. *Id.* He asserts that the same approach should apply to mail processing and delivery costs. *Id.*

The Public Representative contends that because of the two-part bundled services offered by IBRS contracts that include the original shipment and the value added reply service, the product adds to the total competitive product contribution in two ways, expansion of outbound mailings and new inbound mail flow from the use of the return feature. *Id.* at 4. He states that, under the current estimation of contribution method, the proposed contribution is underestimated because the increase resulting from the outbound mail flow is ignored. *Id.* The Public Representative asserts that even if the contribution of IBRS under the current method were negative, total contribution for the combined products would be positive. *Id.* He recommends that the current method of estimating contribution be modified to include outbound mail volume that should also result in more effective pricing for IBRS contracts.

#### IV. COMMISSION ANALYSIS

The Commission must first review the instant contract to ensure its functional equivalence to the contract approved in Docket No. CP2011-59. Second, the Commission must ensure that the instant contract satisfies the requirements of 39 CFR 3015.5 and 3015.7, and 39 U.S.C. 3633.

*Functional equivalence.* The Postal Service states that the contract shares similar cost and market characteristics with the baseline contract. It asserts that the

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<sup>6</sup> The Postal Service uses IBRS contracts for U.S.-based entities that sell lightweight articles to foreign consumers and desire to offer their customers a means to return the articles to the United States for recycling, refurbishment, repair, or value-added processing. There is no outbound component to the IBRS contract.

instant contract meets the pricing formula and classification established in Governors' Decision No. 08-24 which comport with 39 U.S.C. 3633 and the Commission's rules. The Postal Service states that the instant contract differs from the contract in Docket No. CP2011-59 regarding customer-specific information, e.g., customer's name, address, title, and email address of the customer's representative. Notice at 5.

The instant contract appears to be similar to the contract filed in Docket No. CP2011-59 and differs only in minor respects relative to customer-specific information including the identifying information for the mailer's representative. These differences notwithstanding, the Commission concludes that the instant contract may be included in the IBRS Competitive Contract 3 product.

*Cost considerations.* The Commission reviews competitive products to ensure that they meet the applicable requirements of 39 CFR 3015.5 and 3015.7, as well as 39 U.S.C. 3633. The Commission has reviewed the financial analyses provided under seal that accompanies the instant contract as well as the comments filed in this proceeding.

Based on the information provided, the Commission finds that the contract submitted 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 competitive products' contribution to institutional costs (39 U.S.C. 3633(a)(3)). Thus, a preliminary review of the proposed contract indicates that it comports with the provisions applicable to rates for competitive products in 39 U.S.C. 3633.

The Public Representative's contention, that contract-specific costs that reflect, as nearly as practicable, the actual character of the inbound mail flow should be used in the financial analysis, has merit. The Commission therefore encourages the Postal Service to use contract-specific costs, to the extent possible, since use of contract-specific costs may permit more competitive rates.

The Public Representative's second point, that costs and revenues for outbound mail generating IBRS items should be considered with the inbound costs and revenues in evaluating IBRS contribution, is rejected.

The instant contract is part of a product, *i.e.*, IBRS Competitive Contract 3. There is no outbound component to this contract. Because section 3633(a)(2) requires that the revenues for each competitive product cover its attributable cost, IBRS must be evaluated as a stand-alone product. However, this is not simply a compliance issue, but a necessity in determining the financial health of the Postal Service.

Adding the contribution from an outbound product, albeit, one generated by the availability of a simple return mechanism like IBRS, would double count contribution. Using this approach, the total contribution for the Postal Service as a whole would be misstated. For example, the contribution from Product A would count not only for Product A, but also for Product B. Therefore, it would be counted twice. Then, adding the contribution across all products would either overstate or understate the actual contribution from all postal products and services, depending on the mix of positive and negative contribution by product. For these reasons, the contribution from other outbound products should not be used to evaluate the efficacy of IBRS.

However, the Public Representative raises an interesting point. The existence of IBRS may increase the demand for a firm's product that utilizes IBRS as a selling point. This could then increase outbound mail and inbound IBRS as the Public Representative suggests. The Postal Service could avail itself of this opportunity, *i.e.*, increased outbound and inbound mail flow, by creating either a niche product or negotiated service agreement which links the use of outbound mail to inbound IBRS. The Postal Service's PMI and IPAS are excellent outbound products which are already included in existing negotiated service agreements and which produce substantial contribution. IBRS is also an excellent product. This may present an opportunity for additional contribution.

*Other considerations.* In Order No. 680, the Commission granted an extension of the current contract in Docket No. CP2011-59 with this mailer to March 31, 2011. Order

No. 680 at 4. The Postal Service shall notify the Commission of the effective date of the instant contract and notify the Commission if the contract terminates earlier than scheduled.

The instant contract, similar to the previous IBRS competitive contracts, contains price contingency clauses which allow the Postal Service flexibility to change rates without entering a new agreement. The Commission initially reviewed similar provisions in Docket No. CP2009-20.<sup>7</sup> In Order No. 178, the Commission addressed the implications of the contingency clause in the contract in Docket No. CP2009-20, and determined that those conclusions apply to other contracts with similar provisions that specifically permit contingency prices.<sup>8</sup>

In conclusion, the Commission finds that the negotiated service agreement submitted in Docket No. CP2011-61 is appropriately included within the IBRS Competitive Contract 3 product.

## V. ORDERING PARAGRAPHS

*It is ordered:*

1. The contract filed in Docket No. CP2011-61 is included within the IBRS Competitive Contract 3 (MC2011-21) product.
2. The Postal Service shall notify the Commission of the effective date of the instant contract and update the Commission if the contract terminates prior to the scheduled termination date.

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<sup>7</sup> See Docket Nos. MC2009-14 and CP2009-20, Order Concerning International Business Reply Service Contract 1 Negotiated Service Agreement, February 5, 2009, at 9 (Order No. 178); Docket No. CP2010-17, Order No. 377, Order Concerning Change in Prices for International Business Reply Service Contract 1 Negotiated Service Agreement, December 30, 2009.

<sup>8</sup> The Commission explained that the Postal Service must file the changed rates under 39 CFR 3015.5 and give a minimum of 15 days' notice. However, unless the changed rates raise new issues, the Commission found that it would not anticipate a need to act further. See Order No. 178 at 9.

3. The Postal Service shall file any modifications of price based on cost increases or contingency price provisions in the instant contract with the Commission as discussed in the body of this Order.

By the Commission.

Shoshana M. Grove  
Secretary