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ORDER NO. 2175

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

Before Commissioners: Ruth Y. Goldway, Chairman;
Mark Acton, Vice Chairman; and
Robert G. Taub

Competitive Product Prices
Priority Mail
Priority Mail Contract 89

Docket No. MC2014-39

Competitive Product Prices
Priority Mail Contract 89 (MC2014-39)
Negotiated Service Agreement

Docket No. CP2014-72

ORDER ADDING PRIORITY MAIL CONTRACT 89
TO THE COMPETITIVE PRODUCT LIST

(Issued August 29, 2014)

I. INTRODUCTION

The Postal Service seeks to add a new product identified as Priority Mail Contract 89 to the competitive product list.[1] For the reasons discussed below, the Commission approves the request to add Priority Mail Contract 89 to the competitive

[1] Request of the United States Postal Service to Add Priority Mail Contract 89 to Competitive Product List and Notice of Filing (Under Seal) of Unredacted Governors' Decision, Contract, and Supporting Data, August 18, 2014 (Request).

product list and directs the Postal Service to file the amendment described in the Postal Service's response to Order No. 2161 by September 12, 2014.

II. BACKGROUND

On August 18, 2014, in accordance with 39 U.S.C. § 3642 and 39 C.F.R. § 3020.30 *et seq*., the Postal Service filed the Request, along with supporting documents. In the Request, the Postal Service asserts that Priority Mail Contract 89 is a competitive product that establishes rates "not of general applicability" within the meaning of 39 U.S.C. § 3632(b)(3). *Id*. at 1. Among the supporting documents, the Postal Service included a copy of the Governors' Decision authorizing the product, a contract related to the proposed new product, requested changes to the competitive product list, a statement supporting the Request, a certification of compliance with 39 U.S.C. § 3633(a), and financial workpapers. In addition, the Postal Service submitted an application for non-public treatment of materials requesting that redacted portions of the Governors' Decision and the contract, customer-identifying information, and related financial information remain under seal. *Id*., Attachment F.[2]

The contract is intended to take effect one business day following the day on which the Commission issues all necessary regulatory approvals. Request, Attachment B at 4. It is set to expire three years from the effective date unless, among other things, it is terminated or renewed upon written agreement of the parties. *Id*.

On August 19, 2014, the Commission issued an order establishing the two dockets, appointing a Public Representative, requesting supplemental clarifying information, and providing interested persons with an opportunity to comment.[3]

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[2] In its application for non-public treatment of materials, the Postal Service asks the Commission to protect customer-identifying information from public disclosure indefinitely. *Id.* at 7. The Commission has consistently denied similar requests for indefinite protection. *See, e.g.*, Docket Nos. MC2011-1 and CP2011-2, Order No. 563, Order Approving Express Mail Contract 9 Negotiated Service Agreement, October 20, 2010, at 6-7.

[3] Order No. 2161, Notice and Order Concerning the Addition of Priority Mail Contract 89 to the Competitive Product List and Request for Supplemental Information, August 19, 2014.

III. COMMENTS

The Public Representative filed comments on August 27, 2014.[4] No other interested person filed comments. The Public Representative found the requested Postal Service clarification regarding the calculation of quarterly average volume of packages to be sufficient.[5] He concluded that Priority Mail Contract 89 should be categorized as a competitive product and added to the competitive product list and, based on the financial workpapers filed by the Postal Service, it appears that the contract is expected to generate sufficient revenues to cover costs and thereby satisfy the requirements of 39 U.S.C. § 3633(a). PR Comments at 2.

The Public Representative also concluded that the Postal Service's assertions pursuant to 39 U.S.C. § 3642 that the contract is competitive and constrained by the existing market appear reasonable. Based upon these assertions, the Public Representative concludes that the Postal Service's Request to add the Priority Mail contract to the competitive product list is appropriate. *Id*.

The Public Representative reviewed the financial model filed under seal with the Postal Service's Request and concluded that the negotiated prices in the instant contract should generate sufficient revenues to cover costs during the contract year. *Id*. at 3.

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[4] Public Representative Comments on Postal Service Request to Add Priority Mail Contract 89 to Competitive Product List, August 27, 2014 (PR Comments). *See also* Notice of Errata to Public Representative Comments on Postal Service Request to Add Priority Mail Contract 89 to Competitive Product List, August 27, 2014.

[5] *See* Order No. 2161 at 2-3. The Postal Service states that the quarterly average volumes calculation should be based on the total number of quarters from the Effective Date of the contract *divided into* rather than *divided by* the total number of contract packages. It will file an amendment correcting the typographical error in the contract as soon as possible. Response of the United States Postal Service to Request for Supplemental Information, August 20, 2014.

IV. COMMISSION ANALYSIS

The Commission has reviewed the Request, the contract, the supporting data filed under seal, the response to the request for supplemental information, and the Public Representative's comments.

Product list requirements. The Commission's statutory responsibilities when evaluating the Request include assigning Priority Mail Contract 89 to either the market dominant or competitive product list. *See* 39 U.S.C. § 3642(b)(1); 39 C.F.R. § 3020.34. Before adding a product to the competitive product list, the Commission must determine that the Postal Service does not exercise sufficient market power that it can effectively set the price of the product substantially above costs, raise prices significantly, decrease quality, or decrease output, without the risk of losing a significant level of business to other firms offering similar products. *See* 39 U.S.C. § 3642(b)(1). In addition, the Commission must consider the availability and nature of private sector enterprises engaged in delivering the product, the views of those who use the product, and the likely impact on small business concerns. *See* 39 U.S.C. § 3642(b)(3); 39 C.F.R. §§ 3020.32(f), (g), and (h).

The Postal Service asserts that it provides postal services of the kind provided under the contract in a highly competitive market, that other shippers who provide similar services constrain its bargaining position, and that it can therefore neither raise prices substantially above costs or raise prices significantly, nor decrease service, quality, or output without risking the loss of business to competitors. Request, Attachment D at 2. The Postal Service states that the contract partner supports the Request, that expedited shipping is highly competitive, and that the Postal Service is unaware of any small business concerns that could offer comparable services to the contract partner. *Id*. at 3.

The Commission finds that the Postal Service does not exercise sufficient market power that it can effectively set the price of the proposed product substantially above costs, raise prices significantly, decrease quality, or decrease output, without the risk of

losing a significant level of business to other firms offering similar products. The availability of other private sector providers supports this conclusion. The contract partner and the Public Representative support the addition of the Priority Mail Contract 89 product to the competitive product list. Further, there is no evidence of an adverse impact on small businesses. For these reasons, having considered the relevant statutory and regulatory requirements, the comments filed, and the Postal Service's supporting justification, the Commission finds that Priority Mail Contract 89 is appropriately classified as competitive and is added to the competitive product list.

Cost considerations. Because the Commission finds Priority Mail Contract 89 is a competitive product, the Postal Service must also show that the contract covers its attributable costs, does not cause market dominant products to subsidize competitive products as a whole, and contributes to the Postal Service's institutional costs. 39 U.S.C. § 3633(a); 39 C.F.R. §§ 3015.5 and 3015.7. As long as the revenue generated by the contract exceeds its attributable costs, the contract is unlikely to reduce the contribution of competitive products as a whole or to adversely affect the ability of competitive products as a whole to contribute an appropriate share of institutional costs. In other words, if the contract covers its attributable costs, it is likely to comply with 39 U.S.C. § 3633(a).

Based on a review of the record, the Commission finds that the rates during the first year of the contract should cover the contract's attributable costs. 39 U.S.C. § 3633(a)(2). For this reason, it finds that the contract should not result in competitive products as a whole being subsidized by market dominant products, in accordance with 39 U.S.C. § 3633(a)(1). Similarly, it finds the contract is unlikely to prevent competitive products as a whole from contributing an appropriate share of institutional costs, consistent with 39 U.S.C. § 3633(a)(3). *See also* 39 C.F.R. § 3015.7(c). Accordingly, a preliminary review of the contract indicates it is consistent with section 3633(a).

The contract contains a price adjustment provision that adjusts contract rates during subsequent contract years by the most recent cell by cell percent (%) change to

prices of general applicability for Priority Mail Commercial Plus less the discount as illustrated in Table A of the contract. Request, Attachment B at 4. The adjustment provision increases the likelihood that rates will cover attributable costs during subsequent contract years. The Commission will review the contract's cost coverage and the contribution of competitive products as a whole to the Postal Service's institutional costs in the Commission's Annual Compliance Determination to ensure that they continue to comply with 39 U.S.C. § 3633(a).

Other considerations. By its terms, the contract becomes effective one business day after the date that the Commission issues all necessary regulatory approvals. *Id.* The contract is scheduled to expire 3 years from the effective date, unless, among other things, either party terminates the contract with 30 days' written notice to the other party or it is renewed by mutual agreement.[6]

The contract also contains a provision that allows the parties to extend the contract for two 90-day periods if a successor agreement is being prepared and the Commission is notified within at least seven calendar days of the contract expiring.[7] During the extension periods, prices will be adjusted as described in the contract. *Id*. The Commission finds the two potential 90-day extension periods are reasonable because: (1) prices are automatically adjusted upon both parties' agreement of extension, making it likely that the contract will continue to cover its attributable costs;

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[6] *Id.* Should both parties agree to renew the contract, any such renewal is required to follow the requirements of 39 U.S.C. § 3633 and the Commission's implementing regulations of 39 C.F.R. part 3015.

[7] *Id.* As the Commission noted in Order No. 1773, the Postal Service clarified that substantially similar language in Priority Mail Contract 60 contemplates the Postal Service filing any notices of extension with the Commission *at least one week prior to* the expiration of the contract, as opposed to the instant contract's "within at least seven (7) calendar days of the contract expiring." *See* Docket Nos. MC2013-54 and CP2013-70, Order No. 1773, Order Adding Priority Mail Contract 60 to the Competitive Product List, July 8, 2013, at 3; *see also* Docket Nos. MC2013-54 and CP2013-70, Response of the United States Postal Service to Chairman's Information Request No. 1, July 1, 2013, question 2.

and (2) the extension(s) should assist the Postal Service's contract negotiations by providing additional flexibility.

On August 20, 2014, the Postal Service represented to the Commission that it intends to file an amendment to correct the typographical error in the contract as soon as possible. The amendment has not yet been filed. The Postal Service is directed to file the amendment by September 12, 2014.

If the instant contract is terminated prior to the scheduled expiration date, the Postal Service shall promptly notify the Commission.

Within 30 days after the instant contract terminates, the Postal Service shall file the annual (contract year) costs, volumes, and revenues disaggregated by weight and zone associated with the contract.

In conclusion, the Commission approves Priority Mail Contract 89 as a new product. The revision to the competitive product list appears below the signature of this Order and is effective immediately.

V. ORDERING PARAGRAPHS

It is ordered:

1. Priority Mail Contract 89 (MC2014-39 and CP2014-72) is added to the competitive product list as a new product under Negotiated Service Agreements, Domestic. Revisions to the competitive product list and the Mail Classification Schedule appear below the signature of this Order and are effective immediately.

2. The Postal Service shall notify the Commission if the instant contract terminates prior to the scheduled expiration date as discussed in this Order.

3. Within 30 days after the instant contract terminates, the Postal Service shall file the annual (contract year) costs, volumes, and revenues disaggregated by weight and zone associated with the contract.

4. As discussed in the body of this Order, the Postal Service shall file the contract amendment by September 12, 2014.

5. The Secretary shall arrange for publication in the *Federal Register* of an updated product list reflecting the change made in this Order.

By the Commission.

Ruth Ann Abrams
Acting Secretary

CHANGE IN PRODUCT LIST

The following material represents changes to the product list codified in Appendix A to 39 C.F.R. part 3020, subpart A—Mail Classification Schedule. These changes reflect the Commission's order in Docket Nos. MC2014-39 and CP2014-72. The Commission uses two main conventions when making changes to the product list. New text is underlined. Deleted text is struck through.

Part B—Competitive Products
2000 Competitive Product List
*****
Negotiated Service Agreements*
Domestic*
*****
<u>Priority Mail Contract 89</u>
*****

CHANGES TO THE MAIL CLASSIFICATION SCHEDULE

The following material represents a change to the Mail Classification Schedule. The Commission uses two main conventions when making changes to the Mail Classification Schedule. New text is underlined. Deleted text is struck through.

Part B—Competitive Products
2000 Competitive Product List
*****
Negotiated Service Agreements*
Domestic*
*****
Priority Mail Contract 89
*****
2500 Negotiated Service Agreements
*****
2505 Domestic
*****
2505.5 Priority Mail Contracts
*****

- Priority Mail Contract 89

Baseline Reference
Docket Nos. MC2014-39 and CP2014-72
PRC Order No. 2175, August 29, 2014
Included Agreements
CP2014-72, expires August 30, 2017
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