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POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Competitive Product Prices — Docket No. MC2015-40
Priority Mail
Priority Mail Contract 120

Competitive Product Prices — Docket No. CP2015-51
Priority Mail Contract 120 (MC2015-40)
Negotiated Service Agreement

PUBLIC REPRESENTATIVE COMMENTS ON POSTAL SERVICE REQUEST TO ADD PRIORITY MAIL CONTRACT 120 TO COMPETITIVE PRODUCT LIST

(March 12, 2015)

The Public Representative hereby provides comments pursuant to Order No. 2379.[1] In that Order, the Commission established the above referenced docket to receive comments from interested persons, including the undersigned Public Representative, on a Postal Service Request to add Priority Mail Contract 120 to the competitive product list.[2]

The Postal Service's Request includes a Statement of Supporting Justification, a certification of compliance with 39 U.S.C. § 3633(a), a public (redacted) version of Governor's Decision No. 11-6 and related analysis, a public version of Priority Mail shipping services Contract 120, and proposed changes to the Mail Classification Schedule competitive product list with the additions underlined. The Postal Service also filed under seal an unredacted version of Governor's Decision No. 11-6 and Contract 120, and supporting financial data estimating the contract value during the first year.

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[1] PRC Order No. 2379, Notice and Order Concerning the Addition of Priority Mail Contract 120 to the Competitive Product List, March 6, 2015 (Notice).

[2] Request of the United States Postal Service to Add Priority Mail Contract 120 to the Competitive Product List and Notice of Filing (Under Seal) of Unredacted Governors' Decision, Contract, and Supporting Data, March 4, 2015 (Request).

According to the Postal Service, Priority Mail Contract 120 is a competitive product featuring rates "not of general applicability" within the meaning of 39 U.S.C. § 3632(b)(3). Request at 1. The Postal Service also maintains that the prices and classification changes applicable to Contract 120 are supported by Governors' Decision No. 11-6.[3] The Postal Service further asserts that the Statement of Supporting Justification (Statement) provides support for adding Contract 120 to the competitive product list and the compliance of the instant contract with 39 U.S.C. § 3633(a). Request at 2; *Id.*, Attachment D.

The effective date for Contract 120 is one business day following the day on which the Commission issues all necessary regulatory approvals. *Id.*, Attachment B at 2 (Article II). The contract will expire 3 years from the effective date unless either party terminates the contract on 30 days' prior written notification, or other specific events. *Id.,* Attachment B at 3 (Article III).

COMMENTS

The Public Representative has reviewed the Postal Service's Request, the Statement of Supporting Justification, as well as Contract 120 and the financial data filed under seal with the Postal Service's Request. Based upon that review, the Public Representative concludes that Priority Mail Contract 120 should be classified as a competitive product and added to the competitive product list. In addition, it appears that Contract 120 in the first year should generate sufficient revenues to cover costs and thereby satisfy 39 U.S.C. § 3633(a).

Product List Assignment. Pursuant to 39 U.S.C. § 3642, the Postal Service requests that Priority Mail Contract 120 be added to the competitive product list. 39 U.S.C. § 3642 requires the Commission to consider whether "the Postal Service exercises sufficient market power that it can effectively set the price of such product substantially above costs, raise prices significantly, decrease quality, or decrease

[3] Decision of the Governors of the United States Postal Service on Establishment of Domestic Competitive Agreements, Outbound International Competitive Agreements, Inbound International Competitive Agreements, and Other Non-Published Competitive Rates, March 22, 2011 (Governors' Decision No. 11-6).

output, without risk of losing a significant level of business to other firms offering similar products." 39 U.S.C. § 3642(b)(1). Products over which the Postal Service exercises such power are categorized as market dominant while all others are categorized as competitive.

The Postal Service's Statement of Supporting Justification (Statement) makes a number of assertions that address the considerations of section 3642(b)(1). Request, Attachment D at 2. These assertions appear reasonable. Based upon the Statement, the Public Representative concludes that the Postal Service's Request to add Priority Mail Contract 120 to the competitive product list is appropriate.

Requirements of 39 U.S.C. § 3633. Pursuant to 39 U.S.C. § 3633(a), the Postal Service's competitive prices must not result in the subsidization of competitive products by market dominant products; ensure that each competitive product will cover its attributable costs; and, ensure that all competitive products collectively contribute an appropriate share of the institutional costs of the Postal Service. Based upon a review of the financial data, the negotiated prices for Contract 120 should generate sufficient revenues to cover costs during the first year of the contract and therefore meet the requirements of 39 U.S.C. § 3633(a).

As noted above, Contract 120 is expected to remain in effect for a period of three years. During this period, the contract contains a mechanism for the annual adjustment of prices which will improve the likelihood that Contract 120 meets the requirements of 39 U.S.C. § 3633(a) over its lifetime. However, if the Postal Service does not seek a price increase, or proposes a decrease in generally applicable prices for Commercial Plus, the cost coverage for Contract 120 would decline—assuming costs rise over the three-year period.

Finally, the Postal Service must file revenue and cost data for Contract 120 in future Annual Compliance Reports. This data will permit the Commission to annually review the financial results for Priority Mail Contract 120 in future Annual Compliance Determination (ACD) reports for compliance with 39 U.S.C. § 3633(a).

Notwithstanding the conclusion that Contract 120 should generate sufficient revenues to cover costs, the Public Representative notes some initial concern with respect to the estimated volumes utilized in the financial model which accompanies this request. After consultation with the Postal Service, the Postal Service indicates that a standardized volumetric profile is used for new customers with certain mailing characteristics which are incorporated into the Priority Mail Contract financial model. This approach appears to be reasonable, in the absence of actual volume data with which to develop such a profile. However, the Public Representative recommends that additional information be included in the financial model when a standardized volumetric profile is used for partner-profile parcel and flats volumes in Priority Mail Contracts. The Public Representative also recommends that actual volumes be utilized by the Postal Service in lieu of estimated volumes if this contract is renewed or extended.

The Public Representative respectfully submits the foregoing comments for the Commission's consideration.

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