

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

Competitive Product Prices
Priority Mail
Priority Mail Contract 118

Docket No. MC2015-38

Competitive Product Prices
Priority Mail Contract 118 (MC2015-38)
Negotiated Service Agreement

Docket No. CP2015-49

PUBLIC REPRESENTATIVE COMMENTS ON
POSTAL SERVICE REQUEST TO ADD
PRIORITY MAIL CONTRACT 118 TO
COMPETITIVE PRODUCT LIST

(March 18, 2015)

The Public Representative hereby provides comments pursuant to Order No. 2383.¹ 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 118 to the Competitive product list.²

The Postal Service's Request includes a Statement of Supporting Justification (Statement), 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 118, and proposed changes to the Mail Classification Schedule (MCS) Competitive product list with the additions underlined. The Postal Service also filed under seal an unredacted version of Governor's Decision No. 11-6

¹ PRC Order No. 2383, Notice and Order Concerning the Addition of Priority Mail Contract 118 to the Competitive Product List, March 9, 2015 (Notice).

² Request of the United States Postal Service to Add Priority Mail Contract 118 to the Competitive Product List and Notice of Filing (Under Seal) of Unredacted Governors' Decision, Contract, and Supporting Data, March 4, 2015 (Request).

and Contract 118, and a supporting financial model estimating the contract value during the first year.

According to the Postal Service, Priority Mail Contract 118 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 118 are supported by Governors’ Decision No. 11-6.³ The Postal Service further asserts that the Statement provides support for adding Contract 118 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 118 is one business day following the day on which the Commission issues all necessary regulatory approvals. *Id.*, Attachment B at 4 (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.*, (Article III).

Background. On March 4, 2015, in addition to Contract 118, the Postal Service filed requests with the Commission seeking the addition of six Priority Mail contracts to the Competitive product list.⁴ The financial models filed in support of 5 of the 7 Priority Mail contracts were identical in several respects. These Priority Mail contracts were Contract 114, 117, 118, 119, and 120.

The cost coverage for all 5 contracts is identical. Moreover, all 5 contracts have the identical volume distribution by weight. In addition, 3 of the 5 contracts have the same total volume, which coincides with the minimum volume threshold needed to qualify for discounted prices under their respective contracts.

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).

⁴ The six other contracts were Priority Mail Contract 114, 115, 116, 117, 119, and 120.

COMMENTS

The Public Representative has reviewed the Postal Service's Request, the Statement, as well as Contract 118, and the supporting financial model filed under seal with the Postal Service's Request. Based upon that review, the Public Representative concludes that Priority Mail Contract 118 should be classified as a competitive product and added to the Competitive product list. In addition, it appears that Contract 118 in the first year should generate sufficient revenues to cover costs and thereby satisfy 39 U.S.C. § 3633(a). The Public Representative has also reviewed the Priority Mail contracts and supporting financial models for Contract 114, 117, 119, and 120.

Product List Assignment. Pursuant to 39 U.S.C. § 3642, the Postal Service requests that Priority Mail Contract 118 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 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 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 118 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 model, the negotiated prices for Contract 118 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 118 is expected to remain in effect for a period of three years. During this period, the contract includes a mechanism for the annual adjustment of prices which will improve the likelihood that Contract 114 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 118 would decline—assuming costs associated with the contract rise over the three-year period.

To monitor the contract, the Postal Service must file revenue and cost data for Contract 118 in future Annual Compliance Reports. This data will permit the Commission to annually review the financial results for Priority Mail Contract 118 in future Annual Compliance Determination (ACD) reports for compliance with 39 U.S.C. § 3633(a).

Notwithstanding the finding that Contract 118 should generate sufficient revenues to cover costs, the Public Representative notes that similarities in the financial models for Contract 118 and the other 4 Priority Mail contracts appear to be more than coincidental. In response to an inquiry, the Postal Service explained that a standardized volumetric profile is used for new customers with certain mailing characteristics, and is included in the Priority Mail Contract financial model in the absence of partner-specific volume data that could be used to develop the profile.

This approach appears to be reasonable. However, the Public Representative recommends that the Postal Service specifically inform the Commission when a standardized volumetric profile rather than the partner-profile for parcels and flats is used in the financial model for Priority Mail contracts. In addition, the Public Representative recommends that Postal Service use partner-specific volume profile in lieu of the standard volumetric profile if Contract 118 is renewed or extended.

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

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