

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Competitive Product Prices
Priority Mail
Priority Mail Contract 145

Docket No. MC2016-1

Competitive Product Prices
Priority Mail Contract 145 (MC2016-1)
Negotiated Service Agreement

Docket No. CP2016-1

PUBLIC REPRESENTATIVE COMMENTS ON POSTAL SERVICE REQUEST
TO ADD PRIORITY MAIL CONTRACT 145
TO COMPETITIVE PRODUCT LIST

(October 15, 2015)

The Public Representative hereby provides comments pursuant to Order No. 2748.¹ 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's Request to add Priority Mail Contract 145 to the competitive product list.²

The Request includes a Statement of Supporting Justification, a certification of compliance with 39 U.S.C. § 3633(a), a public (redacted) version of Governors' Decision No. 11-6 and related analysis, a public version of Priority Mail shipping services Contract 145, and proposed changes to the Mail Classification Schedule competitive product list with the addition underlined. The Postal Service also filed (under seal) an unredacted version of Governors' Decision No. 11-6, the contract related to the proposed new product, and supporting financial model.

¹ Notice and Order Concerning the Addition of Priority Mail Contract 145 to the Competitive Product List, October 8, 2015 (Order No. 2748).

² Request of the United States Postal Service to Add Priority Mail Contract 145 to Competitive Product List and Notice of Filing (Under Seal) of Unredacted Governors' Decision, Contract, and Supporting Data, October 7, 2015 (Request).

According to the Postal Service, Priority Mail Contract 145 is a competitive product “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 underlying the instant contract are supported by Governors’ Decision No. 11-6.³

The effective date of Priority Mail Contract 145 is two business days following the day on which Commission issues all necessary regulatory approval. Request, Attachment B at 3-4. The contract is scheduled to expire 3 years from the effective date, subject to early termination provisions. *Id* at 4.

COMMENTS

The Public Representative has reviewed the Postal Service’s Request, including the Statement of Supporting Justification, the contract and the worksheets filed under seal with the Request. Based upon that review, the Public Representative concludes that Priority Mail Contract 145 should be categorized as a competitive product and added to the competitive product list. In addition, it appears that Priority Mail Contract 145 should generate sufficient revenues to cover costs in the first year, and thereby satisfy 39 U.S.C. § 3633 (a) during the first year.

Product List Assignment. Pursuant to 39 U.S.C. § 3642, the Postal Service requests that Priority Mail Contract 145 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.

³ Decision of the Governors of the United States Postal Service on the Establishment of Prices and Classifications for 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).

The Postal Service's Statement of Supporting Justification 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 these assertions, the Public Representative concludes that the Postal Service's Request to add Priority Mail Contract 145 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 rates for competitive products 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 spreadsheets and the contract filed under seal with the Request, it appears that the negotiated prices 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) during the first year.

As noted above, Priority Mail Contract 145 is expected to remain in effect for a period of three years. The financial model applies to the first year of the contract only. The contract includes a mechanism for the annual adjustment of contract prices, which should help maintain the contract's ability to meet the requirements of 39 U.S.C. § 3633(a) over the life of the contract. Request, Attachment B at 2-3. However, the Public Representative has some concerns described below.

First, the contract terms include a minimum volume commitment, which increases significantly for the contract years two and three. *Id.* at 2. For the subsequent years, the significant increase in volume of contract packages suggests that the mail mix might change. Hypothetically, a change in the mail mix could cause the cost coverage to fall below 100 percent.⁴ However, the contract terms include a requirement regarding the average sample density of contract packages be maintained at a specified level in any contract quarter and the formula for the amount of penalty

⁴ The proposed contract prices vary by weight and zone. See Public Worksheet "PM145_Public.xlsx", Sheet 'PartnerProfileParcels'.

payments to be paid to the Postal Service otherwise.⁵ *Id.* at 3. The Public Representative acknowledges the importance of these additional contract terms, which should help maintain the contract cost coverage during the subsequent years.

Second, although an adjustment to contract prices is linked to the most recent change in rates of general applicability, there is still a limit on an annual increase in such prices. In other words, for contract years two and three, the increase in contract prices will not exceed the specified limit (even though the prices of general applicability [calculated by the Postal Service for Priority Mail Commercial Plus] increase over this limit). *Id.* The cost coverage might fall below 100 percent if the contract costs increase significantly above the fixed maximum limit set up by the contract terms.

The concerns expressed above are mitigated somewhat by the fact that the Commission will have an opportunity to review the revenue, cost and volume data for Priority Mail Contract 145 in the future Annual Compliance Determination Reports.

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

Lyudmila Y. Bzhilyanskaya
Public Representative

901 New York Ave. NW
Washington, DC 20268-0001
202-789-6849
lyudmila.bzhilyanskaya@prc.gov

⁵ To insure that the volume commitment is satisfied, beginning in the second full contract quarter, the Postal Service will monitor customer's profile by conducting random samples of contract packages. Request, Attachment B at 2.