

BEFORE THE  
POSTAL REGULATORY COMMISSION  
WASHINGTON, D.C. 20268-0001

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Periodic Reporting  
(UPS Proposals One, Two, and Three)

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Docket No. RM2016-2

**COMMENTS OF THE PARCEL SHIPPERS ASSOCIATION**

(January 25, 2016)

Pursuant to Order No. 2793 (October 29, 2015) the Parcel Shippers Association (PSA) respectfully files these comments in response to the petition for a rulemaking to consider three proposals relating to costing.<sup>1</sup>

Founded in 1953, PSA represents companies that sell and ship goods to consumers, and companies that support the parcel shipping industry. A list of PSA members is available on its website, [www.parcelshippers.org](http://www.parcelshippers.org). PSA's mission is to foster competition in the parcel delivery market. It creates value for its members by promoting the best possible service at the lowest possible costs. For competition to succeed it must be fair and PSA has consistently argued for a "level playing field" in the package delivery market.<sup>2</sup>

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<sup>1</sup> Petition of United Parcel Service, Inc. for the Initiation of Proceedings to Make Changes to Postal Service Costing Methodologies, October 8, 2015 ("Petition").

<sup>2</sup> See, e.g., Docket No. R2013-11, Reply Comments of the Parcel Shippers Association, Dec. 6, 2013, at 3; see also Report on Universal Postal Service and the Postal Monopoly, Docket No. PI2008-3, Reply Comments of Parcel Shippers Association, August 4, 2008, at 2 ("PSA agrees that, as suggested by others, the Postal Service should be given substantial flexibility with respect to competitive products to adapt to market forces and compete on a level playing field."); see also Review of the Treasury Report, Docket No. PI2008-2, Comments of Parcel Shippers Association on Treasury Report, April 1, 2008, at 10 ("The overriding purpose of the PAEA in the competitive market was to level the competitive playing field: 'Our bill has the primary goal of allowing the Postal Service to continue to fulfill its universal service mission at a reasonable cost. To achieve this goal, the legislation establishes a modern system for regulating rates, gives needed flexibility to the Postal

Once again the Petitioner (UPS) asks the Commission to increase the amount of costs attributed to Postal Service competitive products.<sup>3</sup> PSA joined with other parties commenting on Proposals One and Two.<sup>4</sup> Those comments explain why the proposed changes to postal costing methods (Proposals One and Two) do not meet the requirements of the Postal Accountability and Enhancement Act (PAEA),<sup>5</sup> do not reflect good costing principles, and should not be approved.

These PSA comments address assertions that market-dominant products are subsidizing competitive products. See, e.g., Petition at 5-6, 8, 9; Proposal One at 10, 11, 25; Proposal Two at 5-6; UPS response to CHIR 1, Question 2, at 5-6. As noted above on page 1, the Postal Service should not be allowed to subsidize competitive products. Fortunately, competitive products are not being subsidized.

As explained by Dr. John C. Panzar in a 2014 report to the Postal Regulatory Commission, the appropriate test for cross subsidization is the incremental cost test.

It is now standard in the regulatory economics literature that avoiding cross-subsidization means that the customers of each product (or group of products) pay more to the firm in revenues than the incremental cost of said product (or group of products).

John C. Panzar, *The Role of Costs for Postal Regulation*, (2014) p. 15.

Competitive product revenues substantially exceed competitive product incremental costs and therefore competitive products are not being subsidized by market-dominant products. The Postal Service Annual Compliance Report for FY 2015 shows competitive

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Service, and includes provisions to ensure a level playing field for the Postal Service and its competitors.' Statement for the Markup of the Postal Accountability and Enhancement Act House Committee on Government Reform by Rep. Henry A. Waxman (May 12, 2004)."

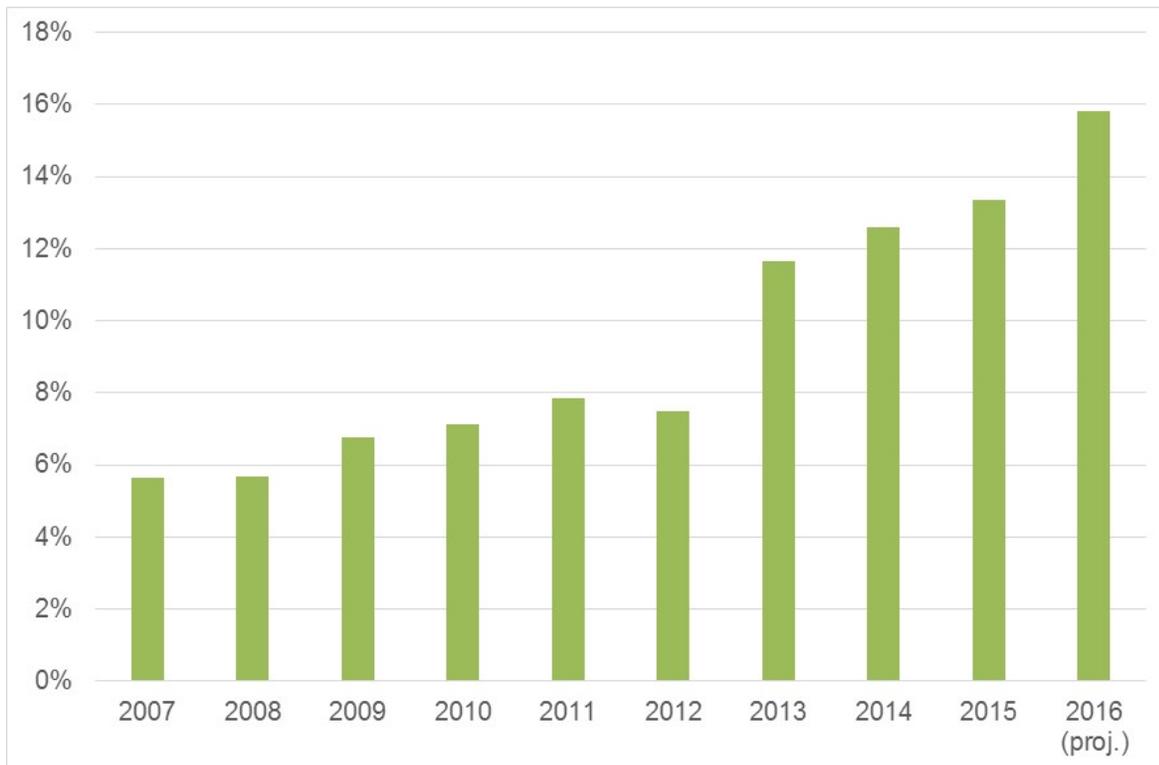
<sup>3</sup> See e.g. Initial Comments of United Parcel Service on Postal Service's FY 2013 Annual Compliance Report, January 31, 2014; Comments of United Parcel Service on Postal Service's FY 2014 Annual Compliance Report, February 2, 2015.

<sup>4</sup> Comments of "Market Dominant Mailers," January 25, 2016.

<sup>5</sup> Pub. L. No. 109-435, 120 Stat. 3198 (Dec. 20, 2006). The PAEA amends many section of title 39 of the United States Code. Unless otherwise noted, section references in these comments are to title 39, as amended by the PAEA.

product revenues were \$16.4 billion, well above competitive product incremental costs (\$12.2 billion).<sup>6</sup> Furthermore, Figure 1 below shows the contribution of competitive products to institutional costs is large, well in excess of the 5.5 percent share required by the Commission under section 3633(a)(2), and increasing.

**Figure 1. Competitive Product Contribution as Percentage of Total Institutional Cost (Competitive Product Share) by Fiscal Year**



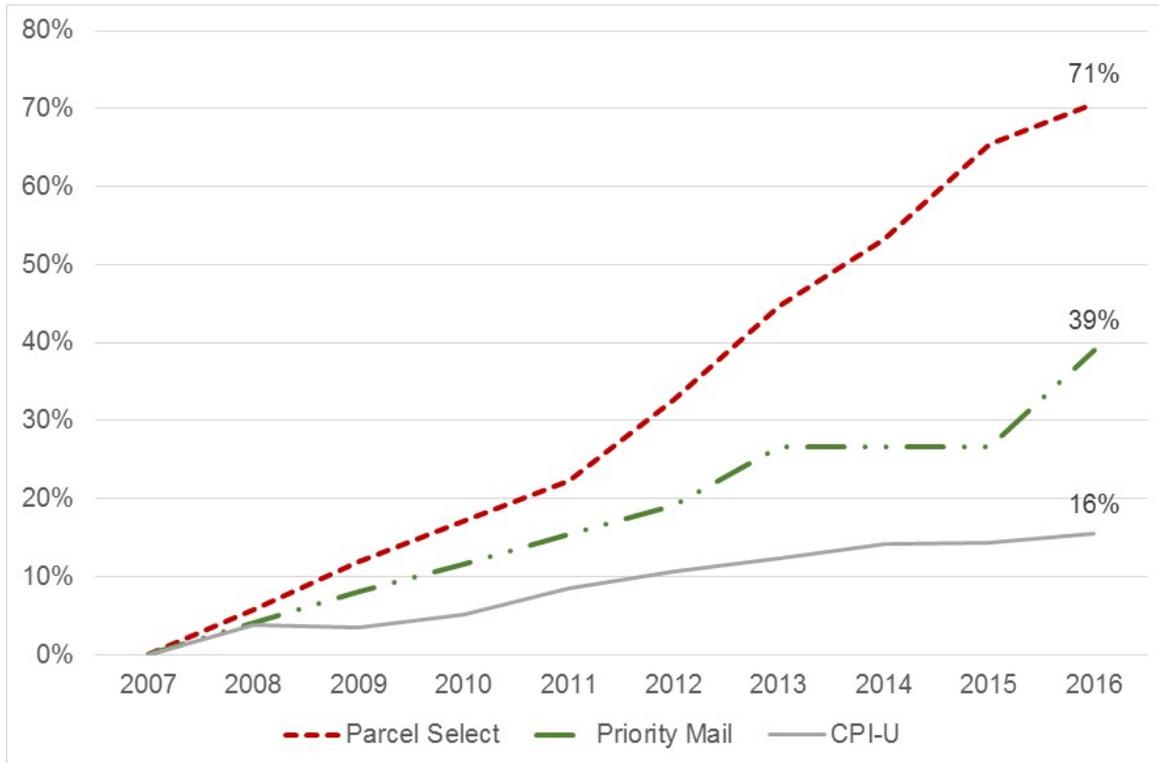
Source: FY 2007 Annual Compliance Determination, U.S. Postal Service, Fiscal Year 2007, p. 24, Table IV-A-1; FY 2008 – FY 2015 Public CRA Reports; FY 2016: Docket No. CP2016-9, Notice of the USPS of Changes in Rates of General Applicability for Competitive Products Established in Governors’ Decision No. 15-1, Filed 10/16/2015, p. 223

While increases in the competitive product share over time may be partly the result of increased competitive product volume from products formerly classified as market dominant and growth of the domestic package delivery market, another factor – the Postal Service substantially increasing competitive product prices – is much more important. As Figure 2 below shows, the Postal Service has increased prices for its competitive products much

<sup>6</sup> United States Postal Service FY 2015 Annual Compliance Report, December 29, 2015 (FY 2015 ACR), at 65. Public portions of the Postal Service’s filing are available on the Commission’s website at <http://www.prc.gov>.

faster than the rate of inflation, and probably much faster than its competitors. Real competitive product price increases of this magnitude are inconsistent with claims that the Postal Service is attempting to subsidize its competitive products.

**Figure 2. Priority Mail and Parcel Select Price Increases Under PAEA**



Source: Docket No. CP2008-3, Notice of Rate Adjustment/Competitive Products, filed 3/12/2008; Docket No. CP2009-8, Notice of Rate Adjustment/Competitive Products, filed 11/13/2008; Docket No. CP2010-8, Notice of Rate Adjustment/Competitive Products, filed 11/4/2009; Docket No. CP2011-26, Notice of Rate Adjustment/Competitive Products, filed 11/2/2010; Docket No. CP2012-2, Notice of Rate Adjustment/Competitive Products, filed 11/22/2011; Docket No. CP2013-3, Notice of Rate Adjustment/Competitive Products, filed 10/11/2012; Docket No. CP2014-5, Notice of Rate Adjustment/Competitive Products, filed 11/13/2013; Docket No. CP2014-55, Notice of Rate Adjustment/Competitive Products, filed 7/1/2014; Docket No. CP2015-33, Notice of Rate Adjustment/Competitive Products, filed 1/26/2015; Docket No. CP2016-9, Notice of Rate Adjustment/Competitive Products, filed 10/16/2015; BLS Data Series CUUR0000SA0, [www.bls.gov](http://www.bls.gov); USPS Fiscal Year 2016 Integrated Financial Plan, p. 2

In support of its cross-subsidization assertion, Petitioner relies heavily on the September 2014 Priority Mail price decrease for heavyweight Priority Mail and a suggested effect of those price decreases on market share. UPS Response to Chairman's Information Request No. 1, Question 2d, December 15, 2015. The reasoning there falls far short of proving the suggested effect for several reasons.

- FY 2015 Priority Mail revenues, which reflect the September 2014 price adjustment, remained well above attributable and incremental costs.<sup>7</sup> FY 2015 Public Cost and Revenue Analysis. Thus, the price adjustment did not result in Priority Mail being subsidized.
- As Figure 2 above shows, the cumulative price increase for Priority Mail under PAEA, a more relevant consideration, is well above inflation.
- While the Postal Service reduced rates for heavyweight Priority Mail rate cells in September 2014, these rate reductions were offset by increases in other Priority Mail rates, making the average September 2014 Priority Mail price zero.<sup>8</sup>
- As Figure 3 below shows, despite the September 2014 Priority Mail price change and the expansion of dimensional weight pricing by its competitors, Priority Mail's share of the Priority Mail/Ground market<sup>9</sup> remained stable and well below the shares of its competitors.

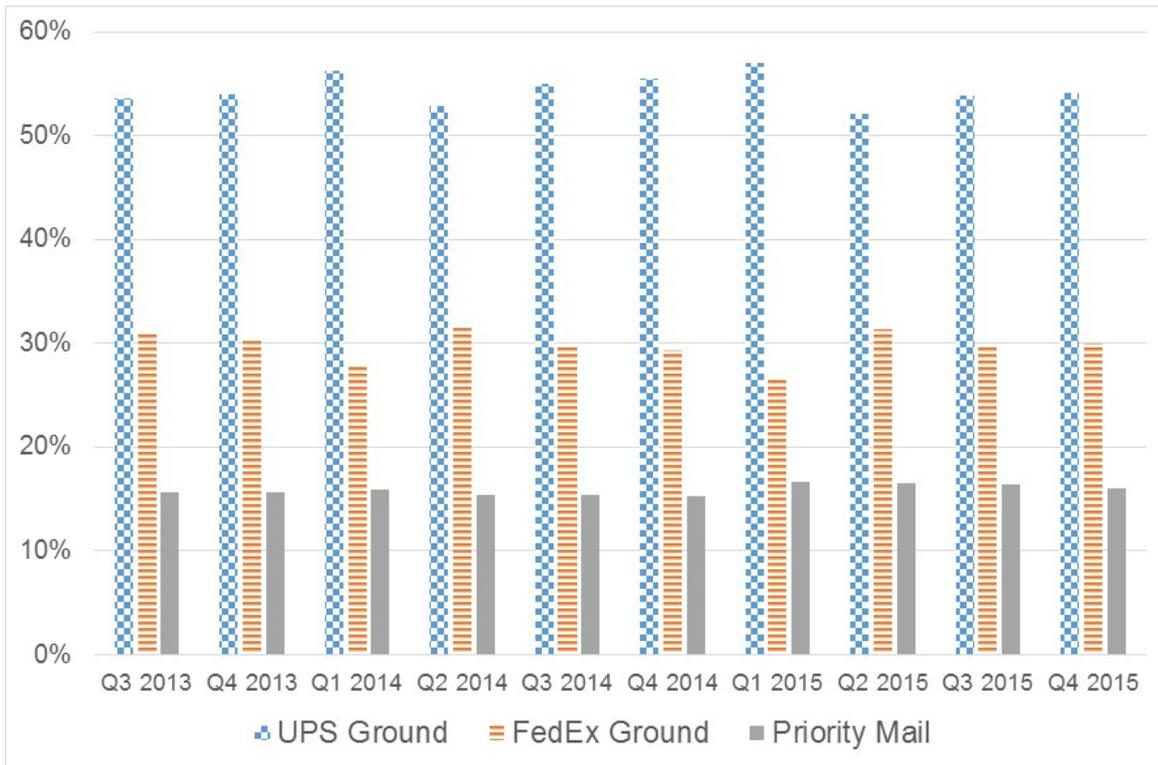
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<sup>7</sup> The Postal Service does not estimate the incremental costs separately for each competitive product, but Priority Mail incremental costs are only slightly larger than attributable costs, as indicated by the small difference between attributable and incremental costs for competitive products as a whole. USPS FY 2015 Annual Compliance Report, December 29, 2015, at 65.

<sup>8</sup> See Docket No. CP2014-55, Public Representative Comments on Postal Service Notice Concerning Changes in Rates of General Applicability for Priority Mail Established in Governors' Decision No. 14-3, at 2.

<sup>9</sup> UPS does not include Parcel Select in calculating the market shares shown in Figure 3. PSA believes that this exclusion is appropriate because, among other reasons, Parcel Select is a hybrid product for which the Postal Service, in general, only provides final delivery.

**Figure 3. Volume Share of Priority Mail / Ground Market by Quarter**



Source: Docket No. RM2016-2, United Parcel Service, Inc.’s Response to Chairman’s Information Request No. 1, CHIR No 1 Market Share Analysis.xls, “PM\_GND Market”, rows 32, 33, & 35 (filed in response to CHIR No. 5, Questions 1 & 3)

If the Postal Service is pricing to increase market share, at the expense of losing potential revenue and contribution, it has been very unsuccessful.

**CONCLUSION**

The Commission should not approve UPS Proposals One and Two because they do not meet the requirements of the PAEA and do not reflect good costing principles. To the extent these proposals are offered to address the alleged cross subsidization of competitive product services by revenues from market-dominant product revenues, they are also unnecessary. There is no cross subsidization.

Additionally, approving these proposals would be harmful to consumers, the Postal Service, and its users. Substantially increasing minimum prices for competitive products

would price the Postal Service out of at least a portion of the competitive delivery market. As the Commission has noted in the context of the appropriate share requirement:

Given a very competitive marketplace where the Postal Service's market share is relatively small, setting the contribution level too high could adversely affect the Postal Service ability to compete.

Order No. 1108 at 2.

Forcing any supplier – in this case, the Postal Service – out of a portion of the package delivery marketplace will reduce competition and result in higher package delivery prices. These higher prices would be harmful to both parcel shippers and their customers, consumers. Additionally, losing volume to competitors will cost the Postal Service contribution. This is not only bad for the Postal Service, but also for its remaining customers who mail letters, flats and other products. It is they who will ultimately pay higher prices to keep the Postal Service solvent.

Respectfully Submitted,

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