

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

ANNUAL COMPLIANCE REPORT,)
2016) Docket No. ACR2016

**REPLY COMMENTS OF
AMAZON FULFILLMENT SERVICES, INC.**

(February 13, 2017)

Amazon Fulfillment Services, Inc. (“AFSI”) respectfully submits these reply comments. These respond to the initial comments filed by United Parcel Service, Inc. (“UPS”) on February 2, 2017.

In its comments, UPS contends that a variety of costing methods currently used by the Postal Service understate—or, more precisely, *might* understate—the costs attributed to competitive products. UPS asks the Commission to “initiate” or “convene” “appropriate proceedings” to consider these issues. UPS Comments at 18. But UPS does not directly ask the Commission to resolve these issues in the current docket: “UPS understands that the ACR process is a narrow proceeding with a limited time frame; hence, UPS is not asking the Commission to resolve *each* issue flagged in these comments during this proceeding.” *Id.* at 3-4 (emphasis added). Indeed, the reality is that none of the issues “flagged” by UPS is properly before the Commission in this proceeding.

The Commission has repeatedly made clear how interested parties may obtain Commission review of alleged anomalies in the existing costing framework: by filing a petition for rulemaking. 2011 Annual Compliance Determination at 119; 2014 Annual

Compliance Determination at 48; 2015 Annual Compliance Determination at 93. The Commission has also emphasized that a petition for rulemaking is more likely to be considered if the petition proposes specific solutions to the alleged costing anomalies:

The Commission welcomes petitions from interested parties that not only investigate anomalies in the methodologies underlying the current cost models, but also present solutions. For example, a party could present an alternate methodology for distributing costs. The Commission encourages interested parties to continue to attempt to identify specific anomalies in conjunction with proposed solutions to correct methodologies that produce anomalous costs.

2011 ACD at 119.

UPS is free to pursue the rulemaking remedy, just as it did in Docket No. RM2016-2, *Periodic Reporting (UPS Proposals One, Two, and Three)*. See *id.*, Order No. 3506 (September 9, 2016), petition for review pending *sub nom. United Parcel Service, Inc. v. Postal Reg. Comm.*, No. 16-1354 (D.C. Cir.). UPS is also entitled to ask the Commission to reopen a previous rulemaking if it believes that the Postal Service has not complied adequately with the Commission's orders in that rulemaking. But UPS is not entitled to propose changes to the existing costing system in the Commission's Annual Compliance Review proceedings under 39 U.S.C. § 3653. Indeed, the Commission reemphasized this point last year in response to comments by an ally of UPS, the American Consumer Institute Center for Citizen Research ("ACI"), proposing that all institutional costs be fully attributed or allocated to individual products:

The scope of the Commission's ACR review is limited to determining the Postal Service's compliance with rates and services in FY 2015. 39 U.S.C. § 3653(b). Accordingly, the issues raised by ACI relating to the costing methodology and cost attribution for Competitive products are more appropriately addressed in a separate proceeding. The Commission is currently considering two proposals submitted by United Parcel Service, Inc. (UPS) that relate to cost attribution for Competitive products. [Citation to RM2016-2

omitted.] As a result, the issues raised in ACI's comments do not warrant initiation of an additional proceeding to investigate the methodology the Postal Service uses to attribute total postal cost.

2015 ACD at 93.

The Commission explained the basis for this policy at greater length in its Annual Compliance Determination for FY2011:

CRA level costs are reasonably accurate for evaluating product costs and related prices. [Citation omitted.] Persuasive evidence is required to discard and replace a litigated costing framework that has been developed and refined over 40 years. Parties alleging that the CRA costing methodology is not reliable must demonstrate flaws underlying the costing methodology or cost collection in order to merit consideration. The anecdotal evidence of possible costing anomalies appearing in the results of the CRA cost models for specific types of costs, as presented in this docket, is not sufficient.

2011 ACD at 119; *accord*, 2014 ACD at 48 (same).

This conclusion is reinforced by the limited scope of UPS's February 2 comments. In those comments, UPS offered only "anecdotal evidence of possible costing anomalies," without proof that they result from actual costing errors, let alone proposed solutions. For example, a purported anomaly repeatedly highlighted in UPS's February 2 Comments and motions for information requests is that the unit cost of competitive products as a whole, and ground products (primarily Parcel Select) in particular, has recently declined. UPS February 2 Comments at 12; Motion of UPS for Issuance of Information Request to the United States Postal Service (January 19, 2017), Question 1; Second Motion of UPS for Issuance of Information Request to the United States Postal Service (January 26, 2017), Questions 9-13.¹

¹ UPS also highlights the growth in total competitive product costs from FY 2015 to FY 2016 as if this growth were somehow problematic. Motion of UPS for Issuance of Information

This trend is not anomalous, but rather the result of a substantial shift in the mix of competitive products from higher-cost products (*e.g.*, Priority Mail) to relatively lower-cost products (*e.g.*, ground, primarily Parcel Select).² Furthermore, within Parcel Select, there has been a shift in the mail preparation mix toward increased downstream induction of mail into the Destination Delivery Unit [DDU], which has further reduced cost per piece. Indeed, UPS itself acknowledges these shifts elsewhere in its comments (at 11), noting that “[a]n increasing share of competitive product volume is drop-shipped at Postal Service Destination Delivery Units.” USPS Response to Chairman’s Information Request No. 11, Question 3. With these changes in mail mix, it would have been anomalous if the unit costs of competitive products (as a whole) and of Parcel Select (in particular) had *not* declined.

Equally important, UPS offers no proof that any of its anecdotes, even if they reflected genuine errors in the current costing system, would reflect errors large enough to offset more than a tiny fraction of the \$6.0 billion in contribution to institutional costs generated by competitive products in Fiscal Year 2016.³ This is a fatal omission. The issue before the Commission in this docket is whether the prices in effect during the fiscal year just ended were in compliance with “applicable provisions of this chapter”—*i.e.*, 39 U.S.C., chapter 36—“or regulations promulgated thereunder.” 39 U.S.C. § 3653(b)(1). For competitive products, the

Request to the United States Postal Service (January 19, 2017), Question 2. It was not. This growth in competitive product cost resulted from an increase in competitive product volume. This volume increase was beneficial because it caused Postal Service revenue to increase more than Postal Service costs, thereby increasing the contribution of competitive products to institutional costs.

² Recent growth in Parcel Select volumes has far outpaced that in Priority Mail. Parcel Select volumes grew from 1.5 billion pieces in FY 2014 to 2.4 billion pieces in FY 2016 while Priority Mail volume only grew from 900 million in FY 2014 to 1 billion pieces in FY 2016. USPS Public Revenue, Pieces, and Weight Reports.

³ FY 2016 USPS Public Cost and Revenue Analysis.

relevant pricing issues are whether competitive products were subsidized by market-dominant products, which they were not, and whether the revenue generated by competitive products in Fiscal Year 2016 covered attributable costs (39 U.S.C. § 3633(a)(2)) plus 5.5 percent of the Postal Service's institutional costs, the minimum contribution currently required by the Commission under 39 U.S.C. § 3633(a)(3). Without a credible showing that the costing errors hinted at by UPS are large enough to be material in this sense, the Commission's inquiry into competitive product pricing in this docket should be at an end.

CONCLUSION

The Commission should find again this year that the revenue from competitive products covers incremental costs and makes a contribution to the Postal Service's institutional costs well above the minimum required by the Commission under 39 U.S.C. § 3633(a)(3).

Respectfully submitted,

/s/

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