

POSTAL REGULATORY COMMISSION

Commission Response to 39 U.S.C. § 407(c)(1), Request for Views in Connection with the 2013 Universal Postal Union Postal Operations Council session in Bern, Switzerland

(April 3, 2013)

Introduction

This document responds to a request from the Department of State, pursuant to 39 U.S.C. § 407(c), requesting the views of the Postal Regulatory Commission concerning proposals to amend the Detailed Regulations of the Acts of the Universal Postal Union (UPU). These proposals will be considered at the UPU Postal Operations Council (POC) session to be held in Bern, Switzerland from April 8-19, 2013. Section 407(c)(1) provides that "[b]efore concluding any treaty, convention, or amendment that establishes a rate or classification for a product subject to subchapter I of chapter 36 [of title 39], the Secretary of State shall request the Commission to submit its view on whether such rate or classification is consistent with the standards and criteria established by the Commission under § 3622." The standards and criteria established by the Commission under § 3622 are limited to market dominant U.S. Postal Service products.

To address the Department of State's request, the Commission reviewed approximately 160 proposals. The Commission did not review proposals that will lapse because the proposals they supported were either rejected or withdrawn at the UPU Congress in the fall of 2012. Proposals for future rates or classifications were also excluded because they typically lack the requisite level of detail needed to develop a view. Each remaining proposal was examined to determine whether the proposal raises a market dominant rate or classification issue, and, if so, whether the proposal is consistent with the criteria established by the Commission under 39 U.S.C. § 3622. If a proposal does not raise a market dominant rate or classification issue, the Commission's view is not required.

The Commission finds that 11 proposals and 1 resolution establish a rate or classification for a U.S. Postal Service market dominant product or service. Eight of the proposals are consistent with 39 U.S.C. § 3622, each of which is discussed separately below. Two of the proposals contain insufficient information for the Commission to make a fully informed determination on their consistency with 39 U.S.C. § 3622 at this time. They are 25.140.1, International Business Reply Service, and 25.193.2, Checking of mails. The Commission also finds proposal 35.129.91, Merchandise return service for the original seller, to be inconsistent with 39 U.S.C. § 3622, and provided its view to the Department of State on this proposal on September 12, 2012. The Commission explains each of its findings concerning the proposals. Proposals that address the same provision of the Detailed Regulations of the Letter Post Convention are discussed in tandem.

The Commission also provides its view on 1 resolution that concerns the thresholds and average number of items per kilogram to avoid sampling costs for exchanges of mail between designated operators in 2014. This resolution will be considered by POC Committee 3, Physical Services, and establishes rates for letter post items. The Commission views this resolution as consistent with 39 U.S.C. § 3622.

A. UPU Letter Post Convention

- 1. Proposal 25.124.3, Special provisions applicable to each category of items**
- 2. Proposal 25.218.2, Request for payment specific to bulk mail**
- 3. Proposal 25.218.1 Rev 1, Request for payment specific to bulk mail**

Summary. Proposals 25.124.3 and 25.218.2 by Morocco are, in essence, the same. Both increase the thresholds above which a designated postal operator may apply bulk mail terminal dues rates to letter post,¹ hence establishing a rate for First-Class Mail International. The bulk mail mechanism of the terminal dues provisions of the UPU Convention allow a designated postal operator to apply rates with a per item and a per kilogram component, versus solely a per kilogram component, to inbound letter post mail that it receives from one sender in another country. Currently, the volume of this mail must be 1,500 letter post items in one day or 5,000 letter post items over the course of two weeks in order to trigger the bulk mail mechanism. The proposals by Morocco increase these thresholds to 10,000 letter post items and 20,000 letter post items, respectively.

By invoking the bulk mail provisions on lightweight mail pieces, the designated postal operator receiving the mail is able to collect more terminal dues revenue by applying per item and per kilogram bulk mail rates. These provisions were initially introduced to prevent arbitrage within the UPU terminal dues system. More specifically, they were intended to prevent industrialized countries and private mail operators from accessing lower terminal dues rates paid mainly by developing countries for mail delivery in other industrialized countries. A threshold was therefore established above which an industrialized country can request the per item/per kilogram rates paid by all industrialized countries (now called target system countries) for mail from developing countries meeting the bulk mail criteria. Developing countries (now called transition system countries) can also invoke per item/per kilogram rates for lightweight inbound mail from other developing countries and industrialized countries. By charging for the actual number of items, versus a per kilogram rate established by the UPU, developing countries can collect higher terminal dues in order to raise inbound revenue. The higher thresholds proposed by Morocco therefore reduce the amount of mail for which an industrialized (target) or developing (transition) country can apply higher terminal dues rates for lightweight mail sent in bulk from an individual sender.

¹ Within the UPU context, "letter post" refers to letters, flat envelopes, and small packets weighing up to 2 kilograms or 4.4 pounds. Letter post is equivalent to the U.S. Postal Service's inbound and outbound First-Class Mail International product.

Proposal 25.218.1 Rev 1 from Cambodia, China, Iran, Korea (Republic), Malaysia, Nepal, Philippines, Samoa, Singapore, Thailand, and Vietnam is similar to proposals 25.124.3 and 25.218.2 by Morocco. Instead of increasing the threshold for invocation of bulk mail rates from 1,500 to 10,000 letter post items from one sender in one day, this proposal increases it from 1,500 to 5,000 letter post items from one sender in one day. However, unlike the Moroccan proposals which also increase the existing threshold for items received from one sender over the course of two weeks, this proposal eliminates the second threshold completely.

View. The Commission views these proposals as consistent with 39 U.S.C. § 3622. In the case of inbound bulk mail, the Commission considered the reduction in the amount of mail that would be eligible for higher terminal dues rates, particularly given the U.S. Postal Service's low cost coverage on inbound letter post at current UPU terminal dues rates.² However, this proposal appears consistent with the U.S. policy in § 407(a)(2) "to promote and encourage unrestricted and undistorted competition in the provision of international postal services and other international delivery services, except where provision of such services by private companies may be prohibited by law of the United States."

The Commission also considered the impact of these proposals on outbound mail. These proposals would result in less outbound letter mail eligible for higher terminal dues rates in other countries by raising the bulk mail thresholds. The Commission took account of the need for predictability and stability in rates for U.S. mailers and the need to maintain extremely high degrees of reliability and speed of delivery. Outbound mail subject to bulk mail rates may be delayed by the receiving country so that the receiving postal operator can count the actual number of pieces, prepare the accounting forms and await payment from the designated postal operator in the country of origin.

With respect to the elimination of the threshold for application of bulk mail rates to letter post items sent from one sender over the course of two weeks in proposal 25.218.1 Rev 1, absence of such a provision does not alter the analysis set forth above.

4. Proposal 25.137.7 Rev 1, Advice of delivery

Summary. This proposal by Switzerland establishes a rate between designated postal operators for the return of advice of delivery notices (return receipts). An advice of delivery, or return receipt, allows the addressee in a destination country to sign and return a card to the mailer in another country indicating that he or she received the letter mail from the mailer. Currently there is no remuneration among designated postal operators to return advice of delivery notices to the original mailer. The Swiss propose a rate equivalent to the rate for the

² The current contribution for inbound international letter post, or First-Class Mail International is very low, with the U.S. Postal Service reporting a negative contribution of over \$65 million in its FY 2012 Annual Compliance Report. However, the Commission anticipates significant improvements in cost coverage in 2014 to 2017 in light of the new terminal dues structure negotiated at the 2012 UPU Congress in Doha, Qatar.

return of an International Business Reply Service (IBRS) item. Also under the Swiss proposal, both advice of delivery and IBRS items would be included in the current threshold of 1,000 IBRS items per country at which the rates are applied.

View. The Commission views this proposal as consistent with 39 U.S.C. § 3622 as it provides revenue and therefore improves cost coverage for a product where no revenue currently exists to compensate for services rendered.

5. Proposal 25.140.1, International Business Reply Service (IBRS)

Summary. This proposal by Greece adds a charge for the conveyance of IBRS items based on the UPU's transit handling fee and changes the methodology used to calculate the air conveyance charge to a more simplified formula.

View. There is presently insufficient information on this proposal and its financial impact on the U.S. Postal Service. The Commission is therefore unable to make a determination on whether or not this proposal is consistent with 39 U.S.C. § 3622. More information is needed on the impact of the change in methodology on the U.S. Postal Service and the U.S. Postal Service's IBRS costs, which it currently does not report. In its FY 2011 and FY 2012 Annual Compliance Determinations, the Commission asked the U.S. Postal Service to report on the feasibility of providing separately reported costs for IBRS. The Commission notes that if this proposal is put forward for further study in the UPU, the Commission should be able to provide a more fully-informed view at that time.

6. Proposal 25.193.2, Checking of mails

Summary. This proposal by Japan establishes a rate at the level of terminal dues for handling inbound letter post items that are damaged. The terminal dues would compensate the receiving designated operator for "the costs incurred in improving the condition of these items."

View. The Commission has insufficient information at this time to provide its view on whether this proposal is consistent with 39 U.S.C. § 3622. While the principle of charging a rate for a cost incurred is consistent with section 3622, the proposal is not developed sufficiently to make a determination. More specifically, the following points are unclear: whether terminal dues is an appropriate level of remuneration for the cost incurred; what constitutes damage and liability; and what is meant by improving the condition of an item. Accordingly, the Commission suggests that this proposal be deferred for further study by the UPU.

7. Proposal 25.211B.1, Terminal Dues, General Provisions

Summary. This proposal by France pertains to letter post mail handled by postal operators providing postal services outside their national territories. Many national postal operators, particularly in Europe, have the commercial flexibility to compete for postal traffic beyond their borders. In the U.S., for example, where there is no monopoly on outbound international mail,

national postal operators from Belgium, France, Germany, New Zealand, Switzerland, and the United Arab Emirates, among others, compete with the U.S. Postal Service and private delivery operators for U.S. customers' outbound international mail.

Operational confusion can result from mail that contains the U.S. mailer's return address in the U.S. Undeliverable mail in the destination country often gets inadvertently returned by the postal operator in the destination country to the U.S. Postal Service. In this situation, the U.S. Postal Service does not receive postage to handle the mail piece. Currently, postal operators do not receive compensation for the return of undeliverable letter post items for which they did not receive postage.

This proposal by France sets a rate for the U.S. Postal Service and other designated postal operators to collect from a postal operator returning to it undeliverable mail for which it has not collected postage. In this instance, it allows the U.S. Postal Service to collect terminal dues revenue from a postal operator returning a letter post item to the U.S. Postal Service in error because of the U.S. mailer's return address in the U.S. Rather, the postal operator returning the piece should direct it to the postal operator identified in the mail piece's indicia, as this was the postal operator that received postage for and handled the piece coming out of the U.S.

View. The Commission views this proposal as consistent with 39 U.S.C. § 3622. It provides remuneration where none currently exists for the U.S. Postal Service to return undeliverable letter post items to U.S. mailers for which it did not collect postage. Furthermore, it assures adequate revenues for the U.S. Postal Service.

8. Proposal 25.215.1, Quality of service linked terminal dues remuneration between designated operators of countries in the target system

Summary. This proposal set forth by the POC amends the potential terminal dues penalties and bonuses for designated postal operators in the target terminal dues system, including the U.S. Postal Service. These penalties and bonuses are linked to the quality of service they provide for inbound international letter post. A designated operator's quality of service is measured against its domestic delivery standards and a target set by the UPU, which is currently 88 percent for the U.S. Postal Service. This proposal amends the automatic bonus for participation in the quality of service link to terminal dues for the U.S. Postal Service from 2.5 percent to 5 percent. It maintains the penalty for not meeting the quality of service target at 0.33 percent for each percentage point under the target. However, it increases the maximum penalty from 5 percent to 10 percent of its terminal dues rate, resulting in terminal dues remuneration at no less than 95 percent, versus the previous 97.5 percent. The changes in the bonus and penalty structure essentially change terminal dues rates for inbound and outbound First-Class Mail International.

View. The Commission views this proposal as consistent with 39 U.S.C. § 3622. The increase in the automatic bonus for participation in the quality of service link to terminal dues will generate more terminal dues revenue for the U.S. Postal Service for inbound international letter

post and assure adequate revenues for the U.S. Postal Service. At the same time, while the increase in penalties could also potentially cause a greater decrease in terminal dues revenue for the U.S. Postal Service, it serves to maintain high-quality service standards.

9. 25.217.1, Mechanism for revising the rates of terminal dues

10. 25.217.2 Rev 1, Mechanism for revising the rates of terminal dues

Summary. Both proposals address a special provision of the terminal dues system known as the revision mechanism. Proposal 25.217.1 was put forward by the POC, while proposal 25.217.2 Rev 1 was put forward by Australia, Brunei Darussalam, Cambodia, China, Iran, Korea (Republic), Malaysia, Nepal, Philippines, Samoa, Singapore, Thailand, Turkey and Vietnam. Currently, terminal dues between countries in the target system and the transition system, as well as between countries in the transition system, are set on a per kilogram basis. An average number of items per kilogram (IPK) of mail determined by a UPU study on mail flows is used to develop the per kilogram rate. The per kilogram rate allows postal operators to avoid the administrative costs associated with the statistical sampling of mail.³

However, when a transition or target system country believes that its flow of letter post mail to or from a transition country deviates from that worldwide average, such that its IPK is over 17 or below 12, it can invoke the revision mechanism. Mail with an IPK over 17 is generally lighter weight. A transition or target country with inbound mail flows with an IPK over 17 based on statistical sampling could then apply the new IPK to the per item/per kilogram rates and obtain more revenue. Similarly, if a transition country's flow to a target country or another transition country is under 12 IPKs, which is generally heavier weight mail, it can pay the receiving designated postal operator less. However, a target country cannot pay lower terminal dues to a transition country.

This proposal by the POC amends the minimum and maximum IPKs for application of the revision mechanism from 12 and 17 to 10 and 15, respectively. This is because an updated flow study showed that the worldwide average IPK of letter post declined from 14.64 to 12.23. The proposal also seeks to lower the threshold at which the revision mechanism can be applied to a mail flow from 100 tons to 30 tons, thereby making more mail eligible for the revision mechanism.

The proposal by Australia, Brunei Darussalam, Cambodia, et al. would maintain the threshold at which the revision mechanism can be applied at 100 tons, thereby rejecting the POC's proposal to change it to 30 tons. This proposal already incorporates the POC's proposal to amend the thresholds for application of the revision mechanism to 10 IPKs and 15 IPKs, even though these new IPKs have not yet been adopted by the POC.

³ Currently the worldwide average IPK is 14.64 items per kilogram.

View. The Commission finds these proposals consistent with 39 U.S.C. § 3622. Both continue to apply a special provision of the terminal dues system that will allow the U.S. Postal Service to receive higher, more cost-based terminal dues rates from transition countries that more accurately reflect a light-weight mail flow.

With respect to proposal 25.217.2 Rev 1, as previously noted, the thresholds for application of the revision mechanism of 10 and 15 have not yet been adopted by the POC. They were proposed by the POC in proposal 25.217.1 and therefore should not be incorporated into proposal 25.217.2 Rev 1 until formally adopted by the POC. In addition, a threshold of 75 tons for application of the revision mechanism was adopted at the UPU Congress, and should replace the 100 ton threshold in proposal 25.217.2 Rev. 1, paragraphs 1 and 1.4.

11. Proposal 35.129.91, Merchandise return service for the original seller

Summary. This proposal by the Netherlands establishes a bilateral merchandise return service for the acceptance of prepaid return parcels. The proposal also establishes rates in the Detailed Regulations of the greater of 85 percent of the designated operator's inward land rates or 2.85 Special Drawing Rights (SDR) (approximately \$4.32) per item and .28 SDR (approximately \$0.42) per kilogram. It is not clear whether these rates would be required in a bilateral agreement.

View. As indicated in its views provided to the Department of State on September 12, 2012, the Commission finds this proposal to be inconsistent with 39 U.S.C. § 3622.

Resolution on the thresholds and average number of items per kilogram to avoid sampling costs for exchanges of mail between designated operators in 2014 (POC 3, Physical Services)

Summary. In 2012, the UPU Congress decided that designated operators in the terminal dues target system will be required to separate their mail by format (letters, large envelopes and small packets up to 4 pounds) starting in 2014. Designated operators in the transition system may separate their mail by format on an optional basis into two categories, letters/large envelopes and small packets.

Article RL 221.1 of the UPU Letter Post Regulations sets a threshold, currently 30 tons, under which designated operators that entered the target system in 2008, which includes the U.S. Postal Service, may agree that it is not cost-effective to statistically sample their mail in order to apply rates with a per item and per kilogram component. Rather, they may apply a per kilogram weight using the worldwide average number of IPKs of mail as determined by a UPU study of global mail flows in 2010.

This proposal prescribes that separate IPKs from the same study will be used for letters, large envelopes and packets instead of one IPK that applies to all shapes. Furthermore, the proposal

maintains the threshold of 30 tons for bilateral agreements to eliminate sampling of mail flows between target system countries. For the exchange of mail with designated operators that entered the target system in 2010 and 2012, the proposal raises this threshold to 75 tons. The IPKs applied ultimately determine the separate rates paid for letters, large envelopes and packets.

View. The Commission views this proposal as consistent with 39 U.S.C. § 3622. It provides for more cost-based revenue for the U.S. Postal Service for inbound letter mail by basing rates on the weights of letters, large envelopes and small packets as three separate categories, versus one rate that applies to all three formats.

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