

Before the
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Competitive Product Prices
Inbound Direct Entry Contracts
With Foreign Postal Administrations

Docket No. MC2008-6

Competitive Product Prices
Inbound Direct Entry Contract (MC2008-6)
China Post Group

Docket No. CP2008-14

Competitive Product Prices
Inbound Direct Entry Contract (MC2008-6)
Hong Kong Post

Docket No. CP2008-15

PUBLIC REPRESENTATIVE COMMENTS
IN RESPONSE TO UNITED STATES POSTAL SERVICE
REQUEST TO ADD INBOUND DIRECT ENTRY CONTRACTS WITH FOREIGN
POSTAL ADMINISTRATIONS TO THE COMPETITIVE PRODUCTS LIST

(August 26, 2008)

In response to Order No. 97, the Public Representative hereby comments on the Request of the United States Postal Service to add Inbound Direct Entry Contracts with Foreign Postal Administrations to the Competitive Products List (Request), assigned Docket Nos. MC2008-6, CP2008-14 and CP2008-15. The Public Representative has had access to, and reviewed, the United States Postal Service's Governors' Decision on Establishment of Prices and Classifications for Inbound Direct Entry Contracts with Foreign Postal Administrations (Governors' Decision No. 08-6) in its original (not redacted) version, and the additional materials submitted under seal. To the Postal Service's credit, this Request provides more data than previous requests; it justifies the

confidentiality of several aspects of the contracts and the accompanying materials. The pricing shell and individual pricing for these contracts enable them to cover their attributable costs, enable competitive products as a whole to cover their costs, and contribute a minimum of 5.5 percent to the Postal Service's total institutional costs.¹ They both appear to be functional equivalents that are squarely within the bounds of Governors' Decision No. 08-6. However, the Commission has not yet approved "inbound direct entry contracts" (IDECs) for the Mail Classification Schedule (MCS). IDECs raise mail classification questions for the Commission which these Comments will identify and queue up for consideration.

The Public Representative must note respectfully that Order No. 97 did not appear in the *Federal Register* until Friday, August 22.² If any member of the public were relying only on the *Federal Register* (instead of the Commission's website, where Orders are posted upon issuance) this afforded only three business days in which to file a timely response. Accordingly, the Commission may wish to consider accepting comments filed after the deadline, and/or reminding the public that they can access any Commission Orders consulting the Commission website, (www.prc.gov) daily at the close of business.

¹ 39 U.S.C. 3633(a) and 39 C.F.R. §3015.7.

² 73 FR 164 (August 22, 2008) at 49723-4

Confidentiality

Order No. 97 was issued the same day as the Commission's Notice of Proposed Rulemaking to Establish a Procedure for According Appropriate Confidentiality (Order 96, August 13, 2008). The new Commission rules amending title 39 of the Code of Federal Regulations (Part 3307 – Treatment of Non-public Information provided by the Postal Service) should establish a clear outline for future requests from the Postal Service. This is welcome news for all interested parties. While these rules await *Federal Register* publication, commentary, replies and publication of the final rules, the guidelines in place in 39 U.S.C. 504(g) are effective³.

The Postal Service Request contains a rationale for maintaining confidentiality concerning pricing, processes which enable discounted pricing, the attendant formulae and other contractual terms which are matters of commercial sensitivity.⁴ Even this minimal explanation is helpful for a public reviewing a matter in which many of the essential terms are withheld from view. The Public Representative has previously recommended that “the Postal Service, as proponent, should justify the specific limits of

³ The Postal Service makes an initial determination on information which is exempt from public disclosure under § 410(c) or 5 USC 552(b). The Commission then shall balance risk of commercial injury to the Postal Service against the public interest in transparency, and make its own determination.

⁴ Postal Service Request, at 2-3.

all such confidentiality requests, if simply to permit identification of, and distinction between, confidential agreements.”⁵ Here, the Postal Service has done so.

Governors’ Decision 08-6

The Governors’ Decision establishes new shell pricing not of general applicability and changes in classification to enable these IDECs. After reviewing the documents under seal, one might note that the Governors’ vote on the shell pricing was unanimously in favor. While a simple majority would suffice for approval of a rate change, the fact that no Governor opposed implementation of this contract formula inspires confidence.

The Statement of Supporting Justification⁶ notes, “[T]he contracts are premised on the offering of prices at a level that provides sufficient incentive for customers to ship specified volumes with the Postal Service rather than a competitor.” Removing costs from the system benefits everyone – not just the parties – because it brings or increases efficiency. This enhancement would seem to be the type of opportunity Congress envisioned when it provided flexibility for competitive product pricing in the PAEA.

⁵ *E.g.*, Docket No. MC2008-5, Public Representative Comments (July 31, 2008), at 3.

⁶ Postal Service Request, Attachment 2, at 4.

Pricing, Cost Coverage and Contribution

The Public Representative acknowledges that the pricing in these IDECs with foreign postal administrations comports with pricing, cost coverage and contribution provisions of title 39. In addition to having the mailer prepare mailings for less costly handling by the Postal Service, the IDECs provide for shipment to specified entry points, minimum volume requirements for shippers, sack handling fees, and stipulate that First-Class and Priority Mail parcels will be subject to the published rates offered to domestic customers. These factors promote the value of these agreements to the Postal Service throughout the one-year life of the contracts.

The pricing agreed to in these contracts appears to generate sufficient revenue to cover attributable costs for this inbound direct entry service, enable competitive products as a whole to cover their costs, and contribute a minimum of 5.5 percent to the Postal Service's total institutional costs.⁷

The Specific Agreements are Functionally Equivalent

The Postal Service persuasively reasons⁸ that the proposed contracts with China Post Group and Hong Kong Post are functionally equivalent. The agreements are both with foreign postal administrations, they cover the same underlying services, and they share the same cost and market characteristics. The foreign postal administrations

⁷ 39 C.F.R. § 3015.7(c).

⁸ Postal Service Request, at 5-6.

have agreed to pre-label parcels, use Postal Service Global Shipping software and tender sacks of mail for direct entry⁹ into the domestic mailstream. The domestic postal products offered in both of the contracts are the same, and published domestic prices are charged for the products from the point of entry. The Postal Service notes, "... [T]he operative distinction of Inbound Direct Entry Contracts with Foreign Postal Administrations is the sack handling activity for which a new fee would be charged."¹⁰ Both contracts are within the boundaries of the shell pricing approved by the Governors' Decision 08-06. The Public Representative would agree that the two contracts are functional equivalents and that both comply with the requirements of title 39 for competitive products. The wrinkle in this otherwise seamless tapestry is the inclusion of inbound First-Class parcels. Although the contracts and the Statement of Supporting Justification note that inbound First-Class Mail parcels would be subject to the published rates offered to domestic customers, inbound First-Class Mail has been heretofore classified as a Market Dominant Product.

Inbound Direct Entry Contracts: Competitive?

Inbound Direct Entry Contracts with Foreign Postal Administrations were proposed in Docket No. RM2007-1 as an addition to the Mail Classification Schedule (MCS) by the Postal Service in its Submission of Additional Mail Classification Schedule

⁹ "Direct entry" after the parcels clear U.S. Customs; see Postal Service Request at 5.

¹⁰ Postal Service Request, Attachment 2, at 4.

Information in Response to Order No. 43, November 20, 2007.(See “Mail Classification Schedule,” 2001 Competitive Product Descriptions, 2612 Inbound Direct Entry Contracts with Foreign Postal Administrations). The proposed MCS language for the Inbound Direct Entry Contracts with Foreign Postal Administrations, included as Attachment A to the Governors’ Decision, contains many of the same provisions that were included in the Postal Service’s original proposed MCS language for IDECs with Foreign Postal Administrations. However, the MCS is authorized and maintained by the Commission. Merely asserting a classification before the Commission does not make it so. Furthermore, “Finding the classification changes reasonable does not bind the Commission to the Postal Service’s determinations on products and services.”¹¹

While the public would likely have little interest in the categorizing of a particular product as long the product covers its costs and is not subsidized by the mailing public, there *is* a public interest in resisting arbitrary changes. As Order 26 Proposing Regulations to Establish a System of Ratemaking (August 15, 2007) noted,

[3007] Commission maintenance of the mail classification schedule does not deprive the Governors of any flexibility to change rates or classes or offer new products. It does, however, assure non-discriminatory service and transparency in a manner contemplated by the statute.¹²

¹¹ Docket CP 2008-3, PRC Order No. 70, April 10, 2008, at 24.

¹² PRC Order No.26, Proposing Regulations to Establish a System of Ratemaking, August 15, 2007, at 49.

Order 26 went on to stipulate “International Customized Mailing Agreements (ICMs), which are mailer-specific agreements subject to minimum revenue or quantity requirements (IMM § 297)”, fall within the competitive products category.¹³ Order 26 also observed, “There is, however, some controversy over the characterization of the remaining international mail services.”¹⁴

The Office of the Consumer Advocate (OCA) suggested that, while each ICM should be categorized as a “product,” it cautioned that:

[I]f an ICMA arrangement involves International Surface Air Lift, the ICMA should be regarded as a competitive product. If, however, an ICMA involves certain single-piece international mail, such as Air Parcels, the ICMA should be regarded as a market-dominant product.”¹⁵

The Commission also found that:

. . . [E]ven if *shipments received by* the Postal Service from foreign posts are construed as *shipments by* the Postal Service, there may be good reason to view such inbound mail as market dominant. The record is not sufficiently developed to enable the Commission to determine what inbound international mail is appropriately classified as “bulk international” and, therefore, a competitive product.(emphasis in original)¹⁶

¹³ *Id.* at 52-3.

¹⁴ *Id.* at 53.

¹⁵ Docket RM2007-1 OCA Comments, June 18, 2007, at 56-57.

¹⁶ PRC Order 26 at 55-6.

IDECs are hybrids. While their provisions mostly regard competitive products, they include inbound First-Class Mail, a market dominant product. Nevertheless, these contracts fall within the rubric of ICMs. Like ICMs, IDECs are arguably products, and there are but two categories of postal products: Market Dominant and Competitive.

Order 26 foresaw this dilemma:

[3021] Regarding inbound international mail, there are two issues. First, the demarcation between bulk and single-piece international mail is less clear.

and:

[3022] Second, it is not apparent that classifying any inbound international mail as a competitive product has the same significance it does for outbound mail.¹⁷

In Attachment A, the description of IDECs notes that “Minimum volume requirements are set by the Postal Service.”¹⁸ However, it is not clear that these requirements would apply to the inbound First-Class parcels. If they were to, this would suggest that IDECs might be seen as a subset of ICMs, and the bulk inbound First-Class parcels could then be categorized as competitive, rather than market dominant.¹⁹ Title 39, section 3622(b)(9) notes that the distinction between market dominant and competitive products should enable allocation of “the total institutional costs of the

¹⁷ PRC Order 26, (both) at 55.

¹⁸ Postal Service Request, Attachment A, at 4 (of 8).

¹⁹ PRC Order 26, at 52-3.

Postal Service appropriately between market-dominant and competitive products.

Section 3622 also instructs the Commission to concurrently “reduce the administrative burden and increase the transparency of the ratemaking process.”²⁰

Title 39 also suggests (at section 3642 (c)) that transfers between market dominant and the competitive product categories may be warranted when transfers “involve only some (but not all) of the subclasses or other subordinate units of the class of mail or type of postal service involved (without regard to satisfaction of minimum quantity requirements standing alone).” The Commission can make such a change upon request or of its own volition.²¹

Accordingly, the Commission can opt to categorize IDECs as competitive products.

Practical Considerations

In November 2007 the Postal Service noted that it had bilateral contracts for outbound and inbound direct entry mailings with foreign postal administrations.²² This practice predated the Postal Accountability and Enhancement Act (PAEA). The Postal

²⁰ 39 USC 3622(b)(6).

²¹ Section 3642(a).

²² Docket RM2007-1 Postal Service Submission of Additional Mail Classification Schedule Information in Response to Order No. 43, November 20, 2007, at 13.

Service also acknowledged numerous contracts with international entities that would fall within five broad categories (“baskets”). Prior to passage of the PAEA, such contracts would not receive scrutiny from the Commission. Now, before implementation, they must seek approval from the Commission – a “preview.” The Commission can later monitor these contracts’ compliance with title 39 in the Annual Compliance Determination – a “review.” Ultimately, the Commission reserves the right to revisit any of its determinations – a potential “three-view.” This increased transparency fulfills the spirit of the PAEA.

Examination of the nature of inbound First-Class Mail within IDECs is not a mere exercise in sophrosyne; market dominant products’ and competitive products’ revenues are now segregated and subject to very different requirements of our underlying organic statute, title 39 as amended by the PAEA.

The Postal Service certified (Attachment D) that:

In Fiscal Year 2007, all outbound international competitive mail accounted for approximately 11 percent of the total contribution by all competitive products. Contribution from Inbound Direct Entry Contracts with Foreign Postal Administrations should be much smaller.

Inbound First-Class Mail comprises only one component – a fraction -- of the IDECs. The IDECs appear generally to display the characteristics of a competitive product. One might say they are predominantly competitive in nature. To paraphrase a maxim attributed to (recent stamp subject and fortieth United States President) Ronald Reagan, “an 80% competitive product is not a 20% market dominant product.”

Conclusion

The statutory threshold for competitive products is a bright line: each must generate sufficient revenue to cover its attributable costs, enable competitive products as a whole to cover their costs, and contribute a minimum of 5.5 percent to the Postal Service's total institutional costs.²³ These Inbound Direct Entry Contracts with Foreign Postal Administrations would appear to meet all three aspects of that standard.

The Public Representative respectfully submits the preceding Comments for the Commission's consideration.

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²³ 39 C.F.R. § 3015.7(c).