

JOINT DISSENT OF ACTING CHAIRMAN ROBERT G. TAUB
AND VICE CHAIRMAN TONY L. HAMMOND

I. INTRODUCTION

We dissent from today's Order. We find that it contradicts established Commission precedent, conflicts with the reality of the marketplace, and will work to the detriment of both the Postal Service and its competitors.

To begin, according to the Order, it is unclear whether UPS and FedEx compete with the Postal Service to deliver parcels. In reply, it would be enough to observe that scarcely anyone who sends a parcel in this country is unaware that there are two major carriers besides the Postal Service ready to deliver it. The competition is obvious.

Perhaps for this reason, the Order implies that the Commission could have been persuaded otherwise, if not for the alleged inadequacy of the Postal Service's evidence. In fact, the Postal Service has thrice appeared before this Commission with the very same evidence, and thrice has the Commission found it sufficient. The Order does not explain why the same evidence is now found wanting.

As a result of today's decision, the Postal Service could lose more than \$100 million in annual revenue, with future losses potentially higher.¹ Equally important, the Postal Service's competitors could face a market that is potentially distorted by an artificially underpriced product.

¹ Approval of the Postal Service's request in this docket would have resulted in implementation of the price change conditionally granted in Docket No. CP2015-33. Based on the calculations and assumptions set forth in the Postal Service's most recent market dominant rate case, implementing that change would have resulted in approximately \$108.2 million of additional annual revenue. See *infra* n.37.

II. REVIEW OF EVIDENCE

A. Docket No. MC2015-7

As noted in the Order, there are two steps to the Commission's section 3642(b)(1) inquiry: (1) market definition, and (2) market power. The Postal Service seeks to satisfy the Commission's market definition assessment by identifying the UPS and FedEx products that, like First-Class Mail Parcels, provide two- to three-day air and ground service. In particular, the Postal Service identifies UPS's 2nd Day Air, 3-Day Select, and Ground products, and FedEx's One Rate, 2-Day, Express Saver, Ground, and Home Delivery products.²

To satisfy the Commission's market power assessment, the Postal Service submits market share estimates sourced from the Colography Group.³ In response to a Chairman's Information Request, it also provides a list of its own prices and, for comparison, the lowest comparable price available from UPS and FedEx.⁴ As illustrated below, this evidence mirrors the evidence the Postal Service brought in each of the past three parcel reclassification cases.

B. Docket No. MC2010-36

To be specific, in its Docket No. MC2010-36 request to reclassify commercial Standard Mail Parcels, the Postal Service sought to satisfy the Commission's market

² Docket No. MC2015-7, Request of the United States Postal Service to Transfer First-Class Mail Parcels to the Competitive Product List, November 14, 2014 (Request), Attachment B at 6.

³ *Id.* at 4.

⁴ Docket No. MC2015-7, Response of the United States Postal Service to Chairman's Information Request No. 1, Question 3, December 16, 2014 (Response to CHIR No. 1).

definition assessment by identifying UPS and FedEx as its primary competitors.⁵ Unlike here, the Postal Service did not show that the UPS and FedEx products provide delivery within the same number of days as the postal product. Nonetheless, the Commission found the Postal Service's evidence sufficient, stating that "UPS and FedEx are formidable competitors for delivery of this product."⁶

To satisfy the Commission's market power assessment, the Postal Service submitted market share estimates sourced from the Colography Group, as well as a comparison of Postal Service, UPS, and FedEx prices.⁷ Relying on this evidence, the Commission found that the Postal Service did not exercise market power, stating that the Postal Service "has *amply demonstrated* there is at least a risk of losing a substantial amount of business if its rates are raised significantly or if it alters its service."⁸

C. Docket No. MC2011-22

Similarly, in its Docket No. MC2011-22 request to reclassify commercial First-Class Mail Parcels, the Postal Service sought to satisfy the Commission's market definition assessment by identifying UPS and FedEx's ground and two-to-three day air

⁵ Docket No. MC2010-36, Responses of the United States Postal Service to Questions 1-2, 5-11 of Commission's Information Request No. 1, December 15, 2010, Attachment A (Standard Mail Parcels Request), at 9-10. While the Postal Service's original request was filed on August 16, 2010, it filed a revised request, cited above, on December 15, 2010, in response to Commission's Information Request No. 1.

⁶ Docket No. MC2010-36, Order Conditionally Granting Request to Transfer Commercial Standard Mail Parcels to the Competitive Product List, March 2, 2011 (Order No. 689), at 16.

⁷ Standard Mail Parcels Request at 4-6.

⁸ Order No. 689 at 16 (emphasis added). *See also id.* at 15 (stating that "section 3642(b) provides that when there is a risk of losing a significant level of business to other firms offering similar products, a product (or subordinate unit) will not be classified as market dominant. *The record demonstrates that such risk exists*") (emphasis added).

services, as well as various consolidator ground services, as its competition.⁹ The Commission again found this sufficient.¹⁰

To satisfy the Commission's market power assessment, the Postal Service submitted market share estimates sourced from the Colography Group.¹¹ Unlike here, the Postal Service did not submit price comparisons.¹² Relying specifically on the market share estimates, the Commission found that the Postal Service did not exercise market power, stating that "[t]hese market shares indicate the presence of significant competition in the marketplace."¹³ Notably, the Postal Service's estimated market share there was greater than its estimated market share in the case now before the Commission.

D. Docket No. MC2012-13

Finally, in its Docket No. MC2012-13 request to reclassify Parcel Post, the Postal Service sought to satisfy the Commission's market definition assessment by identifying UPS and FedEx as its primary competitors.¹⁴ As before, the Commission found this sufficient.¹⁵

⁹ Docket No. MC2011-22, Request of the United States Postal Service Under Section 3642, February 24, 2011 (Commercial First-Class Mail Parcels Request), Attachment B at 8.

¹⁰ Docket No. MC2011-22, Order Adding Lightweight Commercial Parcels to the Competitive Product List, April 6, 2011 (Order No. 710). Nowhere in the order did the Commission question the validity of the Postal Service's market definition.

¹¹ Commercial First-Class Mail Parcels Request, Attachment B at 4.

¹² The Postal Service stated that it was unable to obtain prices for consolidator ground services, because they are non-public. It nonetheless did not submit UPS and FedEx prices, which are public.

¹³ Order No. 710 at 6.

¹⁴ Docket No. MC2012-13, Request of the United States Postal Service to Transfer Parcel Post to the Competitive Product List, April 26, 2012 (Parcel Post Request), Attachment B at 7.

¹⁵ Docket No. MC2012-13, Order Conditionally Granting Request to Transfer Parcel Post to the Competitive Product List, July 20, 2012 (Order No. 1411). As in Order No. 710, the Commission accepted the Postal Service's market definition without further analysis.

To satisfy the Commission's market power assessment, the Postal Service submitted market share estimates sourced from the Colography Group and noted the average difference between its prices and UPS and FedEx prices.¹⁶ Relying on this evidence, the Commission found that the Postal Service did not exercise market power, going so far as to pronounce that "[t]he parcel delivery market is competitive," and that "UPS and FedEx are the dominant carriers."¹⁷

E. Summary

Proceeding forward from the past parcel reclassification cases, one would expect that the Commission would require less evidence for new parcel cases, not more, because it has already concluded that the parcel delivery market is competitive, and it has already concluded that UPS and FedEx compete with the Postal Service to deliver parcels. The Commission has made these findings for lightweight parcels as well as heavy parcels, and for commercial parcels as well as retail parcels. The jurisprudence is consistent and decisive.

Moreover, both the commercial and international equivalents of First-Class Mail Parcels have been reclassified competitive, meaning that most of the elements of the statutory analysis have already been resolved.¹⁸ Therefore, at the very least, presenting the same evidence that the Commission accepted in previous cases, as the Postal Service has done here, should suffice to satisfy the evidentiary burden.

¹⁶ Parcel Post Request, Attachment B at 5.

¹⁷ Order No. 1411 at 6.

¹⁸ For the commercial equivalent, see Order No. 710, *supra* n.10. For the international equivalent, see Docket No. MC2012-44, Order Approving Request for Product List Transfer, September 10, 2012 (Order No. 1461).

III. APPLICABILITY OF ORDER NO. 2306

The Order includes an extensive enumeration of the types of evidence the Postal Service would need to produce to prove that UPS and FedEx compete with it. This represents a dramatic expansion of the evidentiary standard applied in the previous parcel reclassification cases. The Order does not explain what precipitated this expansion, and it does not acknowledge that the previous cases applied a different standard. The only precedent it does cite is Order No. 2306 from Docket No. MC2013-57,¹⁹ a non-parcel case. To the extent that today's Order relies on Order No. 2306 to justify setting aside the Commission's established evidentiary standard for parcel cases, its reliance is unfounded, for two reasons.

First, Docket No. MC2013-57 required the Commission to step outside its traditional area of expertise and consider a market defined more broadly than traditional physical delivery services. In that case, the Postal Service sought to have its round-trip DVD mailer product classified as competitive, based on the existence of a broader entertainment delivery market. To consider the Postal Service's request, the Commission had to assess whether electronic streaming and kiosk-based vending compete with round-trip DVD mail service. Because the Commission lacked experience in the industries comprising the broader entertainment delivery market, it required more evidence from the Postal Service than it had in any other section 3642 case. Order No. 2306 neither stated nor implied that the Commission was thereby establishing a new evidentiary standard for all subsequent section 3642 cases.

Rather, the Commission's practice has always been to apply differing evidentiary standards for different types of section 3642 cases. For proof of this, one need look no further than the issuance earlier this month of Order No. 2639, which approved Competitive International Merchandise Return Service pursuant to a section 3642

¹⁹ Docket Nos. MC2013-57 and CP2013-75, Order Denying Request, December 23, 2014 (Order No. 2306).

analysis.²⁰ Coming over seven months after the issuance of Order No. 2306, Order No. 2639 applied an evidentiary standard that was not just lower than the Order No. 2306 standard, but also lower than the standard applied in the prior parcel reclassification cases. The Commission accepted the Postal Service's assertion of a competitive market on its face, without requiring any evidence, by relying on the Commission's own expertise in such matters.²¹

The second reason that the Order's reliance on Order No. 2306 is unfounded is that Order No. 2306 was issued over a month after the Postal Service filed the instant request. Thus, to deny the request based on Order No. 2306 is to require of the Postal Service the impossible: anticipate a new evidentiary standard before the Commission has articulated it. The Postal Service visibly tailored its request in this case to the evidentiary standard that the Commission consistently applied in the preceding parcel reclassification cases. If the Commission is to change that standard in the middle of an ongoing proceeding, it should notice the public of the change and provide a reasonable opportunity to comment, rather than outright deny the request.

IV. STATUTORY ANALYSIS BASED ON RECORD EVIDENCE

A. Introduction

We have demonstrated above that the Order fails to engage with established Commission precedent in parcel reclassification cases. But more generally, the Order also fails to acknowledge the plain reality of today's marketplace. A First-Class Mail Parcel is a parcel weighing thirteen ounces or under.²² Anyone can walk into a UPS

²⁰ Docket Nos. MC2015-68 and CP2015-99, Order Conditionally Approving Addition of Competitive International Merchandise Return Service Agreements with Foreign Postal Operators (IMRS-FPO) to the Competitive Product List, August 4, 2015 (Order No. 2639).

²¹ *Id.*

²² Mail Classification Schedule 1120.1 (with revisions through August 3, 2015).

Store and send such a parcel to anywhere in the United States. This is known. Anyone can walk into a FedEx Office Print & Ship Center and do the same. This too is known. Anyone can take the same parcel to a third-party shipping store and choose at once from various carriers' shipping options. This, as well, is known.

Yet the implication of today's Order is that the Commission, an expert body specifically designated by Congress to decide such issues, is prevented from reaching these conclusions on its own, unless it is presented with the extensive evidence outlined in the Order, such as "expert testimony, special studies, academic research, industry papers, or other calculations and estimates." The Commission should not circumscribe its own authority in this manner.

Nonetheless, for the sake of completeness, we demonstrate below that the Commission's statutory analysis for reclassification is satisfied by record evidence alone, even without applying the Commission's considerable expertise in these matters.²³

B. Section 3642(b)(1)

As noted previously, the two steps of the Commission's section 3642(b)(1) inquiry are market definition and market power. To define the market, the Postal Service has identified several UPS and FedEx products that provide the same two-to-three day air and ground service that is provided by First-Class Mail Parcels.²⁴ Although the various products include different added features and enhancements, the record shows that they all accomplish the same basic function: transport a lightweight parcel from induction by a retail customer to a specific address. Therefore they are, to

²³ Our analysis focuses on the Single-Piece category of First-Class Mail Parcels and leaves aside for now the Keys and Identification Devices category, because the latter comprises a minor portion of the overall product's volume. A Commission order approving reclassification of First-Class Mail Parcels could well exclude the Keys and Identification Devices category from reclassification.

²⁴ Request, Attachment B at 6.

use the Order's framing, reasonably interchangeable, and as a consequence they serve the same market.

While certain parties have advocated segmenting the market based on geography (specifically, by separating out rural customers), the statute does not impose such segmentation for other competitive products, such as Priority Mail and Express Mail, and neither did the Commission do so when it reclassified the retail-focused Parcel Post product. The parties have not provided any compelling justification for overturning the statute's and the Commission's unified geographic framework.²⁵

Turning to market power, the Commission, like the Department of Justice and the Federal Trade Commission, applies its market power price test based on competitive price levels.²⁶ While it is difficult to determine the competitive price levels with precision, record evidence clarifies their approximate position relative to current prices. The Postal Service lists its First-Class Mail Parcels prices as varying between \$2.32 and \$4.12, based on ounce increment.²⁷ It also states that the lowest private sector price is UPS's \$6.24, followed by FedEx's \$7.50.²⁸ That UPS and FedEx's prices are fairly

²⁵ Moreover, segmentation is not practical. Rural areas exist in every state, in some cases not far from urban areas. Geographic segmentation would require the Postal Service to first classify each post office as urban or rural, and then offer different products and prices based on each post office's designation. It could also require the Postal Service to classify each delivery point as either urban or rural and then assess postage differently based on such classification.

²⁶ See, e.g., Order No. 689. In reclassifying Standard Mail Parcels, the Commission looked past the product's then current prices when applying the market power test because they were artificially low due to regulation, stating that "[a]ny pricing power the Postal Service may enjoy is illusory based on its pricing under one-pound parcels below cost." *Id.* at 16. See also Commentary on the Horizontal Merger Guidelines, United States Department of Justice and the Federal Trade Commission, March 2006, at 1 ("[i]n the context of sellers of goods or services, 'market power' may be defined as the ability profitably to maintain prices above competitive levels for a significant period of time"); and ABA Section of Antitrust Law, Market Power Handbook: Competition Law and Economic Foundations, 2nd Ed., 2012, at 2 ("[e]conomists typically define market power by focusing on the ability to raise price relative to the competitive price level, rather than the current price level").

²⁷ Response to CHIR No. 1, *supra* n.4.

²⁸ *Id.*

close to each other, and far from the Postal Service's prices, indicates that the competitive price levels are significantly higher than current Postal Service prices.²⁹

As for how much higher, using the prices listed above, First-Class Mail Parcels prices would have to be raised between 51 and 169 percent to reach the nearest competitor price. Even if one were to step back from this and very conservatively estimate that a 25 percent price increase would reach competitive levels, section 3642(b)(1) would still be satisfied. That is because there is evidence in the record that an 11 percent price increase already led to a 6.4 percent volume decline,³⁰ and that this decline occurred at a time when the overall parcel market expanded.³¹ In light of these facts, if one were to raise First-Class Mail Parcels prices beyond 25 percent during a time when the market remains constant, there would at the very least be a risk of loss of a significant level of business to competitors.

C. Section 3642(b)(2)

Turning to section 3642(b)(2), the letter monopoly exclusion does not apply to First-Class Mail Parcels. The record shows that First-Class Mail Parcels are largely used for merchandise and do not contain letter content.³² To the extent that a small number of such parcels do contain letters, they will be covered by the section 601(b)(1) exception.

The parties engage in an extensive debate over whether the Postal Service may avail itself of the section 601(b)(1) exception to section 3642(b)(2). This debate

²⁹ Another reason that the Postal Service's prices cannot be taken as indicative of competitive levels is that they are a function of the regulatory framework set forth in section 3622. That framework has specific regulatory goals, none of which is to approximate competitive prices.

³⁰ Docket No. MC2015-7, Comments of GameFly, Inc., December 17, 2014, at 7.

³¹ Docket No. MC2015-7, Reply Comments of the United States Postal Service, January 7, 2015, at 8-9.

³² Request, Attachment B at 4-6.

obscures the rather straightforward legislative intent behind section 3642(b)(2)'s letter monopoly exclusion, which is to ensure that products commonly considered letters remain covered by market dominant regulation irrespective of the presence or absence of market power. The converse of this is equally self-evident: the letter monopoly exclusion was not intended to bar the reclassification of products that are not considered letters. Put another way, it was not meant to become a trap door for parcels.

The Commission has repeatedly accepted the Postal Service's reliance on section 601(b)(1) – in two domestic parcel cases (Docket Nos. MC2011-28 and MC2012-13), in one international parcel case (Docket No. MC2014-28), in the lengthy series of bilateral agreements with foreign postal operators cited by the Postal Service, and more recently in Docket No. MC2015-68. One party objects to this precedent, but it fails to bring a compelling reason to reverse it. The statutory scheme whereby the section 601 exceptions are incorporated into section 3642(b)(2) is ambiguous, and the Commission's established precedent on how to apply section 601(b)(1) remains the most reasonable approach to interpreting the statutory scheme.³³

As a practical matter, even if the Commission were to reverse its section 601(b)(1) precedent, the reclassification could still proceed merely by adding a letter prohibition to the product, an approach that the Postal Service has taken in the past with certain other parcel reclassifications.³⁴

³³ As a result of the Postal Accountability and Enhancement Act of 2006 (PAEA), the Postal Service no longer has authority to issue regulations interpreting or defining the letter monopoly. The Commission now has the authority to promulgate such regulations. See 39 U.S.C. § 601(c).

³⁴ See Standard Mail Parcels Request, *supra* n.5; Commercial First-Class Mail Parcels Request, *supra* n.9.

D. Section 3642(b)(3)

Section 3642(b)(3) sets forth three additional considerations: (1) the availability and nature of enterprises in the private sector engaged in the delivery of the product involved; (2) the views of those who use the product involved on the appropriateness of the proposed action; and (3) the likely impact of the proposed action on small business concerns. The Commission subsumes the first of these considerations into its section 3642(b)(1) analysis. As for the second and third considerations, the views of individual and small business customers, the record indicates that customers have concerns regarding price, rural effects, and service performance reporting.

These concerns are similar in nature and magnitude to the concerns raised in prior parcel reclassification dockets. Reclassifications necessarily implicate pricing issues, and they alter service performance reporting as a matter of course. Regarding rural effects, the Postal Service has not implemented rural surcharges following any of the previous parcel reclassification cases, and it has stated that it will not do so for First-Class Mail Parcels either.³⁵ Similarly, it has not curtailed rural customers' access to reclassified parcels or the service reach of those parcels. Thus, as the Commission found in the prior cases, these concerns do not rise to the level necessary to bar the reclassification.

E. Section 3633

Section 3633 requires that a product being added to the competitive list cover its attributable costs, contribute to institutional costs, and not cause market dominant products to subsidize competitive products. In FY 2014, the cost coverage for First-Class Mail Parcels was 109.3 percent, and the cost coverage for First-Class

³⁵ Request, Attachment B at 7.

Package Service was 126.6 percent.³⁶ Because First-Class Mail Parcels would be subsumed into First-Class Package Service, and in light of the price change that would take effect upon reclassification, the resultant product should continue to cover attributable costs, and competitive products should continue to contribute at least 5.5 percent of institutional costs. It follows from this that competitive products would not be subsidized by market dominant products. Accordingly, the reclassification would not result in a violation of section 3633(a).

V. CONCLUSION

We have shown above that the Order contravenes established Commission precedent on the evidentiary standard for parcel reclassification cases without articulating a justification for doing so. We have also shown that there is sufficient evidence on the record to satisfy the Commission's statutory reclassification analysis. All that remains is to note the troubling real-world effects the Order may have.

First, the Postal Service could lose more than \$100 million in revenue annually, at a time when its continued viability necessitates that it collect all the revenue to which it is legally entitled.³⁷ This amount would likely rise in future years, given the nature of the competitive pricing framework.

Second, the Postal Service's competitors will have to continue competing in a market that could potentially be distorted by an artificially underpriced product. One of

³⁶ Financial Analysis of United States Postal Service Financial Results and 10-K Statement 2014, at 73.

³⁷ This figure is based on the calculations and assumptions set forth in the Postal Service's most recent market dominant price change. See Docket No. R2015-4, Library Reference USPS-LR-R2015-4/1 – First-Class Mail Workpapers, January 15, 2015. Substituting the price change conditionally granted in Docket No. CP2015-33 into the Docket No. R2015-4 workpapers yields additional annual revenue of \$108.2 million. While it is impossible to forecast the revenue effect of today's denial with precision (because the Docket No. R2015-4 assumptions have likely changed by now and because volume responses are unpredictable), this calculation demonstrates the order of magnitude that is at stake – more than \$100 million annually.

the purposes of the PAEA is to ensure that the Postal Service does not undercut its competitors by improperly leveraging a network paid for by monopoly products. The Act's primary safeguard for ensuring this is section 3633, pursuant to which the Postal Service's competitive products must pay a fair share of the cost of the postal network. Section 3633 assumes that products are properly classified on the market dominant and competitive lists; if they are not, then the provision cannot achieve its intended purpose.

Here, by leaving First-Class Mail Parcels market dominant, the Order permits the product to be priced without regard to the cost of the postal network – right now, the product just barely covers its attributable costs, whereas the postal network is an institutional cost. In contrast, when the Postal Service's competitors price their products, they generally must begin at a price floor that covers both attributable and institutional costs if they are to remain profitable. On a practical level, this mismatch between the Postal Service and its competitors potentially leads to artificial underpricing by the Postal Service and a potentially distorted market for everyone, with market share that would have flowed to private sector carriers possibly diverted to the Postal Service, simply due to First-Class Mail Parcels' classification as market dominant.

Robert G. Taub
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