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

Statutory Review of the System for Regulating Rates and Classes for Market Dominant Products

Docket No. RM2017-3

REPLY COMMENTS OF PITNEY BOWES INC.
(March 4, 2020)

Pitney Bowes Inc. (Pitney Bowes) respectfully submits these reply comments in response to Order No. 5337, the Postal Regulatory Commission's (Commission) December 5, 2019, Revised Notice of Proposed Rulemaking (RNPRM).

I. INTRODUCTION AND SUMMARY

The initial comments confirm that the proposed changes to the workshare regulations are improvements and should be adopted with the modifications proposed by Pitney Bowes and others to maximize incentives to promote efficiency. The majority of comments expressed concern that the proposed workshare rules are too permissive, that providing an 85 percent passthrough safe harbor in addition to a waiver process will continue to result in workshare discounts that fail to maximize pricing and operational efficiency and fail to fully compensate mailers and mail service providers for the value of the work they perform on the Postal Service's behalf. The Postal Service is the only party to object on the grounds that the proposed rules are too restrictive. The Postal Service's litany of arguments for more flexibility is strong evidence that there should be less flexibility in the final rule. The Postal Service has made it clear through its comments and its prior pricing practices that it disagrees with the Commission's embrace of efficient component pricing (ECP) and that it will not move workshare discounts closer to ECP on its own. The Commission should adopt clear rules mandating that the Postal Service set prices consistent with ECP, as required by section 3622(b)(1).

These comments also respond to the unsupported allegations of several commenters that the Postal Service's competitive package delivery business is not operating in compliance with the law. As confirmed by the most recent annual compliance report, the Postal Service's competitive products fully comply with all applicable statutory and regulatory pricing requirements and are contributing approximately $5 billion more to institutional costs than the required regulatory minimum.

II. DISCUSSION

A. The Commission's Workshare Rules Should be Adopted with Slight Modifications to Maximize Pricing and Operational Efficiency, Consistent with Objective 1

No commenter disputes that the Commission has the legal authority to establish clear regulatory standards for workshare discounts. The majority of the initial comments support the Commission's proposed revisions to the workshare regulations as improvements and urge their adoption with slight modifications to increase efficiency.[1] Specifically, the comments support the adoption of a two-part rule for workshare discounts set below costs avoided: (1) all workshare discounts not already set at full Efficient Component Pricing (ECP) rates must be moved closer to them, consistent with the Commission's "do no harm" principle, and (2) that the Postal Service must obtain a waiver for any workshare discount that is not moved closer to full ECP rates.[2] The majority of the comments expressed the view that the waivers should be infrequent, strictly enforced, and subject to limitation.[3] Specifically, Pitney Bowes and others advocated that the 85 percent passthrough floor should be included as a limitation on the waiver process, not as an exception to the general rule requiring the Postal Service to set workshare discounts ever closer to ECP.[4]

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[1] *See* Comments of American Bankers Association (Feb. 3, 2020) at 14-16 (ABA Comments); Comments of Discover Financial Services (Feb. 3, 2020) at 16, n.5; Comments of National Postal Policy Council, Major Mailers Association, National Association of Presort Mailers, Association of Mail Electronic Enhancement (Feb. 3, 2020) at 15-19 (Comments of NPPC et al); Comments of Parcel Shippers Association (Feb. 3, 2020) at 8-9 (PSA Comments); Comments of Pitney Bowes Inc. (Feb. 3, 2020) at 2-7 (PB Comments).

[2] *See* ABA Comments at 14-16; Comments of NAPM et al at 17-19PB Comments at 4-7.

[3] *See id*.

[4] *See id*.

The Commission should reject the Postal Service's request to create additional exceptions as inconsistent with Objective 1 and the Commission's "do no harm" principle. The Postal Service's pretexts for more flexibility confirm that the rules need to be tightened, not relaxed, to ensure more efficient workshare prices. The Commission has previously concluded that the Postal Service had the pricing authority to set more efficient workshare discounts but it has not exercised that authority.[5] The Postal Service's initial comments and past practice demonstrate that the Postal Service will not move workshare discounts closer to ECP unless required to do so. A review of the history of the First-Class Mail 5-Digit Automation Letters rate confirms that since R2011-2, the price adjustment has satisfied the Commission's "do no harm" principle only half of the time. The Commission should adopt rules that mandate that workshare discounts are set consistent with ECP, as required by section 3622(b)(1). *See* 39 U.S.C. § 3622(b)(1).

None of the scenarios identified by the Postal Service justify further deviations from setting more efficient workshare discounts.[6] There is no basis for a waiver or exception for workshare discounts subject to a pending cost methodology change. *See* Postal Service Comments at 47. The timing of proposed cost methodology changes is entirely within the Postal Service's control, thus the Postal Service is free to file proposed changes in the costing methodology early enough that they can be appropriately adjudicated before a price adjustment filing. Some costing methodology changes may increase the modeled costs avoided, some may decrease the modeled costs avoided; there is no reason for a waiver or exception from a rule requiring more efficient pricing. As proposed by the Postal Service the exception for pending rulemakings would subvert the statutory delegation of responsibility to the Commission to establish approved costing methodologies. Pitney Bowes would

[5] *See* Docket No. RM2017-3, Order No. 4257, Order on the Findings and Determination of the 39 U.S.C. § 3622 Review (Dec. 1, 2017) at 139, 216-19.

[6] *See* Initial Comments of the United States Postal Service in Response to Order No. 5337 (Feb. 3, 2020) at 46 (Postal Service Comments).

support a separate procedural rule specifying the timing for filing proposed changes to analytical principles to ensure timely resolution before the next scheduled price adjustment filing.

There is also no basis for a waiver for rate deaveraging associated with moving workshare discounts set below avoided costs closer to full ECP rates. The Postal Service cites section 3622(e)(3)(B) to argue for expanding the waiver authority to cover discounts set below avoided costs if the result of moving the discount closer to full ECP rates will require raising a related benchmark price. *See* Postal Service Comments at 47-48. The Commission considered and rejected this argument in Order No. 5337, stating:

> If the Postal Service increases the size of a workshare discount (*e.g.*, sets a workshare discount that is currently below avoided cost closer to or equal to its avoided cost), this would increase the rate adjustment authority for the applicable class. The Postal Service retains flexibility to determine how to use the resulting increase in rate adjustment authority (as well as the other sources of rate adjustment authority for that class). The Postal Service may do any (or all) of the following: increase rates for the affected mailpieces (*e.g.*, raise the benchmark rate), increase rates elsewhere in that class in that rate proceeding (*e.g.*, raise a different rate cell(s)), and/or decline to use all or part of that rate adjustment authority in that rate proceeding (*e.g.*, "bank" all or part of that rate adjustment authority for future use). Although this may increase rates for some mailers, there is no evidence that increasing the size of workshare discounts under 100 percent will cause other rates to reach a level that is not just and reasonable.

Order No. 5337 at 196-97. The Postal Service offers no reason for the Commission to revisit its prior determination.

The Postal Service's example regarding In-County Periodicals substantially overstates the possible rate shock on benchmark prices. *See* Postal Service Comments at 48. No further exceptions are justified, but if the Commission were to entertain such an exception it should be narrowly tailored to apply only to discounts that affect small volume rate categories where the rate impact would be substantial. A broader exception would create significant efficiency losses because there are many important, high-volume discounts (e.g., First-Class Mail 5-Digit Automation Letters) with passthroughs set well below 100 percent the modeled costs avoided.

The Postal Service's arguments for greater pricing flexibility for discounts with passthroughs set below avoided costs should also be rejected. *See id.*, at 48-49. The Commission's proposed rules appropriately seek to prevent efficiency losses caused by workshare discounts that pass through less than 100 percent as well as those that pass through more than 100 percent of the avoided costs. The Postal Service's proposal would nullify the Commission's "do no harm" principle for workshare discounts set below avoided costs by allowing the Postal Service to move farther from an efficient rate schedule over time.

None of the arguments raised by the Postal Service justify deviations from ECP rates for discounts set below avoided costs and none are consistent with Commission's stated commitment to "rigorously enforce adherence to ECP for workshare discounts that are below their avoided costs[,]" an approach that the Commission deemed "necessary to address the Commission's finding that the Postal Service had the ability to adhere to ECP throughout the PAEA era but did not do so." Order No. 5337 at 195.

The Postal Service overstates the "blockiness" issue, *see* Postal Service Comments at 49, especially where the Postal Service has imposed much more significant rate design constraints on itself, for example, the five-cent rounding constraint in First-Class Mail Single-Piece Letters. The Commission has properly noted that concerns about utilizing price cap space, *see id*., within a class are adequately ameliorated by the Postal Service's ability to adjust other rates within the class or to bank the rate authority.

The Postal Service's concerns related to lost economies of scale and density are likewise overstated, *id*., 49-50, and are not a legitimate basis for chronic pricing and operational inefficiency. Most workshare cost savings are in mail processing, which is nearly 100 percent volume variable and, thus, not subject to these effects. Furthermore, even where there are such economies (e.g., transportation and delivery), mail mix shifts will not push workload substantially up the cost curve. Accordingly, the impact of any lost scale or density from increased worksharing is immaterial.

The Postal Service's generalized concern regarding the risk of overestimating the modeled cost avoidance, *id*., at 50, should also be rejected. The Postal Service has failed to cite any specific deficiencies in the approved cost models. The Commission has an open, transparent process that allows the Postal Service, the Commission, or other interested parties to propose changes to improve the accuracy or otherwise refine the approved costing methodologies. Hand-waving concerns regarding overestimation (or underestimation) alone cannot justify a "risk premium" that would bias discounts downward, inefficiently leading to greater average deviations from 100 percent passthroughs as required by Objective 1.

The Postal Service's general appeal to pricing flexibility should likewise be rejected as a basis for deviating from more efficient workshare pricing. The Commission has previously considered and dismissed the argument that requiring more efficient workshare discounts imposes an undue constraint on the Postal Service's pricing flexibility. *See* Order No. 5337 at 179, 193-94. The Commission has correctly observed that there are many dimensions to pricing flexibility and that the Postal Service's pricing flexibility would be largely unaffected by the proposed changes to the workshare rules. *See* Order No. 4257 at 144.

For all of the reasons stated above and in the initial comments of Pitney Bowes and other commenters, the Commission should adopt a modified two-part rule for workshare discounts set below avoided costs, as follows: (1) all workshare discounts not already set at full ECP rates must be moved closer to full ECP rates, and (2) deviations from ECP rates will be granted only where the Postal Service can show via a waiver process that moving discounts toward ECP rates will impede operational efficiency; waiver requests will be strictly enforced and subject to a limitation requiring a minimum 85 percent passthrough.

B. Competitive Products Fully Comply with All Applicable Pricing Standards

Order No. 5337 is appropriately focused on proposed changes to the system of regulating rates for market dominant postal products. Nevertheless, several parties filed comments that touch on competitive products. Some of the comments are helpful. *See* PSA Comments at 2-3 (noting the growing importance of the positive net financial contribution of competitive products to help maintain universal service). Other comments less so. Comments filed by the National Taxpayers Union (NTU) and the American Consumer Institute Center for Citizen Research (ACI) allege without support that the Postal Service's competitive package delivery business is not covering its costs.[7] These allegations are demonstrably false. Public FY2019 annual compliance report (ACR) data confirm that the total aggregate revenues from competitive products exceeded the total group incremental costs of competitive products and that, with few minor exceptions, each competitive product offered by the Postal Service covered its own incremental costs.[8] Thus, the Postal Service's competitive package delivery business continues to operate in compliance with all applicable statutory and regulatory pricing requirements and is not being subsidized.[9] Furthermore, there is no evidence of unfair competition. To the contrary, the Postal Service's package delivery business

[7] *See* Comments of American Consumer Institute Center for Citizen Research (Jan. 31, 2020); Comments of National Taxpayers Union (Feb. 1, 2020).

[8] *See* Docket No. ACR2019, United States Postal Service Annual Compliance Report for Fiscal Year 2019 (Dec. 27, 2019) (FY2019 ACR) at 63, Table 21, "FY2019 Incremental Cost Calculation for Total Competitive Products"; USPS-FY19-1, Public_FY19CRAReport.xlsx, "Cost3"; FY2019 ACR at 64-68.

[9] Pitney Bowes concurs with the Postal Service that the issue of whether a density rate adjustment, if any, should be based upon total volume or market dominant volume has nothing to do with cross-subsidization. Consistent with the common economic meaning of the term subsidy, the prohibition on cross-subsidization of competitive products by market dominant products under 39 U.S.C. § 3633(a)(1) is satisfied by ensuring that the total aggregate revenue from competitive products exceeds the total group incremental costs of competitive products. As noted above, the Commission has repeatedly found that there is no cross-subsidization because competitive product revenues exceed incremental costs. The Commission has also properly concluded that Objective 9, which requires that the Commission design a modern rate regulation system "to allocate the total institutional costs of the Postal Service appropriately between market dominant and competitive products," 39 U.S.C. § 3622(b)(9), is satisfied by the statutory mechanisms established in section 3633(a)(3) and section 3633(b). *See* Order No. 4257 at 246-47. For FY2019 the Commission determined that the minimum required contribution ("appropriate share") of institutional costs to be covered by competitive products was 8.8 percent (approximately $3.1 billion of total FY2019 institutional costs of $35.2 billion). The actual contribution of competitive products in FY2019 was $8.25 billion, or approximately 23.4 percent.

continues to be a bright spot for the Postal Service generating approximately $8.2 billion in contribution to help defray the costs of maintaining a nationwide postal delivery system.[10]

III. CONCLUSION

The Commission properly exercised its legal authority to establish clear regulatory standards for workshare discounts. The majority of the comments confirm that the proposed revisions to the workshare rules are improvements and should be adopted with modifications to maximize pricing and operational efficiency. The Commission should decline the Postal Service's invitation to relax the proposed rules to allow less efficient pricing for workshare discounts set below avoided costs. The Commission should likewise disregard comments raising unsupported allegations regarding the competitive products.

Respectfully submitted:

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[10] *See id*.