

Before the
POSTAL REGULATORY COMMISSION
Washington, DC 20268-0001

Regulations Establishing :
System of Rulemaking : Docket No. RM2007-1

COMMENTS OF THE GREETING CARD ASSOCIATION IN RESPONSE
TO SECOND ADVANCE NOTICE OF PROPOSED RULEMAKING

The Greeting Card Association (GCA) submits the following comments in response to the Second Advance Notice of Proposed Rulemaking in this Docket (Order No. 15, May 17, 2007). We offer suggestions in connection with the first, eighth, and ninth of the nine specific questions framed in the Notice.

I. THE PRICE CAP SHOULD EMPLOY A YEARLY AVERAGE OF CPI-U DATA

In Order No. 15, Question 1, the Commission asked whether the § 3622(d) price cap should be calculated by averaging the most recent monthly CPI-U figure with those for the preceding 11 months and comparing the result with the corresponding statistic for the previous year.¹ The Postal Service had proposed a “point-to-point” comparison, using only the most recent month’s data and comparing that figure with the CPI-U for the same month one year earlier.²

GCA believes that the Commission’s suggested averaging procedure is superior to the point-to-point method, and should be adopted as the basis for the price cap.

¹ Order No. 15, pp. 2-4.

² Reply Comments of the United States Postal Service, Appendix C, pp. 9-10.

Simply as a textual matter, section § 3622(d)(1)(A) would support either method. While that provision is classed as a “requirement” of the new system, the choice of methods to carry it out seems to be within the large area of discretion accorded the Commission as the entity responsible for establishing the new ratemaking system.³ If so, the legislative intent is to be sought less by parsing § 3622(d)(1)(A) than by referring to the objectives the system is to achieve and the factors to be taken into account in creating it.

The most clearly relevant objective is § 3622(b): “predictability and stability in rates.” The charts at pp. 3 and 4 of Order No. 15 demonstrate that the point-to-point method produces wider year-to-year variances in the permissible level of increase. In Figure 1 (2005), the September CPI-U produces a much higher

³ The averaging method, however, may in any event correspond better to the paragraph considered as a whole. Section 3622(d)(1)(A) reads:

(A) include an annual limitation on the percentage changes in rates to be set by the Postal Regulatory Commission that will be equal to the change in the Consumer Price Index for All Urban Consumers unadjusted for seasonal variation over the most recent available 12-month period preceding the date the Postal Service files notice of its intention to increase rates [.]

It is true that the point-to-point method could be defended by reading the phrase “12-month period” as fixing only the time frame for quantifying the change in the CPI-U. The modifying phrase “most recent available” would then serve only to indicate the *final* month of the correct 12-month span, and *only* that month would be relevant in determining the allowable percentage increase.

The averaging method, on the other hand, is consistent with reading “change in the Consumer Price Index . . . over the most recent available 12-month period” to indicate the relevance of *all* the changes in the CPI-U over that period. In support of this argument, it may be pointed out that, if Congress had intended the point-to-point method, it could have said so unambiguously. It might, for example, have used language such as “change in the Consumer Price Index . . . calculated by comparing such Index for the most recent month preceding the date the Postal Service files notice of its intention to increase rates with such Index for the corresponding month of the previous year.”

increase than the averaging method; in Figure 2 (2006), the corresponding month produces a substantially lower one. Neither the greater swings nor what may be called the year-to-year “change of sign” (i.e., by comparison with averaged CPI-U values) would promote either predictability or stability. Again, using September as the example, the 2005 and 2006 averaging-method levels for permissible increases are about 3.3 and 3.7 percent, respectively. The corresponding point-to-point values are 4.7 and 2.1 percent. Apart from any questions of predictability, the point-to-point method would produce less stable rates.⁴

Point-to-point computation, however, also involves substantial risk from the predictability standpoint, for both mail users and the Postal Service. Taking the current First-Class letter stamp as an example, either of the averaging-method values calculated in Order No. 15 would allow a narrow range for the increased rate: 42.353 and 42.517 cents, respectively.⁵ The point-to-point values, on the other hand, imply rates of 43 cents (42.927 cents) and 42 cents (41.861 cents), respectively. Unless the Service could predict, in 2005, that the available 2006-based increase would be less than half as great, it could find itself short of planned-for revenues.

It may be argued, however, that the averaging system also presents revenue risk to the Service. If a major current cost item (e.g., motor fuel) increased sharply toward the end of a rate cycle, the damping effect of the

⁴ That is: even if it were possible to predict in September 2005 that the September 2006 CPI-U change would be 2.1 percent, the implied rate increases would vary more sharply from year to year than under the averaging method.

⁵ These particular values, it is true, imply real-world (integer-cent) rates of 42 and 43 cents, since the rounding provision [§ 3622(d)(2)(B)] refers specifically to the “nearest” whole integer. The point is that the difference from one year to the next is quite small. A difference of 0.05 percent in the 2005 value, for example, would dictate the same 43-cent rate as the 2006 value ($\$0.41 * (1.033 + 0.005) = \0.42558). The same change to the 2006 value under the point-to-point method would still yield a 42-cent rate ($\$0.41 * (1.021 + 0.005) = \0.42066).

method could prevent the Service from recovering the full cost increase in the next set of rates. On the other hand, the Service is now permitted to retain earnings⁶; as GCA argued in its initial comments⁷, this mechanism should be relied on to cover the sort of forecasting failures addressed by the contingency provision in the old statute. In former Commission practice, a sharp, unanticipated rise in an important Postal Service input cost would have fallen into that category.

In support of its point-to-point proposal, the Postal Service quotes a Bureau of Labor Statistics statement that price escalation agreements usually employ that method.⁸ A price cap in a regulatory statute, however, has a quite different function from the price escalator in, e.g., a long-term coal contract. In the regulatory statute a principal – perhaps *the* principal – goal is to require greater productive efficiency on the part of a utility⁹ by capping its prices by reference to an extrinsic standard rather than to the firm’s own incurred costs. In a supply contract, the vendor is not likely to want to disclose its incurred costs to the vendee; the CPI-U standard simply furnishes a convenient escalator that requires only public data. More important, a supply contract with a price escalator commonly will also have a renegotiation or termination provision, if not both. In such a contractual situation the buyer has a way of seeking to modify the price, or of escaping from the contract entirely if it finds a cheaper alternative source of the same input.¹⁰ In the Postal Service’s case – by definition, since the

⁶ 39 U.S.C. § 3622(b)(5).

⁷ Comments of the Greeting Card Association in Response to Advance Notice of Proposed Rulemaking, pp. 8 et seq.

⁸ Reply Comments of the United States Postal Service, Appendix C, p. 10.

⁹ Assumed to enjoy a monopoly, natural or legislative.

¹⁰ There may, of course, be substantial notice periods and termination penalties, but these normally are calculable *ex ante* and can be included in the cost comparison.

system applies only to market-dominant products – there is no such escape route. Finally, contractual price escalators are arrived at by negotiation between autonomous parties and do not (or do not spontaneously) reflect public policy choices made by a legislature. In the postal case, “predictability and stability of rates” is just such a policy choice. If the averaging method better effectuates this mandatory objective, the fact that private contracting parties normally do not adopt it should not deter the Commission from doing so.

Accordingly, GCA urges the Commission to employ its proposed averaging method in constructing the price cap.

II. THE COMMISSION SHOULD RETAIN ITS ESTABLISHED COST ATTRIBUTION METHODS

In Question 8, the Commission observes that the Postal Accountability and Enhancement Act (“PAEA”) raises issues “concerning the need, if any, to modify the Commission’s historic approach” to cost attribution and the use of attributable costs in determining rates. GCA sees no need to alter the Commission’s fundamental attribution approach.

The chief novelty in 39 U.S.C. § 3631(b) is the explicit requirement of “reliably identified causal relationships” as a basis for attribution. Relationships of this kind have been generally recognized as the only appropriate basis for attribution at least since *National Association of Greeting Card Publishers v. U.S. Postal Service*, 462 U.S. 810 (1983) (“NAGCP IV”).¹¹ So far as the actual

¹¹ In that case, the Supreme Court said (462 U.S. at 826):

. . . The Rate Commission has held that, regardless of method, the Act requires the establishment of a sufficient causal nexus before costs may be attributed. The Rate Commission has variously described that requirement as demanding a “reliable principle of causality,” PRC Op. R74-1, p. 94, or “reasonable confidence” that costs are the

reliability of the causal relationships is concerned, the Commission would appear to be complying more than adequately with the new Act if it continues to analyze causation as it has been doing since *NAGCP IV* and Docket No. R84-1.

If that is so, the addition of “reliably identified causal relationships” may still be thought to require explanation. That mandate can be better explained as a precaution, thought to be necessary because of the changed role of cost attribution in PAEA, than as an attempt to reform the attribution process itself. So far as market-dominant products are concerned, the price cap, rather than the attribution-plus-noncost-criteria exercise, is to be the main determinant of rates. Attributable cost as a rate floor is now a directly operative factor¹² only in the

consequences of providing a particular service,” PRC Op. [R]77-1, p. 84, or a “reasoned analysis of cost causation.” PRC Op. R80-1, p. 131. Accordingly, despite the District of Columbia Circuit’s interpretation, the Rate Commission has refused to use general “accounting principles” based on distribution keys without an established causal nexus. . . .

and, subsequently, in approving the Commission’s approach,

The legislative history supports the Rate Commission’s view that when causal analysis is limited by insufficient data, the statute envisions that the Rate Commission will “press for . . . better data,” rather than “construct an ‘attribution’” based on unsupported inferences of causation. PRC Op. R74-1, pp. 110-111.

Id., at 827.

¹² “Directly operative,” because failure to recover attributable cost, as determined by reliable causal relationships, could well establish, in after-the-fact review proceedings, a violation of some more general requirement, such as 39 U.S.C. § 101(d). The attributable cost recovery “requirement” formerly found in 39 U.S.C. § 3622(b)(3) is now a “factor” to be taken into account in establishing the new system for market-dominant products. The Commission may indeed choose to treat it as an actually effective requirement in that context too, but is not specifically directed to do so by the statutory text. If that is the eventual choice, attributable-cost recovery will exist as a requirement for market-dominant products because of the Commission has so determined in the exercise of its § 3622(a) authority; that status will be an outcome of this rulemaking, not a preliminary datum for its conduct.

competitive sector. The new language, then, guards against any temptation to “protect competition” by “attributing” to competitive products costs not reliably shown to be caused by them. Conversely, of course, the requirement that each competitive product cover attributable cost still means that once a causal relationship has been “reliably identified” it must be used; attribution, if legally feasible, is mandatory not optional.

The Commission has also raised the question of the proper classification of retiree health benefit costs, for which an annual contribution by the Postal Service is required under 5 U.S.C. § 8009a(d)(iii)(A).¹³ Consistent with the view expressed above, GCA does not think it possible to justify a blanket classification of this contribution as either “attributable” or “institutional.” To classify the entire contribution as “attributable” simply because it is considered “labor related”¹⁴ would ignore the fact that at the time the underlying labor costs were incurred, substantially less than 100 percent of those costs would have been attributed.¹⁵ It is not easy to see how this would be consistent with a requirement of reliable causal relationships. Classifying the contribution as 100 percent institutional would err in the opposite direction, though for similar reasons. That some of the underlying labor cost (and with it, current “pay as you go” retirement

¹³ Order No. 15, p. 9.

¹⁴ Cf. Comments of United Parcel Service in Response to Advance Notice of Proposed Rulemaking, p. 5. (It is not entirely clear that UPS advocates attribution of the *entire* pool of “prior period retiree and health benefit costs,” but the wording of its comment allows that interpretation.)

¹⁵ The proportion of any given cost element that was attributed, moreover, would have depended on the costing principles then operative. The attribution-maximizing theory of *National Association of Greeting Card Publishers v. U.S. Postal Service*, 569 F.2d 570 (D.C. Cir. 1976) was abandoned after the Supreme Court rejected it in *NAGCP IV*, leading to a substantial drop in the percentage of total costs attributed. Compare Docket R80-1, with total attributable costs equal to 78.6 percent of total mail and services revenue, and Docket R84-1, where the corresponding figure was 65.7 percent. PRC Op. R80-1, App. G, Schedule 1; PRC Op. R84-1, App. G, Schedule 1.

contributions) had been causally attributed in contemporaneous rate cases would be left out of account, even though clearly relevant to the question of causation.

These considerations may point to a policy of attributing some appropriate part of the retiree health benefits contribution. That policy would necessarily reflect such judgments as whether the attribution techniques relied on would be those in use today, or – where these were different – those employed when the Service incurred the particular fraction of the underlying labor costs which is being analyzed. In favor of the latter course is the notion that attribution of the benefit cost associated with, e.g., a given past year should produce, as closely as possible, the results that would have obtained if the benefit cost had been accrued currently at that time. But the main historical shifts in attribution theory stem largely from what the Supreme Court found to be the D.C. Circuit’s misreading of former § 3622(b)(3), and from the Commission’s subsequent abandonment of attribution methods it had adopted to conform to that misreading.¹⁶ It thus becomes highly questionable whether the Commission *should* try to produce results parallel to those the mistaken theory would have generated: § 3631(b) requires that attributions be based on reliably identified causal relations, and during the ascendancy of the *NAGCP I* theory the Commission perforce used “inferences of causation” that would not satisfy that criterion.

III. THE INTERPRETATION OF “PRODUCT”

In Question 9, the Commission lists several types of mail categories and asks, in connection with the attributable-cost recovery rule for competitive products, whether each of them is a “product.” The categories are International Customized Agreements, Negotiated Service Agreements, special

¹⁶ As outlined above, fn. 15.

classifications, and “class[es] not of general applicability.” GCA offers suggestions with respect to the last three.

Special classifications and classes not of general applicability both seem to fall within the PAEA definition of “product” – “a postal service with a distinct cost or market characteristic for which a rate or rates are, or may reasonably be, applied[.]”¹⁷

“Special classifications” is a phrase taken from the 1970 Act, and indeed from a provision that is preserved as a factor in present § 3622(c)(10). Since the Commission has long considered distinctive cost and market characteristics to be the essential basis of classification distinctions, the historic construction of “special classifications” meshes well with the (similarly worded) definition of “product.”

Neither the phrase “classes not of general applicability” nor the concept it expresses is a carryover from the old § 3623. But its function in 39 U.S.C. § 3632(b) seems to be, essentially, to require the Governors to follow one set of mail classification procedures rather than another.¹⁸ Sections 3632(b)(2) and (3) do not suggest that – apart from not applying to the whole Nation or a substantial region – these classes are structurally or functionally unlike generally applicable classes.

Consequently, GCA believes that a special classification or a class not of general applicability that contained just one service – distinctive as regards cost and market, as required by both § 101(6) and traditional classification practice – would be a “product” under PAEA. If such a classification contained more than

¹⁷ 39 U.S.C. § 101(6).

¹⁸ In the case of a generally applicable class, the Governors are to publish their decision and the supporting record in the Federal Register; if the class is not of general applicability, they are to file those materials with the Commission.

one distinct service, however, it would appear, by parity of reasoning, to be a grouping of several such products. And the mandate of § 3633(a)(2) – that the Commission’s rules “ensure that each competitive product covers its costs attributable” – appears to require that each such service meet the attributable cost test individually.¹⁹

Negotiated Service Agreements present a slightly different problem, since it is at least theoretically possible, under PAEA, for an NSA to reflect no distinctive cost or market characteristic.²⁰ It is suggestive, however, that the § 3622(c) provisions governing NSAs include them under the heading of “special classifications.” Thus – for reasons suggested above – an NSA which does exhibit some distinctive cost or market feature would still qualify as a “product.” On the assumption that “special classification” has the same meaning in § 3632 as in § 3622(c)(1), this would be as true in the competitive sector as in the market-dominant system.

Respectfully submitted,

GREETING CARD ASSOCIATION

David F. Stover
2970 South Columbus Street, No. 1B
Arlington, VA 22206-1450
703-998-2568

¹⁹ This presumably does not mean that, e.g., each rate cell of a zoned and weight-rated classification would have to cover (a separately computed) attributable cost. By that level of the taxonomy, the cost- and market-related distinctiveness required to constitute a “product” would normally have ceased to exist.

²⁰ The NSA provisions of § 3622(c)(10) do not use the term “product,” and thus do not entail treating each NSA in the market-dominant sector as a separate product. The Commission most probably could import that or a parallel idea when taking that factor into account in the course of establishing the new system; and an NSA which exhibited a material failure to recover cost could be dealt with in an annual compliance review or on complaint.

703-998-2987 fax
postamp@crosslink.net

June 18, 2007