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**Regulations Establishing System
Of Ratemaking**

Docket No. RM2007-1

**REPLY COMMENTS OF POSTCOM IN RESPONSE TO
SECOND ADVANCE NOTICE OF PROPOSED RULEMAKING**

The Association for Postal Commerce ("PostCom") offers these comments in response to comments filed on the Second Advance Notice of Proposed Rulemaking on Regulations Establishing a System of Ratemaking issued by the Commission on May 17, 2007 ("Second Advance Notice").

PostCom is convinced that the comments that the Commission has received in response to the specific questions propounded in the Second Advance Notice affords the Commission a sound basis for moving expeditiously to the promulgation of regulations that implement the modern system of rate regulation as embodied in the PAEA and as envisioned by Congress. On a number of issues raised by the Commission, there is consensus. These include, for example, the nearly universal agreement that the fixed weight method of computing compliance with the CPI limitation for market dominant products should be adopted. There seems also a general view that certain issues – including several not addressed in the Second Advance Notice – are best dealt with on a case-to-case basis. There are, to be sure, certain points of disagreement because this statute, like all other statutes, is not entirely without ambiguity. As to the questions the Commission has raised with respect to the competitive categories, PostCom generally supports the positions advanced by the Parcel Shippers Association; and, therefore, only brief comment on these matters is warranted.

PostCom has separately joined with other parties to respond to the more controversial proposals advanced by the OCA and will not elaborate on these issues in these Comments.

There remain, therefore, only a few matters as to which reply is warranted. We address these matters in the order they were raised in the Commission's Second Advance Notice.

Question 1: Annual Average Method

The initial comments demonstrate a clear consensus that the use of an annual average method for calculating the CPI cap limitation does not contravene the language of the PAEA and serves the basic purposes of the Act. As a policy matter, all parties – including the Postal Service and the OCA – recognize the annual average method offers greater predictability of rate increases, thereby better serving a fundamental objective of the Act. PAEA Section 3622(b)(2).¹ Where either approach is “permissible” under the statute, the Commission certainly has the discretion to determine the approach that best serves the purposes of the statute. *See Chevron U.S.A., Inc., v. Natural Resources Defense Council*, 467 U.S. 837, 844 (1984). The annual percentage method should be adopted.

Question 2: Altered Rate Design

In its Supplemental Comments on the classification process, the Postal Service makes the point that pricing and classification “are essentially two sides to the same coin.” *Supplemental Comments of the United States Postal Service on the Classification Process at 2* (June 19, 2007). We entirely agree. As we observe in our Initial Comments in this rulemaking proceeding, the distinction between “pricing” and “classification” embodied in the Postal Reorganization Act was never really capable of meaningful application and that the pricing

¹ While the Postal Service had initially proposed the point-to-point method, its latest comments suggest that there may be business reasons to prefer the annual average, and that it does not object to this method provided the Commission finds it is consistent with statutory requirements. *Initial Comments of the United States Postal Service on the Second Advance Notice of Proposed Rulemaking*, PRC Docket No. RM2007-1 (June 18, 2007), at 4.

flexibility accorded the Postal Service under the PAEA carried with it a great deal of flexibility as to changes in rate design, as well. *See Initial Comments of PostCom* at 6 (April 6, 2007).

In our view, the change which the PAEA makes with respect to the role of the Commission in classification matters forms an essential predicate for the sound resolution of how the Commission should deal with “altered rate designs” in the course of its review of a Postal Service Notice of Rate Change that includes such change. Analytically, the question embraces two types of rate design changes. In one situation, the change in rate design involves mail that already exists in the mail stream. In that case, the Postal Service’s position that historical billing determinants should be augmented with the best available estimates is entirely reasonable. *Initial Comments of United States Postal Service on Second Advance Notice* at 6-8 (June 18, 2007). The level of detail supplied by the Postal Service in framing its estimates will, of course, depend on the nature and degree of the rate design change. Major overhauls of a class – such as that recently carried out with respect to Periodical rates – plainly will require considerably more information than other, more straightforward changes. That, however, is a matter of degree and cannot be rigidly codified into a go-no go rule.

This contextual approach to the altered rate design question is not novel. As a practical matter, the Postal Rate Commission has, in the past, relied on the Postal Service’s best available data for purposes of assessing the effect of classification changes. *See, e.g., Opinion and Recommended Decision*, PRC Docket No. R2006-1 at 265 (where the Commission acknowledged the high degree of uncertainty surrounding the accuracy of the data used to set NFM rates but nonetheless recommended the rate design). The introduction of a more streamlined ratemaking process which is intended to give the Postal Service – working with its mailing customers – greater flexibility in the shaping of its products affords no reason to change that approach. Moreover, given the short period of time that the PAEA provides for the Commission to conduct its review of a Postal Service Notice of Rate Change, there is little

meaningful alternative except to treat the Postal Service's best available estimates of volume as presumptively valid. The attempt to examine in detail either or both historic mail characteristic studies or prospective volume estimates in the context of a review under Section 3622(d), threatens to bog down a process that will be impossible to complete in the time frame the law provides.

The situation with a wholly new "product" (however that term may ultimately be defined) is different. There is a clear consensus that compliance with the CPI cap under Section 3622(d) should be based on historic volume weights. It logically follows that new products for which no historic billing determinants are available simply cannot be incorporated into that analysis. Because the product has not previously existed in the mailstream, it cannot affect the calculation of the average price change for the class. Once again, this is an approach which closely parallels the approach taken by the Postal Rate Commission in the past. *See Opinion and Recommended Decision*, PRC Docket No. MC2004-5, at 20 (where the Postal Service offered no quantitative volume history or forecast for Repositionable Notes, yet the Commission stated it had no reason to disagree with the Postal Service's assessment that the volumes "were not expected to be particularly large").

The fact that the statute places primary control over rate design in the hands of the Postal Service does not mean that the Postal Service has unfettered discretion as to these matters. In its Supplemental Comments, the Postal Service recognizes that mailers need advance notice and the opportunity to express their views on changes in rate design, whether involving wholly new products, products with existing mail characteristics, or changes that have no price effect whatsoever. The Postal Service commits to providing mailers with notice and the opportunity for comment well in advance of the filing of a Notice of Rate Change. *Postal Service Supplemental Comments* at 11-12. PostCom entertains no doubt that the Postal Service will

honor this commitment. Moreover, the PAEA provides for a recourse to the Commission by affected mailers should the Postal Service fail to do so. *See* PAEA at Section 3662.

Question 3: Review of Worksharing Discounts

Boiling the process of statutory interpretation down to the essential, Section 3622 (d)(1)(C)(iii), read together with Section 3652(b)(1), makes plain that the only issue that the PRC may raise upon review the Postal Service’s Notice filing is of any noncompliance with the CPI price cap limitation established in Section 3622(d)(1)(A). Thus, the PAEA contemplates that procedural mechanisms available to the Commission to review any compliance issues raised with respect to worksharing discounts are only the annual compliance determination under Section 3653 (taking action pursuant to Sections 3653(c) and 3662), or a complaint proceeding initiated under Section 3662. Where “Congress has directly spoken to the precise question at issue,” this Commission must “give effect to the unambiguously expressed intent of Congress.” *Chevron U.S.A., Inc., v. Natural Resources Defense Council*, 467 U.S. 837, 843 (1984).

Question 6: Information Regarding Competitive Products

PostCom supports the positions taken by the Parcel Shippers Association in response to the Commission’s question 6 concerning the information needs to assess whether competitive products are being subsidized by market dominant products. The Postal Service filing of CRA type information annually at the end of each fiscal year is sufficient to enable the Commission to enforce the PAEA’s provisions protecting against cross-subsidies.²

Question 8(c): Treatment of Retiree Health Benefits

PostCom agrees with the position expressed by the Alliance of Nonprofit Mailers and Magazine Publishers of America, Inc. (“ANM-MPA”) regarding the treatment of the Retiree

² We note that there is confusion as to the status of Bulk Parcel Return Service (“BPRS”). Since BPRS is only available to Standard Mail parcels, it is plainly a market dominant product; we do not read PSA’s Comments to contend otherwise.

Health Benefit costs. These costs are overwhelmingly institutional costs: the obligations funded by the payments required by Section 803 of the PAEA consist almost entirely of retiree health benefits that, although payable in future years, were earned by postal employees in previous years. As ANM-MPA succinctly stated in its May 7, 2007 Reply Comments, “[s]ince there is no causal relationship between these costs and current or future volumes, these costs must be treated as institutional.”

PostCom further observes that while the Commission’s question was directed to address competitive products under Section 3633(a)(2), whatever approach is taken with respect to classifying costs as either institutional or attributable with respect to competitive products should equally apply to the Market Dominant classes under Section 3622(c)(2).

Question 9(b): The Definition of “Product”

The Commission has raised the question of whether each Negotiated Service Agreement is a distinct “product” in the context of competitive products. PostCom defers to the views expressed by the Parcel Shippers Association in its comments on this point. *PSA Comments* at 11-13 (June 18, 2007). That is, we agree that it is appropriate to treat customized agreements and specialized classifications as “effectively rate cells” within a subclass of the -- largely deregulated -- competitive products categories.

A somewhat different issue arises with respect to NSAs – and to the meaning of the term “product” – in the market dominant category. In its Supplemental Comments, the Postal Service asserts that the term “product” should be defined at the class level. To the extent that it is also referring to competitive categories, there is no material difference between the Postal Service’s position and that taken by PSA. To the extent, however, that the Postal Service means that the “product” should be applied at the subclass-class level in the case of market dominant products, the Postal Service’s position needs to be qualified in two important respects.

First, with respect to the potential for transfer of products between the market dominant and competitive categories, the statute itself makes clear that the term “product” encompasses more than the subclass as a whole. Subsection (c) specifically provides that transfers pursuant to the provisions of Section of 3642 are subject to that section even though the transfer might involve some (but not all) of the subclasses within a class or “other subordinate units” of the class. Thus, even under a general rule that defines “product” at the highest level of aggregation, transfers, for example, of the NFM or Standard Parcel categories within the Standard Regular subclass can only be carried out in accordance with Section 3642. The Commission’s rules must reflect this.

Second, the Postal Service’s position that the term “product” effectively means subclass must be qualified in application to Negotiated Service Agreements in the market dominant group. Market dominant products are, of course, rate regulated under the price cap regime. But NSAs, including the existing NSAs, all of which involve market dominant products, do not fit within the general price cap rate structure: the actual rate that a mailer under a market dominant NSA pays is not determined by the rate schedule; it is defined by the contract. This is true even though the rate or the discount may be based upon or otherwise derived from the general rate schedules of the market dominant class from which the NSA emerged.

If, therefore, the NSA is treated as a “subclass” for purposes of computing the permitting the CPI increase applicable to other products within the subclass or class to which the NSA has been assigned, the calculation of the before and after rates average revenue per piece will be skewed by the effective average revenue per piece of the NSA. Furthermore, treating each NSA as a subclass will inhibit creativity in the deployment of future NSAs. At present, each of the five NSAs extant is class specific in that it applies to mail or a subset of mail that falls within either, but not both, of First Class or Standard Regular. There is

nothing, however, in the PAEA which is intended to prevent the Postal Service and mailers from creating what may be called hybrid NSA that embrace mail matters that would otherwise fall into more than one of the existing classes or subclasses within the market dominant group.

For these reasons, in PostCom's view, each NSA should be viewed as a distinct "product" on its own. Each is a special and separate classification provided for pursuant to section 3622(c)(10). As a result, volumes covered by an NSA should not be included in the CPI cap for any class.

Respectfully submitted,

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