

Before the
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Notice of Price Adjustment)

Docket No. R2008-1

PUBLIC REPRESENTATIVE COMMENTS
IN RESPONSE TO NOTICE OF PRICE ADJUSTMENT
FOR MARKET-DOMINANT POSTAL PRODUCTS
AND LIMITED CLASSIFICATION CHANGES
(March 3, 2008)

The Public Representative hereby comments on the Postal Service's notice of price adjustment for market-dominant postal products and limited classification changes ("hereafter "USPS Notice")¹ These comments also discuss the Postal Service's Schedule of Regular and Predictable Rate Changes filed concurrently with the USPS Notice. The Commission's notice and order in this proceeding (hereafter "Order No. 59") established a 20-day period for public comment on the planned price adjustments, extending through March 3, 2008.²

I. Overview

Commission review of the USPS Notice will consider, among other things, the "objectives, factors and requirements of the PAEA, including referenced postal policies,

¹ "United States Postal Service Notice of Market-Dominant Price Adjustment," February 11, 2008.

² "Notice and Order on Planned Rate Adjustments for Market Dominant Postal Products and Limited Classification Changes," Order No. 59, February 14, 2008. This order designated the undersigned as Public Representative to represent the interests of the general public in this proceeding.

Commission rules, and public comments.” (Order No. 59 at 6 citing Rule §1010.13(b).) Among the factors listed in §3622 of the PAEA to be considered by the Commission is “the effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters.” (§3622(c)(3).) Thus, the PAEA distinguishes the interests of the general public from the interests of business mail users and enterprises in the private sector engaged in the delivery of mail matter other than letters. Having been designated to represent the interests of the general public, the Public Representative focused on the interests of the general public as distinct from the interests of the other groups included in §3622(c)(3) of the PAEA.

II. Mandatory Requirement Limitation

Order No. 59 declares “public comments *should focus primarily on whether the planned rate adjustments comply*” with the mandatory requirements of the PAEA. (Emphasis added, Order No. 59 at 6; see §3010.13(b).) The mandatory requirement applicable here is an annual limitation of 2.9 percent on price adjustments as provided by §3010.11,³ calculated with the formula in §3010.23(b) to determine the allowable percentage changes in rates.

The Public Representative, with technical assistance, has reviewed on behalf of the general public, the USPS Notice including the appendices and workbook attachments for conformity with applicable Commission rules, the mandatory requirement, and other policies of the PAEA. The USPS Notice is particularly clear and

³ The additional requirement of the maximum size of unused rate adjustment authority in §3010.28 is inapplicable as there is no unused authority available for this first price adjustment filing.

useful. It includes tabulations demonstrating the percentage increases, by class, of the proposed price adjustments. The billing determinants used for calculating percentage price increases and passthrough percentages of workshare discounts are also readily available. Moreover, the explanations in the USPS Notice about modifications from previous proceedings are helpful. The presentation of the information, together with the documentation provided in the USPS Notice required by the Commission's rules, and data available from the Annual Compliance Report has facilitated expeditious review and significantly reduced the need for additional information to review the USPS Notice. The comments below point to a few areas that would benefit from additional information and explanation from the Postal Service.

Mail volumes for each rate cell are the most important factor in calculating the percentage of rate increases proposed for compliance with the mandatory requirement. The relevant volumes are the most recent 12 months of Postal Service billing determinants, with reasonable adjustments identified and explained to account for classification changes. (§3010.23(d).) The volume of mail, or service, for each rate cell is multiplied by (1) the planned rate and the products are summed and then (2) by the current rate and the products are summed. The results of the first step are divided by the results of the second step and 1 is subtracted to obtain the percentage change in rates. (§3010.23(b).) In this proceeding, the resulting percentage must be equal to or lower than the currently applicable annual limitation percentage of 2.9 percent. The Commission's rules require the Postal Service to provide all information and calculations used to develop any adjustments and to explain why they are appropriate. (§3010.23(d).)

The volumes applied by the Postal Service for First-Class Mail and Special Services in the 2007 Annual Compliance Report were adjusted to produce the Postal Service's volumes used in this docket.⁴ To the extent the Commission's review of the Annual Compliance Report leads to further adjustment of those volumes, corresponding adjustments must be made to the volumes used for determining compliance with the mandatory price adjustment limitation and to recalculate the unused rate adjustment authority. Overall, based on the information currently available, it appears that the price adjustment for each class of mail falls within the mandatory allowable percentage.

III. The USPS Notice Complies with the Following Filing Requirements

Also important is whether the USPS Notice has included the information required to conform with the applicable Commission rules for this Type 1-A price adjustment, the usual type of adjustment to rates of general applicability.⁵ The USPS Notice conforms to the following applicable filing requirements in the Commission's rules:

§3010.2 (b). The USPS Notice includes a table of any remaining unused rate adjustment authority in each class for use in subsequent determinations of unused rate adjustment authority. (USPS Notice at 5.)

As noted above, if volumes are adjusted pursuant to the Annual Compliance Review sufficient to impact any percentage price adjustment, the remaining unused rate adjustment authority must also be modified.

⁴ USPS Notice, Attachment USPS-R2008-1/1.

⁵ Part 3010 (§3010.3), issued pursuant to 39 U.S.C. 3622(d)(1)(D). The Postal Service's filing states that it believes it has complied with the rules but moves for waiver of the provisions of the rules to the extent it has not fully complied with the provisions of the rules. (USPS Notice at 1, fn.) As discussed,

§3010.3(b). The limitations on rate adjustments, by class, are determined by §3010.11 and §3010.12. Rate adjustments that exceed the current annual limitation of 2.9 percent are prohibited. The USPS Notice includes a table of proposed changes, by class, all of which are less than the mandatory annual limitation. (USPS Notice at 5.) The rate increases in each class appear to fall below the annual limitation.

§3010.7(d) The Schedule for Regular and Predictable Rate Changes was filed on February 11, 2008, within 90 days of the December 10, 2007, effective date of Rule 3010.7.⁶

§3010.14(a) The USPS Notice includes four types of required general information: proposed rate schedules and their effective dates, evidence of public notice of the rate adjustment, and the name of the Postal Service official who will respond to requests for additional information.

§3010.14(b) Supporting technical information and justifications are included in the USPS Notice. The rule includes a list of ten types of information to be included in the notice. The Postal Service has provided the amounts, schedules and justifications required by the rule. However, as discussed below, the Commission must determine whether the justifications provided for some situations are compliant with the PAEA.

herein, a limited number of deficiencies should be corrected by the Postal Service rather than waived by the Commission.

⁶ Order No. 43 adopting the rule was issued on October 29, 2007, but the rule did not become effective until December 10, 2007 after publication in the Federal Register. (Order No. 43 at 109; 72 Fed. Reg. 64155 (November 15, 2007).)

The USPS Notice also refers to several limited classification changes relating to single-piece domestic International Mail and Periodicals. (Order No. 59 at 2.) The changes to single-piece domestic International Mail are appropriate and conform to the Commission's rules and the requirements of the PAEA.

IV. Periodicals and Recovery of Attributable Costs

Rule 3010.14(b)(7) requires a discussion demonstrating how the proposed rate adjustments are designed to "properly take into account the factors listed in 39 U.S.C. 3622(c)." One of those factors is the "requirement" that each class or type of mail bear the costs attributable to each class or type of mail. The USPS Notice indicates Periodicals rates do not recover their attributable costs in contradiction to the factor in §3622(c)(2) of the PAEA.⁷ However, the USPS Notice provides a rationale for the shortfall in the proposed Periodicals rates. (USPS Notice at 18.)

For several reasons, it is uncertain how much the percentage of Periodicals attributable costs recovered will improve during FY2008. It is apparent that recent rate changes in FY2007 will improve the recovery of attributable costs. The current Periodicals rates did not become effective until July 15, in the fourth quarter of FY2007, when Periodicals prices were overhauled.⁸ Those prices included some incentives to yield cost savings. The Commission found in Docket No. R2006-1 that the rates in effect since July of FY2007 would "exceed attributable costs by a small margin."⁹ The

⁷ See USPS Notice at 17-18. See also, "Summary of Revenue and Cost for Major Service Categories," CRA FY2007 filed in ACR2007. Total Periodicals cost coverage is 83.01 percent.

⁸ Attachment USPS-R2008-1/3 at 2.

⁹ Docket No. R2006-1, Op. at ¶ 5776.

new higher rates proposed here will be effective for the latter part of FY2008 and should increase the recovery of attributable costs. New equipment is being installed to improve the efficiency of Periodicals processing and deliveries that may serve to reduce costs. Finally, the Postal Service states it has “assembled a task force...to understand and reduce Periodicals costs...consistent with section 708 of the PAEA.” (USPS Notice at 18.) Section 708 of the PAEA (not codified) provides that the Postal Service and the Commission shall study and report to Congress Periodicals costs and opportunities to improve efficiencies of Periodicals’ service. Taken together, Periodicals may significantly improve the recovery of their attributable costs in the near future.

Periodicals rates provided revenue that was less than attributable costs during FY2007. However, given the recent significant changes offering potential for improvement, and other uncertainties, at this time, neither the Commission nor the Postal Service is able to estimate with any degree of certainty the outcome of these various changes on Periodicals cost recovery during FY 2008. With these uncertainties, the planned Periodicals rate adjustments should not be found to be inconsistent with applicable law and an amended notice of rate adjustment pursuant to Rule 3010.13(c) would not be appropriate.

The Commission should therefore refrain from considering remedial steps to encourage compliance with the PAEA. If the Periodicals situation does not improve after further experience with the new rate incentives, new processes, and the installation of new equipment, together with revenue from the proposed rate increases during this fiscal year, then the Commission should consider appropriate action. The remedial steps may be taken either pursuant to a rate adjustment filing or an Annual

Compliance Review or even pursuant to a complaint filing to bring Periodicals revenue in line with Periodicals attributable costs.

V. Worksharing

A. Benchmarks

In Docket No. R2006-1, the Commission rejected the Postal Service's proposal to de-link the BMM (Bulk Metered Mail) benchmark from the First-Class single piece letter rate. In this docket, the Postal Service has calculated its First-Class BMM discounts such that the appropriate relationship between First-Class and BMM is consistent with the Commission's approved methodology. Other relationships between discounted First-Class bulk rates continue to be based on cost saving differences. However, it is of concern that the benchmark calculations for future filings may attempt to de-link the First-Class single piece letter rate from the BMM benchmark. As the Commission has previously pointed out in two recent rate proceedings, this benchmark:

...represents not only that mail most likely to convert to worksharing, but also, to what category current worksharing mail would be most likely to revert if the discounts no longer outweigh the cost of performing the worksharing activities.¹⁰

The impact of de-linking the BMM benchmark discount from the single-piece First-Class letter rate will have the impact of separating the commercial rates from the First-Class rates. It is important that the Commission reiterate its stance on using the First-Class single-piece letter rate as the benchmark for calculating the BMM rate.

¹⁰ Docket No. R2006-1, Op. at ¶ 5109; Docket No. R2000-1, Op. at ¶ 5089.

B. Justifications Provided Pursuant to Rule 3010.14(6)

1. Worksharing Passthroughs in Excess of 100 Percent

The worksharing passthrough for First-Class nonautomation presort cards is 157.2 percent.¹¹ This is significantly higher than the costs avoided and would not be in compliance with the PAEA unless the Postal Service justifies the excess as permitted by §3622(e)(2) of the PAEA. The price increase of only 0.4 percent closes the current gap of 2.1 cents between these nonautomation cards and Mixed AADC automation cards to 1.9 cents. The Postal Service's justification for not reducing the discount further is that it would cause a price *reduction* for the nonautomation category that would implicitly encourage the use of nonautomation presort cards, contrary to its policy of promoting automation. (USPS Notice at 27.)

The Postal Service fails to assert that its reasoning complies with the statutory requirements of §3622(e) permitting exceptions to the rule limiting passthroughs to costs avoided. However, the Postal Service's explanation appears to meet the criteria of §3622(e)(2)(A)(ii), but the justification does not meet the additional mandatory requirement in subpart (A)(i) that the discount is either associated with a new postal service or a change to an existing postal service, or with a new workshare initiative related to an existing postal service. This additional justification is needed to justify an exception to the rule. Neither does the Postal Service's explanation meet the requirement in the latter half of subpart (A)(ii) that the workshare activity is to be phased out over a limited period of time. These shortcomings are the same deficiencies noted in the Commission's information request relating to First-Class 5-digit presort letters and

¹¹ USPS Notice, Appendix B.

Standard Mail, but that information request does not specifically refer to the nonautomation presort cards violation.¹²

2. Workshare Passthroughs Substantially Below Avoided Costs

Section 3010.14(6) requires an explanation for discounts that are set substantially below avoided costs. The First-Class Mail presorted business parcels are substantially below avoided costs: slightly above 30 percent of avoided costs—3-digit at 30.2 percent and 5-digit at 30.3 percent of avoided costs. This is a new rate category,¹³ and the Postal Service explains the passthroughs are similar to those recommended in Docket No. R2006-1. However, the Commission's Opinion also noted its expectation the Postal Service would develop accurate cost and volume data so that future rates could more accurately track costs.¹⁴ The Postal Service has not explained the status of that study or why it has not adjusted the passthrough on the basis of its experience with cost and volumes in order to provide for a more normal passthrough.

C. Contributions of First-Class Single-Piece and Workshared Mailpieces

In Docket No. ACR2008, it has been claimed the contribution to institutional costs of single-piece First-Class Mail provides a rate preference vis-à-vis workshared presort letters which should be eliminated by the Postal Service in future rate adjustments.¹⁵ This claim is based upon the principle that the application of efficient component pricing (ECP) requires equivalent contributions from these types of mail. However, ECP does

¹² "Commission Information Request No. 1," February 26, 2008.

¹³ Docket No. R2006-1, Op. at ¶ 5188.

¹⁴ *Id.*

¹⁵ Docket No. ACR2007, "Comments of National Postal Policy Council," at 6-7.

not require single-piece First-Class letters to make the same contribution to institutional costs as First-Class workshared mail. ECP principles apply to mail within the same subclass.¹⁶ From a cost and market perspective, single-piece and presort workshared mail have been redefined as different products. The contribution of single-piece First-Class Mail should not, therefore, be expected to match the contribution of workshared First-Class Mail. Because single-piece First-Class letters and cards are now a different product than First-Class workshared products, the relatively lower contribution by First-Class single-piece mail is not inconsistent with the principles of ECP.

VI. Schedule of Regular and Predictable Rate Changes

Pursuant to Rule 3010.7(a), (b) and (c), the Postal Service filed, concurrently with its notice of price adjustment, a Schedule of Regular and Predictable Rate Changes to be maintained by the Commission indicating the Postal Service expects to change the relevant prices in mid-May of each year and that the price changes for all Market-Dominant classes will equal, on average, the price cap limitation applicable to that year.¹⁷

Although this Schedule may appear to conform to the letter of the Commission's rule, the proposed Schedule provides limited information and, in effect, fails to comply with the Commission's rule. The Schedule's stated expectation to change rates in mid-May of each year (in compliance with §3010.7(b)) provides a measure of certainty about

¹⁶ Docket No. R2006-1, Op. at ¶ 4032.

¹⁷ "United States Postal Service Filing of Schedule of Regular and Predictable Price Changes," February 11, 2008.

future rate increases that has never before been provided by the Postal Service. But, overall, the schedule does not meet the spirit of Rule 3010.7(c) which provides:

The schedule for Regular and Predictable Rate Changes shall provide an explanation that will allow mailers to predict with reasonable accuracy the amounts of future scheduled rate changes.

The statement that the price changes for all market-dominant classes will equal, on average, the price cap limitation applicable to that year, is nothing more than the basic statutory limitation and provides very limited useful substantive information except that the Postal Service does not expect to accrue very much unused rate authority.

The rule in §3010.7(f) allows the Postal Service for “good cause shown” to vary rate adjustments from those estimated in the Schedule. This indicates the Commission anticipated the Schedule would contain specific estimates of future rates, not the gross generalizations at the *class* level provided by the Postal Service. Rather, a fair reading of the rule is that it require a good faith estimate of the direction and amount of *all* future *rate* changes. The provision that the Schedule shall provide “the amounts of future scheduled rate changes” is specific. (§3010.7(c).) The proposed Schedule is overly broad because it refers only to price changes by classes. The rule refers to rate changes, without consolidation into classes. Rate changes occur, at the minimum, at the rate category level.

The Postal Service should provide within the Schedule of Regular and Predictable Rate Changes an explanation of the future adjustments it anticipates in each rate category so mailers can predict with reasonable accuracy the future magnitude of their postage. For instance, in First-Class, the Postal Service appears to be applying a policy at variance with the usual expectation that rates will increase more

or less proportionately across-the-board. The Postal Service has reduced by 4.5 cents the additional ounce applicable to presorted letters to the price charged for automation letters from 17 cents down to 12.5 cents.¹⁸ This price adjustment *reduces* some First-Class presorted nonmachinable and machinable rates, with relatively large reductions in heavier presorted mailpieces. Table I shows that the rates for First-Class presorted machinable letters of 2, 3 and 3.5 ounces and the rates for First-Class presorted nonmachinable letters of 3 and 3.5 ounces will be reduced significantly.

Table 1
First-Class Rates

Machinable Presorted Letters

<u>Ounces</u>	<u>Proposed Rate</u>	<u>Current Rates</u>	<u>% Chg</u>
1 oz	0.394	0.373	5.6%
2 oz	0.519	0.543	-4.4%
3 oz	0.644	0.713	-9.7%
3.5 oz	0.769	0.883	-12.9%

Non-Machinable Presorted Letters

<u>Ounces</u>	<u>Proposed Rates</u>	<u>Current Rates</u>	<u>% Chg</u>
1 oz	0.594	0.543	9.4%
2 oz	0.719	0.713	0.8%
3 oz	0.844	0.883	-4.4%
3.5 oz	0.969	1.053	-8.0%

In the same vein, rates for First-Class 3-digit and 5-digit automation flats, in all weight categories from 1 to 13 ounces, would decline while ADC and Mixed ADC rates in all weight categories would increase.

¹⁸ USPS Notice at 14.

Table 2

First Class Flats

<u>Ounces</u>	<u>Proposed Rates</u>			
	<u>5-Digit</u>	<u>3-Digit</u>	<u>ADC</u>	Mixed <u>ADC</u>
1 oz	0.364	0.479	0.57	0.702
2 oz	0.534	0.649	0.74	0.872
3 oz	0.704	0.819	0.91	1.042
4 oz	0.874	0.989	1.08	1.212
5 oz	1.044	1.159	1.25	1.382
6 oz	1.214	1.329	1.42	1.552
7 oz	1.384	1.499	1.59	1.722
8 oz	1.554	1.669	1.76	1.892
9 oz	1.724	1.839	1.93	2.062
10 oz	1.894	2.009	2.1	2.232
11 oz	2.064	2.179	2.27	2.402
12 oz	2.234	2.349	2.44	2.572
13 oz	2.404	2.519	2.61	2.742

<u>Ounces</u>	<u>Current Rates</u>			
	<u>5-Digit</u>	<u>3-Digit</u>	<u>ADC</u>	<u>ADC</u>
1 oz	0.383	0.484	0.567	0.686
2 oz	0.553	0.654	0.737	0.856
3 oz	0.723	0.824	0.907	1.026
4 oz	0.893	0.994	1.077	1.196
5 oz	1.063	1.164	1.247	1.366
6 oz	1.233	1.334	1.417	1.536
7 oz	1.403	1.504	1.587	1.706
8 oz	1.573	1.674	1.757	1.876
9 oz	1.743	1.844	1.927	2.046
10 oz	1.913	2.014	2.097	2.216
11 oz	2.083	2.184	2.267	2.386
12 oz	2.253	2.354	2.437	2.556
13 oz	2.423	2.524	2.607	2.726

<u>Ounces</u>	<u>% Change</u>			
	<u>5-Digit</u>	<u>3-Digit</u>	<u>ADC</u>	Mixed <u>ADC</u>
1 oz	-5.0%	-1.0%	0.5%	2.3%
2 oz	-3.4%	-0.8%	0.4%	1.9%
3 oz	-2.6%	-0.6%	0.3%	1.6%
4 oz	-2.1%	-0.5%	0.3%	1.3%
5 oz	-1.8%	-0.4%	0.2%	1.2%
6 oz	-1.5%	-0.4%	0.2%	1.0%
7 oz	-1.4%	-0.3%	0.2%	0.9%
8 oz	-1.2%	-0.3%	0.2%	0.9%
9 oz	-1.1%	-0.3%	0.2%	0.8%
10 oz	-1.0%	-0.2%	0.1%	0.7%
11 oz	-0.9%	-0.2%	0.1%	0.7%
12 oz	-0.8%	-0.2%	0.1%	0.6%
13 oz	-0.8%	-0.2%	0.1%	0.6%

If the Postal Service expects to pursue a policy of reducing these particular rates further in the future, this information would enhance the predictability of individual rate changes, a predictability that is not in the Schedule filed by the Postal Service.

There is another example where a statement of Postal Service intentions would enhance the value of the Schedule of Regular and Predictable Rate Changes. The Postal Service says its “general approach to international special services has been to set fees for those services that are similar to the fees for the equivalent domestic service.” (USPS Notice at 23.) This, too, is a Postal Service policy appropriate for inclusion in the Schedule of Regular and Predictable Rate Changes.

If the Postal Service anticipates these types of adjustments will continue with the next rate increase, then for the benefit of mailers, the Postal Service should include that information in the Schedule. Unless further details of this type are provided, the Schedule is incomplete and misleading to the general public, including non-profit mailers who use presorted postage, who could refer to the schedule for substantive information.

The laudatory purpose of the Schedule is to provide a measure of guidance to mailers unfamiliar with the direction and magnitude of recent and likely future rate changes at the rate category level. The Schedule also provides a forum for the Postal Service to indicate its current expectations about future rates. Also, to assist mailer planning, a more detailed Schedule would eliminate the need to research recent postal rate case data and workpapers to discern the likely direction and magnitude of future rate changes.

VII. Special Services Cost Allocation to Competitive Products

Section 3621(a) of the PAEA identifies Special Services as a Market-Dominant product. The Postal Service appears to attribute the Special Service costs to the Market-Dominant Special Services.¹⁹ One would expect that the associated revenues would be recorded as Market-Dominant as well.

In those instances where a Special Service product breaks even, it would seem irrelevant whether the Special Service product is classified as a Market-Dominant or as a Competitive service. However, if the Special Service product is losing money (*i.e.* revenues do not cover costs) and is used primarily by Competitive products, then Market-Dominant products are being placed at a disadvantage because they are required to absorb the loss. Alternatively, if the Special Service product is profitable, then Market-Dominant products are unduly credited with the revenues. In FY2007, Special Service revenues were approximately 3.7 percent (\$2,698.2 / \$73,766.5 million)²⁰ of total mail and services revenues. The §3622(b)(8) objective requires the modern system for regulating rates and classes for Market-Dominant products to be just and reasonable. Therefore, it would appear reasonable that Special Services product revenues and costs be allocated between Market-Dominant and Competitive products, as appropriate.

¹⁹ "Response of the United States Postal Service to Commission Information Request No. 2," Question 2, February 11, 2008.

²⁰ Docket No. ACR2007, USPS-FY07-LR-1.

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

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