

**BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON DC 20268-0001**

NOTICE OF PRICE ADJUSTMENT

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Docket No. R2008-1

**COMMENTS OF
ALLIANCE OF NONPROFIT MAILERS,
AMERICAN BUSINESS MEDIA,
DOW JONES & COMPANY,
MAGAZINE PUBLISHERS OF AMERICA, INC.,
THE MCGRAW-HILL COMPANIES, INC., AND
THE NATIONAL NEWSPAPER ASSOCIATION, INC.
(March 3, 2008)**

Pursuant to Order No. 59, Alliance of Nonprofit Mailers (“ANM”), American Business Media (“ABM”), Dow Jones & Company, Inc. (“Dow Jones”), Magazine Publishers of America, Inc. (“MPA”), The McGraw-Hill Companies, Inc. (“McGraw-Hill”) and the National Newspaper Association, Inc. (“NNA”) respectfully submit these comments on the rate changes proposed by the Postal Service in this docket. The purpose of these comments is to anticipate and respond to the contention of Valpak Direct Marketing Systems, Inc., and Valpak Dealers’ Association, Inc. (collectively “Valpak”) that the current or proposed rates for Periodicals mail are unlawfully low because they fail to produce enough revenue to cover the attributable costs of the class as a whole, and the Postal Service therefore should be required to increase Periodicals rates enough to eliminate the alleged shortfall, even if the increase exceeds the PAEA price cap, 39 U.S.C. § 3622(d).¹

¹ We respond to this claim because Valpak has raised it repeatedly in recent Commission filings, and is likely to reassert the issue in its March 3 comments. See Docket No. RM2007-1, Valpak Reply Comments (May 7, 2007) at 13-19; *id.*, Valpak Comments (Sept. 24, 2007) at 17-20; Docket No. ACR2007, Valpak Comments (Jan. 30, 2008) at 9, 21, 44-51. The necessarily compressed procedural schedule in this

If Valpak in fact renews its claims in this docket, the Commission should deny them on three grounds. First, the purpose of this proceeding is to take a quick review of the proposed rate changes to determine whether the increases comply with the cap imposed by 39 U.S.C. § 3622(d). Whether rates cover costs is beyond the scope of this proceeding. Second, even if cost coverage were properly at issue here, there is no basis for finding that the revenue from the proposed rates would fail to cover the total attributable costs of Periodicals mail. Third, and in any event, the Postal Accountability and Enhancement Act (“PAEA”) does not authorize rate increases in excess of the limits imposed by 39 U.S.C. § 3622(d) merely because a class of mail would otherwise fail to cover attributable costs. We discuss each point in turn.

I. WHETHER PERIODICALS RATES COVER COSTS IS AN ISSUE BEYOND THE SCOPE OF THIS PROCEEDING.

Both the language and administrative history of 39 C.F.R. § 3010.13 make clear that the cost coverage of Periodicals mail is an issue beyond the proper scope of this proceeding. Rule 3010.13(b)(1) and (2) state that public comments on a proposed rate adjustment of general applicability “should focus primarily on whether [the] adjustments comply with” the “annual limitation established in rule 3010.11” (the CPI-based cap) and “the limitations established in rule 3010.28” (the application of previously unused rate adjustment authority).

docket does not authorize the filing of replies after March 3. To ensure a complete record, we therefore respond to Valpak now. The arguments set forth in this response are similar to those we made in our February 13 reply comments in Docket No. ACR2007.

In establishing this rule, the Commission emphasized that “one of Congress’s main motives in enacting the PAEA was to simplify and expedite the setting of postal rates. . . . The Commission also concludes that Congress expected that a modern system for regulating rates and classes would afford the public and the Commission only a limited period of pre-implementation comment and review.” Order No. 43, Docket No. RM2007-1, *Regulations Establishing A System Of Ratemaking* (Oct. 29, 2007) at ¶¶ 2025-2026. In light of these policies, and the 45-day period of advance notice of proposed rate changes referenced in 39 U.S.C. ¶ 3622(d)(1)(C), “the inference is strong that Congress contemplated that complicated or subjective compliance issues would be addressed during the annual compliance review, or through the complaint procedures of section 3662.” *Id.* at ¶ 2026. Hence, the Commission “can give close scrutiny to only a limited number of compliance issues in the time available before rate changes are implemented,” *Id.* at ¶ 2029.

Moreover, the Commission’s response to Valpak’s request that pre-implementation review should also consider attributable cost coverage issues, *id.* at ¶ 2030, underscores this point. As the Commission noted, the “merits of one attribution methodology relative to another is an example of an issue that is too complex to be re-evaluated in a pre-implementation context.” *Id.* at ¶ 2031. Without determining the correct attribution methodology and the effect of recent, current and imminent operational changes on cost levels and cost avoidances, it is not possible to make an informed decision about the attributable cost coverages or worksharing passthroughs.

For all of these reasons, questions about the coverage of attributable costs by Periodicals Mail (or any other class of mail) should be considered, if at all, in subsequent annual compliance review proceedings or in complaint proceedings.

II. THERE IS NO BASIS FOR FINDING THAT THE PROPOSED PERIODICALS RATES WOULD GENERATE TOO LITTLE REVENUE TO COVER ATTRIBUTABLE COSTS.

There is no basis for finding that the proposed Periodicals rates will be noncompensatory. The Postal Service has proposed to increase the current rates by essentially the rate of inflation as measured by the CPI, and the increases thus should recoup the cost increases incurred by the Postal Service since the R2006-1 rates took effect. Valpak has made no showing that the R2006-1 rates are noncompensatory. As explained by the undersigned parties in their joint reply comments to the Commission on February 13, 2008, in Docket No. ACR2007, the CRA data relied on by Valpak as evidence to the contrary significantly understate the cost coverage of Periodicals mail under the proposed rates.

First, the CRA calculates coverage ratios by reference to the aggregate revenue earned during the entire fiscal year at issue. The current set of Periodicals rates, which represented an average increase of 11.8 percent over the prior rates, did not take effect until July 15, 2007, more than nine months into FY 2007. For the portion of FY 2007 when the R2006-1 rates were in effect, the same CRA data would show that the coverage ratio exceeded 90 percent—even *assuming no change in mailer behavior or the CRA methodology*. Docket No. ACR2007-1 ANM-MPA Comments (Jan. 30, 2008) at 4. Valpak, while offering the unexceptionable observation that this one correction

alone would not eliminate the entire coverage shortfall reported by the CRA, does not dispute that the correction is warranted. Valpak at 47-48.

Second, the accuracy of the attributable cost data on which Valpak relies has been seriously questioned. See, e.g., PRC R97-1 Op. & Rec. Decis. (May 11, 1998) at ¶ 3148 (acknowledging that the automation refugee issue “warrants systematic investigation”); PRC R2000-1 Op. & Rec. Decis. (Nov. 13, 2000) at ¶¶ 3011-3015, 3076, 5592-93. In recognition of this fact, Section 708(a) of the PAEA specifically directs the Postal Service and the Commission to conduct a joint study of, *inter alia*, “the quality, accuracy and completeness of the information used by the Postal Service in determining the direct and indirect postal costs attributable to periodicals.”

Third, as the Commission specifically found in R2006-1, the worksharing incentives for periodicals, and the strengthening of those incentives in R2006-1, are inducing major changes in mailer behavior that should further close the reported gap between revenues and costs in FY 2008 and future years. R2006-1 Op. & Rec. Decis. at iv; ANM-MPA at 5-6 (providing several examples of changes in publisher and printer behavior that have already occurred).² Valpak has not considered this effect.

Fourth, both the anticipated deployment of the Flats Sequencing System (“FSS”) and a number of other Postal Service cost reduction initiatives should further reduce Periodicals costs in FY2008 or soon thereafter, as the Commission found. ANM-MPA 6-8. Valpak derides these initiatives on the ground that past cost savings initiatives

² Although Periodicals mailers may disagree about the extent or timing of these changes, none dispute that the changes have occurred, are occurring, and will continue to occur in the future.

have “consistently failed” to produce full cost coverage for Periodicals mail during the past 11 years. Valpak 21, 45-46. But the track record of the Postal Service’s cost saving initiatives under the cost-plus ratemaking regime of the PRA clearly sheds no light on how the Postal Service will perform now that the regulatory rate ceiling has been decoupled from the Postal Service’s actual costs of service. Under the old law, the Postal Service could always come back to the Commission and ask for more money if the anticipated cost savings did not come to pass. Under the new law, the Postal Service’s inability to raise rates faster than overall inflation provides a much stronger incentive to make sure that the savings are actually realized. That change in incentives is the very point of incentive ratemaking.³

The Postal Service’s February 11 “Notice of Market-Dominant Price Adjustment” in the present docket recognizes these facts:

The FY 2007 Annual Compliance Report indicated that Periodicals was the only class of mail that did not cover its attributable costs in the last fiscal year (Factor 2). However, the new price structure for Periodicals was only in effect for a small part of FY 2007. The cost coverage calculated for FY 2007 is therefore based primarily on the costs and revenues that resulted from the Docket No. R2005-1 prices. The new price structure is expected to have cost-savings benefits as mailers respond to the incentives it creates. An increase in May of this year, in conjunction with the increase of last July and with increased mailer response to the incentives created by the new structure, should help move Periodicals towards cost-compensatory status (Factor 2, Objective 8). The Postal Service is also working to further understand and reduce Periodicals costs, and has assembled a task force for that purpose, consistent with section 708 of the PAEA.

³ See *Revisions to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, Order No. 561, FERC Stats. & Regs. ¶ 30,985 (1993) (“*Order No. 561*”) at 30,948-49 & n. 37, *aff’d*, *Ass’n of Oil Pipelines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

USPS Notice of Market-Dominant Price Adjustment (filed Feb. 11, 2008) at 19. Likewise, the Postal Service's February 13 reply comments in Docket No. ACR2007 noted (at pp. 4-5) that:

Even more fundamentally, Valpak completely disregards the circumstances regarding Periodicals. Late in FY 2007, a significantly revamped price structure was implemented for Outside County Periodicals. Of course, during FY 2007 mailers had little opportunity to adjust to the new framework. [footnote omitted] Going forward, however, this price structure is expected to produce significant cost-savings benefits as mailers respond to the incentives it creates. . . . [A] May [rate] increase this year, in conjunction with the increase of last July and with increased mailer response to the incentives created by the new structure, should help move Periodicals towards cost-compensatory status. Furthermore, the Postal Service is also working to further understand and reduce Periodicals costs, and has assembled a task force for that purpose, consistent with section 708 of the PAEA.

III. PAEA DOES NOT AUTHORIZE RATE INCREASES IN EXCESS OF THE LIMITS IMPOSED BY 39 U.S.C. § 3622(d) MERELY BECAUSE A CLASS OF MAIL WOULD OTHERWISE FAIL TO COVER ATTRIBUTABLE COSTS.

The notion that PAEA imposes an absolute requirement that rates for each class cover attributable costs suffers from an insurmountable defect. While 39 U.S.C. § 3622(c)(2) specifies the coverage of attributable costs as a ratemaking "factor," the law does not authorize the Commission or the Postal Service to impose rate increases that exceed the CPI-based adjustment index established by 39 U.S.C. § 3622(d) merely because Periodicals rates would otherwise fail to satisfy this factor. As previously explained by ANM, MPA and other parties in Docket No. RM2007-1, the language, legislative history, and economic policies of Section 3622(d) preclude the Commission

from allowing the attributable cost floor to trump the rate cap for individual classes of mail.⁴

If a particular class or service is not bearing its attributable costs, the Postal Service (or, under procedures authorized by the Act, the Commission) certainly may continue to increase the rates for that class or service by the full amount of the CPI, even if rates for other classes are increased by smaller amounts, until full coverage of attributable costs is attained, and/or the Postal Service may or should continue to work to lower the costs of the class, as the Postal Service has said it is doing. This interpretation of the statute gives effect to both the rate cap provisions of Section 3622(d)(1) and the attributable cost factor set forth in Section 3622(c)(2), without frustrating the intent of Congress.⁵

A. The Language of PAEA

39 U.S.C. § 3622, the cornerstone of PAEA, imposes an absolute limit on overall percentage increases in rates for a class, with only narrow exceptions. Section 3622(d)(1)(A) specifically provides that “The system for regulating rates and classes for market dominant products *shall . . . include an annual limitation on the percentage changes in rates to be set by the Postal Regulatory Commission that will be equal to the*

⁴ Docket No. RM2007-1, ANM-MPA comments (April 6, 2007) at 2-10; *id.*, ANM-MPA comments (May 7, 2007) at 2-3; *accord, id.*, ABM comments (April 6, 2007) at 3-4; *id.*, NNA comments (April 6, 2007) at 3-10; USPS comments (April 6, 2007) at 22-23.

⁵ Valpak objects to this remedy on the ground that CPI-compliant rate increases could take “at least a decade—and perhaps far longer” to eliminate a coverage shortfall. Valpak 50. For the reasons noted at pp. 6-8 above, the factual premise of this objection is unfounded: Periodicals mail is almost certainly far more compensatory than Valpak has assumed. In any event, Valpak’s objection to the statutory balance struck by Congress is one properly addressed to Congress, not the Commission.

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 on which the Postal Service files notice of its intention to increase rates. 36 U.S.C. § 3622(d)(1)(A) (emphasis added). Similarly, Section 3622(d)(1)(D) specifically directs the Commission to “establish procedures whereby the Postal Service may adjust rates *not in excess of the annual limitations under subparagraph (A).*” *Id.* § 3622(d)(1)(D) (emphasis added). Neither provision creates any exception for mail that would otherwise fail to cover attributable costs.

Section 3622(d) also specifies that changes to the CPI shall constrain rate increases separately for each class of mail. Section 3622(d)(2)(A) provides that “the annual limitations under paragraph (1)(A) *shall apply to a class of mail*, as defined in the Domestic Mail Classification Schedule as in effect on the date of enactment of” PAEA. *Id.*, § 3622(d)(2)(A) (emphasis added).⁶ This provision, like Sections 3622(d)(1)(A) and (D), contains no restriction or exception for mail that would otherwise fail to cover attributable costs.

Section 3622(c)(2), which directs the Commission, “in establishing or revising” a “modern system” of ratemaking, to “take into account . . . the requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to each class or type of mail service through reliably identified causal relationships plus that portion of all other costs of the Postal Service reasonably assignable to each such

⁶ The intent of Congress to make the CPI cap a limit on each class of mail is also evidenced by Section 3622(d)(2)(B), which allows the Postal Service to round rates and fees to the nearest whole integer, “if the effect of rounding *does not cause the overall rate increase for any class to exceed the Consumer Price Index for All Urban Consumers.*” 36 U.S.C. § 3622(d)(2)(B) (emphasis added).

class or type,” does not support a contrary result. The structure and organization of Section 3622 make clear that the factors of § 3622(c) do not and cannot trump the CPI cap established by § 3622(d). Language much more direct and precise than “take into account” would have been necessary to support the conclusion that Congress meant to allow the attributable cost floor to override the price cap.

Section 3622 establishes a hierarchy of regulatory authority. At the bottom are Section 3622(c)(2) and the thirteen other factors enumerated in § 3622(c)(1) through (14). Section 3622(c) merely requires that the Commission, in establishing and revising a system of ratemaking for market-dominant products, “take” these factors “into account.” Above the factors enumerated in § 3622(c) are the nine “objectives” enumerated in § 3622(b): the Commission is directed to design the ratemaking system “to achieve” those objectives. *Id.*

At the top of the hierarchy, however, is the CPI-based cap established by § 3622(d)(1). This is the only ratemaking standard that the legislation requires the Commission to enforce as an absolute command (“shall . . . include”). Moreover, § 3622(d)(2)(A) specifically states that, “except as provided under” § 3622(d)(2)(C)—*i.e.*, the provision authorizing catch-up recovery of previously unused index authority—“the annual limitations under paragraph (1)(A)”—*i.e.*, the annual cap on increases established by reference to the CPI under § 3622(d)(1)—“*shall apply to a class of mail*” (emphasis added). Section 3622(d)(1)(E) establishes a separate exception for exigent circumstances. By establishing the CPI cap as a mandatory constraint on each rate class (“shall apply”), § 3622(d)(2)(A), enumerating only two exceptions to it, §§ 3622(d)(2)(C) and 3622(d)(1)(E), and directing that the CPI cap shall be binding

“except as provided” by those exceptions, § 3622(d)(2)(A), Congress has foreclosed any exception to the CPI cap based on any other “objective,” “factor” or other provision of PAEA.

Allowing Section 3622(c)(2) to override the *specific* provisions of Section 3622(d) limiting annual rate increases to the CPI (§ 3622(d)(1)(A)) and applying the annual limitation separately to each class of mail (§ 3622(d)(2)(A)) would invert this clear statutory hierarchy. Such an expansive reading of § 3622(c)(2) would also violate the “fundamental rule of statutory construction” that, when two statutory provisions are arguably in conflict, “specific provisions trump general provisions.” *Navarro-Miranda v. Ashcroft*, 330 F.3d 672, 676 (5th Cir. 2003).

Our reading of the statute finds further support in Section 3622(d)(1)(D), which directs the Commission to “establish procedures whereby the Postal Service may adjust rates *not in excess of the annual limitations under subparagraph (A).*” 36 U.S.C. § 3622(d)(1)(D) (emphasis added). Allowing the attributable cost factor of § 3622(c)(2) to trump the CPI cap on classwide rate increases would effectively read the qualifying phrase “not in excess of the annual limitations under subparagraph (A)” out of § 3622(d)(1)(D).

Moreover, the absence of any exception to the CPI cap for classes that do not cover attributable cost contrasts starkly with the explicit and unambiguous wording of the handful of provisions of PAEA creating exceptions to the CPI cap or imposing an attributable cost floor on rates:

- (1) The exigent circumstances provision, Section 3622(d)(1)(E), authorizes rates to be increased by more than the CPI in “extraordinary or exceptional circumstances” within the meaning of that provision. The existence of the exception, and the procedures required for invoking it, are explicitly stated in Section 3622(d)(1)(E).
- (2) The banking provision, Section 3622(d)(2)(C), allows rate increases to exceed the annual CPI increase in certain circumstances when the Postal Service has not increased rates by the full amount of the CPI in previous years. The existence of this exception is expressly stated in Section 3622(d)(2)(C). So are the limits on use of this catch-up provision: “the rate increase may not exceed the annual CPI cap “for *any class or service* . . . by more than 2 percentage points.” 39 U.S.C. § 3622(d)(2)(C)(iii)(IV) (emphasis added).
- (3) Section 3633(a)(2) states that the Commission “shall” promulgate regulations to “ensure” that “each competitive product covers its costs attributable,” § 3633(a)(2). There is no comparable provision in PAEA for market dominant products.

The enactment of these explicit exceptions to the CPI, and the absence of any comparable exception for the failure of a market-dominant mail class to cover attributable costs, argue against inferring the existence of the latter exception. “When Congress provides exceptions to a statute,” the “proper inference . . . is that Congress considered the issue of exceptions and, in the end, limited the statute to the ones set

forth.” *United States v. Johnson*, 529 U.S. 53, 58 (2000); accord, *TRW Inc. v. Andrews*, 534 U.S. 19, 28-29 (2001).

In short, the language and structure of PAEA demonstrate that when Congress intended to create an exception to the CPI cap, or to make recovery of attributable costs a requirement in ratemaking, Congress did so expressly. The absence of any such provision in Section 3622(d) requires the inference that Congress intended the CPI cap to be binding, irrespective of the level of the attributable costs of a particular class of mail.

Valpak has made no attempt to reconcile its position with these provisions. Valpak has relied instead on 39 U.S.C. §§ 3653(c) and 3622(c), which direct the Commission to take “appropriate action” to “achieve compliance with the applicable requirements,” as evidence that the attributable cost floor of 39 U.S.C. § 3622(c)(2) trumps the index-based cap of § 3622(d). See Docket No. ACR2007, Valpak Comments (Jan. 30, 2008) at 48-49. This approach, however, simply begs the question. Sections 3653(c) and 3662(c) are enforcement mechanisms, not independent sources of substantive ratemaking standards. If rates for a class of mail are at the maximum level permitted by 39 U.S.C. § 3622(d), they are “in compliance with the applicable provisions of this chapter” within the meaning of § 3653(b)(1) whether or not the resulting revenue covers attributable costs. See pp. 7-12, *supra*. Without any basis for a finding of noncompliance, no remedial action by the Commission under § 3662(c) is “appropriate” under § 3653(c).⁷

⁷ The February 28 testimony of Professor Frank A. Wolak before the Subcommittee on Federal Workforce, Postal Service, and the District of Columbia of the House Committee on Oversight and Government Reform suffers from a similar error. Professor Wolak argues that the Commission should scrutinize proposed rate changes

B. Legislative History

The legislative history of the PAEA provides further confirmation that Congress intended the index mechanism set forth in Section 3622(d)(1) to impose an absolute limit on overall increases in rates for market-dominant mail classes in any given year, with no exceptions other than the two specified for exigent circumstances and the catch-up recovery of previously unused CPI authority. The legislative history reveals that Congress (1) was aware that a CPI-based cap increases could result in the failure of some mail classes to cover attributable costs, and (2) considered creating an exception to the cap in this circumstance, but (3) ultimately declined to do so.

Congress was well aware during the deliberations leading to the enactment of PAEA that a CPI cap on rate increases might result over time in the failure of one or more classes of mail to cover attributable costs. For example, at a 1999 hearing on the proposed “Postal Modernization Act of 1999” (H.R. 22), a prominent industry witness specifically proposed that the legislation allow above-index rate increases when “the Postal Service is not covering its costs in a class of mail”:

The third area when there could be some circumstances to go beyond the index, would be when a specific rate is too low, the Postal Service is not covering its costs in a class of mail. We think the Postal Service should have to go to the Regulatory Commission and adjust, one time, the index, make an adjustment in the index, to increase the rates for that class on a one-time basis and then go on, under the current provisions, with the index previously set by the Regulatory Commission for the remainder of the 5 years.

before they take effect to verify that they comply not only with the CPI cap but also with the attributable cost floor—and at the rate category level as well as the classwide level. The short answer is that Congress and the Commission have rejected the proposal to expand pre-effectiveness review proceedings into mini-rate cases. The merits of this policy decision are not open to reconsideration in this docket.

See H.R. 22, *The Postal Modernization Act of 1999*, Hearings Before the Subcommittee on the Postal Service of the Committee on Government Reform, U.S. House of Representatives, 106th Cong., 1st Sess. at 374 (testimony of Jerry Cerasale, Senior Vice President, Direct Marketing Association).⁸

Reflecting these concerns, early drafts of the legislation that culminated in PAEA would have relieved the Postal Service from the CPI cap for particular classes of mail that failed to cover attributable costs, either at the outset of the new ratemaking regime or later on. The predecessor of PAEA introduced by Congressman McHugh in 1996, for example, would have established an attributable cost floor with priority over the other factors specified in Section 3622(c). H.R. 3717, the proposed “Postal Reform Act of 1996,” would have required the Commission, in establishing “baseline rates” for future index adjustments, to give weight to the factors and policies of the legislation in a “descending order of priority” enumerated in the draft legislation. The very first factor listed in the bill—and thus the factor to be given the highest priority—was the requirement that each class of mail or type of mail service bear its attributable costs. See H.R. 3717, 104th Cong., 2d Sess. (1997), § 1001 (proposed revisions of 39 U.S.C. § 3622(b)). This hierarchy was omitted, however, from the version of the legislation that ultimately became law. In the law as ultimately enacted, attributable cost coverage was

⁸ Likewise, Postmaster General Potter testified in 2004 that, because an imperfectly crafted price cap could be harmful “given the volatility of today’s marketplace,” the price cap should “be constructed to recognize the many cost factors which enter into the ratemaking process, many of which are beyond our control.” *The Postal Service in Crisis: A Joint Senate-House Hearing on Principles for Meaningful Reform*, Joint Hearing Before the Committee on Government Reform, U.S. House of Representatives, and Committee on Governmental Affairs, U.S. Senate, 108th Cong., 2d Sess. 63 (2004) (“2004 Joint Hearings”).

relegated to a factor to be considered by the Commission in establishing the ratemaking system, rather than an absolute requirement directly governing the rates themselves.

Congress also considered—but did not enact—provisions authorizing special index adjustments when a class of mail subsequently fails to cover its attributable costs. For example, the Senate bill (S. 662), as reported by the Senate Committee on Homeland Security and Governmental Affairs to the full Senate in 2005, included a provision that would have allowed the Postal Service to apply unused rate increase authority in two specified circumstances, one of which would have allowed the use of previously unused pricing authority when a class failed to cover its attributable costs. As proposed in the reported version of S. 662, 39 U.S.C. § 3622(d)(2)(C) would have provided:

(C) BANKING UNUSED PRICING AUTHORITY – Notwithstanding paragraph (1), *for any class or service that failed to recover its attributable costs in the previous fiscal year, or for any classes and services when the Postal Service has operated at a loss for the last 2 years, rate increases may exceed the Consumer Price Index for all Urban Consumers by the amount increases in the previous year were less than Consumer Price Index for All Urban Consumers.*

See S. 662, § 201 (proposed § 3622(d)(2)(C)) (July 14, 2005); *Congressional Record*, Feb. 9, 2006, at S913. That provision, however, was deleted before S. 662 passed the Senate. See *Congressional Record*, Feb. 9, 2005, at S926, S929; *Congressional Record*, Dec. 8, 2006, at H9162. Neither that bill nor the legislation that Congress ultimately enacted in December 2006 contained any provision authorizing (let alone requiring) above-index rate increases for classes that failed to cover attributable costs.⁹

⁹ The bill enacted by the House, H.R. 22, did not contain any provision regarding unused rate authority. See, e.g., H. Rep. No. 109-66, Part I, 109th Cong., 1st Sess. 3-4, 46-48 (2005).

The omission from PAEA of limiting language in the earlier draft bills that would have allowed above-CPI rate increases for mail classes that fail to cover their attributable costs warrants the conclusion that the omission was intentional. “Few principles of statutory construction are more compelling than the proposition that Congress does not intend *sub silentio* to enact statutory language that it has earlier discarded in favor of other language.” *Benjamin v. Fraser*, 343 F.3d 46-47 (2d Cir. 2003) (quoting *INS v. Cardoza-Fonseca*, 480 U.S. 421, 442-43 (1987)); accord, *Nuclear Information and Resource Service v. U.S. Dept. of Transportation Research and Special Programs Administration*, 457 F.3d 956, 962 (9th Cir. 2006); *City of Jacksonville v. Dept. of Navy*, 348 F.3d 1307, 1312-1313 (11th Cir. 2003); *State of Rhode Island v. Narragansett Indian Tribe*, 19 F.3d 685, 700 (1st Cir. 1994).

C. Allowing An Attributable Cost Floor To Trump The Rate Cap For Individual Classes Would Undermine The Incentive For Efficiency That Congress Intended The Index To Create.

The decision of Congress to omit any exception to the CPI cap for market dominant mail classes that fail to cover attributable costs was entirely rational. Allowing an attributable cost floor to trump the Section 3622(d) rate cap would undermine one of the central purposes of the index mechanism: creating an incentive for the Postal Service to control its costs. As the Postal Service has noted:

A price cap system . . . provides greater incentives for efficiency due to the fact that it fundamentally changes the relationship between cost and price. Thus, reading this factor [§ 3622(c)(2)] as “requiring” that every class of mail cover its costs, regardless of the ceiling imposed by the cap, would eviscerate the framework set forth by Congress.

Docket No. RM2007-1, Initial Comments of the USPS (April 6, 2007) at 22-23.

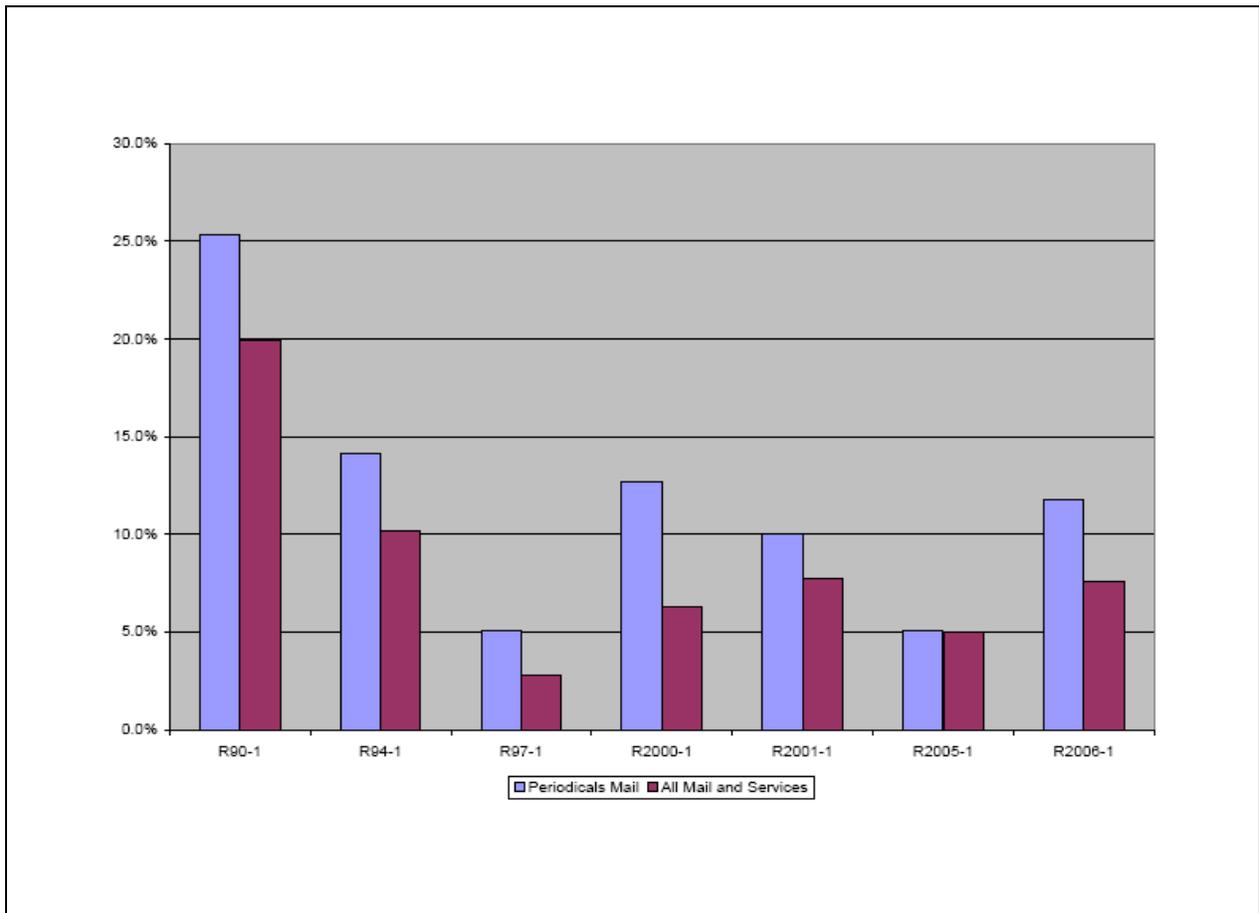
The fundamental logic of incentive ratemaking is to provide incentives for a regulated carrier to hold its cost increases below the level of the index, by “severing the linkage under traditional cost-of-service ratemaking” between a regulated company’s costs and rates.¹⁰ To create the desired incentive, however, the commitment not to allow an above-index rate increase if the regulated entity fails to control its costs must be credible; if that entity believes that nonrecovery of actual costs may plausibly cause the regulator to relent, the index mechanism loses its effectiveness as a control on costs.¹¹

Allowing the Postal Service to breach the rate cap on the theory that one or more mail classes would fail otherwise to cover attributable costs would have this very effect. Allowing above-index rate increases on this ground would restore the link between Postal Service rates and costs—first for relatively low markup classes such as Periodicals Mail and Media and Library Mail, and then for other classes with progressively higher markups. At the extreme, the Postal Service could allow its reported costs to increase by such a wide margin in a single year (perhaps by recognizing in a single year costs otherwise reported in multiple years, or by increasing significantly the percentage of total costs that are treated as attributable) to justify a breach of the rate cap for every major class of mail.

¹⁰ *Revisions to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, Order No. 561, FERC Stats. & Regs. ¶ 30,985 (1993) (“*Order No. 561*”) at 30,948-49 & n. 37, *aff’d*, *Ass’n of Oil Pipelines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

¹¹ Michael A. Crew and Paul R. Kleindorfer, “A Critique of the Theory of Incentive Regulation: Implications for the Design of Performance Based Regulation for Postal Service,” in Crew and Kleindorfer, eds., *Future Directions in Postal Reform* (2001) (a “chorus of economists” has focused on “regulatory commitment as the Achilles heel of” price cap regulation).

The history of Periodicals rates since 1990 confirms that this is not a frivolous concern. Despite the rapid growth of worksharing (and related cost-saving efforts such as barcoding) by periodical publishers in recent years, Periodicals rates have suffered above-average increases in every rate case since R90-1, except for the largely across-the-board increase of R2005-1:



The cause of any revenue shortfall for Periodicals mail is not the inadequacy of the rate increases allowed by the Commission since 1990, but the Postal Service's failure to control its costs. The consequences of this failure should be borne by the

Postal Service, not the Periodical mailers, who have already experienced outsized rate increases for the past decades. Such an outcome is hardly unfair to the Postal Service. To the contrary, it is precisely the outcome that index-based ratemaking is intended to achieve.

D. The Purported Failure Of Periodicals Revenue To Cover Attributable Costs Does Not Constitute An Exigent Circumstance Under 39 U.S.C. § 3622(d)(1)(E).

Valpak, apparently recognizing that failure to cover attributable costs may be insufficient legal justification for rate increases in excess of the CPI cap in a “conventional rate case” under 39 U.S.C. § 3622(d), suggests in the alternative that the Postal Service would be “compelled by PAEA” in this circumstance to file an “exigent rate increase” under 39 U.S.C. § 3622(d)(1)(E). Docket No. ACR2007, Valpak Comments (Jan. 30, 2008) at 51 n. 22. Here again, Valpak misreads the statute.

The exigency clause allows (but does not require) the Postal Service to increase rates faster than the CPI if the Commission finds, after the Postal Service so requests, that (1) “extraordinary or exceptional” circumstances have rendered index-based rate increases inadequate to cover the Postal Service’s costs, *and* (2) an additional increase is “reasonable and equitable and necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.” 39 U.S.C. § 3622(d)(1)(E). The circumstances that the drafters had in mind as sufficiently extraordinary to constitute exigent circumstances were national emergencies comparable in scale and severity to the “terrorist attacks of September 11,

2001, and the subsequent use of the mail to transmit anthrax . . .” H. R. Rep. No. 108-31, 108th Cong., 2d Sess. 11, 43 (2004).

Even a moment’s thought makes clear that the failure of Periodicals revenue to cover attributable costs (as computed by the CRA) satisfies neither requirement of the exigency clause. First, this circumstance can hardly be described, even on Valpak’s terms, as “extraordinary or exceptional.” Valpak’s own comments acknowledge that Periodicals mail (according to the CRA methodology cited by Valpak) has had a cost coverage of less than 100 percent “consistently . . . over a period of many years . . . repeated over a decade.” Docket No. ACR2007, Valpak Comments (Jan. 30, 2008) at 21, 45-46; *id.* at 46 (table summarizing CRA data for 1997 through 2007). Whether the shortfall calculated in the CRA reflects economic reality or is merely an artifact of the CRA methodology, a situation that has persisted for 11 years in a row is neither “extraordinary” nor “exceptional.”

Second, Valpak has failed to show that raising Periodicals revenue to 100 percent of attributable costs (again, according to the CRA methodology relied on by Valpak) is “necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.” Even the asserted FY 2007 revenue shortfall of \$447.7 million,¹² as inflated as that figure is,¹³ amounts to only about ½ of one percent of the Postal Service’s total revenue in the same year.

¹² Docket No. ACR2007, Valpak Comments (Jan. 30, 2008) at 46.

¹³ See pp. 4-7, *supra*.

CONCLUSION

For the foregoing reasons, the undersigned parties respectfully request that the Commission should authorize the Periodicals rates at issue in this docket to take effect without modification.

Respectfully submitted,

/s/

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