

BEFORE THE  
POSTAL REGULATORY COMMISSION  
WASHINGTON, DC 20268-0001

Report on Universal Postal )  
Service and the Postal Monopoly )

Docket No. PI2008-3

**VALPAK DIRECT MARKETING SYSTEMS, INC. AND  
VALPAK DEALERS' ASSOCIATION, INC.  
REPLY COMMENTS REGARDING UNIVERSAL POSTAL SERVICE  
AND THE POSTAL MONOPOLY  
(August 1, 2008)**

The Postal Accountability and Enhancement Act ("PAEA"), Public Law 109-435, requires the Commission to "submit a report to the President and Congress **on universal postal service and the postal monopoly** in the United States...." § 702(a)(1) (emphasis added). The Commission opened Docket No. PI2008-3 to receive comments for consideration in the preparation of its report. Initial comments were filed by June 30, 2008, and reply comments are due by August 1, 2008. Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. (hereafter "Valpak") submit these joint reply comments in response to the initial comments of several parties.

**1. Below Cost Rates for Periodicals**

The Commission's Notice, issued April 18, 2008, invited parties to comment, *inter alia*, on:

*Rates and Affordability of Service.* Universal service charges prices that are fair, reasonable, nondiscriminatory, and based on a fair and equitable apportionment of costs.

In response to this invitation, Magazine Publishers of America, Inc. (“MPA”) asks that special lower rates for Periodicals be found mandated not by a public policy favoring ECSI (“educational, cultural, scientific, and informational”), but by the universal service obligation (“USO”), stating that:

a longstanding element of **universal service**, now codified at 39 U.S.C. § 3622(c)(11), **requires** not only the universal delivery of Periodicals mail, but **delivery at special rates**. [Comments of MPA, p. 3 (emphasis added).]

The Nation Company L.P. and the Magazines of Politics, Policy, and Current Events Coalition (“MPPACE”) want the USO stretched to cover still lower rates for Periodicals (which likely are already below attributable cost for most or all of the publications represented by MPPACE), as well as better service (which would require the Postal Service to incur even higher uncompensated costs for periodicals):

It is perhaps time to re-evaluate the 1970 Postal Reorganization Act and its requirement that the USPS, and **each class of mail, pay its own way, and to instead look toward other sources of revenue to maintain our current system**. A market-based service is not what the architects of our laudable postal system envisioned 200 years ago. We urge that **current levels of service be maintained and enhanced**. We also urge that, in light of the invidious effect on smaller **periodicals** such as ours, magazines the [founding] fathers thought critical to a flourishing democracy, the 2007 **radical rate restructuring** be revisited. [Comments of Nation Company and MPPACE, p. 2 (emphasis added).]

Lastly, American Business Media (“ABM”), points out that:

no one—not even American Business Media—would contend that the postal rates established by Congress for the 200 years prior to the Postal Reorganization Act of 1970 reflected a fair and equitable allocation of costs. Rather, they reflected policy decisions that, in turn, led to **a rate schedule rife with non-**

**compensatory rates, cross subsidies** and, probably, excessive rates. [Comments of ABM, p. 5 (emphasis added).]

ABM fails to mention that the inevitable effect of cross-subsidies and below-cost rates for periodicals doubtless was to spawn and support many publications whose existence, from an economic perspective, depended on continued subsidization of their distribution costs. Then, in a thinly-veiled plea for higher subsidization for those publications which it represents, ABM states that:

even though affordable rates are a sine qua non of universal postal service, **it is not necessary**—for this purpose—**that those rates be based upon a “fair and equitable” allocation of costs.** Rather, history shows all too well, a movement toward rates with greater cost recognition may be inconsistent with the provision of universal service, and it would be worthwhile for the Commission to address this tension. [*Id.*, pp. 5-6 (emphasis added).]

In light of the above comments from various representatives of mailers that use the Periodicals class, a reminder that USO stands for “universal service obligation,” **not** “universal subsidy obligation,” may be in order. For instance, MPA is quick to cite to 39 U.S.C. § 3622(c)(11), the “ECSI” provision, but it does not mention 39 U.S.C. § 3622(c)(2), which **requires** that each class of mail pay its attributable costs.<sup>1</sup> The ECSI provision calls for a reduced markup **above costs**, not continuing cross-subsidies to support a Periodicals rate structure that fails to cover attributable costs. Any structure of rates that does not result in revenues that exceed attributable costs should not be considered affordable. The ECSI

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<sup>1</sup> Nor does MPA mention that, for the last 11 years, revenues from Periodicals have failed to cover their attributable costs. *See* Docket No. ACR2007, Valpak Initial Comments (Jan. 30, 2008), pp. 44-48. Nor does MPA mention that PAEA contains other rate-setting factors, all of which are on par with one another.

provision cited by MPA is contained in PAEA (and was contained in the Postal Reorganization Act of 1970 (“PRA”)), but it pertains to rates, not service, and Valpak would oppose transforming a statutory rate provision into a component of the Postal Service’s universal service obligation.

**2. The Concept of Affordable Rates Does Not Justify Subsidized Rate Structures that Do Not Cover Attributable Costs**

As ABM’s comments note (along with comments by a number of other parties), affordable rates are a *sine qua non* of universal postal service. MPA expressed its belief that the CPI-based cap is “the best way to ensure affordability while providing sufficient pricing flexibility to enhance operational efficiency and grow mail volumes.” Comments of MPA, p. 7. Defining “affordable rates” can be a difficult assignment in any context, but especially so in the context of the Postal Service’s USO and its current circumstances. Indeed, many parties have discussed the tension created by declining volumes (especially of First-Class Mail), increasing costs, the CPI cap, and the need to maintain rates as close to current (affordable) levels as possible.

What is affordable for one individual or firm may not be affordable for others. For all those who currently can afford to use, and are using, the mail, doubtless others always exist who cannot afford whatever the current rates are, or whose usage would increase if only current rates were lower. That is the essence of an economist’s demand curve. By way of illustration, the Postal Service Comments (filed on June 30, 2008) indicates at 11 that “[i]n 1845 and 1851, Congress passed laws slashing postage rates, which increased access to the mail system by making its use more affordable.”

With respect to Periodicals, for example, if current rates (which, collectively, do not cover attributable costs) were to be **reduced by 50 percent**, a small host of new publications could be expected to appear, and the continued existence of most, if not all, would be predicated on perpetuation of the substantially-reduced, below-cost rate. And, if the Postal Service were to offer distribution **free of charge** to Periodicals, the resulting response might be vast. Even though these rate breaks would enrich the publishers of many for-profit periodicals, they would not be good postal policy.

Since the time of the founding fathers, over 200 years ago, thousands of periodicals (including newspapers) have been born, only to disappear over time. This turnover among publications has occurred despite the historical cross-subsidies and non-compensatory rates mentioned by ABM. A variety of reasons explain the disappearance of now-defunct publications. Succinctly, though, at some point the balance between their revenues and costs (including the cost of distribution) made most of them economically non-viable, at which point they ceased publication.

### **3. The USO Justifies Subsidies to Disadvantaged Groups of Mail Users, Not Products**

The USO, however defined, will doubtless require that the Postal Service provide segments of the public with various **services** (not products) that do not cover their cost, *e.g.*, operate small, uneconomic post offices, or deliver mail in rural areas to low-density, sparsely-populated routes that receive only a modicum of mail. The obligation to provide certain postal services at a loss necessarily means that such services must be subsidized. Historically, the postal monopoly has provided the means for the Postal Service to augment its revenues and help offset losses from the provision of subsidized services. This has been the case especially

since 1970, when Congress enacted the Postal Reorganization Act and sought to put the Postal Service on an essentially self-sustaining basis. Thus, it is entirely appropriate for the Commission to consider the role of the monopoly in supporting the USO.

Within the context of a wide-ranging study of the USO, however, it is not appropriate to consider special pleas for additional subsidies to selected periodicals (or any other product, for that matter), as put forth by The Nation Company and MPPACE.<sup>2</sup> Increasing the level of subsidization to publications that do not cover their attributable cost — whether they be existing publications or publications newly-established in response to an increase in the subsidized postage rate — is not the way to reduce and eliminate the current deficit between periodicals' revenues and attributable costs. Nor is it appropriate for a study of the USO by the Commission to usurp Congressional authority and (i) “re-evaluate the 1970 Postal Reorganization Act ... and ... look [for] other sources of revenue” (as suggested by MPPACE), or (ii) overlook and circumvent the requirement of PAEA that each class of mail pay its attributable costs, or (iii) re-visit the appropriateness of cost-based rates, as suggested by ABM.

Congress debated and negotiated PAEA over a decade, and during that time Congress heard the “founding fathers” argument and had ample opportunity to re-institute cross-

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<sup>2</sup> Even within the Periodicals class, there are conflicts. For example, those publications with little or no advertising receive a rather substantial subsidy from other publications that contain a high percentage of advertising matter. Should advertising budgets migrate from periodicals to the Internet, any ability of the Periodicals class to cover its attributable costs would be seriously jeopardized, and those publications whose rates are now heavily subsidized by the advertising revenues of other publications could be at risk of substantial rate increases. Conversely, if advertising in periodicals somehow were to flourish over current levels, the need for rate increases in Periodicals would diminish.

subsidies and non-compensatory rates similar to those that may have prevailed prior to postal reorganization. By enacting the Postal Reorganization Act of 1970, and then by enacting PAEA in its present form less than two years ago, Congress explicitly rejected that approach. The USO study mandated by PAEA is not, and should not be construed as, an invitation for the Commission to legislate a new ratemaking structure to benefit periodicals at the expense of all other mailers.

Respectfully submitted,

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