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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON DC 20268-0001

ANNUAL COMPLIANCE REPORT, 2008	))	Docket No. ACR2008

REPLY COMMENTS OF
NATIONAL POSTAL POLICY COUNCIL
(February 13, 2009)

The National Postal Policy Council ("NPPC") respectfully submits these reply comments concerning the Postal Service's Annual Compliance Report ("ACR") for Fiscal Year 2008. We respond here to the initial comments of American Postal Workers Union, AFL-CIO ("APWU")—and, in particular, to APWU's claim that the existing "workshare discounts for First-Class Mail Presort Letters/Cards and the elimination of the Bulk Metered Mail (BMM) benchmark do not comply with the requirements of the PAEA." APWU Comments (Jan. 30, 2009) at 1.

APWU has advanced claims of this kind repeatedly in litigation since the beginning of 2008. In Docket No. R2008-1, for example, APWU singled out the delinking proposed by the Postal Service as a ground for rejecting the rate changes:

> [T]he Postal Serve has again de-linked workshare discounts from single piece First Class letter rates by using a workshared mail piece as its benchmark. Notwithstanding the fact that the proposed workshare discounts have been carefully calculated to skirt this issue, it is important that the Commission reiterate the fact that the BMM First Class letter remains the benchmark that must be used to calculate workshare discounts for First Class letter mail.

Docket No. R2008-1, *Notice of Price Adjustment*, APWU Comments (March 3, 2008) at 2-3. *Accord*, Docket No. ACR2007, *Annual Compliance Report*, APWU Comments

(Jan. 31, 2008) at 2-3; Docket No. PI2008-3, *Report on Universal Postal Service and the Postal Monopoly*, APWU Initial Comments (June 30, 2008) at 5-6.

With equal regularity however, the Commission has declined to adopt APWU's reading of the statute. In Docket No. R2008-1, the Commission, after noting APWU's challenge to the proposed delinking, held that the "workshare discounts" proposed by the USPS for First-Class Mail "satisfy the requirements of 39 U.S.C. § 3622(e)" and allowing them to take effect without modification. Docket No. R2008-1, Order No. 66 (March 17, 2008) at 22 & 57; Docket No. ACR2007, *Annual Compliance Determination* (Mar. 27, 2008) at 63-64 (noting but declining to resolve issue).

APWU's latest comments offer no justification for a different outcome. It is time for the Commission to put an end to this issue by expressly holding that PAEA leaves the Postal Service free to establish rate differentials between Presort and Single-Piece First-Class Mail that exceed that cost differences between the two products.

First, APWU's assumption that rate differentials between Single-Piece and Presort mail are constrained by the limits on "workshare discounts" imposed by 39 U.S.C. § 3622(e) ignores the statutory scheme. The primary mechanism established by Congress for enforcing compliance with Section 3622(e) is the Commission's review of the Postal Service's annual compliance report under 39 U.S.C. §§ 3652 and 3653. Section 3652(b), however, clearly limits the required information about "workshare discounts" to rate differentials *within* "each market-dominant product." As the Postal Service has correctly noted, the language of 39 U.S.C. § 3652(b),

> which directs the Postal Service to provide the specified workshare data "*with respect to each market-dominant product* for which a workshare discount was in effect," suggests that the proper analysis is to measure

> worksharing differences on an intraproduct, rather than inter-product, basis. This is buttressed by the fact that section 3652 generally requires the reporting of data by product.

USPS FY 2008 Annual Compliance Report (December 29, 2008) at 50-51. In Docket No. RM2007-1, the Postal Service proposed a mail classification schedule ("MCS") that defined Presort and Single-Piece First-Class Mail as separate products. The Commission expressly approved this bifurcation over APWU's objections. Docket No. RM2007-1, *Regulations Establishing A System of Ratemaking*, Order No. 43 (Oct. 29, 2007) at ¶¶ 4013-4018. While rate relationships between separate products may give rise to challenges under other statutory provisions (e.g., inadequate rate differentials may be challenged as anticompetitive, unreasonable or discriminatory), the bifurcation of Single-Piece and Presort First-Class into separate products clearly bars a challenge to rate differences between the two products under Section 3622(e).

Second, while circumstances may warrant recombining two products into one product in appropriate circumstances, APWU has made no such showing here. The notion that the only distinction between Single-Piece and Presort First-Class Mail is just "the presorting and prebarcoding done to these letters" (APWU Comments at 3) ignores the fundamental cost and market differences between the two kinds of First-Class Mail. Even the Greeting Card Association, a perennial ally of APWU on issues relating to the relationship between Single-Piece and Presort rates, has conceded that the two products are fundamentally different:

> The costs are clearly different for those letters/postcards that are entered in bulk and meet the many eligibility characteristics for bulk prices, as opposed to those pieces that are entered individually; indeed, the costs for bulk First-Class Mail have been separately reported in the CRA for many years. Also, on a broad level, the nature of the communication and its purposes differ between bulk and single piece letters/postcards, with the

> former generally used for business applications involving groups such as customers and the latter generally used for individual correspondence or transactions. Thus, from both a cost and a market perspective, bulk letters and postcards are a much different product than are single-piece letters and postcards.

Docket No. ACR2007, *Annual Compliance Report*, Reply Comments of GCA (Feb. 13, 2008) at 4 (quoting with approval PRC Docket No. RM2007-1, USPS Submission of Initial Mail Classification Schedule In Response to Order No. 26 (Sept. 24, 2007) at 12).

Third, APWU makes much of the Commission's dictum in ACR2007 that "[w]hether or not a rate differential is a worksharing discount may depend, in part, on whether the categories in question have substantially similar demand characteristics." APWU Comments at 1-2 (quoting *FY 2007 Annual Compliance Determination* at 63-64). But analysis of the evidence on cost and demand characteristics in this docket makes clear that the rate differentials proposed by the Postal Service between Presort and Single-Piece First-Class Mail, rather than too large, are almost certainly too small, and that the relief sought by APWU would make matters worse.

Specifically, the evidence submitted by the Postal Service in this docket indicates that the own price elasticities of Single-Piece and Presort First-Class Mail are roughly the same: -0.218 for Single Piece letters and -0.250 for Presort letters.[1] By contrast, the average percentage *markup* of Single-Piece First-Class letter mail over attributable costs (67.1 percent) is only about *one-third* the corresponding percentage markup over attributable costs generated by Presort First-Class letter mail (198.1 percent).[2] Hence,

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[1] USPS, Econometric Demand Equation Tables for Market Dominant Products as of November 2008 (submitted to PRC on January 16, 2009).

[2] *See* USPS FY 2008 Annual Compliance Report (Dec. 29, 2008) at 18, Table 1, "cost coverage" column. The percentage markup is the cost coverage minus 100 percent.

the Postal Service almost certainly could improve its financial position by reducing Presort First-Class rates (or increasing them at a below-average rate) and using the resulting headroom under the CPI cap for First-Class Mail to raise Single-Piece Class rates.[3]

We are not asking the Commission to impose such a rate rebalancing in this docket. At a minimum, however, the Commission should refrain from forcing the Postal Service to move in the opposite direction. A narrowing of the rate spread between Presort and Single-Piece First-Class Mail would needlessly worsen the Postal Service's already-significant shortfall in contribution to institutional costs. At a time when the Postal Service's financial situation has been described as "grave"[4] and a "crisis,"[5] APWU's agenda is a luxury that the Postal Service and the American public cannot afford.

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[3] This conclusion is a corollary of the standard economic formula for maximizing the overall profit of a multi-product firm, with or without an overall regulatory constraint on profits. *See* William J. Baumol and David Bradford, "Optimal Departures From Marginal Cost Pricing," 60 *Amer. Econ. Rev.* 265-283 (June 1970); Jean-Jacques Laffont and Jean Tirole, *A Theory of Incentives in Procurement and Regulation* 30-31 (1993).

[4] Statement Of Postmaster General/CEO John E. Potter Before The Subcommittee On Federal Financial Management, Government Information, Federal Services And International Security Of The Committee On Homeland Security And Governmental Affairs United States Senate (January 28, 2009).

[5] Statement of PRC Chairman Dan G. Blair before the Senate Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security (January 28, 2009).

CONCLUSION

NPPC respectfully requests that the Commission find that the rate differentials between Presort and Single-Piece First-Class Mail in effect during FY2008 did not exceed the maximum levels allowed by law.

Respectfully submitted,

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