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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

NOTICE OF PRICE ADJUSTMENT	Docket No. R2009-2

RESPONSES OF THE UNITED STATES POSTAL SERVICE
TO QUESTIONS 1-9 OF CHAIRMAN'S INFORMATION REQUEST NO. 3
(March 2, 2009)

Chairman's Information Request (CIR) No. 3 was issued on February 23, 2009. The request sought answers no later than March 2, 2009. Attached are the Postal Service's responses to questions 1-9. One response refers to materials filed separately in the non-public annex. A separate notice of filing is submitted today for those materials.

Respectfully submitted,

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UNITED STATES POSTAL SERVICE RESPONSE TO
CHAIRMAN'S INFORMATION REQUEST NO. 3

1. Please refer to Workpaper, USPS-R2009-2/1, First-Class Mail, at 4. It states "A volume adjustment factor of 1.1167 was applied to all rate groups to match with the total FCMI [First-Class Mail International] volume in the FY 2008 RPW Report (Revenue, Pieces, and Weight Report). The volume adjustment factor was derived by dividing total RPW volume by total billing determinant volume." Also, please refer to the Excel file, CAPCALC-FCMI-FY2009.xls, worksheet FY 2008 FCMI.

   a. Please explain the reason(s) underlying the difference between the RPW and the billing determinants that prompted development of an adjustment factor.
   b. Please provide the "total RPW volume" figure and the "total billing determinant volume" figure used to derive the volume adjustment factor.
   c. Please provide an electronic spreadsheet using the volume adjustment factor to calculate the FCMI letters, flats, and parcels volumes presented in worksheet FY 2008 FCMI. The electronic spreadsheet provided should show all formulas and calculations.

RESPONSE:

a. The adjustment factor was used to align the total billing determinant volume with that reported in the RPW. This is consistent with last year's methodology. Since these are weighting factors, the application of the adjustment factor has little effect on the overall distribution.

b. The FY 2008 RPW volume for FCMI is 395,954,815 and the FCMI billing determinant volume is 354,575,362. In the preparation of this response, an error was found that is discussed in section c.

c. ChIR.3.Q.1.2.FCMI_SIRVO-FY2008.xls is an Excel file attached to this response electronically. The FY 2008 FCMI worksheet of that file shows the application of the volume adjustment factor in cell L88 to the rate group billing determinant totals. The unadjusted tables for FCMI Letters, Flats, and Parcels are given in rows 1-70. The flats table is a combination of the flat volume after the May 2008 increase with all letter volume from four to sixty-four ounces before the May 2008 increase. The adjusted tables for letters, flats, and parcels are given in rows 94-121.

Due to the omission of some of the quarterly FCMI billing determinants in the file that grouped letters and flats, the data was recast in the REVISED FY 2008 FCMI worksheet of ChIR.3.Q.1.2.FCMI_SIRVO-

FY2008.xls. A revised factor of 1.05323 is applied to the combined FCMI Letters and Flats billing determinant total of 362,853,626 to match the RPW volume of 382,168,704. For FCMI Parcels, a revised factor of 1.11341 is used to match the RPW volume of 13,786,111. The unadjusted tables for FCMI Letters, Flats, and Parcels are given in row 1-70. The adjusted tables for letters, flats, and parcels are given in rows 93-120.

2. Please refer to Workpaper, USPS-R2009-2/1, First-Class Mail, at 6. It references a "volume adjustment factor of 1.07944" for FCMI cards, and the derivation of this factor by "dividing total RPW volume by total billing determinant volume." Also, please refer to the Excel file, CAPCALC-FCMI-FY2009.xls, worksheet FY 2008 FCMI CARDS.

   a. Please explain the reason(s) underlying the difference between the RPW and the billing determinants that prompted development of an adjustment factor.
   b. Please provide the "total RPW volume" figure and the "total billing determinant volume" figure used to derive the volume adjustment factor.
   c. Please provide an electronic spreadsheet using the volume adjustment factor to calculate the FCMI card volumes presented in worksheet FY 2008 FCMI CARDS. The electronic spreadsheet provided should show all formulas and calculations.

RESPONSE:

a. The adjustment factor was used to align the total billing determinant volume with that reported in the RPW. This is consistent with last year's methodology. Since these are weighting factors, the application of the adjustment factor has little effect on the overall distribution.

b. The FY 2008 RPW volume for FCMI Cards is 24,078,992. The FCMI Cards billing determinant volume is 22,306,849.

c. ChIR.3.Q.1.2.FCMI_SIRVO-FY2008.xls is an Excel file attached to this response electronically. The FY 2008 FCMI CARDS worksheet of that file shows the resulting application of the volume adjustment factor in cell K14 to the rate group billing determinant totals.

3. Please refer to Table 1 below concerning Outside County Periodicals.

Table 1			
Type of Worksharing	**Discount**	**Cost Differential**	**Passthrough**
Docket No. R2008-1*			
Pre-Sorting			
3-Digit Automation Letter	$0.015	$0.003	437.3%
Docket No. R2009-2**			
Presorting			
3-Digit Automation Letter	$0.020	$0.002	1000.0%
* USPS Notice of Market-Dominant Price Adjustment, February 11, 2008, App._B_ Passthrough Tables.xls, Sheet: Periodicals Outside County			
** USPS Notice of Market-Dominant Price Adjustment, February 11, 2009, App._B_ Passthrough Tables.xls Sheet: Periodicals – OC Pcs.			

a. Please confirm the accuracy of Table 1. If not confirmed, please modify the table accordingly.
b. Please clarify and expand the justification for increasing the discount for presorted 3-Digit Automation Letters.

RESPONSE:

a. Confirmed.
b. While the discount increases even though the cost difference narrows, it is important to note the relatively small volume of mail involved. The 3-Digit Automation Letter category contains only 0.3 percent of Periodicals volume. The rate design for Periodicals is very complex, and this particular element of it, including the resulting discount, was part of an iterative process that needed to balance several goals. Those goals include staying within the cap, and keeping the overall postage changes within a narrow band. In any event, this particular discount was a byproduct of that process, and the resulting passthrough is greater than 100 percent. Due to the very small volume, the Postal Service does not contend that any section of 3622(e)(2) other than (C) necessarily applies.

4. Please refer to USPS-FY08-04, Excel file, "08 Special Services BD.xls," and Library Reference R2009-2/5, Excel file, "Capcal-SpecServ-FY09.xls." The table below, which shows reported Standard Bulk Mail Permits, is based on the foregoing files.

Table 2			
USPS-FY08-04		**R2009-2/5**	
Revenue (1)	$58,775,909 (2)	**Revenue** (3)	$58,892,295 (4)
Estimated permits: Regular Nonprofit	246,492 85,688	**Estimated Permits:** Regular Nonprofit	246,980 126,939
Total Permits	332,180	**Total Permits**	373,919

a. Please confirm the accuracy of Table 2. If not confirmed, please modify the table accordingly.

b. Please reconcile the Billing Determinants in column (2) with the Billing Determinants in column (4).

RESPONSE:

a. Confirmed.

b. The data presented in column 2 are correct. Column 4 and R2009-2/5 should contain the same data as column 2.

5. Please refer to the United States Postal Service Notice of Market-Dominant Price Adjustment, February 10, 2009, at 24. It states, "[t]he creation of new Mailing Agent prices within the Gold and Platinum tiers is intended to better align the revenue source with the source of the costs of providing the service." Also, please refer to Library Reference, R2009-2/5, Excel File, "Capcal-SpecServ-FY09.xls," worksheet "Confirm".
   a. For a mailer acting as a mailing agent, what are the current and planned fees for the Gold and Platinum subscription levels?
   b. Please provide the percentage increases represented by the planned increase in fees.
   c. Please explain how the new mailing agent fees better align revenues and costs within the Gold and Platinum tiers.

RESPONSE:

a. The fees for Gold and Platinum subscription levels today are $6,500 and $23,500. The planned prices for mailing agents are $10,000 and $250,000, respectively.

b. The percentage increases are 53.8 percent for Gold and 963.8 percent for Platinum.

c. The major costs for Confirm are tied to capacity and development costs. Capacity is directly tied to scan usage. So, as Confirm customers use more scans, they are driving costs up. Mailing agent subscribers use more scans than do mail owner subscribers. In October 2008, mailing agent subscribers accounted for 59 percent of scans. The five largest mailing agent subscribers accounted for 36 percent of all scans, but these five mailing agents contributed only 12 percent of FY 2008 revenue.

Moreover, Confirm development costs tend to be driven by mailing agent subscriptions. Most of the Postal Service's programming enhancements to Confirm are completed to meet the needs of mailing agent subscribers, and primarily benefit them.

Therefore, the planned mailing agent prices would improve the alignment of revenues with costs for Confirm.

6. Please refer to Library Reference R2009-2/5, Excel File, "Capcal-SpecServ-FY09.xls," worksheet "Hardcoded Data." The table, "Necessary Weighted Fees for Certain Fees, where volume has to be derived" uses fees from Docket Nos. R2005-1 and R2006-1 to calculate the weighted fees for certain Special Services (Business Reply Mail and Address Change for Election Boards). For FY 2008, the partial year fees that were in effect were from Docket Nos. R2006-1 and R2008-1. Please explain the use of partial year fees from Docket Nos. R2005-1 and R2006-1 to calculate the FY 2008 weighted average fee rather than the most recent partial year fees from Docket Nos. R2006-1 and R2008-1.

RESPONSE:

The use of Docket Nos. R2005-1 and R2006-1 prices was an error. The table should have been updated to reflect the Docket Nos. R2006-1 and R2008-1 prices in place during Fiscal Year 2008. The correct table would look like this:

Necessary Weighted Fees for Certain Fees, where volume has to be derived.

Product	R2006-1	R2008-1	Weighted Price
Business Reply Mail			
Permit and Account Maintenance Fees			
Permits	175.00	180.00	176.94
Account Maintenance Fee	550.00	565.00	555.81
Quarterly Fee	1,800.00	1,855.00	1,821.31
Non-Letter Monthly Fee	900.00	930.00	911.62
Mailing List Services			
Address Changes to Election Boards	0.28	0.32	0.30

7. Please refer to Library Reference R2009-2/5, Excel file, "Capcal-SpecServ-FY09.xls" and Word file, "Preface.doc", which provides certain information regarding Library Reference R2009-2/5. Also, please see Tables 3 and 4 below.

Table 3	
USPS Proposed Adoption Rates for Full Service Address Correction Service	
First-Class Mail	
Electronic	20%
Automated	42%
Periodicals	
Electronic	48%
Standard Mail	
Electronic	35%
Automated	51%
Bound Printed Matter	39%

Table 4	
USPS Proposed Weighted Confirm Transactions	
Tier	**Transactions**
Bronze	7
Additional Scans	0
Silver	20
Additional Scans	0
Gold	
Mail Owner	80
Other	50
Additional Scans	20
Platinum	
Mail Owner	30
Other	15
Total Subscribers	202
Additional IDs	
Quarter	74
Annual	309

a. Section B of "Preface.doc" explains any adjustments to the Special Services Billing Determinants. Section B states that for Address Correction Service (ACS) the "cap compliance calculations have been adjusted to reflect a reasonable expectation of how many existing ACS pieces will qualify for Full Service ACS." Table 3 above lists the "reasonable expectation" adoption percentages estimated by the Postal Service.

i. Please confirm the accuracy of Table 3. If not confirmed, please modify the tables accordingly.

ii. Please explain the bases for the specific adoption rates and provide all worksheets related thereto.

b. Section B states that for Confirm Service, the "weight adjustments for the Gold and Platinum splits were based on current subscription levels" and that the "adjustment for the Bronze tier was based on estimated scan usage."

i. Please confirm the accuracy of Table 4. If not confirmed, please modify the tables accordingly.

ii. Please explain the bases for the adjustments to the Bronze, Gold, and Platinum tiers and provide all worksheets related thereto.

RESPONSE:

a. i. Confirmed, except that the First-Class Mail electronic adoption rate is 25 percent, not 20 percent as shown in the table.

ii. The Postal Service provided adoption rates for each class of mail (as well as some specific price categories) for the period before November 29th and the period after November 29th. The Full Service ACS benefits would be available at one adoption rate for 29 weeks prior to Full Service pricing becoming effective, and at a second adoption rate after the Full Service price differentials are implemented (for the final 23 weeks of the year).

Automated ACS to Full Service ACS

The adoption rates for automated ACS presented in table 3 were derived by weighting the before and after adoption rates for the classes (or price categories if applicable[1]) by the proportion of the year that the adoption rate

[1] When there were different adoption rates for each price category the adoption rates for the categories were weighted to create a class adoption

would be in effect (29/52 and 23/52, respectively). Next, the weighted adoption rate was applied to the FY 2008 ACS volume.

Electronic ACS to Full Service ACS

Adoption rates for customers currently using Electronic ACS are likely to be lower than for those customers already using Automated ACS. Mailers of letter-shaped mail using Electronic ACS could have obtained significant savings in ACS expenditures by using an Intelligent Mail barcode (IMb) and requesting Automated ACS, even without the introduction of Full Service ACS. Therefore, these customers have already identified themselves as less likely or quick to make the jump to full service Intelligent Mail. But for flat-shaped mail this is the first opportunity mailers have to get an ACS price lower than the electronic price. As such, it is likely that there will be significant interest in moving to Full Service for mailers of flat-shaped mail.

The relevant worksheet is provided as an electronic attachment to this response, with the Excel file name ChIR.3_Qu7a ACS Worksheet.xls.

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rate. For example, in the case of First-Class Mail (FCM) the following process was used:

1. The weighted adoption rates based on time were calculated. In the case of flats this was (25%*29+44%*23)/52 = 33%.
2. Second the volumes of the FCM categories represented by the adoption rate was determined (21,290,705 for Letters and Cards and 221,644 (33%* 663,528) for Flats).
3. The adoption rate for the class was derived by summing the adoption volumes and dividing by total volume. (21,290,705+221,644)/ 50,736,646 = 42%.

b. i. Confirmed. This table represents a good faith attempt to redistribute the FY 2008 volume into the new pricing structure.

ii. The adjustments were not the result of a direct mapping of individual Confirm subscribers. A snapshot of Confirm subscriber scan usage, along with some user characteristics (e.g., number of IDs) was used as a starting point for remapping FY 2008 Billing Determinant data into the new pricing structure. However, the seasonal nature of Confirm scan usage by some subscribers made it necessary to apply judgment when making the mapping decisions. The Confirm snapshot contains user-specific data that could be used to identify Confirm subscribers, even though the customer names are omitted. As such, this worksheet is being filed under seal as USPS-R2009-2/NP1 in the non-public annex.

Bronze – Some Silver and Gold subscribers will be able to meet their scan usage requirements with a Bronze subscription at a considerable savings, and so are expected to use the Bronze Tier.

Gold – Some Platinum subscribers who are mailing agents were mapped to the Gold tier, and would meet their scan requirements by buying additional scans, rather than subscribing at the new mailing agent Platinum Tier. A mailing agent Gold subscription with 2 additional IDs (a total of three as is included in the Platinum tier) can use more than 1.7

billion scans before their Confirm expenditure hits $250,000, the new Platinum mailing agent price.

Platinum – Based on estimates of Confirm usage, a very small number of Platinum subscribers who are mailing agents (five) are expected to use 1.7 billion or more scans. Another ten current Platinum subscribers are expected to subscribe at the new mailing agent Platinum tier, in recognition of the Postal Service's lack of specific knowledge about each Confirm subscriber's business plans, and whether the mailing agent Gold subscription is better for each subscriber. [2]

[2] The volumes could have been adjusted in ways that would have resulted in a lower reported overall percentage change in price using the same new prices for Confirm. For example, a more aggressive remapping would have led to many fewer mailing agents with Platinum subscriptions, and a very large increase in the number of additional scans used for Gold subscriptions. But the transient behavior of some Confirm subscribers, and the expiration of subscription periods during a year make it difficult to identify exactly how many scans a subscriber uses. Therefore a less aggressive remapping was chosen to ensure that any modifications would result in a lower reported percentage change in price, ensuring that Special Services as a class does not exceed the price cap.

8. Please refer to Library Reference R2009-2/5, Excel file, "Capcal-SpecServ-FY09.xls", Worksheets 'Cap Cal Details', 'Cap Cal Page', and 'Address Correction'.
   a. The 'Cap Cal Details' worksheet, cell B14, shows Total Before Rates revenue for Address Correction Services of $53,688,323, which excludes the total before rates revenue for Full Service. The 'Cap Cal Page' worksheet, cell B3, shows Total Before Rates revenue for Address Correction Services of $71,029,871. Please reconcile the two, and explain the exclusion of the Full Service revenue in the 'Cap Cal Details' worksheet.
   b. For the 'Address Correction' worksheet, please confirm that the Before Rate revenue for Bound Printed Matter – Full Service is $76,016 (304,065 * $0.25). If you do not confirm, please explain.

RESPONSE:

a. Cell B14 in the 'Cap Detail Page' worksheet erroneously omitted cell B13 from its formula.

b. Confirmed.

9. While the Postal Service indicates its intention to implement the majority of rates on May 11, 2009, the discounts for full-service IMb and Personalized Stamped Envelopes will be implemented on later dates. This complicates the calculation of percentage change in rates under Commission rule 3010.23, which is generally designed to evaluate sets of rate changes that are to be simultaneously implemented. The Postal Service's calculations appear to treat the IMb discounts in a manner consistent with that contemplated for seasonal or temporary rates. However, unlike seasonal or temporary rates, the IMb rates are intended to be permanent once implemented.

When rate changes are implemented simultaneously, the application of the Commission's rules serves to function as a cap on rates. In contrast, if rate changes are implemented at different times, with adjustments made to the volume weights, the cap may be seen as more akin to a cap on revenues (or average revenues). The accuracy of the cap calculations is also dependent on the assumption that the next adjustment cycle will not be less than or more than one year.[3]

a. Please discuss the strengths and weaknesses of the approach taken in the filing.
b. Please discuss the strengths and weaknesses of potential alternate approaches, including filing a separate notice of rate adjustment or mail classification proceeding closer to the implementation date.

RESPONSE:

In Question 9, the Commission asks the Postal Service to address the strengths and weaknesses of the approach used to incorporate the effects of mid-year price changes into the price cap calculation. It also asks the Postal Service to address the strengths and weaknesses of potential alternative approaches. The Postal Service has been able to identify only one plausible alternative to the approach it has taken.[4] This alternative would involve omitting

[3] Based on the planned implementation date, the billing determinant weights for the IMb discounts are developed by multiplying the post-implementation adoption percentages by the quotient of 23 divided by 52. The 23/52 factor represents the assumption that the set of rates in the notice will be in effect for 52 weeks, but the IMb rates will only be in effect for 23 of those weeks.

[4] In fact, this was the alternative identified in the Chairman's Information Request.

from the May price changes any notice of adjustment in prices because of the full service IM implementation, but filing a separate Notice of Price Adjustment closer to the planned implementation date of a price incentive. This later Notice would not only implement the incentive (i.e. lower prices) for participating mailers, but concurrently also adjust upwards the prices paid by non-participants to offset the estimated effects of the new discount on revenue. On the whole, the Postal Service finds that this alternative is inferior to the approach used by the Postal Service under the circumstances that prevail in the present situation.[5]

Before specifically responding to these requests, the Postal Service would like to address what it believes are some misconceptions contained in the preamble to the question. The first is reflected in the statement that "the IMb rates are intended to be permanent once implemented." While the Postal Service does not intend the IM Full Service Program incentive to be a seasonal price adjustment, and it expects that an incentive will likely continue throughout the May 2010 to May 2011 twelve-month period as well, the Postal Service does not expect the incentive to become a permanent part of the pricing schedules.

[5] That is not to say that other courses of action do not exist, but the Postal Service has not found any without fatal flaws. For example, the Commission could avoid the issues posed by mid-year price changes by prohibiting them altogether. This would, however, violate the principle of pricing flexibility that is at the core of the PAEA. Alternatively, mid-year price changes could be entered into the cap calculation as if they were in place for a full twelve months. But this approach would give the Postal Service the ability to raise prices (the "push-up" effect) for phantom price reductions that may exist for only a few days or weeks of the year. And, in symmetric fashion, the Postal Service would be penalized by having to count against its price cap late-year price increases as if they had been in place the full year. The perverse incentives of this approach are obvious: take all price increases on day one of the year and defer all price reductions until as late in the year as possible.

As discussed in the Postal Service's February 24th response to the Chairman's Information Request No. 2, Questions 2(e), 3(e), 4(e) and 5(e), the Postal Service envisions that eventually the incentive would no longer be relevant or meaningful and would be phased out.

The other misconception is that the adjustments made by the Postal Service have somehow transformed the price cap to a cap on revenues. The formula for the price cap calculation in Commission rule 3010.23(c) requires both a price and a volume for each price category. In its cap calculation, the Postal Service adjusted the billing determinants to reflect the volumes that would be paying the incentive prices and those that would pay the base prices.[6] This is not a cap on revenues. Upon implementation, the prices for each category will be fixed, but the volumes in each category will not. Depending on how the volumes in each pricing category compare to the adjusted billing determinants used in the price cap calculation formula, the revenues earned by the Postal Service for that pricing category will be higher or lower than the revenues shown in the price cap calculation, as is the case with every price category. The Postal Service's revenues for a single pricing category, or for a mail class as a whole, are neither guaranteed nor capped.[7]

[6] The cap compliance calculations may have not expressly recast volumes into line-item categories, but that would have the same effect as the methods followed that calculated the revenue reduction (using the FY08 billing determinants as a base) due to the incentives being implemented on November 29, 2009.

[7] While some might maintain that the approach used here by the Postal Service could perhaps be construed as a move somewhat in the direction of a cap on *estimated* revenues, as the following discussion in its entirety demonstrates, this approach, as a practical matter, is nonetheless manifestly

The Commission's rules do not have a set of procedures that exactly match the situation at hand.[8] The rules do not anticipate and establish procedures for every conceivable situation that might arise under the broad pricing latitude granted the Postal Service by the PAEA, and appropriately so. The only way to ensure that all circumstances would be covered by previously established detailed rules of procedure would be to narrow the Postal Service's pricing options to just a handful of permissible choices. Such regulation would be excessively heavy handed and would undermine and contradict the intent of the PAEA to "allow the Postal Service pricing flexibility" (Objective 4 of section 3622). In light of the Commission's wise decision to develop rules to provide a robust framework within which the Postal Service can exercise its pricing freedom and the Commission can exercise its oversight responsibilities, both the Postal Service and the Commission must use reasonable judgment in applying the existing rules to situations not explicitly spelled out and specifically provided for. The current situation falls into that category.

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superior to any available alternative. As the Commission itself has observed when proposing its price cap rules, once adjustments in billing determinants are required to account for classification changes, any pure price cap regime is likely to be "imperfect." Order No. 26 (August 15 2007), Docket No. RM2007-1, at 35. And as the Commission likewise suggested when adopting final rules, the appropriate means to accommodate potential real world complications in its untested new rules would be to monitor the rules as utilized and evaluate their effectiveness in successfully implementing the intent of the PAEA. Order No. 43 (Oct. 29, 2007), Docket No. RM2007-1 at 51. The Postal Service submits that its utilization of the rules in this instance is, in fact, fully in accord with the intent of the PAEA price cap regime.

[8] Rule 3010.22 addresses the situation where "a notice of rate adjustment is filed less than 1 year after the last Type 1—A or Type 1—B notice of rate adjustment." This does not describe the present circumstances where a deferred price change is noticed fully one year after the previous notice.

(a) In its efforts to apply the Commission's rules for price changes, the Postal Service determined that the most appropriate way to incorporate several deferred price changes was to announce them with the rest of the pricing adjustments and to adjust the billing determinants used in the rule 3010.23 price cap calculation to reflect the part-year nature of the price changes. The Postal Service understands that the approach it has used is not perfect. Its imperfections arise, as the Commission's preamble suggests, from its treatment of price changes that are likely to be in place for the full pricing year May 2010 to May 2011, by using volume weights that apply only during the May 2009 to May 2010 pricing implementation year and that reflect the mid-year implementation date. The Postal Service understands that the approach it has used could, in theory, be used to announce an exceptionally large price increase for a particular category or class of mail, but defer implementation until just before the start of the next pricing year. The cap calculation would give this large increase only a small weight since its duration in the implementation pricing year would be small, but the large increase would be essentially "baked into" the beginning prices for the subsequent pricing year.

The Postal Service's current application of this "advance notice" approach does not manipulate prices in the fashion described. Moreover, the Postal Service has made it clear that it has no intent to manipulate the timing of pricing decisions to frustrate and nullify the price cap. *See* Postal Service Reply Comments in Response to Order No. 26 (October 9, 2007), Docket No. RM2007-1, at 39-40. Indeed in the Intelligent Mail Full Service Program incentive example given by the Commission, a lower, not a higher, price will be "baked into" the current prices when the time for subsequent price adjustments rolls around in May 2010.

The Postal Service has made clear the business rationale behind its Full Service Program incentive pricing in its filings before the Commission and in its public statements to the mailing community. The pricing incentive for the IM Full Service Program is intended to encourage mailers to make the changes they need to participate in the Full Service Program. The program is not yet fully operational, but is expected to be ready in the fall of this year. Consistent with that schedule, the incentive was deferred until the program was ready to accept participants and provide the full benefits encompassed by the program. For many mailers, getting ready for the Full Service Program requires not insignificant time and investment. Sufficient advanced notice plus a full commitment to specific pricing incentives, such as those contained in the Notice of Price Adjustment, were indispensable for many mailers to commit the resources needed to be ready to adopt the Full Service Program when it becomes available this fall.

The foregoing illustrates several of the key strengths of the Postal Service's approach. First, announcing an incentive (or, similarly, a disincentive) price well in advance of the price implementation date gives the mailing community needed time to take the actions necessary to benefit from the incentive, or alternatively, to avoid the disincentive price. Mailers have frequently expressed the view that it is difficult for them to respond to price changes because of lengthy commitments they make with suppliers and their customers. Transition time is important to the mailing community. The Postal Service's approach affords greater adjustment time than the alternative.

The second key strength is that a deferred price change carries a much greater degree of commitment than a simple statement of intent. One might possibly respond to the advanced notice argument, above, by claiming that a simple announcement that the Postal Service expects to implement such and such price incentive at such and such future date would work the same effect. This is not the case. A Notice of Price Adjustment is a formal public commitment by the Governors to change specific prices in specific ways. Unless further action is taken by the Governors of the Postal Service, or the prices are found illegal by the Commission, those prices will be implemented. The history of the Intelligent Mail program is ample demonstration that statements of general intent made during the planning phases can change. The Postal Service is convinced that no lesser commitment than a Notice of Price Adjustment by the Postal Service may be required to persuade some mailers to plan to participate in the Full Service Program. To put it in other words, a price change contained in a Notice of Price Adjustment is as real as it gets.

Another strength of the Postal Service's approach is that it is likely to result in better alignment of pricing incentives with the timing of the events they are supposed to influence. This point might be better illustrated if the pricing incentive to adopt the Full Service Program were implemented, not as a price reduction for those who participated, but as a higher price for those who did not.

Suppose that the Postal Service were planning to raise the prices of all automation mail that did not adopt the Full Service Program on November 29. Under the alternative approach, the Postal Service would wait until that date approached and then file a separate Notice of Price Adjustment for the higher price. And, assuming that conditions were then such that this price increase was within the then-published cap (a situation that is, in itself, a source of uncertainty), the change in the pricing would have to be reflected in the subsequent omnibus Notice of Price Adjustment filed (presumably) the next February. The Postal Service would then face not only the uncertainty over its ability to make the necessary price change within the cap, but also with the decision of whether it wanted to "spend" part of next year's price cap this November. Under some circumstances, the Postal Service might opt for the sure thing and not defer the price increase, implementing it along with the rest of the price changes in May. In this case, not being able include a deferred price increase in the original package of price increases would have led to higher "disincentive" prices being charged before the Full Service Program were fully in place and without any option for mailers to take to avoid the higher disincentive price. This kind of outcome is certainly not desirable from either the mailers' perspective or the Postal Service's, but, considering the uncertainties inherent in the alternatives, the Postal Service might feel compelled to choose it as the lesser of two evils.

The Postal Service's preferred approach removes many of the elements of uncertainty for both the mailers and the Postal Service, allows more time to adjust to committed pricing incentives, and aligns incentives better with the events they are designed to influence, thereby improving the overall predictability of prices and the transparency of the pricing process.

(b) Many of the strengths and weaknesses of the alternative approach, filing a separate notice for a mid-year price adjustment as the prospective implementation date approached, have been discussed in the previous subpart (a) as weaknesses / strengths in contrast to the corresponding strengths / weaknesses of the Postal Service's approach. For this reason, subpart (b) of the response will largely present the strengths and weaknesses of the alternate approach without repeating discussions that were already presented in subpart (a).

The strength of the deferred notice approach is that it does not allow the Postal Service to manipulate the rules so as to "bake in" an excessive price increase and circumvent the price cap.[9] So, if the Commission were to suspect that the Postal Service's purpose in using its preferred approach was to get around the price cap, requiring the provisions of rule 3010.22 to be used for all part year price changes would (in theory) would close off that possibility.

The weaknesses of the deferred notice approach are the flip sides of the strengths of the advance notice approach that the Postal Service used. It does not provide the same degree of clear and unequivocal advance notice of price changes to the mailing community, leaving open the possibility that some

[9] That is not the situation here, however. The Postal Service's decision to not defer the notice does not cause a circumvention of the cap. Also, in this situation the per-piece amounts of the price adjustments are very small.

customers may not respond to upcoming incentives until they see an actual notice filed with the Commission. Valuable time could be lost and the incentive power of the pricing could be seriously eroded.

Furthermore, the uncertainty over what the future cap might be and how much of the (unknown) next year's cap the Postal Service may wish to "spend" on the mid-year pricing change may induce the Postal Service to avoid the flexible option of implementing mid-year adjustments altogether, by bringing forward the changes to the omnibus implementation date or, alternatively, postponing them until the beginning of the following pricing year. At the very least, it would serve to discourage the Postal Service from committing publicly to the specifics of mid-year pricing changes until it were much closer to the implementation date and the statutory minimum notice period for a Notice of Price Adjustment. Only at that time could the "cost" of a price change to the Postal Service be more certainly evaluated.

In addition to these shortcomings, the deferred notice approach has several others. First, it would appear to require the Commission to decide the maximum notice period that could be used when the Postal Service announced its pricing adjustments. Any price change that exceeded the maximum notice period (when the notice for the omnibus price adjustment was filed) would require its own separate filing. The Postal Service recalls that when the Commission was developing its rules, it stated quite unequivocally that the statutory 45 day notice period was the minimum acceptable notice period [Order No. 26, para. 2020] and even observed that the Postal Service's self-imposed minimum 90-day notice period "allows only a brief period" for review [Order 43, paragraph 2058]. To the Postal Service's knowledge, the Commission has never discussed what notice period, if any, should be deemed "too long" from the perspective of giving the public appropriate notice. Indeed, its rule 3010.10(b) states that the Postal Service is "encouraged" to provide notice "as far in advance of the 45-day minimum as practicable, especially in instances where the intended price changes include classification changes or operations changes likely to have a material impact on mailers." In light of the Commission's stance to date, requiring the deferred Notice of Price Adjustment approach for mid-year price adjustments would seem to attenuate the Commission's support of longer, rather than shorter periods of public notice.

Second, requiring mid-year price changes to have their own notices would multiply the administrative burden (on the Postal Service, the Commission and the mailing community) of preparing, filing, reviewing and responding to pricing changes. If mid-year pricing changes occurred only once every few years this added burden might not loom large. But there is nothing in the law or the rules to restrict the number of mid-year changes that the Postal Service in the exercise of its pricing flexibility might decide were appropriate. If each one required separate notice, the Postal Service might find its pricing flexibility eroded merely from considering the cost of the added administrative burden exercising its pricing flexibility would entail. Moreover, applying this scenario under the current circumstances would subject mailers who for whatever reason do not participate in the IM Full Service program to two separate prices changes, one in May to account for the general price adjustment, and one later to account for the push-up effect of the new lower rates for program participants. The aggregate effect of these rate increases would be higher than the one increase implemented in May under the Postal Service's approach. So not only would these mailers be burdened with higher rates going forward, but they would also have to deal with two price increases within the same year.

Finally, it is hard to see how requiring the Postal Service to defer filing a Notice of Price Adjustment until it fell within a specified window would be consistent with the PAEA's objectives of promoting predictability in prices (Objective 2) and reducing administrative burden and increasing transparency (Objective 6). In fact, the deferred notice approach is an inferior mechanism compared to the advance notice approach in achieving each of these objectives, as has already been discussed above.

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document in accordance with Section 12 of the Rules of Practice and Procedure.

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