UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

Notice of Price Adjustment	Docket No. R2009-2

COMMENTS OF THE
ASSOCIATION FOR POSTAL COMMERCE

(March 2, 2009)

Pursuant to Order No. 180, the Association for Postal Commerce ("PostCom") respectfully submits these comments on the price and classification changes proposed by the Postal Service in this docket. These comments focus on the penalty or surcharge of seven cents per piece proposed by the Postal Service for Standard Mail that the Postal Service finds to violate the Move Update address change requirements.

SUMMARY OF COMMENTS

The proposed surcharge is excessive, unrelated to the costs imposed on the Postal Service by nonconforming mail, and therefore unjust and unreasonable within the meaning of 39 U.S.C. §§ 404(b), 3622(b)(8) and 3622(c)(5). Accordingly, the Commission should decline to recommend the seven-cent surcharge. Alternatively, the Commission should limit the application of the surcharge to the particular pieces in a mailing that fail to meet the Move Update requirements, rather than the entire mailing.

ARGUMENT

In its Notice of Price Adjustment, the Postal Service states that in November 2008, it changed its "mail preparation standards to require Standard Mail customer to use an approved Move Update method to update their mailing list with change-of-address information," and that mailers "who do not comply with the new Move Update standard are not eligible Standard Mail prices." United States Postal Service Notice of Market Dominant Price Adjustment ("USPS Notice") at 18. To provide a fallback rate for Standard Mail mailings that violate Move Update requirements, the Postal Service proposes that all pieces in a non-compliant Standard mailing pay a penalty or surcharge of seven cents above the otherwise applicable Standard Mail rate. *Id* at 18 and Appendix A, p. 15.

The Postal Service's Notice of Price Adjustment and supporting workpapers, however, do not claim that the amount of the per-piece charge has any relationship to the added costs incurred by the Postal Service from noncompliance with Move Update requirements by Standard Mail, and no relationship appears to exist. For letters weighing less than 3.3 ounces, a penalty of seven cents amounts to a rate increase of at least 27 percent over the otherwise applicable Standard Mail rate per piece. The Postal Service has offered no evidence that the average costs incurred by the Postal Service in disposing of undeliverable-as-addressed ("UAA") pieces in noncompliant Standard Mail mailings equal either seven cents per piece or 27 percent of the otherwise applicable postage. *See* USPS-R2009-2/2 (Standard Mail Cap Compliance), LFP Revenue@New Prices.xls (attached Excel worksheet at lines 146-149) (showing anticipated revenue from seven-cent surcharge, but not costs of noncompliance with Move Update).

The unreasonableness of the seven cent surcharge is compounded by the Postal Service's intention to impose it on every piece in a noncompliant mailing—not just the pieces in the mailing with stale addresses. This meat-axe approach is likely to magnify the Postal Service's windfall from the surcharge, since only a small fraction of the pieces in a noncompliant mailing typically have stale addresses.[1]

The punitive nature of the surcharge is heightened by the error rates of the Move Update methods that the Postal Service has made available to mailers. The Postal Service has announced that it will use MERLIN to screen mailings for Move Update compliance. MERLIN, however, has an error rate of several percent. So do all of the Move Update methods available to mailers. These error rates appear likely to exceed the allowed tolerance ranges. The Postal Service has informed mailers that the initial tolerance level will be 30 percent—i.e., a mailing will be accepted as Move Update-compliant if 70 percent of the addresses tested are found to be compliant. To some mailers, this may appear on first blush to be a comfortably wide tolerance range, it is unclear, however, whether the full audience of mailers comprehends how the Postal Service actually intends to calculate the error rate. Particularly, our members reporting business activity more recent than the change of address data are concerned they will be required to expend excessive resources demonstrating compliance.

Moreover, the Postal Service has announced plans to reevaluate the threshold every four months.[2] Further tightening of the threshold increases the likelihood that even

[1] Failure to use a Move Update method typically causes only a small fraction of the addresses in a mailing to be UAA. Only a small fraction of addresses change each year. According to Postal Service sources, the typical match rate for $NCOA_{Link}$ is five percent.

[2] http://ribbs.usps.gov/mtac/documents/tech_guides/MTAC0209/MTAC%20Wed/006_Mehra2009Feb18MoveUpdateMTACv2.ppt#468,9,Move Update Verification

more mailers making a good faith effort to comply with the Move Update requirement will be required to expend an extraordinary level of resources demonstrating such compliance.[3]

This draconian penalty scheme is clearly at odds with PAEA, including 39 U.S.C. §§ 404 (which requires that rates be reasonable and equitable), 3622(b)(8) (which requires that rates be just and reasonable), and 3622(c)(5) (which requires that rates be set to take into account "the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service"), and 3622(b)(2) (which requires that rates be reasonably predictable and stable). Although the Commission does not appear to have adjudicated the reasonableness of penalty or fallback rates under these provisions, the overwhelming weight of precedent under the cognate provisions of other regulatory statutes makes clear that a regulated monopoly may not impose a penalty or surcharge that bears no reasonable relationship to the costs created by the activity or condition that gives rise to the penalty or surcharge.

While regulated carriers are generally permitted to charge penalty fees as a method of ensuring compliance with rules and regulations, such fees must be just and reasonable and have a rational basis. Even an otherwise permissible penalty can become unjust and unreasonable if it diverges significantly from the costs incurred by the carrier as a result of noncompliance. *See Union Pac. R.R. Co. v. Bay Area Shippers Consolidating Ass'n, Inc.*, 594 F.2d 1291, 1294 (9th Cir. 1979) (expressing concern that

[3] It also may lead the Commission to question what tolerance was used to calculate the revenue estimates presented in the Postal Service workpapers, and the applicability of that tolerance for the full fiscal year. *See* USPS-R2009-2/2 (Standard Mail Cap Compliance), LFP Revenue@New Prices.xls (attached Excel worksheet at lines 146-149) (showing the anticipated revenue from seven-cent surcharge).

penalty charges that more than tripled the applicable shipment rates could be excessive, especially when the railroad could not "suggest a rational relationship between the costs that misdelivery of a manifest may impose on the carrier and the apparently severe consequences that it visits on the shipper").[4]

In *Petition for Declaratory Order of Lehigh Valley R.R. Co.*, 353 I.C.C. 518 (1977), the Interstate Commerce Commission applied these standards to overturn a penalty scheme remarkably similar to that present here. In that case, a consolidator sought to take advantage of a discounted rate offered by a railroad for certain shipments of mixed commodities. The discounted rate applied, however, only if every car in the shipment satisfied certain weight and commodity mix standards. In each of the consolidator's shipments, several individual cars did not meet these standards. The railroad responded by applying the non-discounted rate to the entire shipment. On petition for a declaratory order, the ICC ruled that the application of the non-discounted rate to cars that did meet the discount tariff requirements was unreasonable even if specified by the tariff. *Id.* at 527. Instead, the ICC held, the railroad should have charged the discounted rate on cars that met the requirements and the non-discounted rate only on

[4] *See also Order Instituting Rulemaking to Implement Portions of AB 117 Concerning Community Choice Aggregation*, 2004 Cal. PUC LEXIS 609, 50-51 (Cal. PUC 2004) (holding that imbalance penalties imposed by a utility "should include fees that bear a reasonable relationship to the costs the utilities will incur as a result" of the customer's conduct); In the Matter of Generic Docket to Address Performance Measurements and Enforcement Mechanisms, 2002 N.C. PUC LEXIS 523, 127-29 (N.C. PUC 2002) (rejecting a proposed penalty on the grounds that it was not "directly tied to the economic significance of the noncompliance"); *In the Matter of Tariff Revision, Designated as TA3-487*, 201 Alas. PUC LEXIS101, 4-5 (Reg. Comm'n. Alas. 2001) (holding a premature cancellation penalty excessive and not just and reasonable and limiting the penalty to the savings the customer achieved by entering the long term contract); *Petition of Dairylea Cooperative Inc. to Establish an Open Access Pilot Program for Farm and Food Processor Electricity Customers*, 1997 N.Y. PUC LEXIS 497, 8-12 (N.Y. PSC 1997) (rejecting a proposed penalty that was "far in excess of . . . costs" in favor of one that more closely tracked the costs caused by noncompliance).

those cars that did not. *Id*. In reaching this decision, the ICC relied on the cost characteristics of the shipments—while it was appropriate to apply the higher rate to non-qualifying cars because they differed from qualifying cars in essential aspects, there was no basis for applying the higher rate to cars that had exactly the weight and mixture characteristics contemplated by the discount rate tariff. *Id.* at 526. The Commission explained its decision as follows:

> "[P]etitioner seeks to collect undercharges which penalize cars loaded in full compliance with the mixture rule in the same manner as cars loaded in violation of the rule. The severity of that penalty is reflected in the fact that the average charge applied to a carload complying with the rule is more than double the amount the charge on that identical carload would have been had it been shipped with another carload containing a like mix of traffic. While we recognize a theoretical operational distinction between multicar movements of mixed freight under item 13555 and multicar movements under item 135, we are convinced that such a wide spread cannot be justified on the basis of a difference in character of the mixed freight in some other car in the same shipment. Since no other justification has been offered, we are of the view that exaction of the applicable charges would be unjust and unreasonable as to cars which meet the item 13555 mixture requirements."

Id. at 526.

The logic of *Lehigh Valley* applies with equal force here. The seven-cent surcharge proposed by the Postal Service should apply only to the portion of the mailing determined to have stale addresses, because only those addresses have the potential to require costly manual disposition as a result of their staleness. Thus, if sampling indicates that five percent of the pieces in mailing have stale addresses, the seven cent surcharge should be imposed only on those pieces. This approach better aligns the penalty with costs while still providing an effective deterrent to the submission of non-compliant mailings. As the ICC reasoned in *Lehigh Valley*, "Use of the rates determined in the above manner is believed justified in the particular situation because, while

recognizing the need for more than a token penalty to discourage repetitive tariff violations it limits the penalty to the particular traffic that actually produces the violation." *Id*. at 526.

The Postal Service, confronted with these criticisms, has sought to portray the seven-cent penalty as a *benefit* for mailers on the theory that the alternative would have been to charge noncompliant mailings the full single-piece First Class Mail rate. USPS Notice at 18. This is a false dichotomy, however. The Postal Service, having imposed Move Update requirements on Standard Mail, is obligated to establish a rate differential for noncompliance that has a rational relationship to the added costs that noncompliance imposes. An unlawfully high rate may not be justified on the ground that the alternative rate would have been even higher.[5]

Finally, a windfall penalty cannot be justified solely on the grounds of its deterrent effect. By that logic, any penalty, not matter how unrelated to costs, could pass muster. The case law cited above clearly rejects this position.

Moreover, the Postal Service has offered no evidence that the actual rate of noncompliance with Move Update by users of Standard Mail makes an above-cost surcharge penalty necessary. As the Postal Service itself acknowledges in the preface to its workpapers, compliance with Move Update is expected to be "virtually universal" and only "a small fraction of mailings might not comply"—in fact, only "one tenth of one percent" of Standard Mail pieces are likely not to comply. USPS-R2009-2/2 (Standard

[5] Likewise, the seven cent penalty may not be justified on the that the First-Class rate structure has a surcharge of similar magnitude for noncompliance with Move Update. Undeliverable First-Class Mail is generally entitled to forwarding or return to the sender. Standard Mail is generally not entitled to these costly and labor-intensive services.

Mail Cap Compliance) at Section IV. Given the expected compliance rate, the requirement for any penalty is dubious at best, much less one so divergent from the costs non-compliance would impose on the Postal Service.

CONCLUSION

The Postal Service's proposal to impose a penalty or surcharge of seven cents per piece on all pieces in any Standard Mail mailing that the Postal Service decides is out of compliance with Move Update standards in unjust and unreasonable. The proposed penalty is unrelated to the costs imposed on the Postal Service by non-compliance with Move Update procedures, and would vastly exceed those costs. The Postal Service has put forth no rational basis for imposing a penalty of this magnitude. The failure to justify this penalty is particularly egregious in light of the uncertainty surrounding the Move Update verification procedures the Postal Service is in the process of implementing.

For these reasons, the Commission should either reject the proposed surcharge or, alternatively, limit its application to the mailpieces in a Standard Mail mailing that actually have stale addresses.

Respectfully submitted,

Ian D. Volner
David M. Levy
Rita L. Brickman
Matthew Field
VENABLE LLP
575 Seventh Street, N.W.
Washington DC 20004
(202) 344-4800

Counsel to Association for Postal Commerce

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