

Before the
POSTAL REGULATORY COMMISSION
Washington, DC 20268-0001

Consideration of Workshare :
Discount Rate Design : Docket No. RM2009-3

COMMENTS OF THE GREETING CARD ASSOCIATION

The Greeting Card Association (GCA) files these Comments pursuant to the Commission's Order No. 243 (July 10, 2009). GCA earlier filed initial comments pursuant to Order No. 192.¹

For reasons developed in these Comments, GCA believes that the Commission should retain the existing theory of worksharing rate design in First Class. Notwithstanding the substantial changes made by, and since, enactment of the Postal Accountability and Enhancement Act of 2006 (PAEA), the historical continuity between today's Presort categories and those created in the 1970s remains. The new statute, appropriately read, does not require that linkage to be severed.

I. The statutory issue

A. *The Postal Service's statutory theory.* The Postal Service, first in response to Chairman's Information Request No.1 in Docket R2009-1 and then in more detail in its Initial Comments in this Docket², has set out a legal theory under which the Commission would be compelled, regardless of economic or rate design considerations, to treat Single-Piece and Presort as entirely separate entities between which no worksharing relationship exists, or could exist. The Ser-

¹ Initial Comments of the Greeting Card Association (May 26, 2009).

² Initial Comments of the United States Postal Service, pp. 2, 14-17.

vice's legal theory is basic to the whole inquiry, both for that reason and because it allows the Service to evade various issues under § 3622(e), which otherwise must be resolved. Consequently, we begin with it.

The Postal Service's statutory theory, briefly, is that –

- (1) Section 3652(b), which requires reporting of certain worksharing-related data as part of the annual compliance review process, refers to “products.”
- (2) Therefore, data describing the relationship between two “products” are not required to be reported.
- (3) Section 3622(e), which sets forth the substantive rules governing work-sharing discounts, should not be read as covering situations as to which no data need be reported – presumably since, without the relevant data, the criteria of § 3622(e) could not be applied.
- (4) Consequently, a relationship between two mail categories each of which is a separate “product” is not a worksharing relationship within the meaning of § 3622(e).
- (5) Finally, because such a relationship is not a worksharing relationship subject to § 3622(e), the rates in which it is expressed need not conform to the principle that discounts should be no greater than avoided costs.

GCA believes that this statutory theory is unsound. If we are correct, it follows that the Commission is not barred as a matter of law from retaining the existing benchmark and can consider it on its merits.

B. *The Postal Service’s statutory interpretation proceeds backward.* An odd feature of the Service’s theory is that, while internally coherent, it proceeds by first construing a reporting provision (§ 3652(b)) whose function is to support administration of a set of substantive rules (§ 3622(e)). Next, on the basis of its interpretation of the reporting provision – an interpretation which is by no means the only one possible³ – it proceeds to narrow drastically the scope of the substantive provision.

That this is what the Service is doing is clear from its Initial Comments:

. . . The scope of section 3622(e) should therefore be construed in a manner consistent with section 3652(b). Indeed, the two provisions are complementary, in that section 3652(b) mandates the provision of information necessary to apply the standards set forth in section 3622(e) (i.e., to determine whether the 100 percent threshold has been crossed, and thus whether it is necessary to determine whether one of the specified exceptions applies). . . .

As such, it is illogical to suggest that section 3622(e) would apply to a relationship for which section 3652(b) does not mandate the provision of cost information. . . .^[4]

GCA suggests that a more straightforward procedure would be to analyze the *substantive* provision to see what relationships it is fairly read to cover, and only then to check that interpretation by reference to the *reporting* provision.⁵ This procedure would lay the major, or at least the initial, emphasis where it belongs – on the substantive rate policy Congress enacted. The Service’s procedure, by contrast, begins from a (needlessly) restricted construction of an aux-

³ See pp. 6-8 below.

⁴ Postal Service Initial Comments, p. 15.

⁵ If a preliminary reading of § 3622(e) had classed as “worksharing” some relationship as to which § 3652(b) clearly could *not* be construed as calling for data reporting, then the interpretation of § 3622(e) would have to be reconsidered.

iliary provision and uses that construction to narrow the substantive rule – essentially without independent analysis of the substantive rule’s own language.⁶

C. *Independently interpreting § 3622(e)*. Following our own suggested procedure, we turn first to § 3622(e):

(e) WORKSHARE DISCOUNTS. –

(1) DEFINITION. – In this subsection, the term “workshare discount” refers to rate discounts provided to mailers for the presorting, prebarcoding, handling, or transportation of mail, as further defined by the Postal Regulatory Commission under subsection (a).

This definition nowhere refers to “products.” Congress might, for example, have said “rate discounts provided to mailers *of a product* for the presorting, prebarcoding, handling, or transportation of mail” (or “of such product”), and thereby indicated that a rate differential between, e.g., the Single-Piece and Mixed AADC Automation Presort products was *not* to be considered a workshare discount.⁷ It did not so restrict its definition. Thus if the eligibility conditions for a mail category include mailer-provided presorting, prebarcoding, handling, or transportation, it appears that a rate differential between it and a similar category with no such conditions would *prima facie* constitute a workshare discount.

It is noteworthy, in this connection, that the definition of “workshare discount” is subject to elaboration by the Commission “under subsection (a).” Subsection (a) – i.e., § 3622(a) – is the basic Congressional mandate that the Commission “by regulation establish (and . . . from time to time thereafter by regulation revise) a modern system of regulating rates and classes for market-dominant

⁶ GCA of course agrees with the Postal Service’s general proposition that these two provisions should be construed together (Postal Service Initial Comments, pp. 14-15). In our view, however, doing this requires attention to the intrinsic meanings of *both* sections. The Postal Service instead focuses on interpreting one provision (§ 3652(b)) and bases its reading of § 3622(e) on that interpretation, rather than independently analyzing the latter section.

⁷ The example ignores the difficulties, discussed below, which arise from the possibility that mail categories historically considered as the terms of a worksharing relationship may later be designated as separate products – as has occurred in First Class.

products.” Thus the Commission’s authority to “further define” the definition of “workshare discount” is assimilated to its most fundamental assignment under Title II of PAEA. Whether a relationship between (components of) two separate products can still be a worksharing relationship is an appropriate issue for resolution under this authority, since it is an important structural issue in creating a “modern system” of postal ratemaking. If the answer were not immediately clear from the text of § 3622(e)(1), the remedy would appear to be clarification by the Commission through rulemaking, and not resort to a doubtful construction of an auxiliary data-reporting provision.

In our Initial Comments, at pp. 3-4, we posed the hypothetical case of a type of mail comprising two categories designated as “products,” and differing only in that one was presorted and the other not.⁸ A rate differential reflecting the presortation cost savings would thus be a “workshare discount” under the plain language of § 3622(e)(1). Only by adopting the Service’s narrow construction of § 3652(b) and reading it back into § 3622(e) could one arrive at the (counterintuitive) result that these two products were not in a worksharing relationship and that the rate difference between them was not a workshare discount.

Section 3622(e)(2) states the general substantive rule for workshare discounts (along with a number of exceptions):

(2) SCOPE. – The Postal Regulatory Commission shall ensure that such discounts do not exceed the cost that the Postal Service avoids as a result of workshare activity, unless – [specification of several exceptions].

⁸ Such categories would each be “a postal service with a distinct cost or market characteristic for which a rate or rates are, or may reasonably be, applied[.]” 39 U.S.C. § 102(6) (defining “product”). The distinctive characteristic in this case would be the presort-related cost differential. Each category would therefore qualify as a “product.”

Here again there is no limitation on the basis of product boundaries: the rule is simply that if there is workshare activity and the Service offers a discount for it, the discount shall not exceed the savings.

Thus it appears that nothing in § 3622(e) counsels against treating an inter-product relationship, in appropriate cases⁹, as a worksharing relationship. Where the historic development of a category such as Presort, as well as its present eligibility requirements, suggest that it exists essentially because of its worksharing potential, there is every reason to presume that it stands in a work-sharing relationship to its non-workshared counterpart.

But it is still logically possible, if perhaps unlikely, that, as the Service suggests, § 3652(b) has some bearing on the question, so that provision must be interpreted as well.

D. *Interpretation of § 3652(b)*. Section 3652(b) reads:

(b) INFORMATION RELATING TO WORKSHARE DISCOUNTS. – The Postal Service shall include, in each report under subsection (a), the following information with respect to each market-dominant product for which a workshare discount was in effect during the period covered by such report:

(1) The per-item cost avoided by the Postal Service by virtue of such discount.

(2) The percentage of such per-item cost avoided that the per-item workshare discount represents.

(3) The per-item contribution made to institutional costs.

⁹ What cases are appropriate is, of course, an important question in itself. It should be noted in this connection that First Class is the only major market-dominant class which (i) comprises both workshared and non-workshared mail, and (ii) as to its non-workshared component, exhibits marked heterogeneity as regards mailpiece configuration (as would be expected of an “anything mailable” class).

The Postal Service appears to read the introductory sentence as though it mandated a report “with respect to each market-dominant product *within which* [or *between components of which*] a workshare discount was in effect[.]”¹⁰ This is an unduly narrow reading. It would not, for example, accommodate the hypothetical case outlined on p. 5: in that case, the presorted product contained no distinguishable components but was merely a workshared version of the non-presorted product. On the Service’s reading, apparently, the rate differential between them would not be a workshare discount even though, apart from the worksharing involved, there would be no reason for it to exist. The statutory phrase “product *for which* a workshare discount was in effect” (italics added) can equally well be read to include the case where a discount was established to reflect worksharing savings as between a non-workshared product and one that is, e.g., presorted.¹¹

As regards the concrete case before the Commission – the relationship between Single-Piece and Presort – the Postal Service’s interpretation is similarly questionable. There is apparently no dispute that a substantial part of the cost difference between them is worksharing-related. The Postal Service observes that as between Single-Piece and Presort, “the average cumulative letter mail cost avoidance is under 8 cents, or just above half of the CRA attributable cost difference.”¹² The Service uses this statistic to emphasize the non-worksharing distinctions between Single-Piece and Presort, which we of course recognize as well. The fact remains, however, that Presort rates are what they are, to a very significant degree, because worksharing avoids costs and is customarily rewarded with correspondingly lower rates. The Postal Service’s reading of § 3652(b) would require the Commission to pretend that this 8-cent worksharing

¹⁰ The Postal Service says approximately this at p. 21 of its Initial Comments.

¹¹ And, particularly, a case where when this relationship was established there was no question of separate “products” and no dispute that it rested on worksharing. That is the case in First Class. Until issuance of the September 2007 Mail Classification Schedule, both presorted and single-piece First-Class Letters inhabited a single subclass, although presort discounts in First Class had been in place for more than 30 years. See Postal Service Initial Comments, pp. 3 et seq.

¹² *Id.*, Technical Appendix, p. A-2.

cost avoidance is nonetheless *not* connected with worksharing, simply because Single-Piece and Presort are now designated as separate products.

E. *Preliminary summary.* Thus far we have demonstrated that (i) the better procedure for interpreting the relevant PAEA provisions is to start with the substantive rules of § 3622(e) rather than with the auxiliary reporting provisions of § 3652(b); and that (ii) the language of neither provision requires, or even supports, the construction the Service advocates. Thus as a matter of law the Commission is free to retain the existing benchmark structure if rate policy considerations support it.

There is, however, another reason to reject the Service's legal approach. That theory entails a legal consequence which in GCA's view disqualifies it as a tenable reading of PAEA.

F. *Reading § 3622(e) out of the statute.* If, as a matter of law, there could be no worksharing relationship between different products, it would follow that dividing one product into two, three, or *n* fragments and designating each as a product on its own footing, would obliterate existing relationships universally recognized as worksharing. We are of course not suggesting that the Postal Service wishes to embark on a course of unlimited product segmentation. But the possibility is logically entailed by its legal theory; and that fact, we suggest, makes the theory untenable.

A "product," as noted earlier, is a postal service having a distinct cost or market characteristic for which a rate or rates are or could be charged. Thus under § 102(6), each current component of First-Class Presort could be made a separate product. Each, clearly, is a postal service under § 102(5). Each has a distinct cost characteristic, most often relating directly and uniquely to worksharing activity. A different rate or set of rates is charged for each one. Therefore, on the Postal Service's interpretation, the relationship between, e.g., 3-Digit and

5-Digit Automation Letters could instantaneously cease to be a worksharing relationship, even though neither the mail nor the uses to which mailers put it had changed in the slightest. No more would be required than a classification action, whereby each presort level became a separate product. From this it would follow that none of the intra-Presort relationships would be subject to § 3622(e), and its general rule that discounts must not exceed avoided cost could be ignored.

GCA submits that the Commission should reject an interpretation whose logical outcome is to excise § 3622(e) from the statute.¹³

II. The argument from ratemaking policy

A. *Introduction.* The second branch of the Postal Service's position invokes the policies said to underpin PAEA as a whole:

. . . Second, as a matter of policy, under the current circumstances within First-Class Mail, rigidly focusing on estimates of avoided costs, to the exclusion of other factors such as cost coverages, unit contributions, previous percentage rate increases, market differences, and similar trends in customer responses to price changes, would not achieve the benefits which application of the new workshare provisions were intended to achieve when applied within products.¹⁴

To support this view, the Postal Service refers to the developmental history of First-Class worksharing discounts, arguing that while these rates were being introduced and were penetrating the market, the "rate category" approach (i.e., a unitary Letters subclass with Single-Piece and Presort rate categories, the latter priced by reference to avoided cost) protected "status quo" customers from excessive increases. Moreover, discounts equal to avoided cost sent "appropriate price signals" to potential Presort customers "fac[ing] the choice of whether or not

¹³ Of course, reading § 3652(b) to accommodate the reporting of data for inter-product relationships which rest on worksharing would remedy this problem: designating what were formerly rate categories as separate products would not change the reporting requirement as to them.

¹⁴ Postal Service Initial Comments, pp. 2-3.

to undertake the worksharing necessary to qualify for the new prices[.]”¹⁵ Subsequently, however, it became possible to collect separate Presort costs, with the result that the total attributable cost difference between Single-Piece and Presort was greater than the worksharing cost avoidance.

The Postal Service argues that this circumstance, or more precisely the resulting disparity in unit contribution, “undermines the ‘equity’ analysis.”¹⁶ “It is not necessarily equitable,” the Service continues,

to shield “status quo” customers by capping discounts at avoided costs, when single-piece customers are not contributing to institutional cost recovery on either the same percentage or *unit* basis as Presorted customers.

Moreover, the Service argues, what was appropriate in the startup phase of worksharing is not appropriate now that Presort is a mature product:

. . . The notions that Single Piece customers are “status quo” customers, and that the predominant consideration in setting Presorted prices must be to avoid creating any upward pressure on the institutional cost burden placed upon those customers relative to the burden they bore when separate Presort pieces did not exist, are thoroughly outdated concepts.^[17]

B. *“Equity” is not a concept limited to the introduction of new rate categories.* The Postal Service’s argument appears to rely significantly on the assumption that the “equity” argument in favor of cost-avoidance-based discounts applies only when these discounts are being introduced, and that when the customer bases of the workshared categories have become essentially fixed, it is no longer valid. GCA does not agree.

Section 3622(b) includes, among mandatory objectives under PAEA,

¹⁵ Id., p. 6.

¹⁶ Id., p. 7.

¹⁷ Id., p. 18.

(8) To establish and maintain a just and reasonable schedule for rates and classifications, however the objective under this paragraph shall not be construed to prohibit the Postal Service from making changes of unequal magnitude within, between, or among classes of mail.

The first clause, which is the one of interest here, is not limited temporally. If a relationship between the Single-Piece and Presort rates in First Class is, for whatever reason, unjust and unreasonable¹⁸, it is so whether or not Presort is a newly-introduced category. The Service seems, at times, to argue as though the sole rationale for basing worksharing discounts on avoided cost was to avoid drastic price increases while Presort rates were being introduced and were attracting mail volume from Single-Piece. Efficiency as well as equity concerns justify use of the benchmark, however, and both are permanent concerns in ratemaking.

Two features of the “just and reasonable” objective merit emphasis here: (i) the provision calls for a just and reasonable *schedule* – implying that relationships among rates, and not just individual rates considered in isolation – must be just and reasonable, and (ii) it directs that the just and reasonable schedule be *maintained*. The latter requirement¹⁹ implies that even after a set of worksharing categories has been established and become a mature service offering, the relationship between worksharing and single-piece rates must continue to be a just and reasonable one.²⁰

In Docket R2006-1, for example, the Commission found that “[d]e-linking the rate design does not fairly and equitably balance the interests of all First-

¹⁸ GCA believes that to a substantial, though so far undetermined, extent, § 3622(b)(8) addresses the same kinds of concerns covered by the “fair and equitable” language of former § 3622(b)(1).

¹⁹ Which is carried over from former § 3622(b)(1).

²⁰ It is significant that § 3622(e) makes separate provisions for the establishment of new or changed workshare discounts and the reduction or elimination of existing ones. See pp. 14 et seq., below.

Class mailers within the subclass . . . and does not fairly allocate costs unaffected by worksharing.”²¹ By March 2007, when this Recommended Decision was issued, it was a plausible contention (and some witnesses had specifically argued) that Presort was a mature service offering and that “the days of large mass conversion from single-piece mail to presort mail [were] largely over[.]”²² Yet equity concerns bulked large in the Commission’s decision not to adopt the First-Class delinking proposal. They remain relevant here.

C. The Postal Service’s rate policy arguments in relation to its legal theory. So far we have treated the Postal Service’s ratemaking policy arguments as though they were separable from the statutory theory which we criticize in Part I. In fact, they are not. That statutory theory enables the Service to treat the Single-Piece/Presort relationship as something other than worksharing, and thereby to avoid questions of both statutory language and rate policy which, once recognized, bear significantly on the issues before the Commission.

We have explained above why, in our view, the Commission should reject that legal theory. In what follows, we will assume for argument’s sake that the Service’s legal theory has not been adopted, and that Single-Piece and Presort do stand in a worksharing relationship.

Statutory changes and historical development notwithstanding, Presort still involves actual worksharing.²³ Concentration on the gross cost difference, reflected in the CRA, between Single-Piece and Presort may tend to obscure the fact that the Presort product is based on worksharing. This is true, first, because of its historical origins. When presort discounts were introduced there was, as

²¹ PRC Op. R2006-1, ¶ 5090.

²² *Id.*, ¶ 5069 (citing American Bankers Association witness Christopher D. Kent).

²³ At least two of the functions specified in § 3622(e)(1) as grounds of workshare discounts – pre-sorting and prebarcoding – are clearly relevant.

the Postal Service points out²⁴, no way for existing cost systems to isolate the worksharing-related differences between presorted and non-presorted mail. As worksharing savings constituted the parameter of interest, per-operation costs were modeled and built into the discounts as negative elements (avoidances). Thus worksharing and the efficiencies promised by its rational use were the *raison d'être* of the original discount programs.

What has changed since then is not the centrality of worksharing, but the circumstance that the CRA now provides an apparently comprehensive view of the gross cost difference between the Single-Piece and Presort mailstreams. As noted earlier, worksharing cost avoidances make up about half that difference. Arguing that because worksharing does not account for the entire difference in unit cost, the Commission should ignore the large fraction for which it does account is not a prescription for just and reasonable – or even simply reasonable – ratemaking. Thus the problem of how (and, indeed, whether) to recognize the *non-worksharing-related* component of the gross difference – a problem the Service's statutory theory enables it to avoid – has to be faced.

D. *The question of pricing flexibility.* The Postal Service argues that one main purpose of PAEA was to endow it with greater pricing flexibility, and that adherence to a cost-avoidance approach for First-Class Presort rates undercuts that statutory policy.²⁵ The general proposition as to flexibility is true enough, but

²⁴ Postal Service Initial Comments, pp. 5, 6-7.

²⁵ The Postal Service says, for example, that

. . . Presorted and Single-Piece First-Class Mail are fundamentally distinct types of mail, and it would therefore be counterproductive to allow one aspect of rate design (maintaining price differences that rigidly match estimated cost avoidances across components of the two different products) to become the exclusive driver, or even just the primary driver, of relative prices between the two products.

Initial Comments, p. 17. And later, somewhat more broadly –

. . . When pricing Presorted First-Class Mail, the Postal Service needs to be cognizant of its product cost coverage, its product contribution to institutional costs, the different markets in which it competes, and the likely response in those markets to Presorted

it does not follow that the established technique of constructing Presort rates conflicts with it.

If the Service's legal theory were valid – that is, if despite the real-world causal facts reflected in the cost systems and through the BMM benchmark, Single-Piece and Presort were in no sense in a worksharing relationship – then it might be true that using worksharing-based techniques to develop Presort rates would unduly limit the Service's pricing options. But since there is a worksharing relationship between these mail types, the question is no longer one of *generalized* flexibility in pricing. Instead, it turns on the more specialized provisions of § 3622(e), in which Congress laid down a specific rule – subject to a number of exceptions – for worksharing discounts. In other words, the degree of pricing flexibility the Service enjoys with respect to worksharing discounts is defined by § 3622(e) and not simply by the broad and unspecific language of § 3622(b)(4).

E. *Section 3622(e) provides ample rate flexibility.* Looked at objectively, § 3622(e) can hardly be called inflexible. The Commission is to insure that discounts do not exceed avoided cost unless –

(A) the discount is –

(i) associated with a new postal service, a change in an existing postal service, or with a new work share initiative associated with an existing postal service; and

(ii) necessary to induce mailer behavior that furthers the economically efficient operation of the Postal Service and the portion of the discount in

product price changes. Consideration of these factors by no means presupposes that estimated cost differences between Presorted mail and single-piece mail should therefore be ignored. Under the PAEA, price increases between the Presorted product and the Single-Piece product are necessarily interrelated, because the price cap applies to First-Class Mail as a whole. But, as a matter of policy, it simply makes no sense to assert that the foundation for the entire Presorted pricing structure must be based on a single estimated cost link between the Presorted product and a separate product, Single Piece.

Id., pp. 18-19.

excess of the cost that the Postal Service avoids as a result of the work-share activity will be phased out over a limited period of time;

(B) the amount of the discount above costs avoided –

(i) is necessary to mitigate rate shock; and

(ii) will be phased out over time;

(C) the discount is provided in connection with subclasses of mail consisting exclusively of mail matter of educational, cultural, scientific, or informational value; or

(D) reduction or elimination of the discount would impede the efficient operation of the Postal Service.

Section 3622(e)(3) provides further insulation for existing discounts:

(3) LIMITATION. – Nothing in this subsection shall require that a work-share discount be reduced or eliminated if the reduction or elimination of the discount would –

(A) lead to a loss of volume in the affected category or subclass of mail and reduce the aggregate contribution to the institutional costs of the Postal Service from the category or subclass subject to the discount below what it otherwise would have been if the discount had not been reduced or eliminated; or

(B) result in a further increase in the rates paid by mailers not able to take advantage of the discount.

The first feature of interest in these provisions is that they require quantification of the avoided cost. Subparagraph (A)(ii) and subparagraph (B) as a whole require that the “amount of the discount above costs avoided” be known. Paragraph (D) in effect requires it too, since the issue there is how a known reduction in the discount (i.e., down to avoided cost) would affect the efficiency of postal operations. The computations required by paragraph (3) appear to require much the same thing. So far, the BMM benchmark has been found the most satisfactory way of quantifying avoided cost. There seems to be no reason why – assum-

ing the applicability of one or more of the § 3622(e) exceptions – it could not serve the same function in that context.

While Congress' decision to enact a specific rule, and several specific exceptions, exclusively for worksharing discounts ought to dispose of the "pricing flexibility" question, it is still of some interest to see whether the types of flexibility § 3622(e) provides do respond to the Postal Service's concerns as expressed in its comments.

Taking the question at its narrowest – i.e., as restricted to the issue of reducing an existing discount which exceeds avoided cost – we see that the Service is not required to reduce the discount if doing so will cost it volume and aggregate contribution in the affected category (§ 3622(e)(3)(A)). If the Postal Service can show such an effect, the discount need not be reduced. The Service's (by no means unrealistic) speculation that Presort customers faced with smaller discounts may reduce their usage can thus be dealt with under the worksharing provisions *once the necessary factual premises are established*.

We emphasize the last phrase because the questions implicit in the various § 3622(e) exceptions are empirical ones. They do not arise under the Postal Service's legal approach, which simply makes § 3622(e) irrelevant. Nonetheless, they, and the factual bases for answering them, are important for reasons relating to the basic efficiency of postal prices.

F. *The importance of efficient prices.* The general rule of § 3622(e) is not a merely arbitrary enactment but an expression of the basic principle of efficient pricing in a setting where a monopolist does not enjoy monopoly power over all the subservices comprising its product. The efficient component pricing principle, endorsed and used by the Commission, requires that the competitive subservices be priced at their average incremental cost, which is, for present purposes, equivalent to the rule of § 3622(e)(2). Consequently, it makes good sense for

per-piece cost avoidance to be the “foundation” of worksharing rates, even if it is not also their final determinant. Section 3622(e) appears to be designed around the twofold principle that (i) worksharing discounts *ideally* should be equal to avoided cost, for reasons of (at least) efficiency, but (ii) under some circumstances compromise between this ideal and other concerns may be necessary. Since these other concerns are likely to be class- or time-specific, it also makes sense to require them to be established empirically as the basis for departing from the general cost-avoidance rule.

A principal concern expressed by the Postal Service is loss of Presort volume:

. . . Once mail owners and consolidators have invested in equipment and determined procedures for presorting mail, it is unlikely that they would abandon these procedures and choose to send their mail via Single-Piece First-Class Mail if Presort First-Class Mail prices were to increase. But while raising Presorted prices (lowering the “discounts”) may not drive customers to Single-Piece, it could drive them out of the mail altogether. For example, a bank considering mailing notices to cardholders advertising optional new service features is unlikely to ponder whether to send the notices as Single-Piece or Presort. the bank is far more likely to consider whether to send them by mail at all, particularly if many of the same customers can be reached with the same message via the Internet.^[26]

This concern is clearly legitimate, but the Postal Service has not faced the question whether it could be dealt with under the provisions of § 3622(e). If the Service’s concern is – as would be expected – the aggregate contribution lost when Presort mail leaves the system, then § 3622(e)(3)(A) is directly in point.²⁷ If the Service can show that reducing the discount will lower aggregate contribution from Presort, it need not reduce the discount even if it exceeds avoided cost.

²⁶ Postal Service Initial Comments, pp. 18-19.

²⁷ If the Service found that the loss of revenue required raising Single-Piece rates in order to bring an overall First-Class increase as close as necessary to the price cap, § 3622(e)(3)(B) would be relevant too.

In some situations, however, the perceived risk might be that customers, discouraged by the smaller discount, would perform less worksharing on unchanged volumes of mail. Here again the Postal Service is protected – by an extremely broad exception, § 3622(e)(2)(D), which allows a discount greater than avoided cost if reducing it “would impede the efficient operation of the Postal Service.” If customers’ worksharing activity in this case were materially less costly per unit than performance of the same function by the Service, then its discontinuance presumably would reduce operating efficiency, and paragraph (2)(D) would be available.²⁸

In short, the provisions Congress enacted to govern worksharing discounts contain ample flexibility to deal with concerns like those the Postal Service raises. The Commission does not have to choose between adopting the Service’s questionable legal theory, on the one hand, and condemning the Service to suffer any potential bad consequences of adhering strictly to the avoided-cost rule on the other. The Commission can reject the legal theory (as we believe it should) and call upon the Service to cope with any such consequences under the comprehensive exceptions built into § 3622(e).

III. Practical ratemaking problems

The third aspect of the Postal Service’s position is that, apart from the supposed requirements of § 3652(b) and the policy arguments against tying Presort rates to a cost-avoidance benchmark, it is difficult and may be impossible to construct a satisfactory set of First-Class rates under the simultaneous constraints of (i) the whole-cent stamp price convention, (ii) the price cap, and (iii) the cost-avoidance benchmark for Presort rates. This argument does not, or

²⁸ If the customers’ cost to perform the operation turned out to be *greater* than the Service’s, of course, the “worksharing” was inefficient to begin with, and should not be encouraged by a discount at all. The same would be true if a once-useful worksharing activity had, by reason of operational or technological changes, become unhelpful or even burdensome for the Postal Service. See PRC Op. R2006-1, ¶¶ 5176, 5179 (elimination of discount for Carrier Route Automation Letters).

does not explicitly, depend on dubious legal interpretations or ideas of ratemaking policy on which reasonable students could differ. The Service's (somewhat simplified) examples²⁹ make it appear to be a matter of fairly uncomplicated arithmetic.

The evident problem with the argument, and the examples supporting it, is twofold:

- (1) It assumes that, if the avoided cost standard applies at all, no departure from it is possible – notwithstanding the flexibility provided by § 3622(e) itself; and
- (2) It does not consider whether changing some feature of First-Class rates other than the avoided-cost principle would serve to unjam the machinery. In particular, the suggestion, previously made³⁰, that the whole-cent convention could be changed is not considered.

We will deal with the whole-cent issue first – though that discussion will lead back into a discussion of the ratemaking flexibility § 3622(e) provides – and will begin with the Service's simplified example. Before taking up the inquiry, however, we should emphasize that changing the whole-cent convention is offered as an illustration of how the mechanical rate-fitting difficulties the Postal Service points to could be alleviated. It should *not* be considered for implementation until there is adequate assurance that the general public would find it ac-

²⁹ Initial Comments, pp. 21-26.

³⁰ By the Public Representative in Public Representative Comments in Response to Notice of Proposed Rulemaking on Application of Workshare Discount Rate Design Principles (May 26, 2009), pp. 20-21, and by both the Public Representative and GCA at the August 11, 2009, Public Forum in this Docket. The Public Representative suggests a stamp price free to come to rest at any appropriate tenth of a cent; GCA, for reasons of public convenience (particularly in very small stamp sale transactions), believes a half-cent convention would be a more useful starting point for the investigation.

ceptable.³¹ Discouragement of Single-Piece mailing would be no less harmful a result than discouragement of Presort.

The example assumes –

- two categories, Single-Piece and Presort (the latter represented by the Mixed AADC rate);
- equal weighting of the two categories;
- an annual adjustment (cap) of 1.0 percent; and
- a whole-cent convention for the Single-Piece price.

Table 1 on page 23 of the Service’s Initial Comments deduces from these premises a rate-history scenario in which the Single-Piece rate remains constant over three years of increases, while the Presort rate increases 2.1 percent or more in each of the three years.

We have recalculated Table 1 with a half-cent, rather than a whole-cent rounding convention³²:

³¹ Research on this issue should cover such questions as: How prevalent are sales of single stamps? How does the public perceive the equity of requiring a single-stamp purchaser to pay (in some years) an extra half-cent? Does the public believe that pricing stamps at “two for X cents” – as grocery stores often price consumer goods – is inappropriate for the Postal Service? Would the realization that in a “half-cent” rate year the purchaser of two stamps could save a half-cent make a difference to public views? and so on.

³² We have added column (c), showing, for Years 1-3, the Single-Piece rate as calculated without regard to any rounding convention.

Table A

Year	(a) Cap	(b) Overall rev/pc inflated by Cap	(c) Calcu- lated Sin- gle-Piece Rate	(d) Rounded Single- Piece Rate	(e) Effective Change	(f) Effective Presort Price	(g) Effective Change
0 (base)		41.1	44.0			38.2	
1	1.0 %	41.5	44.4	44.5	1.1 %	38.5	0.8 %
2	1.0 %	41.9	44.9	45.0	1.1 %	38.9	0.9 %
3	1.0 %	42.3	45.3	45.5	1.1 %	39.2	0.9 %

It appears, therefore, that much of the inflexibility of which the Service complains is due to the whole-cent convention.

It may be objected, of course, that the half-cent convention appears to make matters worse, if the Presort rate is set exclusively by reference to the worksharing cost avoidance. Because the Single-Piece rate is higher, in each increase year, than in the Service's Table 1, and because the cost avoidance is assumed to increase *pari passu* with the price cap, the total revenue generated seems to violate the cap even more substantially than it does in the Service's second example (Table 2, Postal Service Initial Comments, p. 24).

We must point out, however, that the unacceptable results the Postal Service shows in Table 2 are what they are principally because the analysis begins with the existing 38.2-cent Presort rate. This rate incorporates a discount substantially larger than 100 percent of avoided cost. In Table 2 it is shown as scaled down to avoided cost in Year 1. Thus the discount shrinks (from $44.0 - 38.2 = 5.8$ cents to 4.5 cents) at the time of the Year 1 increase. The resulting Presort rate ($44.0 - 4.5 = 39.5$ cents) cannot help generating excessive revenue under a price cap not designed to accommodate an abrupt change in underlying rate theory.³³ Table B, below, shows that if the Presort rate had been based on

³³ A similar problem would arise under the hypothetical half-cent convention, where the newly-rebased Presort rate would be $44.5 - 4.5 = 40.0$ cents.

avoided cost in Year 0, the overall increase would be much smaller: 1.1 percent rather than 1.5 percent. The overage would thus be 0.1 percent rather than 0.5 percent.

Table B

Year	(a) Cap	(b) Overall rev/pc inflated by Cap	(c) Calculated Single-Piece Rate	(d) Rounded Single-Piece Rate	(e) Effective Change	(f) Effective Presort Price	(g) Effective Change	(h) Overall Price Change
0		41.8	44.0	44.0		39.5		
1	1.0 %	42.2	44.4	44.5	1.1 %	40.0	1.2 %	1.1 %

The problem exhibited in the Service's Table 2, accordingly, lies not in the avoided-cost benchmark itself but in the fact that it is not now being observed. Indeed, the 0.1-percent overage in Table B can be accounted for by the rounding of the Single-Piece rate from 44.4 to 44.5 cents.³⁴ It does not result from use of the avoided-cost benchmark.

A sudden transition from a 38.2-cent Presort rate to an avoided-cost-based rate 1.3 cents higher clearly might have undesirable volume effects, if Presort exhibits any marked price sensitivity. The Postal Service, equally clearly, should avoid such effects if it can. Section 3622(e), however, contains mechanisms for avoiding sudden transitions. In particular, § 3622(e)(2)(B) allows a discount to exceed avoided cost if –

- (B) the amount of the discount above costs avoided –
 - (i) is necessary to mitigate rate shock; and
 - (ii) will be phased out over time[.]

³⁴ If the rounding increment is assumed away, then 0.1 cent ÷ 42.2 cents = 0.24 percent more revenue *with* rounding; and since by hypothesis Single-Piece and Presort are each weighted 50 percent, half this result, or 0.12 percent, is attributable to the rounding.

The provisions of PAEA which govern workshare discounts are sufficient to deal with the difficulties of accommodating a class-wide price cap, a practicable Single-Piece stamp rate, and economically efficient workshare discounts.

To summarize:

- The Commission need not, and should not, adopt an artificially narrow construction of § 3622(e) in order to resolve the mechanical problem of combining an avoided-cost benchmark with the class-wide price cap;
- Given adequate assurance of its acceptability to the mailing public – a caveat that cannot be too strongly emphasized – a half-cent stamp price convention would be a simple and effective way of alleviating this problem; and
- The Service should use the legitimate opportunities provided by § 3622(e) to apply the avoided-cost benchmark flexibly, rather than viewing it as a rigid rule which serves only to make rational First-Class rate design infeasible.

IV. Summary and conclusion

GCA submits that –

- In arguing that the Commission may not, as a matter of law, treat the Single-Piece/Presort relationship as worksharing, the Postal Service advocates an untenable and, in particular, unduly narrow interpretation of §§ 3622(e) and 3652(b) – and, very significantly, one which entails the possibility of reducing § 3622(e) to a nullity;

- While the Postal Service is correct that *as a general matter* PAEA seeks to endow it with more ratemaking flexibility, it ignores the flexibility which § 3622(e) provides *specifically for worksharing discounts*;
- The Postal Service points to practical difficulties in combining a price cap, a whole-cent letter stamp convention, and a cost-avoidance benchmark for Presort; but on analysis these turn out to be mainly due to (i) the whole-cent convention and (ii) the fact that in current Presort rates the cost-avoidance benchmark has been ignored.

GCA recommends that the Commission –

- Clarify by rule (what we believe is already clear from the statute) that the cost-avoidance rule of § 3622(e) and its various exceptions, and the data-reporting requirements of § 3652(b), do apply to worksharing-based relationships spanning product boundaries;
- Reaffirm the appropriateness, as a matter of ratemaking principle, of the avoided-cost (BMM) benchmark for First Class;
- Consider, so far as may be necessary for efficient implementation, issuing policy guidance with respect to the scope and appropriate use of the § 3622(e) exceptions; and
- Once it is reasonably certain that the change would be accepted by the general public, give serious consideration to replacing the whole-cent letter stamp convention with a half-cent convention, to alleviate the mechanical problem of constructing efficient, equitable First-Class rates under a price cap.³⁵

³⁵ GCA would be prepared to cooperate with the Postal Service and other interested parties in testing the suitability of a half-cent convention.

Respectfully submitted,

GREETING CARD ASSOCIATION

David F. Stover
2970 South Columbus Street, No. 1B
Arlington, VA 22206-1450
(703) 998-2568
(703) 998-2987 fax
E-mail: postamp@crosslink.net