Postal Regulatory Commission
Submitted 8/31/2009 1:08:01 PM
Filing ID: 64486
Accepted 8/31/2009

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Notice of Price Adjustment
for Certain Presorted First-Class Mail

Docket No. R2009-5

COMMENTS OF THE PUBLIC REPRESENTATIVES
(August 31, 2009)

On August 11, 2009, the Postal Service filed a notice with the Postal Regulatory Commission (Commission) of a proposed adjustment in the prices for certain First-Class Mail presorted letters, flats and cards sent by qualifying mailers.[1] The adjustment is referred to as the "First-Class Mail Incentive Program" ("FCM Incentive Program" or "Program"). *Id.* The Postal Service's notice was filed pursuant 39 U.S.C. 3622 and 39 CFR Part 3010.

The Commission's Order No. 276, issued August 13, 2009, designated a Public Representative in this proceeding and established August 31, 2009, as the deadline for filing initial comments.[2] Pursuant to Order No. 276, the Public Representatives hereby files their initial comments.

I. INTRODUCTION

The Postal Service states in its August 11 Notice that the FCM Incentive Program has been proposed as a way "to encourage communication using the mail between businesses and their customers during these challenging economic times." Notice at 2. The hope is that "a short-term incentive to use the mail and stabilize or grow volume could help keep businesses in the mail, provide a base for growth in the

[1] United States Postal Service Notice of Market-Dominant Price Adjustment, August 11, 2009 ("August 11 Notice" or "Notice"). The Postal Service also refers to the qualifying presorted pieces as non-parcel First-Class Mail. *Id*.
[2] Subsequent to the issuance of Order No. 276, Staff Member Katalin K. Clendenin was designated to provide technical assistance in this proceeding.

future, and improve the future profitability of the Postal Service. *Id.* at 3. The Program "is expected to make a positive contribution to institutional costs." *Id*.

II. PROGRAM SUMMARY

The basic parameters of the FCM Incentive Program can be summarized as follows:

- The Program will be in effect from October 1 through December 31, 2009. *Id*.
- Eligible mailers must have mailed 500,000 or more non-parcel First-Class Mail pieces between October 1 and December 31in both 2007 and 2008, either through permit accounts owned by the mailer or set up by a Mail Service Provider on behalf of the mailer. *Id*.
- Mail Service Providers are to be excluded from the Program. *Id*. at 4.
- Eligible mailers will receive a 20 percent rebate "calculated as the average revenue per piece for all eligible mail volume during the program period multiplied by the incremental volume above the threshold during the program period." *Id*. at 3-4.
- The rebate threshold volume will be a company-specific volume calculated (a) "by computing the ratio of the October 1 – December 31, 2008 non-parcel First-Class Mail presorted volume to the October 1 – December 31, 2007 non-parcel First-Class Mail presorted volume", and (b) by multiplying that ratio "by the company's October 1 – December 31, 2008 non-parcel First-Class Mail presorted volume…." *Id*. at 3.
- Mailers whose actual mail volume during the period from October 1, 2009, through December 31, 2009, exceeds their threshold will receive a rebate of 20 percent. *Id*. at 2-3.
- To prevent previously planned mailings from being

> shifted from September, 2009, into October, 2009, or from January, 2010, into December, 2009, each mailer's September, 2009, and January, 2010, actual volumes will be compared to the respective month's threshold (calculated in the same way as the ratio used to establish the threshold during the Program period) and, if those actual volumes fall short of the threshold for that month, the shortfall will be deducted from the qualifying incentive volume. *Id*. at 4.

Administratively, the Program will operate in the following manner:

- Each potential Program participant will be contacted by the Postal Service and advised of the Program.

- Mailers interested in participating in the Program may enroll by providing historic mail volume data by month and by company or MSP permits used. Volume data must be supported and certified.

- A procedure is prescribed for resolving any disagreements over a mailer's volume.

- Mailers who are not contacted by the Postal Service, but wish to participate, are instructed to contact the Postal Service to obtain an eligibility determination.

- Rebates will be calculated and credited to each company's permit trust account no earlier than 30 days after the end of the Program period.

- Within 90 days after the payment of incentive rebates, the Postal Service will submit a report to the Commission on the results of the Program. *Id*. at 6.

The Postal Service projects revenue increase of approximately $43 million net of rebates. Of this amount, the Postal Service estimates that approximately $31 million will be the result of new volume and $12 million will be due to a buy up to First-Class Mail from Standard Mail. The total increase in contribution is projected to be approximately $24 million, with $16 million produced by new volume and $8 million generated by the buy up from Standard Mail. Administrative costs are estimated to be approximately $809,000.[3] Additional volume is estimated to produce enough contribution to ensure adequate First-Class Mail cost coverage.

III. COMMENTS

The Public Representatives support implementation of innovative programs, like the one proposed in this proceeding. If the Program functions as intended, mailers will be able to increase mailings at a lower cost and the Postal Service will generate additional contribution. The Postal Service is to be commended for moving aggressively to increase mail volumes in a manner which provides tangible and potentially important benefits to its customers. Moreover, the information gained from the FCM Incentive Program may lead to the implementation of future programs that address the needs of mailers and foster further increases in mail volumes.

While the Public Representatives support approval of the Program, they have several questions and concerns which they believe the Commission should consider in reviewing and acting on the proposal.

A. Period Covered by the Program

The FCM Incentive Program is to be in effect from October 1, 2009 through December 31, 2009. The reason for selecting this period is not explained. Nevertheless, the Public Representatives are aware of no reason why this period would not be appropriate.

---

[3] This projection consists of program support by dedicated Postal Service personnel ($450,000); analytical support by contractors ($100,000); registration website creation ($9,000); and production of customer print communications ($250,000). *Id. at 7.*

B. Program Eligibility

As proposed, the Program will be open to customers who mailed 500 thousand or more non-parcel First-Class Mail pieces between October 1, and December 31, in both 2007 and 2008, through permit accounts owned by the mailer or set up on behalf of the mailer by an MSP. The Notice does not indicate the basis for selecting these eligibility criteria. Nor does the Postal Service estimate how many mailers are potentially eligible to participate in the Program. Unless problems with the proposed eligibility limitations are identified by other commenters, the Public Representatives would have no reason for not accepting the Postal Service's proposed criteria.

MSP's utilizing their own permits would be excluded from the Program in an apparent attempt to ensure that the Program's benefits inure to the originators of the mail by protecting the Postal Service from the combination of volumes by multiple mail owners onto an MSP's permits in order to optimize discount-qualifying volumes by merely shifting existing volumes around in order to receive a discount.[4] Assuming the basic eligibility criteria summarized above are approved, this latter limitation would appear to be both understandable and acceptable.

C. Migration

The FCM Incentive Program seeks to avoid volume shifting of First-Class Mail from the shoulder months of September, 2009, and January, 2010, into the Program months of October, 2009 through December, 2009. These adjustments to a mailer's qualifying incentive volumes are an appropriate means of offsetting shifts of mail volumes from the shoulder months and should mitigate or eliminate any artificial inflation of qualifying incentive volumes that would otherwise be produced.

The Postal Service also asserts that it "expect[s] about 103 million pieces to buy up from Standard Mail…." Notice at 7. However, in the Summer Sale proceeding in

[4]The Summer Sale Program approved by the Commission in Docket No. R2009-3 excluded MSP's for this reason. PRC Order No. 219, Order Approving Standard Mail Volume Incentive Pricing Program, June 4, 2009 (Order No. 219), at 3, 5.

Docket No. R2009-3, the Postal Service stated that First-Class Mail would not be expected to migrate to Standard Mail because of the special features available with First-Class Mail.[5] This latter statement implies no cross-price elasticities between First-Class and Standard Mail. But if there are no cross-price elasticities between Standard and First-Class Mail, it is inconsistent to assert in this proceeding that Standard Mail customers can be expected to buy up to First-Class Mail because of the rebate incentives of the FCM Incentive Program. The Postal Service should be required to explain this inconsistency.

D. Volume Thresholds and Magnitude of Rebates

The volume threshold methodology for the FCM Incentive Program differs significantly from the volume threshold methodology used in the Summer Sale Program approved in Docket No. R2009-3. The threshold in the FCM Incentive Program is calculated using two earlier periods (October 1 – December 31, 2007; and October 1 – December 31, 2008), both of which are the same calendar months that the FCM Incentive Program will be in effect during 2009 (*i.e.,* October 1 – December 31). By contrast, the threshold in the Summer Sale Program utilized was calculated using two earlier periods (October 1, 2008 – March 31, 2009; and October 1, 2007 – March 31, 2008), that differed from the calendar months that the Summer Sale was to be in effect during 2009 (*i.e.*, July 1 – September 30).[6]

The Postal Service offers no explanation for changing the method used to calculate the volume threshold. In particular, the Postal Service fails to explain why the Summer Sale relied upon more recent months to estimate mail volume trends than does the FCM Incentive Program. To insure an understanding of the FCM Incentive Program before it acts on the proposal, the Commission should require the Postal Service to provide an explanation of the assumptions underlying and reasons for selecting the

[5] Response of the United States Postal Service to Chairman's Information Request No. 1, Docket No. R2009-3,Q.2a.
[6] United States Postal Service Notice of Market-Dominant Price Adjustment, May 1, 2009 (Summer Sale Notice) , at 3-4.

periods used to calculate the volume threshold and to explain the reason for using a volume threshold method that differs from the method used in the Summer Sale.

The Program as proposed incorporates a 20 percent discount. It is unclear how the Postal Service decided this discount level or whether the Postal Service considered any lower level of discount. A lower discount level might generate more contribution for the Postal Service despite potentially lower volumes being mailed. Given the fact that this is only the Postal Service's second attempt to implement a program of this nature and in light of the apparent likelihood that product cost coverages will not be impaired by rebates of this magnitude, the Public Representatives believe the 20 percent discount to be at a reasonable inducement to increase mail volumes.

E. The Requirements of Rule 3010.14 and Rules 3001.190, *et seq.*

1. The Requirements of Rule 3010.14

Rule 3010.14 (b)(1) through (4) generally requires that a notice of rate adjustment be accompanied by calculations of cap and price changes. In its Notice, the Postal Service relies upon the temporary nature of the Program and the uncertainty over the amount of new volume that will be generated to propose that for purposes of price cap compliance it treat the Program in a manner that is mathematically analogous to negotiated service agreements as provided in rule 3010.24. The Postal Service therefore intends to ignore the effect on the price cap that results from the price decrease produced by Program rebates. For the reasons given by the Postal Service, the Public Representatives do not oppose this approach.

In its August 11Notice, the Postal Service includes a discussion of why it believes that the proposed rate adjustment satisfies the requirements of rules 3010.14(b)(5) through (8). That discussion addresses how the proposal is designed to help achieve the objectives of 39 U.S.C. 3622(b); and how the proposal takes into account the factors of 39 U.S.C. 3822(c). Notice at 8-13.

With respect to the objectives of section 3622(b), the Postal Service asserts that the Program "does not substantially alter the degree to which First-Class Mail prices already address these objectives, or they are addressed by the design of the system itself (Objectives 1,2,3,6,7,8, and 9)." Notice at 10. In addition, the Postal Service states that the FCM Incentive Program is an example of the increased flexibility provided to the Postal Service by the Postal Accountability and Enhancement Act (Objective 4); and that the objection of ensuring adequate revenues to maintain financial stability (Objective 5) would also be furthered by the Program's incentive to increase mail volumes and its support for a key customer segment. *Id*. at 10. The Public Representatives do not take issue with these assertions.

With respect to the factors of section 3622(c), the Postal Service alleges that the Program "does not substantially alter the degree to which First-Class Mail prices address … Factors 1, 4, 5, 6, 8, 9, 10, 11, 12, 13, and 14…." With respect to the remaining factors, the Postal Service claims: that the Program addresses Factor 3 by providing assistance to a key customer segment during the severe economic downturn; and that the Program will not affect the ability of First-Class Mail to cover attributable costs. *Id*. at 12-13. Again, the Public Representatives do not dispute these assertions.

2. The Requirements of Rules 3001.190, *et seq.*

In its response to a Chairman's information request, the Postal Service states that the incentives in FCM Incentive Program are not worksharing discounts, but are analogous to declining block discounts offered in Negotiated Service Agreements (NSAs):[7]

> It [the incentive offered in the Program] is exactly analogous to the declining block rate discounts offered in various NSAs (with, in this case, only one block)….

The Postal Service goes on to state that the incentive offered in the Program "should be evaluated in the same way NSA discounts have been; that is, based on their likely efficacy in encouraging growth in volume." *Id*.

[7] Responses of the United States Postal Service to Chairman's Information Request No. 1, August 21, 2009, Question No.4.

Despite its acknowledgement that the FCM Incentive Program rebates operate in a manner analogous to discounts in NSAs and that these incentive rebates should be evaluated in the same way as NSA discounts, it has not sought to provide the information required by rules 3001.190, *et seq.* of the Commission's regulations. Nor does the Postal Service appear to intend that the report that it files at the conclusion of the Program will contain the analysis that the Commission has previously required for NSAs. That analysis has been regularly required since the Commission's April 21, 2006 Opinion and Further Recommended Decision in Docket No. MC2004-3.[8]

The Public Representatives respectfully request that the Commission request the Postal Service to provide the information required by rule 3001.190 for review before acting on the proposed FCM Incentive Program. The Postal Service should also be required to present information in its final report on the Program that permits the analysis described in PRC Opinion and Recommended Decision, MC2004-3, ¶¶5001-38. The Commission has stated that that analysis is important in order "[t]o satisfy the requirements of the statute … [by demonstrating] … a reasonable likelihood of resulting in a net increase in contribution above which the contribution would have been absent the discount [footnote omitted]." *Id.* ¶5010. Moreover, as the Commission stated in a subsequent Opinion[9]:

> The [MC2004-3] analysis … may be used as an after-the-fact evaluation to determine whether, given a known after-rates volume, an agreement was beneficial to the Postal Service.[31]
>
> ---
>
> [31] *See, e.g.,* FY2007 Annual Compliance Determination, March 27, 2008.

PRC Opinion and Recommended Decision, MC2007-4 at 45. The MC2004-3 analysis is an important tool for ensuring that discounts do not produce revenue leakage and that the desired increases in contribution are achieved.

---

[8] PRC Opinion and Further Recommended Decision, MC2004-3, ¶¶5001-38. PRC Opinion and Recommended Decision, MC2005-3; PRC Opinion and Recommended Decision, MC2007-4; and PRC Opinion and Recommended Decision, MC 2007-5.
[9] PRC Opinion and Recommended Decision, MC2007-4 at 45.

F. Effects on Worksharing Discounts

The Postal Service has also addressed the potential effect on workshare discounts. Notice at 13-14. The Postal Service asserts, and there appears to be no obvious basis for disputing, that "[t]o the extent that the program affects discounts between presort categories, it will shrink them." *Id*. at 13. Finally, the Postal Service states, and the Public Representatives do not dispute, that the FCM Incentive Program will have no impact on preferred rates. *Id*. at 14.

G. Evaluation of the Program

The Postal Service plans to evaluate the Program at its conclusion. It indicates that measuring incremental revenues and volume growth will be its primary measures of the Program's success.

The FCM Incentive Program provides the Commission with its second opportunity to learn from a Postal Service promotional pricing program. The first opportunity will come when the Postal Service files its report on the Summer Sale Program.[10] In its Notice, the Postal Service proposes a report containing the following types of information:

> (1) monthly information for eligible First-Class customers under seal;
>
> (2) publicly available monthly information for eligible First-Class customers in aggregated form;
>
> (3) monthly permit volumes for Standard Mail letters and flats for each eligible First-Class Mail user under seal; and
>
> (4) the actual administrative costs of the Program.

[10] That report is to be filed within 90 days after payment of the incentive rebates. Notice at 6.

Notice at 6.

The Public Representatives agree that the foregoing information should be included in the report, and urges the Commission to require inclusion of the following additional information.

(1) a narrative discussion of any problems experienced with implementation of the Program;

(2) identification of any necessary or desirable improvements to Postal Service data systems identified as a result of implementing the Program;

(3) a summary of customer expressions of satisfaction or dissatisfaction with the Program; and

(4) a discussion of any generic weaknesses with, or strengths inherent in, the FCM Incentive concept; and an identification or discussion of any other information gained from the Program which the Postal Service deems to be relevant or pertinent.

In addition, the Postal Service should be required to include in its report the information needed to perform the analyses described in the Opinion and Recommended Decision in Docket No. MC2004-3 and subsequent cases.[11]

The submission of such a report should not be an undue burden inasmuch as the information identified is, in a number of cases, information that the Postal Service has expressly identified as information that it expects to obtain and analyze. The purpose of the recommendation is simply to ensure that the Postal Service shares its Program experience with the Commission. This will provide a foundation not only for the formulation of future programs by the Postal Service, but for Commission evaluation of future such programs. Moreover, the production of this information is entirely consistent with the PAEA's emphasis on increased transparency.

[11] Note 8, *supra.*

IV. CONCLUSION

In conclusion, for the reasons stated above, we the Public Representatives believe the First-Class Mail Incentive Program is an innovative use of the pricing flexibility granted by the PAEA and, with the administrative and operational experience gained, could pave the way for additional equally innovative plans in the future involving yet more customers and, if deemed appropriate, additional products. We recommend approval of the Program subject to the suggestions presented in the foregoing comments.

Respectfully submitted,

Richard A. Oliver

Richard A. Oliver

Katalin K. Clendenin

Katalin K. Clendenin

Public Representatives for
Docket No. R2009-5

901 New York Avenue, N.W.
Suite 200
Washington, DC 20268-0001
Phone: (202) 789-6878
Fax: (202) 789-6891
E-Mail: richard.oliver@prc.gov
katalin.clendenin@prc.gov

August 31, 2009