

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

**Notice of Price Adjustment and
Classification Changes Related to
Move Update Assessments**

Docket No. R2010-1

**SUPPLEMENTAL COMMENTS OF THE
ASSOCIATION FOR POSTAL COMMERCE,
DIRECT MARKETING ASSOCIATION, INC.
AND ALLIANCE OF NONPROFIT MAILERS**

The Association for Postal Commerce (“PostCom”), Direct Marketing Association (“DMA”) and Alliance of Nonprofit Mailers (“ANM”) respectfully submit these supplemental comments in response to four items filed by the Postal Service too late for a response in the comments filed by the undersigned parties on November 4, 2009: (1) the Postal Service’s November 3 response to Chairman’s Information Request No. 1; (2) the Postal Service’s November 9 supplemental response to CIR No. 1; (3) the November 13 “Follow-Up Materials Related to November 12, 2009 Technical Conference”; and (4) the November 16 “Additional Item of Follow-Up Material Related to November 12, 2009 Technical Conference.”

SUMMARY

The fundamental thrust of the supplemental materials submitted by the Postal Service is that the volume of mail that will be subject to the surcharge is so small that the Commission should simply ignore the operational, policy and legal issues that fatally infect this proposal. This, the Commission cannot, and surely should not, do. In fact, the

supplemental materials abjectly fail to address the issues that have been raised in this docket, and indeed raise new questions concerning the reliability of the tests upon which the Postal Service purports to rely and the revenues that the seven-cent surcharge is projected to generate. As we discuss below:

1. The overwhelming consensus of comments establish that the key elements of determining whether a mailer passes or fails the Move Update performance based verification (“PBV”) remain undefined and unknown. The Postal Service has conceded as much in the supplemental submissions. As a result, neither we nor the Commission have any way of knowing whether the Move Update tests conducted at acceptance units accurately or faithfully reflect how the pass-fail standard actually will be applied. The results of these MERLIN acceptance unit tests as a measure of impact on mailers are unreliable at best, and when joined with the Postal Service's insistence on the unilateral right to alter the tolerances, can be given no credence whatsoever.

2. The data the Postal Service has submitted with the supplemental filings disclose that, for both First-Class and Standard Mail, the costs that the Postal Service incurs in forwarding and returning First-Class Mail and disposing of undeliverable-as-addressed (“UAA”) Standard Mail are reflected in the rates. While this fact does not necessarily rule out an additional surcharge for noncompliance with Move Update standards if properly justified as a deterrent to noncompliance, the Postal Service still has made no attempt to explain why nothing less than seven cents will deter uneconomic conduct.

3. The Postal Service announces, for the first time, that the seven-cent surcharge will apply *only* to mail that fails the PBV process and that the default rate for

after-the-fact audits will be the single-piece First-Class mail rate. The Postal Service has also indicated that the pass-fail standards in the full audits will differ from the standards that apparently will apply to PBV. This disconnect further undermines any justification for the seven-cent surcharge: It means that the total penalties actually paid by mailers (whether or not they initially passed the PBV procedure) will, perversely, depend on the class of mail used and the degree of worksharing performed. Deterrence is not justified by irrational variations in penalties, nor will it be accomplished by such an incoherent and inconsistent regime, the irrationality of which cannot be explained away by vague promises of refunds .

4. In light of these recent disclosures, the Postal Service’s revenue estimates are as unreliable and legally questionable as the PBV testing standards that will actually be applied and the rationale for the seven-cent penalty.

In our view, the Commission has no choice. It can not abdicate its responsibilities under the PAEA. It must, therefore, apply the “Scottish verdict”—not proven—and reject this proposal without prejudice.

We emphasize that the mailing industry’s objections are based not on any disagreement with the fundamental objective – quality and accurate addresses – but on the ambiguous standards by which mailers will be tested, the unknowns about PBV, and the long-standing doubts about the testing methodology often used to verify mailers’ compliance – MERLIN and inconsistently-performing personnel. At this point, the Postal Service’s proposed rules for evaluating achievement of this goal are too undefined, and the processes too unreliable, to pass muster under 39 U.S.C. § 3622(d) and the just and reasonable standards of Title 39.

I. KEY ELEMENTS OF THE PROPOSED STANDARDS AND PROCEDURES REMAIN UNSPECIFIED.

The overwhelming consensus of comments—from the Postal Service’s largest and most sophisticated customers—establish that key elements of what mailers must do to avoid seven-cent penalties remain undefined and unknown. Since filing this docket, the Postal Service has disclosed little if any guidance to mailers. *See* Comments of PostCom *et al.* at 4-5, 16-18; Comments of Association for Mail Electronic Enhancement at 2; Notice of Questions Received Regarding Technical Conference, National Postal Policy Council Question 3.

This concern is apparently shared by the Postal Regulatory Commission. Question 4(a) of the Chairman’s Information Request No. 1 (“CIR 1”), recognizing that the proposed rules are underspecified, requested that the Postal Service explain the proposed Move Update assessment standards:

The MCS is being developed as a stand-alone document with either limited or no reference to the other documents or parties (*e.g.*, the DMM, IMM, or ‘as specified by X’). So that the pertinent parameters of the service or product can be fully described in the MCS, please explain what is meant by each use of the phrase “as specified by the Postal Service” in the proposed MCS language.

The purported clarification offered by the Postal Service—to replace “as specified by the Postal Service” with “add \$0.07 per assessed piece, for mailings that fail a Performance Based Verification at acceptance”—is completely circular. It does not answer the unresolved question of *what* will cause mailings to “fail a Performance Based Verification at acceptance.”

II. THE POSTAL SERVICE’S REVENUE IMPACT ANALYSIS UNDERSTATES THE AMOUNT OF ADDITIONAL REVENUE GENERATED BY THE SEVEN-CENT PENALTY BECAUSE THE STANDARDS THAT THE

POSTAL SERVICE PROPOSES TO APPLY ARE NOT THE SAME STANDARDS USED DURING THE TESTS EARLIER THIS YEAR.

The Postal Service's supplemental filings still leave unknown how much additional revenue the seven-cent penalty will generate. The Postal Service's estimates in this docket purportedly rely on the results of Move Update tests performed at acceptance from April to August 2009. The Postal Service's supplemental filings purport to show that the net revenue increase will be small. *See, e.g.*, Response of the Postal Service to CIR 1, Q 3(b); Revised Appendix B1 to Postal Service Notice of Market Dominant Price Adjustment and Classification Changes ("Revised Appendix B1") (purportedly showing that only about 1/10 of 1% of 1C and Standard pieces will get assessed a penalty). But, as the Postal Service's supplemental filings confirm, this assumption is both unverifiable and implausible. The standards that apparently will apply if the Commission approves the penalty proposal appear to differ from the standards used in the tests earlier this year. Hence, it is impossible to determine whether the effective percentage increase in First-Class and Standard Mail rates will comply with the CPI price cap imposed by 39 U.S.C. § 3622(d).

A. Standard vs. Individual Matching Logic

The Move Update tests performed from April through August 2009 grossly understate the amount of additional revenue that the seven-cent penalty will generate because, in part, these tests appear to have not treated family move matches as Move Update failures (whereas the Postal Service proposes to do just that beginning in January).

Until now, the Move Update rules allowed mailers to comply with Move Update by implementing address changes only for the individuals who submitted the change-of-address orders, without implementing address changes for other members of the same household. This is accomplished by selecting the desired processing mode (each of which uses a different matching logic, or combination thereof) when processing address lists through the NCOA^{Link} Product. The “Required Text Document,” which the Postal Service publishes and requires NCOA^{Link} providers to distribute to their clients, describes the five types of processing modes available in NCOA^{Link} as follows:

Standard Processing Mode (S)

- Standard Processing Mode requires inquiries in the following order:
 - Business – Match on business name.
 - Individual – Match on first name, middle name, surname and title required. Gender is checked and nickname possibilities are considered.
 - Family – Match on surname only.
- **Under no circumstances shall there be a “Family” match only option.**

Business and Individual Processing Mode (C)

- The NCOA^{Link} customer may choose to omit all “Family” match inquiries and allow only “Individual” and “Business” matches to be acceptable. This matching process is also known as C Processing Mode.

Individual Processing Mode (I)

- The NCOA^{Link} customer may also choose to omit “Business” match inquiries when processing individual names for mailing lists that contain no business addresses.

Business Processing Mode (B)

- The NCOA^{Link} customer may choose to process for only “Business” matches when processing a “Business-to-Business” mailing list which contains no residential (Individual or Family) addresses.

Residential Processing Mode (R)

- The NCOA^{Link} customer may choose to omit “Business” match inquiries and allow only “Individual” and “Family” matches to be acceptable under Residential Processing Mode. This matching process is also known as R Processing Mode.

In the current proceeding, however, the Postal Service has changed its position. It now indicates that the Move Update component of PBV will use Standard Matching Logic to test all mailings, and that failure to update the address of any family member of an individual who has submitted a change-of-address order will be viewed as deficient for purposes of calculating the seven-cent penalty.¹

This is a significant change. According to the Postal Service, six to 43 percent of all matching failures result from family moves. As noted in the parties’ November 4 comments, there are many circumstances (e.g., divorce, college matriculation or other circumstances in which a household breaks up) in which use of Standard Matching Logic would expose the mailer to substantial legal liability. As a result, many mailers cannot use Standard Matching Logic.

Appendix B1 of the Postal Service’s Notice and other Postal Service documentation do not reveal whether the Move Update tests used to generate the data showing relatively low penalty percentages used Individual or Standard Matching Logic.

¹ See Publication 363, Question 48 (“A mailer’s choice to disregard certain address updates provided through Move Update products does not entitle the mailer to continue to claim postage discounts where the update of the address is a prerequisite to getting the discount.”). Postal Service representatives confirmed this position at an MTAC meeting on October 28, 2009, and advised the attendees that the new position would be embodied in a DMM Advisory in the near future.

Given the much higher failure rates that result from treating Standard Matching Logic (i.e. family) matches as Move Update failures, it appears that the tests used Individual Matching Logic, and thus grossly understate the amount of additional revenue that the seven-cent penalty will generate.

B. Treatment of Moved Left No Address (“MLNA”) and Closed PO Box (“BCNA”) Matches.

The Postal Service’s revenue impact analysis also appears to take no account of matching failures resulting from MLNA and BCNA matches.

As noted in the comments of PostCom *et al.* (at 9-10), MLNA and BCNA codes, because not mailer-generated, have generally not been considered Move Update violations. The Postal Service now takes the opposite position. At the November 12, 2009 Technical Conference, the Postal Service explicitly stated that MLNA and BCNA matches would be treated as outdated addresses. This change-of-position is also likely to cause MERLIN/PBV to report a significant number of additional Move Update failures. According to Postal Service estimates, MLNA and BCNA matches account for approximately 17 percent of the new address information contained on the NCOA^{Link} file. See Required Text Document at 1. Like the use of Standard Matching Logic, there is no indication in the Postal Service workpapers that the April through August tests reflected the Postal Service’s decision to treat MLNA and BCNA matches as deficient, and the relative values suggest that the tests did not.

C. Effect Of Future Changes In Tolerance Threshold.

The Postal Service's revenue impact analysis assumes a 30 percent tolerance threshold, which the Postal Service says it will implement at the outset. But the Postal Service has admitted in its response to CIR1, Question 6, and restated at the Technical Conference, that it reserves the right to change the 30 percent tolerance level unilaterally, without further Commission review. *See* Response of the Postal Service to CIR 1, Question 6. Reducing the tolerance threshold would cause the number of pieces assessed a penalty to increase dramatically. *See* Revised Appendix B1 Monthly Data Worksheet (showing number of test mailings that received failure scores of 20-30% and 10-20%).

D. What Are The "Before" Rates?

At earlier stages in this proceeding, the Postal Service tried to finesse the issue of compliance with the CPI cap imposed by 39 U.S.C. § 3622(d) on the theory that the proposed penalties are smaller than (1) the maximum amount that could be collected as an after-the-fact revenue deficiency (i.e., the full difference between discounted rates and the full single-piece First-Class rate) or (2) under the "current" MCS (i.e., the penalties that would otherwise take effect on January 10, 2010).

The first comparison, however, is meaningless: the Postal Service is not proposing the right to forego the collection of traditional revenue deficiencies. Hence, the relevant comparison is between (a) the current revenue deficiency penalties and (b) those penalties *combined with* the proposed penalties. Moreover, the Postal Service also appears to be proposing to *expand* the traditional revenue deficiency penalties. Under current practice, revenue deficiency claims are frequently settled based on default rates below the single-piece First-Class rate. This recognizes the reality that even mailings that

do not comply with Move Update can provide significant savings to the Postal Service from presorting, barcoding, destination entry, and other forms of worksharing. Now, however, the Postal Service suggests that the single-piece rate is going to become the default rate for traditional after-the-fact Move Update revenue deficiency assessments. That implies a further increase in revenue per piece, which the Postal Service's analysis of its compliance with CPI cap completely ignores.

Comparison with penalties that would take effect on January 10, 2010, is equally baseless. Those rates are not in effect now. And, for the reasons explained in these comments and in our November 4 comments, the likely financial impact of the current proposal—even with the 30 percent threshold—appears to be far higher than the Postal Service's financial impact projections for the version of the penalties proposed in Docket No. R2009-2 but suspended until January 2010.

III. THE SEVEN-CENT PENALTY FOR “BAD” ADDRESSES ABOVE THE 30 PERCENT THRESHOLD IS UNJUST AND UNREASONABLE.

A. Seven Cents Not Justified As Compensation.

The Postal Service's supplemental filings confirm that the size of the penalty is not justified in terms of compensation. As the Postal Service has conceded, the penalty is in no way related to the costs created by UAA mail; accordingly, the penalty is not just and reasonable.²

² See, e.g., *Union Pac. R.R. Co. v. Bay Area Shippers Consolidating Ass'n, Inc.*, 594 F.2d 1291, 1294 (9th Cir. 1979) (expressing concern that 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”).

In its response to CIR 1, the Postal Service admits that the “goal is not to cover the costs of UAA pieces, but instead to provide an adequate incentive to mailers to take action to eliminate the UAA pieces from their mailings. There is no fixed relationship between the assessment charge and UAA costs.” Postal Service Response to CIR 1, Question 3(b). Similarly, the Postal Service concedes that that the seven-cent charge “was not designed with explicit reference to the UAA costs for mail pieces or mailings that exceed the tolerance.” Postal Service Response to CIR 1, Question 3(b). In fact, there was not even an *implied* reference to these costs, much less an explicit one. There was no reference, period.

The Postal Service has submitted a spreadsheet (“TechConf UAA Cost Table.xls”) purportedly showing that the cost per piece of forwarding, destroying or returning to sender an average piece of UAA Standard Mail is about 5.2 cents. *See* Follow-Up Materials Related to November 12, 2009 Technical Conference, Item 2. This spreadsheet, however, provides the estimated average figure for *all* shapes of Standard Mail, including parcels and NFMs. In response to CIR 1, Question 1, the Postal Service states that it will not be assessing the seven-cent penalty against Standard Mail parcels and NFMs, apparently because the MERLIN equipment is not designed to handle them. Disposition of UAA letters and flats, however, clearly costs less than the disposition of UAA parcels and NFMs. The former on average weigh less, are less bulky, and can be processed and transported more quickly and cheaply. The inclusion of parcels and NFMs in the calculation, therefore, artificially inflates the average cost of UAA mail in this spreadsheet. It is likely that the average cost to the Postal Service of UAA Standard Mail letters and flats—the only shapes subject to the PBV assessment—is significantly less

than 5.2 cents. The seven-cent penalty, therefore, is even further out of step with the Postal Service's costs than the supporting materials suggest.³

B. Seven Cents Not Justified For Deterrence.

A penalty that does not exactly track costs could conceivably be justified as a means of deterring Move Update violations. But the particular penalty proposed by the Postal Service cannot be supported on such grounds, primarily because the Postal Service has offered no evidence whatsoever that the adoption of the penalty will substantially reduce the percentage of First-Class and Standard mail that actually violates Move Update.

The Postal Service confirms that it intends to retain the right to assess after-the-fact revenue deficiencies against mailings that violate Move Update requirements *in addition to* MERLIN/PBV "assessments" at the point of acceptance. *See* Postal Service Response to CIR 1, Question 5. But the Postal Service also asserts, for the first time, that the seven-cent surcharge is applicable *only* to mail that fails the PBV process, and that the default rate for computing after-the-fact revenue deficiencies will be the single-piece First-Class mail rate. As a result, the potential exposure for after-the-fact revenue deficiencies is considerably larger than potential exposure to a seven-cent penalty at acceptance. *See* Follow-up Materials Related to November 12, 2009 Technical Conference at 2 (explaining that the seven-cent penalty would be credited against any assessed revenue deficiency, thereby implying that revenue deficiencies based on the same Move Update failures would be substantially greater than the seven-cent PBV

³ The 5.2 cent cost estimate is even further from the mark if, as appears possible, flat-shaped mail will not be tested at many facilities. The Postal Service has taken inconsistent positions on whether flats can be processed on MERLIN.

assessment). As mailers are already subject to significant penalties for violations of Move Update requirements, the notion that the PBV assessment will provide a significant additional incentive is both unproven and implausible.⁴

Furthermore, there is also indication that the pass-fail standards in the full audits will be different than the standards which apparently will apply to PBV. In other words, mailpieces that failed the PBV test at acceptance may be found during an after-the-fact audit to have satisfied the Move Update requirements after all. This disparate application of two tests makes the justification for the seven-cent surcharge even more untenable. Deterrence cannot be accomplished by such an incoherent and inconsistent regime. Unless mailers clearly understand what they must do to avoid the seven-cent penalty, they cannot be effectively deterred.

Finally, the Postal Service indicated at the Technical Conference that the seven-cent penalty could be refunded if a mailer could demonstrate that it was in fact complying with Move Update procedures. The only way to effectively appeal a Move Update assessment is to invite a full audit, because it is only in a full audit that a mailer can show that it rejects family moves and obtains addresses directly from consumers. *See* “Additional Item of Follow-Up material Related to November 12, 2009 Technical Conference” (filed Nov. 16, 2009) (attachment summarizing documentation that mailer would need to supply). But defending Move Update compliance on an address-by-address basis is exceedingly costly and time-consuming. Neither mailers nor the Postal Service have the time or personnel to engage in such audits except in extraordinary cases. Hence, the PBV assessment provides no more incentive to comply with Move Update

⁴ Capping the sum of the original postage plus the seven cent penalty at the single-piece rate also injects a serious element of discrimination into the penalty scheme.

than the possibility of an audit. Even if a mailer is worried about incurring the assessment, it knows the ultimate test is whether it can justify its practices in a Move Update audit. The mailer has no incentive to take additional steps to comply with the specific PBV standards; it will rely on the Move Update standards it already has in place.⁵

IV. THE POSTAL SERVICE’S RESERVATION OF THE RIGHT TO MAKE UNILATERAL CHANGES IN THE RULES WOULD USURP THE COMMISSION’S REGULATORY AUTHORITY.

Rather than establishing definite standards for the assessment of Move Update penalties, as the Commission expressly requested in Question 4 of the CIR, the Postal Service proposed new, equally hollow, MCS language. Under the revised language, the codified standard for assessing the Move Update penalty at acceptance would be to “Add \$0.07 per assessed piece, for mailings that fail a Performance Based Verification at acceptance.” Because there are no published guidelines setting forth what a mailer must do to comply with Move Update, Postal Service has effectively defined “failure” broadly enough to change other conditions for penalty in virtually any way it chooses. *See* Postal Service Response to CIR 1, Question 4(a).

In addition, the Postal Service has confirmed that it reserves the right to reduce the 30 percent tolerance level “as necessary to ensure that address quality improves” unilaterally, without further Commission review. *See* Postal Service Response to CIR 1, Question 6. As PostCom *et al.* argued in their November 4 comments, allowing the Postal Service to retain this much discretion would abdicate the Commission’s oversight

⁵ This lack of incentive highlights the absurdity in establishing different standards for compliance in the audit process and PBV.

authority over rate and classification changes. Reductions in the tolerance level would effectively imposing new rates on a substantial number of mailers.⁶ If the Postal Service could do this without filing the change in threshold (or other rule) with the Commission, then the Commission could not longer ensure that the rates remained just, reasonable, and nondiscriminatory. Delegating such authority to the Postal Service thus would subvert the oversight authority that the PAEA has delegated to this Commission. *See* Comments of PostCom *et al.* at 30-33.

⁶ These are not just theoretical concerns. Senior Postal Service operational officials have indicated that the tolerance level for the readability of IMb barcodes by MERLIN, originally set at 70 percent, will increase to 80 percent on November 30, and increase further 90 percent in the not-to-distant future.

CONCLUSION

For the foregoing reasons the Commission should reject the Postal Service's notice as unsupported, without prejudice, and require the filing of a better supported proposal. The Commission should make clear, however, that a resubmitted proposal should include standards that are sufficiently specified to put mailers and the Commission on notice of (1) all material Move Update requirements, (2) the rules the Postal Service intends to apply in the Move Update verification process, and (3) the revenue effect of the proposal in light of those requirements and rules.

Respectfully submitted,

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