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

Annual Compliance Report, 2009) Docket No. ACR2009

REPLY COMMENTS
OF
AMERICAN BUSINESS MEDIA
(February 16, 2010)

Pursuant to Order No. 380, American Business Media hereby submits these Reply Comments in response to the initial comments of Valpak.

Valpak once again argues that Periodicals rates are unlawfully low and that the Commission must step in to "move the class toward compliance with 39 U.S.C. section 3622(c)(2) over an established period of time." Valpak comments at 17-18. Initial comments filed in this docket by ABM and Time Warner, Inc., showed, once again, that Valpak errs in elevating the attributable cost coverage objective over the statutory price cap, although Valpak appears to be backing away, albeit slowly, from its earlier, more adamant contentions in this regard.

Yet Valpak has not backed away from the assertions made in Docket No. ACR2008 that the Commission should order the Postal Service to direct that Periodicals rates should be reconfigured to change "price signals," an action, Valpak again claims (at 15), could reduce losses greatly within the Periodicals class. Valpak bases its proposal on the proposition—totally unsupported in its comments—that "it appears that the Postal Service earns a profit on many periodicals while losing substantial amounts on others."

As ABM explained in its initial comments in this docket, and as shown in great detail in Time Warner's initial comments, the increasing gap between Periodicals revenues and alleged attributable costs is explained largely by Postal Service failures to respond appropriately to decreasing flats volume and to process on machines many Periodicals that are indeed machinable. No "price signals" will solve these problems. If a finely presorted, machinable piece of Periodicals mail in a large palletized bundle is sorted by hand, no change in price signals will reduce the loss on that piece.

In addition, if the Commission were to follow Valpak's suggestion and direct the Postal Service to impose future rate increases only or primarily on high cost/low revenue copies of publications (assuming that they could be identified and the Postal Service could do so), and if all affected publications pay those much higher rates, because of the price cap, costs and revenues for the class would be precisely the same as those produced by a more balanced approach that considers not only cost incurrence but impact on mailers. Any revenue gap will remain.

Valpak recognized in Docket No. ACR2008 that this scenario of mostly smaller publications paying much higher rates would not play out that way. As it stated there (Initial Comments at 13), an alternative is that many publications would be forced to cease publication altogether, and the Postal Service would benefit from the decline in "money-losing volume."

ABM's response in Docket No. ACR2008 bears repeating here:

> We suppose that Valpak would applaud the disappearance of what must be thousands of small, "money losing" publications as a means of eliminating a portion of the Periodicals revenue shortfall. As a purveyor of pure advertising material, Valpak appears not to understand the special importance of the editorial content of Periodicals and the longstanding Congressional, PRC and Postal Service recognition of the need maintain

> a broad and diverse Periodical mailstream. As American Business Media stated in Docket No. ACR2007, what Val Pak proposes is analogous to amputating an infected limb rather than administering antibiotics. We doubt that Congress sought to require this result when it passed the PAEA.

Valpak's discussion of price signals suggests that a change in pricing could produce a change in mailer worksharing behavior that, in turn, could reduce costs more than revenues, although such changes in recent years do not appear to have had that effect.

Thus there are three theoretical reactions by Periodicals that under Valpak's proposal would bear all or most of future increases designed to promote "efficiency." All of these would be likely to occur in some unknown ratio: (1) mailers could pay the new rates (despite the burden), (2) they could change their mailing practices or (3) they could cease publication. In the first of these scenarios, the principle Valpak espouses would not be advanced, because, as shown above, the coverage would remain the same. In the second, it is possible in theory that the revenue/cost gap would be diminished, although there is good reason to believe that the impact would be minimal (as discussed immediately below). In the third, the gap might be narrowed, but the Periodicals class and the American people would be irreparably injured.

We have addressed the first and third of these possibilities. The second—a possible change in mailer behavior—deserves additional scrutiny. American Business Media has never contended that the manner in which Periodicals mailers prepare and present their mail is unaffected by the combined printer and Postal Service prices they face, but it has contended—and continues to contend—that there are practical limits to the speed with which and the degree to which mailers may change.[1]

There comes a point when existing incentives are sufficient to promote changes at or close to the theoretical limit to changes in mailer behavior. We are just about at that point. The Periodicals industry is facing unprecedented financial challenges, such that publishers would not out of arrogance, ignorance or stubbornness continue to mail in sacks if they could mail on pallets and would not refuse to participate in available co-mail programs on philosophical or other grounds. Both palletization and co-mailing have increased in recent years because, when available, they save publishers money, and to some extent these practices ought to continue to increase without new "price signals." The oppressive rate increases recommended by the Commission and, unfortunately, accepted by the Governors of the Postal Service in R2006-1 made sure of that.

As a result, there has been a meaningful and steady decrease in those mailing practices that require the Postal Service to handle mail inefficiently and a steady increase in the amount of worksharing and co-mailing, which represents the epitome of changed mailer behavior that price signals are designed to induce. The amount of co-mailing will continue to increase, as printers add more high-cost capacity and develop better practices, but that increase does not depend on still stronger price signals and may be affected adversely by the financial challenges now faced by the printing industry. Unfortunately, however, the efficiency with which the Postal Service handles this mail has not increased commensurately with the changed mailer behavior.

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[1] For a thorough discussion of the impediments to such changes, see American Business Media's initial and reply briefs in Docket No, R2006-1 and ABM's comments in Docket No. ACR2008.

Although American Business Media firmly believes that pricing changes will do little to close the revenue gap, unless they drive many thousands of publications from the mail, it appears from the data offered to the Commission that the problem may not be as serious as first appears, as Time Warner shows in its initial comments. The solution lies in changes to Postal Service operating procedures, not in rates. Moreover, as ABM explained in its initial comments, the huge and inappropriate cost burdens imposed on all classes of mail by the overpayment of retiree health care costs, the overpayment of CSRS retirement costs, and the Commission's insistence that mail processing costs are 100% volume variable (and thus attributable) despite evidence and the Postal Service's own contrary views contribute substantially to the stated gap between Periodicals attributable costs and revenues.

While Valpak (at 16) disparages the as-yet unrevealed conclusions of the Joint Task Force created for the very purpose of analyzing Periodicals rates, revenues and costs and rejects sight unseen any findings that study may produce, ABM suggests that the work of the Task Force, along with the additional procedures announced by the Commission to address the Postal Service's financial crisis, will provide a framework for addressing Periodicals that is far superior to Valpak's unrelenting attack on a portion of the Periodicals class.

Respectfully submitted,

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