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Washington, DC 20268-0001

Annual Compliance Report, 2009 Docket No. ACR2009

REPLY COMMENTS OF THE GREETING CARD ASSOCIATION

I. INTRODUCTION

In these Reply Comments, GCA responds to the filings made on or about February 1, 2010, by the Public Representative and a number of industry participants, and to various contributions in the February 17, 2010, Public Forum. These comments often refer to, or repeat, assertions and arguments made earlier in this Docket or in other Dockets. GCA discussed many of these issues in our December 23, 2009, response to the Public Representative's motion and our February 5, 2010, initial Comments. To avoid repetition, we respectfully request the Commission to consider those documents as incorporated, where necessary, in this submission.

At the outset, we would emphasize that the Commission's assignment under § 3653 is to determine whether the rates in effect since May 2009 violate any provision of chapter 36 of PAEA or any regulation implementing that chapter. Many of the comments filed so far raise issues which, while interesting and important, are not necessarily, or even appropriately, decided in this compliance review. The belief, expressed in some of the comments, that current rates are not well designed does not amount to an assertion (much less a showing) that they are unlawful.[1] Since the arguments have been made, however, GCA will of necessity include in this filing its responses to them.

[1] While we strongly disagree with the Public Representative's proposal to remedy the deficit solely through rate increases, and with his legal arguments, he has properly observed the distinction between disliking a set of rates and being prepared to call them illegal.

In Part II, below, we discuss first the issues directly bearing on the legality of the 2009 rates. Part III takes up issues raised by other participants in this proceeding that are not necessarily part of the Commission's Annual Compliance Determination herein.

II. LAWFULNESS OF THE 2009 RATES

It seems helpful to sort the issues regarding the lawfulness of the existing set of Postal Service rates into three categories:

A. Those involving the adequacy of the Service's total revenue as judged by the standard of "financial stability" (39 U.S.C. § 3622(b)(5));

B. Those raised by the failure of some classes or products to recover their attributable costs (39 U.S.C. § 3622(c)(2)); and

C. Those concerning workshare discounts – in particular, whether, in given situations, the "cost avoided" rule of § 3622(e)(2) applies at all, or is mooted by applicability of one of the statutory exceptions, or is in fact being violated.

A. Overall revenue adequacy

1. The Public Representative has submitted detailed arguments and numerical examples seeking to show (i) that because of recent and expected Postal Service deficits, the existing rates violate § 3622(b)(5), and (ii) what rate changes would be necessary to cure the deficits. As GCA has previously pointed out[2], the

[2] Reply of the Greeting Card Association to Motion of the Public Representative for Production of Estimates of Rate Adjustments (December 23, 2009), pp. 2-9 ("GCA Reply"); and see GCA's Comments responding to Commission Information Request No. 1 (February 5, 2010) ("GCA CIR Comments").

Public Representative's position depends on a misreading of both subsection (b)(5) and of the factual situation causing the deficits. Briefly:

- The Postal Service's rates are not the only, nor the most significant, cause of the deficit. Exogenous financial burdens, either direct (e.g., the unrealistic prefunding schedule for retiree health benefits) or indirect (e.g., political interference with needed streamlining of the upstream network), are much more substantial problems, and are not cured by raising rates in the short run (such as FY 2010). Designing rate increases to cover the entire deficit – without regard to its multiple causes or to the predictable volume losses – is simply not a reasonable procedure.

- Section 3622(b)(5) is not dominant over the other objectives, "each of which," according to § 3622(b), "shall be applied in conjunction with the others[.]" The Public Representative has converted the undoubted importance of the deficit issue into an imaginary rule of law making "adequate revenues" the predominant rule of ratemaking.

- Section 3622(b)(5) aims at financial stability, which is not the same thing as "adequate revenues." Congress deliberately substituted the financial stability standard for the much stricter breakeven rule of former § 3621. That a deficit exists does not, therefore, mean that the rates responsible for the present level of revenues are unlawful. Moreover, as has been true in the past[3], restoration of financial stability – in light of the above-described reasons for instability – cannot be expected in a year or two.

The Public Representative's February 2 Comments largely repeat the (b)(5) arguments to which GCA replied in our two earlier filings, cited in fn. 2 above. We respectfully refer the Commission to those documents for detailed comment.

[3] Even, as we have pointed out, under the stringent breakeven rule of the 1970 Act. GCA CIR Comments, pp. 6-7.

2. The Public Representative now argues, in addition, that two provisions of PAEA, both dealing with the allocation of costs, provide independent grounds for the Commission to declare the existing rates unlawful.[4] Neither one does.

The two provisions are § 101(d):

> (d) Postal rates shall be established to apportion the costs of all postal operations to all users of the mail on a fair and equitable basis.

and § 3622(b)(9):

> (9) To allocate the total institutional costs of the Postal Service appropriately between market-dominant and competitive products.

The latter provision, like § 3622(b)(5), is one of the objectives to be achieved in setting up the PAEA system of ratemaking. As the Postal Service and others have pointed out, it does not apply directly to rates.[5] Section 101(d), however, is a global policy directive which presumably does bear directly on rates. We therefore deal with it first.

At the outset, we note that § 101(d) does not clearly fall within the scope of the Commission's remedial powers in the annual compliance process. Those powers rest on the results of the compliance review itself, in which the Commission is directed to

> . . . make a written determination as to –
>
> (1) whether any rates or fees in effect during such year (for products individually or collectively) were not in compliance with applicable provisions *of this chapter* (or regulations promulgated thereunder)[.]

[4] Public Representative Comments, pp. 11-12, 14.

[5] Response of the United States Postal Service to Commission Information Request No. 1, pp. 2-3; Initial Comments of Time Warner Inc. on ACR2009 Pursuant to Order No. 380, pp. 2 et seq.

(Italics added.) Section 3653, from which this quotation comes, is part of ch. 36; § 101(d), however, is part of ch. 1. The literal language of the Commission's compliance review charter, therefore, does not contemplate use of § 101(d) as grounds for remedial action.

More significantly, however, the Public Representative seems to misconstrue § 101(d) itself:

> The Postal Service has failed to comply with postal policy set forth in section 101(d) of the PAEA to apportion *all* operating costs to all users of the mail on a fair and equitable basis.[[6]]

But the statutory phrase "to apportion the costs of all postal operations" does not mean the same thing as "to apportion *all* operating costs." The Public Representative appears to take "costs of all postal operations" as meaning "all costs of postal operations," when in fact it need mean (and most obviously means[7]) only that no category of postal operating costs (such as city carrier time or vehicle service) was to be allocated otherwise than fairly and equitably. It should be recalled, in this connection, that present § 101(d) was re-enacted unchanged from its 1970 form. In the 1970 Act, the recovery of all costs was insured by § 3621.[8] Congress had no need to insist on full cost recovery through rates in the general policy sections, having done so in the contemporaneous ratemaking provisions. The independent force of § 101(d) seems rather to be that *whether or not full costs are recovered in fact,* there is to be no unfairness in the allocation of the costs which are recouped through rates.

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[6] Id., p. 14.

[7] There seems to be no reason why, if Congress had meant "all operating costs," it would not have used just those words.

[8] Which, as we pointed out in an earlier filing (GCA CIR Comments, pp. 6-7), seems to have incorporated a substantially stricter breakeven test than current § 3622(b)(5). It is also worth noting that for years after § 101(d) was written, the Postal Service did *not* recover all its operating costs from mail users. Public service appropriations, as authorized by § 2401(b)(1) as it then stood, continued until 1984.

Finally, of course, it is hard to see why a reasonable draftsman would express a full cost recovery requirement in terms of *allocation* of costs among users.

This last observation applies as well to the Public Representative's use of § 3622(b)(9). It is true that this provision speaks of allocating "*total* institutional costs." Its obvious thrust, however, is to require the Commission to create mechanisms to allocate those costs properly between the two broad sectors of traffic provided for (so far as rates are concerned) by §§ 3622 and 3633. Again, this is most straightforwardly read to mean that no subcategory of institutional costs was to be excluded from the market-dominant-vs.-competitive allocation process. Reading it, as the Public Representative apparently does, to mean also that every dollar of institutional cost must be (currently) recovered, as well as properly allocated, raises significant issues.

First, since the Public Representative's interpretation would amount to a full cost recovery mandate on an annual basis, we must again ask why Congress did not simply retain the language of former § 3621 – either as an absolute requirement or, at a minimum, as a § 3622(b) objective – rather than

- restricting it[9] to the "extraordinary and exceptional" circumstances of a § 3622(d)(1)(E) exigency case; and

- devising a looser "financial stability" standard for § 3622(b)(5).

Secondly, the practical consequences of reading § 3622(b)(9) as the Public Representative reads it tell against the correctness of that reading. For example, suppose that a set of rates, when implemented, fully meets the allocation requirement of subsection (b)(9). Later in the year, a sharp downturn in sys-

[9] Amended by adding the reference to "best practices," which does not seem to be material to the present issue.

temwide volume results in failure to recover all of the Service's institutional costs (i.e., an overall deficit). Nothing has changed as regards the allocation of institutional costs between competitive and market-dominant products, as embodied in the rates. On the Public Representative's view, however, the deficit would, without more, cause those rates, lawful when implemented, to violate § 3622(b)(9) retroactively.

There is an inherent logical problem in the Public Representative's effort to use cost allocation provisions as if they were full cost recovery mandates: these two aspects of postal finance depend on entirely different metrics. The (appropriate) allocation of costs can be, and often is, assessed by looking at unit costs and unit rates. In judging a set of rates under, e.g., § 101(d), it would be natural to use unit contribution figures. If product A contributes 10 cents/piece to institutional costs, we can compare that figure with product B's 0.1 cent/piece, in the course of evaluating the allocation of institutional costs. These unit statistics, however useful they are for examining cost allocations, are not designed to record or predict total revenue. They cannot tell us whether the Postal Service will recover less than, the exact amount of, or more than its total operating costs in a given year. Conversely, it is at least logically possible for the Service to recover all its costs under a rate schedule incorporating seriously flawed cost allocations.[10] This circumstance suggests strongly that Congress did not mean to convey, in either § 101(d) or § 3622(b)(9), the additional notion – related to the total revenue-cost balance – that rates in effect during a sustained deficit period are for that reason unlawful under one or both of those provisions. They address the quality of the cost allocations used in, or resulting from, the ratemaking process, and nothing more.

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[10] This is true not least because the appropriateness of cost allocation is itself partly a matter of statutory interpretation. For example, a decision on what mail classes Congress intended to benefit from "ECSI" consideration (former § 3622(b)(8), now § 3622(c)(11)) clearly affects institutional cost allocation, but would be most unlikely to affect the Service's ability to recover all its operating costs.

B. Availability of § 3653 remedies to correct "violations" of § 3622(b) or (c)

Some participants have questioned whether the Commission can use the broad remedial powers granted by § 3653(c) to correct an inconsistency between existing rates and an objective or factor listed in § 3622(b) or (c).[11] The answer to this question may vary depending on the type of problem perceived, but it can most usefully be introduced in the overall-deficiency context.

The argument against applicability of the § 3622 criteria rests on the basic proposition that the objectives and factors are directed to the Commission as instructions for the establishment of a "modern system for regulating rates and classes for market-dominant products,"[12] but not to the Postal Service as requirements to be observed in establishing rates. As a matter of syntax, this seems clearly true. That, however, does not end the matter.

Whether, in a § 3653 proceeding, the Commission may rely on an objective or factor in finding a rate or rates noncompliant seems to depend more on whether the § 3622 element not "complied with" lends itself to being incorporated in the "modern system" established pursuant to § 3622(a), and has been so incorporated.[13] For example, 39 CFR § 3010.14(b)(7) requires the Service to show how the rates proposed in an annual price-cap filing promote the objectives and take proper account of the factors. If the Service did not properly explain how a particular product's new rates took account of § 3622(c)(2) (attributable cost recovery and contribution to institutional cost), and the rates appeared

[11] See the filings cited in fn. 5 above. Others, including the Public Representative, treat at least some of these criteria as directly applicable.

[12] 39 U.S.C. § 3622(a).

[13] There are, of course, statutory mandates which do apply directly to rates: the most prominent example may be § 3622(e)(2), which instructs the Commission to "ensure" that worksharing discounts not falling under a stated exception do not exceed avoided cost. Such direct commands are not relevant to this discussion, even though noncompliance with them would be an appropriate issue in a § 3653 proceeding.

in the relevant compliance review to have yielded less than attributable cost, the Commission might well be on firm ground in requiring corrective action: the cost recovery factor was incorporated in the ratemaking system as a result of the (rulemaking) judgment that below-cost rates were generally not acceptable.[14]

This is true in the example above because – most likely, *only* because – the problem exists entirely *within* the structure of rates established by the Service's filing: it has been created by rates that, for whatever reason, were set too low to recover attributable costs.[15] This is why the blanket inclusion in Rule 3010.14(b)(7) of all the § 3622 objectives and factors does not justify a similar approach to the current overall revenue deficiency, in reliance on the "adequate revenues" term of § 3622(b)(5). First, the global deficiency problem, as we pointed out in earlier filings, is *not* inherently or even predominantly one caused by an error in setting rates. Besides, "adequate revenues," in subsection (b)(5) is logically subordinate to "financial stability," and thus does not amount to a breakeven requirement which any one year's rates could be said to violate.

C. Classes or products which fail to recover attributable costs

Some participants[16] raise the question whether – leaving aside the possible across-the-board use of § 3622(b)(5) as advocated by the Public Representative – the fact that some classes or products recover less than attributable cost requires the Commission to raise their rates as a deficit-correction measure. The preceding section of these comments, and particularly the example on pp. 8-9,

[14] Section 3010.14(b) is of course a regulation promulgated under ch. 36, for purposes of 39 U.S.C. § 3653(b)(1), so that noncompliance with it would ground a remedy. Whether it would be productive to raise the rates to attributable-cost recovery level in one fell swoop is of course a different question.

[15] Including, of course, the cases in which those costs were misestimated at the outset or increased unforeseeably during the rate cycle.

[16] Valpak and Time Warner, in particular, have furnished detailed presentations on this set of issues. Initial Comments of Time Warner Inc. on ACR2009 Pursuant to Order No. 380, pp. 4 et seq.

suggest that the attributable-cost recovery factor of § 3622(c)(2), incorporated in Rule 3010.14(b)(7), might prompt such an action in any case. GCA, accordingly, does not think it is necessary to speculate at length on the relationship between the *overall* deficit and the classes or products which currently do not cover attributable cost.[17] The deficit is, in any case, substantially greater than could be cured by repricing all these classes and products to cost-recovery levels (even assuming no resulting volume losses).

The more pressing issue in this connection is the relationship between § 3622(c)(2) and the price cap. At various times, commenters have argued that the price cap controls even when, as a matter of arithmetic, observing it would prevent the rates from being raised to attributable-cost recovery levels.[18] This argument rests largely on the demotion of the attributable-cost recovery standard to a factor to be taken into account in setting up the modern system of regulation; the price cap, on the other hand, is styled a "requirement" for that system.[19] Time Warner, for example, relies on James I. Campbell's interpretative paper[20] for the proposition that only a § 3622(d)(1)(E) exigency case or invocation of the banking provisions can justify imposition of above-the-cap rates.

As far as the normal Postal Service-initiated rate change is concerned, this may well be true. The broader question is whether the same standards apply when the issue is whether the Service has complied with the provisions of ch. 36 and with regulations adopted by the Commission under it. Suppose, for ex-

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[17] However, the distinction drawn above between problems existing entirely within a given structure of rates and those caused in major part by exogenous factors (and so not clearly soluble by tinkering with rates) is relevant here too.

[18] Valpak and the Public Representative espoused the opposite view in Docket ACR 2008. In this Docket, see Public Representative Comments on Annual Compliance Report 2009, pp. 33-36; and, for the contrary view that the cap controls, Time Warner Initial Comments, pp. 4-11.

[19] Section 3622(d), which includes instructions for establishing the price cap mechanism, is entitled "Requirements."

[20] Time Warner Initial Comments, p. 5.

ample, that a substantial[21] deficit is demonstrably due to the Service's failure to establish rates sufficient to recover costs – that is, *not* due to exogenous problems not curable by raising rates. The Commission's remedial powers under § 3653(c) are those available under § 3662(c), which, significantly, include "ordering unlawful rates to be adjusted to lawful levels[.]" The Commission could use that authority to order the Service to file an exigency case aimed at recovering all its costs. Even under the standard enunciated in the Campbell paper, therefore, the Commission seemingly could call for rate increases that would, or at least could, exceed the price cap.[22]

D. <u>Worksharing discount problems</u>

Section 3622(e) sets out a general standard for worksharing discounts, along with several exceptions. The Commission is directly instructed to "ensure" that, save when an exception applies, such discounts do not exceed the cost avoided by the worksharing. Thus the question considered in the preceding section does not arise with regard to worksharing rates.

The central issue, however, so far as First Class is concerned, is whether the Bulk Metered Mail benchmark, which the Postal Service has abandoned in recent rate adjustments[23], is to remain the governing legal standard. Docket RM2009-3 was established to settle this question. While GCA has advocated retention of the BMM benchmark and criticized the statutory argument the Postal Service advances to justify delinking of the First-Class letter products, we also

[21] More specifically: too large to be curable by rate increases equal to or less than the price cap.

[22] Whether such action would be feasible in every case would depend on the relationship between the "underwater" classes or products and the Postal Service's overall financial situation. An exigency increase is permissible only if "reasonable and equitable and necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States." 39 U.S.C. § 3622(d)(1)(E).

[23] The history is usefully summarized in the Initial Comments of American Postal Workers Union, AFL-CIO, pp. 2-4.

believe – for reasons of orderly administration, if nothing more – that Docket RM2009-3 is the proper forum for a decision on this question. Underlying the BMM benchmark question, as presented by the Postal Service's actions, is the methodological issue of whether Presort rates are still to be regarded as work-sharing discounts. The Service's position logically requires that they not be.[24] If that position were accepted, it would, as the Service points out, mean that § 3622(e) has no bearing on the matter. It seems evident that an annual compliance review is not a suitable forum for questions of this kind, if only because it is aimed at uncovering and correcting instances of actual noncompliance with the statute. While GCA agrees with most of the substance of APWU's criticisms of the present Presort rates, we believe that the question should be dealt with, as the Commission originally intended, in Docket RM2009-3.

This, however, is not the end of the matter. As we explain in section B of the next Part, existing Presort rates are lower than they would be under efficient pricing *even if delinking were accepted.* That this is not an abstract matter of theory is suggested, first, by the Postal Service's pressing need for more revenue[25], as well as by the directive expressed in § 3622(b)(1): that the modern system of regulation "maximize incentives to reduce costs and increase efficiency." Needlessly low Presort rates serve neither to lower costs nor to increase efficiency.

III. ISSUES OF RATE POLICY AND RATE DESIGN

This section of our Reply Comments focuses on the comments made on February 1, 2010 by Pitney Bowes (PB) and February 2 by the Public Representative. We also reference certain comments made by DMA (and others) in

[24] See Docket RM2009-3, Initial Comments of the United States Postal Service, particularly pp. 14 et seq. As we have noted, this position rests on a reading of the statute which GCA considers untenable. See Docket RM2009-3, Initial Comments of the Greeting Card Association, pp. 1-7.

[25] Or, more specifically, not to forego revenue which it could collect without depressing volume.

RM2009-3, as the DMA comments from that case are referenced in the PB comments in the instant case.[26]

A. Issues concerning institutional cost contribution, elasticity measurement, and efficient worksharing rates

1. *Relative contributions to institutional cost*. In this case PB has reiterated a point it and others[27] have also made more than once in RM2009-3; namely, that the unit contribution of First Class Presort letters to Postal Service institutional costs exceeds that of First Class Single Piece letters. PB then argues that the reason Presort contributions are "high" is because Single Piece contributions are "low". As a remedy, PB quotes DMA's call in RM2009-3[28] for an increase in Single Piece rates. There are two points to be made in this regard.

a. First, it is not appropriate to compare the cost coverage that the individual consumer or general public pays for Single Piece postage with *just* the Presort cost coverage large bulk mailers pay, as many or most of these mailers also send large volumes of Standard Mail advertising letters along with Presort letters. Such a comparison may seem natural as long as one focuses exclusively on unit rates and unit contributions. However, from a broader perspective – that of customer class compared with customer class – it is not hard to see the fallacy involved. Comparing the *overall* cost coverage of the consumer and large bulk mailers sending First Class, the differences are much smaller than PB alleges (or non-existent) because of the much lower unit cost contributions of the Standard Mail also sent by those bulk mailers.

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[26] Docket ACR2009, Comments of Pitney Bowes, February 1, 2010, p 1; Docket RM2009-3, Comments of Direct Marketing Association, September 11, 2009, p. 4 (referenced as pp. 5-6 in Pitney Bowes Comments.); RM2009-3, Comments of Pitney Bowes,

[27] See, for example, RM2009-3, Comments of Pitney Bowes, September 11, 2009, pp. 9-10..

[28] See Docket RM2009-3, Comments of the Direct Marketing Association, September 11, 2009, especially p. 4 et seq. See also, in that docket, Comments of the National Postal Policy Council on Order No. 243, p. 28.

Another way to visualize the fallacy in PB's argument is to recognize that, while letter mail is organized under discrete class or product definitions, mailers are not. The economic impact on a given bulk mailer (e.g., a large financial institution) is best seen by assessing the average cost of a piece of its letter mail – regardless of MCS designation – rather than by notionally splitting the company into a "First-Class Presort mailer" and a "Standard mailer." From the standpoint of a just and reasonable rate schedule (39 U.S.C. § 3622(b)(8)), this overall-impact criterion is thus more useful. This is particularly true where two mail products are alternatives (e.g., a bulk mail user wishing to advertise a product or service may use either First Class or Standard, depending on the balance between cost/piece and promotional effectiveness). Household mailers, of course, do not have such choices within the postal system; their only letter-mail alternative is the Internet.[29] We suggest that when, as here, the key issue is the overall financial viability of the Postal Service, it is more appropriate to look at the large-scale effects of rates on discrete customer classes (and their likely reactions thereto) than to parse unit rates and cost coverages.

For example, using the weighted average volumes of the largest financial institutions from publicly available survey data in **Table 1**, the recent unit contributions that consumers paid for Single Piece letter postage was 18 cents, while the weighted average unit contribution the largest banks paid for bulk letter mail

[29] It should also be borne in mind that equality of per-piece contribution, while it has an equitable dimension, is also *in appropriate circumstances* an efficiency concern. Where the conditions for efficient component pricing exist (which may no longer be the case in First Class), equal per-piece contributions are an outcome of pricing the non-monopoly subservices at levels which leave the incumbent indifferent as to who provides them. The commenters who point to the current inequality of contribution within First Class, however, also advocate recognition of the complete separateness of Presort and Single-Piece. If that view were accepted, it would mean that Presort was *not* a workshared version of Single-Piece within a single letter-mail market – making equality of contribution as between Single-Piece and Presort pieces irrelevant. The same comment applies, of course, to the Postal Service's insistence that Mixed AADC Presort Letters are not Single-Piece or even Bulk Metered Letters minus a few unwanted subservices, but an independent product with an individualized cost basis. (It should also be pointed out that MAADC Letters constitute an extraordinarily small volume on which to expect to construct a credible measured cost.) It would also mean that the related "equity" argument – i.e., that Single-Piece receives a "preference" (see Docket RM2009-3, Comments of National Postal Policy Council, p. 3) – must be subjected to analysis under the normal rule that undue discrimination is an issue as between *similarly situated* customer classes. We suggest that it would not survive that analysis.

was 18.6 cents.[30] It is a legitimate question in the current economic and finance environment, when we focus on the long-run economic stability of the Postal Service, whether financial institutions generally are paying their fair share[31] of postal institutional costs when they have benefited disproportionately from the growth in customers, revenue and profit that postal services have created for those institutions.

Table 1
Large Bulk Mailers Pay the Same Institutional Costs as the Consumer

	2005 Volumes	Weights	Individual Consumer Contributions	Weighted Average of Large Banks' Contributions
Single Piece Mail			0.180	
Workshared Mail	7,837,075	70.9%	0.229	0.1624
Standard Mail	3,216,491	29.1%	0.080	0.0233
Total	11,053,566			0.1860

Source: Banks' mail volumes from ABA, Postal Operations Survey Report, October 2006.
Individual Contribution data from ACR 2009 (Cost and Revenue Analysis).

b. The second point is that First Class letter mail contributions generally are high today because Standard Mail letter contributions are low, *not* because Single Piece letter mail contributions are too low. This point is made abundantly

[30] Weights of First Class letter mail volumes for First Class and Standard are from the ABA Postal Survey, 2006, p. 15
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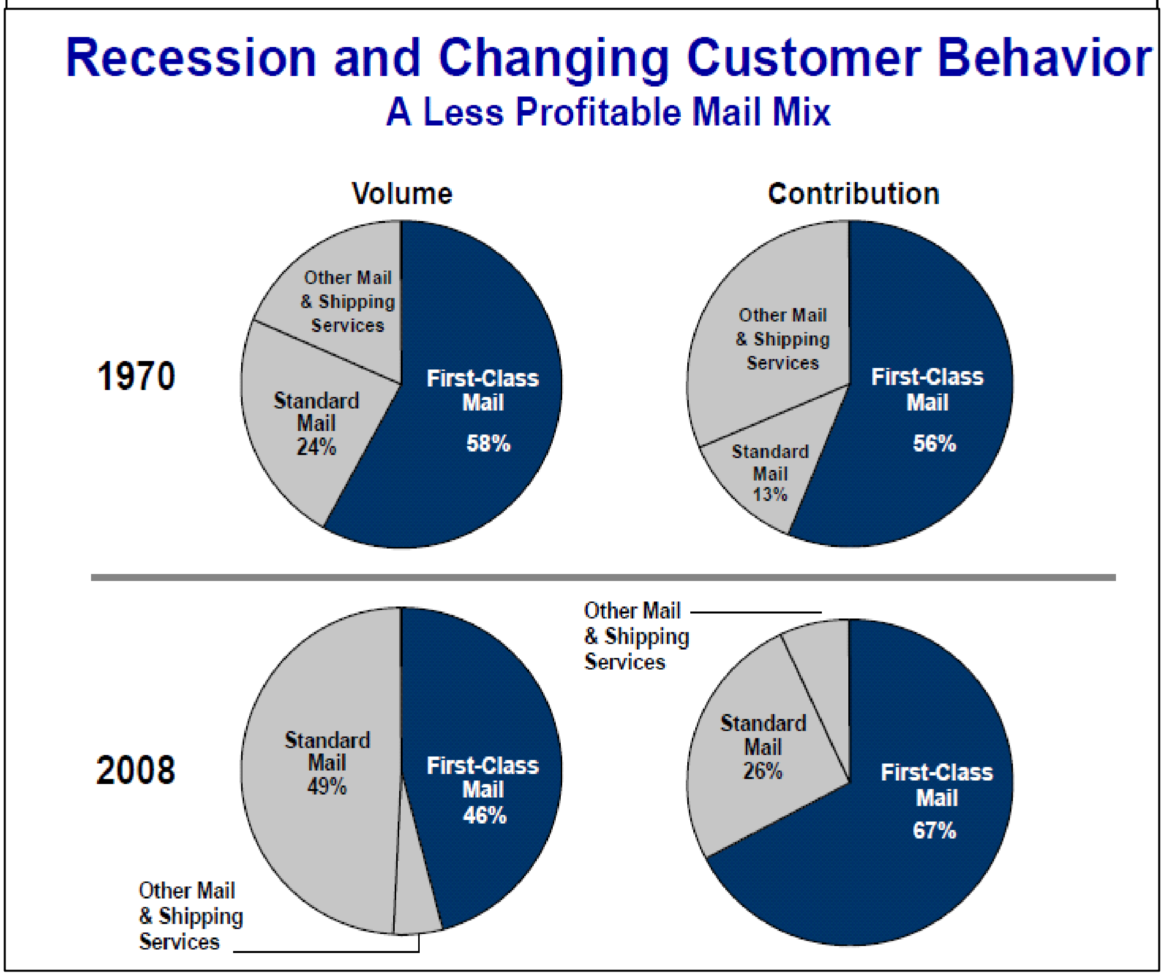
[31] Or, if one prefers, a share which would do substantially more to sustain a viable postal system than it would detract from the welfare of the mailers in question.

clear from a recent Postal Service set of pie charts, “Recession and Changing Customer Behavior.”[32] The pie charts in **Figure 1** examine the changing mix of letter mail volumes and the accompanying changes in contributions between 1970 and 2008.

Figure 1



In 1970, First Class Mail was 58% of total Postal Service volume and made 56% of the total contribution to institutional costs. By 2008 First Class Mail had fallen to 46% of total volume, yet was called upon in the ensuing rate struc-

[32] U.S. Postal Service, “A New Business Model for the United States Postal Service”, Presentation to APWU by Mary Ann Gibbons and Linda Kingsley, November 20, 2009, p. 12.

tures to support a much higher level of contribution than the 56% share it provided in 1970. By 2008, First Class Mail was paying 67% of the Service's total contribution, completely out of proportion (by 1970 standards) to its 46% share of postal volumes.

By way of contrast, Standard Mail's percentage of total Postal Service volume more than doubled between 1970 and 2008, to 49%, while Standard Mail's contribution on that volume in 2008 was only 26% of total institutional costs, well under half that of First Class.[33] The change in First Class Mail volumes over those four decades was small compared to the explosive growth of Standard letter mail. If Standard Mail's contribution reflected its volume growth, the contribution First Class Mail makes would be a lower percentage of total institutional costs than it was in 1970, not a higher one. The Presort contribution in particular would be lower than it is.

Here again, focusing on unit rates and coverages is misleading. Large bulk mail organizations producing substantial volumes of both Presort and Standard Mail may complain about Presort's "high" contribution, but when the overall impact of mail usage on such organizations is examined it is apparent that – in contribution terms – they are enjoying a bargain on their Standard Mail. The remedy is not to load more institutional costs on the general public – which, as noted above, has no alternative but to leave the postal system altogether – but to raise the contribution from Standard Mail if the chosen objective is to reduce it for Presort.

2. *Demand elasticity estimates.* In their early February comments in ACR2009, both Pitney Bowes and the Public Representative note the new demand data presented to the Commission by the Postal Service on January 20, 2010. In particular, PB highlights the fact that the new demand data shows Pre-

[33] While other mail and shipping services had a smaller percentage contribution in 2008 than it did in 1970, unlike Standard Mail its percentage of total volume also fell between those years.

sort is far more "price sensitive" than Single Piece.[34] Both participants, however, accept the new demand data without question. A closer look suggests that a number of questions badly need answering.

The following chart, **Table 2**, puts the Presort elasticity issue in its proper perspective. It shows that the Postal Service's own price elasticities for Single Piece and Presort were relatively close in R2006-1 and the first two annual compliance reviews. While the Postal Service has sought to "de-link" Presort from Single Piece letter mail from R2006-1 on, through ACR2008, it has not been able to demonstrate that Presort and Single Piece demand elasticities are sufficiently different as to constitute evidence, on the demand side, that they are two distinct products. In this case, however, it has almost doubled the Presort elasticity it calculated for the first two annual compliance reviews while slightly reducing the elasticity for Single Piece.

Table 2

Postal Mail Volume Elasticities Over R2006-1 to ACR2009

	Own Price Elasticity			
	R2006-1	ACR2007	ACR2008	ACR2009
Single Piece	-0.184	-0.232	-0.218	-0.192
Work Shared	-0.130	-0.246	-0.250	-0.436
Standard Regular	-0.296	-0.368	-0.311	-0.244
Standard ECR	-1.079	-0.711	-0.911	-0.839

Sources:

R2006-1 data from USPS, R2006-1, LR-L-64.exe, file, LR-L-64.doc.

ACR2007 data from USPS, Letter from R. Andrew German to Steven W. Williams Regarding Demand Analysis Material, Periodic Reports/Data Reports, filed on, 1/16/2008, file, MD.Demand.EquationTables.doc.

ACR2008 data from USPS, United States Postal Service FY 2008 Demand Analysis Materials Market Dominant, Periodic Reports/Data Reports, filed on 1/16/2009, Market_Dominant.zip, file, DemandEquationTables.doc.

ACR2009 data from USPS, Market Dominant Demand Analysis Materials in Response to Rule 3050.26, Periodic Reports/Data Reports, filed on 1/20/2010, Market_Dominant.zip, file, DemandEquationTables(md).doc.

[34] ACR 2009, Comments of Pitney Bowes Inc. February 1, 2010, p. 1.

However, the spike in the Presort elasticity is not based on using the same demand equation methodology as that used in the first two ACRs'. Indeed, so many changes were made in the demand side models for ACR2009 that a separate 13-page document accompanies the Postal Service filing entitled "Changes to Econometric Demand Equations for Market Dominant Products since January, 2009".

There are three points to be made: (1) a number of the changes made in the Presort equation have no clearly apparent function other than raising the elasticity; (2) the sheer discontinuity between previous Presort elasticity calculations and the new one calls the results into question; and (3) as demand side factors, and not just cost factors, influence rates and revenues, under Section 3652 (a) (1), all Postal Service or Postal Service sponsored work on demand equations should be subject to the same scrutiny and approval by the Commission as part of the annual compliance review process under PAEA as the cost calculations now are.

First, with respect to the change in the Presort own price elasticity, the largest single explanation is the inclusion of a "lag 4" variable that has not been employed in the first two annual compliance reviews. Yet, the lag 4 variable is not even discussed in the body of the13-page explanation of changes to the econometric demand equations.[35] The inclusion of a lag 4 variable explains 75 percent of the change in Presort elasticity between the 2008ACR and the 2009ACR, from – 0.250 to – 0.436.

Table 3 is a summary of the demand equation variables used for Presort since the R2006-1 rate case. It enables us to trace what has happened to the values of demand side variables which, when added, constitute the own price elasticity. The lag 4 variable was last used in R2006-1 and "explained" the entire long run own price elasticity of -0.1299. The "current" elasticity variable and the

[35] It is mentioned in a footnote that seeks to explain why it is not a "change" in methodology.

first three lags were all zero. Most of the modeling done in the first two annual compliance reviews resulted in non-zero values for the current and first three lag variables. For example, the current variable was estimated at – 0.116 in ACR2007, but only – 0.025 in ACR2008.

Table 3

ECONOMETRIC DEMAND EQUATIONS FOR FIRST-CLASS WORKSHARED LETTERS OVER 2006-2009

ACR2009			ACR2008			ACR2007			R2006-1		
	Coefficient	T-Statistic		Coefficient	T-Statistic		Coefficient	T-Statistic		Coefficient	T-Statistic
									Constant	-0.7563	-3.4105
Own-Price Elasticity			Own-Price Elasticity			Own-Price Elasticity			Own-Price Elasticity		
Long-Run	-0.436	-5.395	Long-Run	-0.25	-3.325	Long-Run	-0.246	-3.855	Long-Run	-0.1299	-2.201
Current	-0.129	-1.284	Current	-0.025	-0.365	Current	-0.116	-3.542	Current	0.000	0.000
Lag 1	-0.004	-0.032	Lag 1	-0.088	-2.259	Lag 1	-0.077	-3.75	Lag 1	0.000	0.000
Lag 2	-0.154	-1.174	Lag 2	-0.097	-2.503	Lag 2	-0.04	-2.681	Lag 2	0.000	0.000
Lag 3	-0.01	-0.08	Lag 3	-0.039	-1.053	Lag 3	-0.013	-1.284	Lag 3	0.000	0.000
Lag 4	-0.139	-1.343							Lag 4	-0.1299	-2.201
Cyclical Employment (lag 2 quarters)	1.132	7.954	Avg. First-Class Worksharing Discount	0.096	21.73	Avg. First-Class Worksharing Discount	0.134	39.88	D1_3WS_FIT	0.098	9.867
Logistic Time Trend	0.186	21.05	Avg. Standard Regular Letters Discount	-0.079	-1.885	Avg. Standard Regular Letters Discount	-0.055	-1.672	D3R_NCR_L	-0.111	-3.359
Number of Broadband subscribers			(relative to First-Class)			(relative to First-Class)					
* EMPL_TN_L	-11.26	-18.74	Employment	0.731	6.143	Employment	0.424	5.606	STR	0.534	5.398
			Number of Broadband subscribers			Number of Broadband subscribers (since	-0.441	-14.28	BROADBAND(-4)	-0.085	-0.124
			Constant since 2002Q4	-0.218	-2.184				BROADBAND4_D02	-2.113	-3.368
			Trend since 2002Q4	-0.008	-2.248						
Dummy Variables			Non-Linear Intervention: MC95-1			Non-Linear Intervention: MC95-1 (1996Q4)			Dummy Variables		
Fall, Election Years	0.007	1.34	$\omega_0 \cdot P_t + \omega_1 \cdot (P_t+\delta P_{t-1}+\delta^2 P_{t-2}+\delta^3 P_{t-}$			$\omega_0 \cdot P_t + \omega_1 \cdot (P_t+\delta P_{t-1}+\delta^2 P_{t-2}+\delta^3 P_{t-3}+\ldots)+$			MSADJ	-0.055	-6.144
MC95-1 (1996Q4)	-0.072	-7.956	ω_0: Pulse Value	-0.051	-3.472	ω_0: Pulse Value	-0.061	-3.251	MC95	-0.056	-8.005
2009Q4	0.019	1.342	ω_1: Pulse Value, lagged one quarter	-0.068	-7.73	ω_1: Pulse Value, lagged one quarter	-0.071	-6.427			
			ω_2: Long-Run Step Value	0	--	ω_2: Long-Run Step Value	0	--			
			δ: Rate of Adoption	0.987	72.94	δ: Rate of Adoption	0.993	84.54			
Seasonal Coefficients			Seasonal Coefficients			Seasonal Coefficients			Seasonal Coefficients		
Gregorian Time Periods			Gregorian Time Periods			Gregorian Time Periods			Gregorian Time Periods		
September	0.342	1.482	September	0.232	1.504	September	0.012	0.095	SEPT	0.317	1.478
October	-0.309	-1.478	October	-0.249	-1.496	October	-0.156	-1.119	OCT	0.317	1.478
November 1 – December 10	0.378	2.541	November 1 – December 10	0.375	2.895	November 1 – December 10	0.326	3.003	NOV1_DEC10	0.317	1.478
December 11 – 17	0.662	0.993	December 11 – 17	0.934	3.897	December 11 – 17	0.599	2.917	DEC11_17	0.619	2.874
December 18 – 31	-0.419	-0.548	December 18 – 31	-0.983	-1.61	December 18 – 31	-0.906	-1.748	DEC18_31	0.619	2.874
January – March	0.232	1.426	January – March	0.333	2.409	January – March	0.315	2.69	JAN_FEB	0.283	1.318
April 1 – 15	-0.563	-1.363	April 1 – 15	-0.804	-1.884	April 1 – 15	-0.603	-1.675	MARCH	0.283	1.318
April 16 – May	0.232	1.978	April 16 – May	0.203	1.734	April 16 – May	0.067	0.681	APR_MAY	0.283	1.318
									JUNE	0.718	1.106
-			-			-					
Gregorian Quarters, 2000 – ff.			Gregorian Quarters, 2000 – ff.			Gregorian Quarters, 2000 – ff.			Gregorian Quarters, 2000 – ff		
Quarter 1 (October – December)	0.071	0.605	Quarter 1 (October – December)	0.136	1.4	Quarter 1 (October – December)	0.113	1.382	GQTR1	-0.062	-13.741
Quarter 2 (January – March)	-0.071	-0.478	Quarter 2 (January – March)	-0.195	-1.647	Quarter 2 (January – March)	-0.213	-2.114	GQTR2	0.071	20.344
Quarter 3 (April – June)	0.048	0.924	Quarter 3 (April – June)	0.091	2.285	Quarter 3 (April – June)	0.092	2.722	GQTR3	-0.166	-1.144
Quarter 4 (July – September)	-0.048	--	Quarter 4 (July – September)	-0.031	--	Quarter 4 (July – September)	-0.007	--	GQTR4	0.158	1.082
REGRESSION DIAGNOSTICS			REGRESSION DIAGNOSTICS			REGRESSION DIAGNOSTICS					
Sample Period	1994Q1 – 2009Q4		Sample Period	1991Q1 –		Sample Period	1991Q1 –		Sample Period	1991Q1 –	
Autocorrelation Coefficients	None		Autocorrelation Coefficients	AR-4: -0.461 (-4.274)		Autocorrelation Coefficients	AR-4: -0.437 (-3.081)		Durbin-Watson	1.752	
Degrees of Freedom	41		Degrees of Freedom	41		Degrees of Freedom	39		Degrees of Freedom	38	
Mean-Squared Error	0.000115		Mean-Squared Error	0.00015		Mean-Squared Error	0.00011		Mean-Squared Error	0.0001	
Adjusted R-Squared	0.983		Adjusted R-Squared	0.985		Adjusted R-Squared	0.990		Adjusted R-Squared	0.989	

What is striking about the latest Presort own price elasticity is that the results for most variables appear to "build" on the *highest* values of each realized in model structures of previous years. Thus, the lag 4 variable of – 0.1299 in R2006-1 is reintroduced in ACR2009 at a value of – 0.139. The current variable of – 0.116 in ACR2007 is estimated at – 0.129 in the ACR2009, and does not resemble any other estimates made previously, which are – 0.0 and – 0.025. Similarly, the lag 2 variable in ACR2009, at – 0.154, appears to build on the value achieved in the ACR2008 model structure of – 0.97, the previous high of recent modeling.

The ACR 2009 Presort demand equation changes the sample period from 1991Q1 forward to 1994Q1 forward – again without explanation, as with the inclusion of a lag 4 variable. By contrast the sample period for Single Piece continues to start with 1983Q1. In general, much less work appears to have been applied to the Single Piece demand equation than the Presort demand equation. And the result (perhaps not surprisingly) is that the Single Piece demand equation produces an elasticity of -0.192 that is well within the range of recent estimates: -0.184 to -0.218.

The lack of continuity between the Presort elasticity number presented in ACR2009 and those produced in the very recent past calls into question its validity and possibly the choice of processes underlying its production.

In GCA's view, the Commission should provide the same oversight and approval process for methodological changes to the demand data submitted in the annual compliance review as it currently does for the cost data. This is especially true this year in light of the acknowledged large number of changes made in this work, and the controversy surrounding the credibility of the new Presort elasticity calculation.

Subsection 3652(a)(1) requires the compliance report to "analyze costs, revenues, rates and quality of service, using such methodologies as the Commission shall by regulation prescribe…." As regards demand elasticity work that is submitted in the ACR process, changes in methodology bear on rates as well as volumes (and hence revenue) under § 3652(a)(1). As the Commission has stated in RM2009-1 and -10 among other places, these rules "require the Postal Service to obtain advance approval in a notice and comment proceeding under 5 U.S.C. 553 whenever it seeks to change the analytical principles that it applies in preparing the periodic reports to the Commission required by section 3652 of the PAEA."[36]

GCA believes that in its FY 2009 Annual Compliance Report, the Postal Service made changes in several areas in its demand analyses that appear to be methodological changes, i.e. changes in analytic principles.[37] These changes go beyond a simple updating of input data and were not considered in any of the rulemakings initiated in the interim period between the Commission issuing its most recent Annual Compliance Determination (ACD) and the Postal Service's filing of its ACR filed in Docket No. ACR2009. Thus, the ACR represents the first opportunity for the Commission, the public, and the postal community to review the changes in the demand analyses.

B. Worksharing rates and delinking

In ACR2009, the Postal Service effectively has renewed its call for de-linking Presort rates from Single-Piece rates in First Class in the way it has constructed its demand equations. The equation for Single Piece no longer includes a variable for worksharing discounts. This is a substantial change from Docket R2006-1, where Postal Service witness Thress had to *impose* a restraint such that the volume of mail leaving Single Piece in response to an increase in the workshare discount exactly equaled the added volume in Presort.[38] In that proceeding, GCA witness Dr. James A. Clifton found that the coefficient for the workshare discount variable in the Single Piece demand equation was *positive*, not negative as Mr. Thress's imposed constraint of one-for-one conversion re-

[36] Docket RM2009-10, Order No. 339, November 13, 2009, p. 1.

[37] Cf. the Commission's statement on pages 1-2 of its January 12, 2009, "Order on Apparent Methodological Changes and Setting Date for Technical Conference," in Docket ACR2008.

[38] Docket R2006-1, USPS -T-7, p. 53, lines 11-16.

quired. In response to USPS/GCA-T-1-84, Dr. Clifton stated why that discount variable would likely have a positive sign in a mature worksharing environment:

> Suppose a credit card company, incentivized by an increase in a worksharing discount, sends one or more advertising letters by First Class or Standard Mail asking a potential customer to sign up for its credit card. When a potential customer signs up, several things happen in the First Class mailstream volume. To begin with, a welcome letter and the new plastic card will be sent at First Class workshared rates. The cardholder then begins using the card and a monthly bill becomes generated and is also sent at First Class workshared rates. All of this extra volume in workshared mail is not the result of conversion from single piece, but the result of the propensity of businesses to want to grow their companies, aided in this example by a greater worksharing discount initially.
>
> Consistent with my econometric analysis and the specification of my single piece demand equation, deepening worksharing discounts now generate greater single piece volume, not less as in witness Thress' demand equation. For each monthly credit card billing statement sent, a payment must be made and most of these will be made by single piece mail. The extra workshared bills generate more single piece volume, not less in this cycle of growth in credit card customers. In this real world example which typifies a substantial amount of letter volume increases, there is no conversion of single-piece letter mail….

The Postal Service, in ARC2009 and RM2009-3, evidently now agrees with Dr. Clifton's econometric finding in R2006-1 that there appears to be little or no more conversion of Single Piece letter mail. However, it has not considered the implication of "no conversion" for the determination of Presort discounts, (or 'workshared rates' under de-linking). The economic rationale for setting Presort rates based on *Postal Service* opportunity costs is no longer sound where there is little or no more conversion.

The reason for this has been explained well in the telecom deregulation debate, and it applies to postal economics as well. For example, in listing several assumptions which must be valid for efficient component pricing to hold, Columbia University Professor Eli Noam points out, following Rosston and Teece:

> The determination of the interconnection fee is based on the assumption that the entrant will divert traffic from the incumbent. But it is incorrect to assume that each call being handled by the new entrant would have otherwise been handled by the incumbent firm. On the contrary, the entrant, to the extent that it lowers charges or provides better or new service, will expand the total number of calls. Suppose the entrant adds only new customers, then the charge it pays should not include them as the opportunity cost to the incumbent, particularly if there is excess network capacity.[[39]]

In this respect, efficient pricing in a mature Presort industry, and in a setting where the Service no longer has a fully effective monopoly of the delivery subservice[40], cannot be based simply on setting (discounted) rates equal to (opportunity) costs *avoided* by the Postal Service. Under these conditions, the access fee[41] paid by private mail processors to enter the postal network should be scaled so that they can cover their own costs of producing bulk mail plus the opportunity cost of capital. This is sufficient incentive to ensure worksharing in mail processing because Postal Service wage rates used in the "costs avoided" methodology are so much higher than those the Presort industry actually pays. To set such access fees lower than private mail processors' costs creates its own distortion from efficient pricing for mail processing services. Such fees encourage inefficient entry from supra-normal profitability, with resulting excess capacity that does not change the fees, which are set by the Postal Service.[42] Furthermore,

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[39] Noam, Eli M., *Interconnecting the Network of Networks,* (Cambridge, MA: MIT Press, 2001), p. 89. G. Rosston and D. Teece, "Competition and 'Local' Communications: Innovation, Entry and Integration," Columbia Institute for Tele-Information Working Paper Series 674, 1993, p. 38.

[40] These two postulates – a Presort industry in which conversion or reversion between Single-Piece and Presort is essentially a thing of the past, and a postal environment in which formerly captive Single-Piece customers have a substitute for at least their (highly important) transactional mail in the form of the Internet – are generally agreed to be realistic today.

[41] That is, the rate for workshared mail.

[42] Note also that the ECPR now applied to Presort discounts does nothing and has done nothing to eliminate the source of the Postal Service's own inefficiency in automated mail processing, namely the compensation costs of mail processing clerks, which are set by union contract and well above a competitive market price for similar services. ECPR has helped the lowest cost producers do more of the country's mail processing, as have earlier discount methodologies since 1976, but especially in a mature worksharing environment the rule has not removed distortions

by proposing to set discounts equal to the total cost difference between work-shared and non-workshared mail at USPS wage rates, delinking also has this effect. Indeed, the market distortions would be even greater under de-linking than they are now under current worksharing discounts and Presort rates.

One of the arguments *for* delinking, in fact, is precisely that conversion has ceased to be important. In its Initial Comments in Docket RM2009-3, the Postal Service presented a table suggesting that "Presorted is essentially a mature product, and that the conversion of Single Piece mail to Presorted has generally run its course."[43] From this, the Service argued that "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."[44] Now if this reasoning were accepted, and it were also conceded (as the Service argued) that a number of other market-related factors must be considered in (separately) pricing Presort, it would seem to follow that *neither* the cost avoided by reference to the Bulk Metered Mail benchmark *nor* the full cost difference recorded in the CRA would be a suitable criterion for efficient Presort rates. The starting point should instead be the one suggested above: an access fee to the postal delivery network just low enough to allow the presorter to cover its costs (including a normal return).

C. The Public Representative and the consumer

The Public Representative's comments in this Docket make the following statement:

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from efficient pricing in mail processing from either the private sector or the Postal Service. The competition engendered from excess capacity may have shifted excess profitability from Presort bureaus to their customers, but that does not change the inefficiency of the USPS pricing for the private sector.

[43] Docket RM2009-3, Initial Comments of the United States Postal Service, pp. 19-20.

[44] Id., pp. 20-21.

> Ratcheted rate increases of several pennies for single-piece First-Class rates amounting to a few percentage points could "save the service" currently enjoyed, in some cases demanded, by many mailers and the public, including the demand to keep post offices open. Moreover, rate adjustments that better reflect the full cost of services would more closely adhere to accepted economic principles.[[45]]

And further,

> Another relevant factor when considering the appropriateness of rate level adjustments is the level of its First-Class Mail letter rates compared to that of other postal services around the world. . . . The First-Class Mail letter rate would remain a bargain even if significant rate level adjustments were applied to the Postal Service rates. Moreover, the rates of other nations may also ratchet-up over the next two years as well.[[46]]

GCA has previously pointed out the inappropriateness of dollar-denominated, and thus exchange-rate-dependent, comparisons with foreign letter rates, particularly when the dollar is weak internationally.[47]

It is likewise highly misleading to compare stamp rates in the United States with those of other countries, because the U. S. Postal Service is unique in size, with economies of scale and scope and advanced technology unmatched by any other post. If the Postal Service's letter rate is a "bargain" it is probably because the Service can afford, better than any other postal system, to offer its customers that rate.[48] Moreover, in his international comparisons, the Public Representative fails to acknowledge that other countries, unlike the United States, have no other considerable source of mail volume and revenue than that tied to their stamp rates. For example, no other country has the volume of adver-

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[45] Docket ACR2009, Public Representative Comments on Annual Compliance Report, 2009, p. 30.

[46] Id., p. 31.

[47] GCA Reply, pp. 9-10.

[48] GCA also made this point in opposing the Public Representative's motion for rate estimates. Ibid.

tising mail that the United States enjoys in its Standard Mail classification. GCA, as the trade association speaking for the citizen mailer, is disappointed to see these insubstantial arguments repeated in the Public Representative's most recent Comments.[49]

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The Public Representative's comment about covering the full costs of the mail can be interpreted in two ways; it is not clear whether it suggests that Single-Piece First Class is not covering its costs, or simply that a *systemwide* structure of rates which would not leave the Postal Service in the red would "more closely adhere to accepted economic principles." If the latter truism is the intended meaning, it would be difficult to disagree with – but it also adds nothing to the Public Representative's faulty arguments that the existing rates are actually unlawful and can be changed under § 3653. If the Public Representative is focusing on Single-Piece, he has failed to cite any studies suggesting that the much higher rate structure of Single-Piece mail is not covering its full attributable costs – let alone providing 18 cents/piece toward institutional costs. Any objective view of delivery costs, most of which are institutional, shows that First Class Mail bears a disproportionate share of those compared with Standard, as is clear from Figure 1 and our discussion surrounding it.

GCA regrets having to reiterate arguments already made against the Public Representative's proposals regarding the letter stamp and the citizen mailer who buys and uses it. It remains true, however, that the greatest challenge to the long-run viability of the Postal Service is diversion to e-media. Mail that con-

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[49] It is also worth noting, in view of the Public Representative's continued advocacy of a drastic increase in the Single-Piece rate, that the citizen mailer has recently made large contributions to the Postal Service's income. In May of 2009, First Class Single-Piece rates were raised by 4.76%, well above the 3.814% price cap for First Class Mail as a whole. Presort rates were raised by 3.02%, well under the CPI ceiling. High Density and Saturation letter rates in Standard Mail were raised by only 1.24%, well under the Standard Mail price cap of 3.781%. Standard automation letters (classification 1220) were raised by 3.82%, not materially above the Standard Mail price cap, unlike Single-Piece letters. We understand, of course, that within First Class the integer-cent convention plays a large role in determining a given year's relative increases as between Single-Piece and Presort. Our point is that the letter stamp is not a "bargain" because it has been treated with abnormal leniency in rate adjustments; it has not been.

tains nothing but information – which, for the household, means essentially transactional mail – is the prime candidate for conversion to the Internet. This is true not least because the businesses with which the household engages in the transactional-mail dialogue have strong incentives to promote – and commonly do promote – conversion of the entire hard-copy interaction to one conducted on-line. To concentrate rate increases on the letter stamp would simply accelerate the volume decline in Single-Piece mail – which, in vanishing, would take much Presort mail with it. Moreover, mail which is not "pure information" – that is, mail such as a greeting card or personal letter, which has value to the recipient simply as a tangible artifact – pays the same Single-Piece rate as the household's bill payments. Such mail is much less subject to Internet diversion, but it too would be powerfully discouraged by disproportionate increases.

IV. SUMMARY

For the reasons set out above, GCA urges the Commission –

- To recognize that the Postal Service's deficit is not the result of its rate schedule but, primarily, of exogenous burdens placed on the Service; that the deficit cannot be cured by a fly-up in rates; and that restoration of financial stability is not a task for a single year's compliance review, especially in 2010;

- To make it clear, in particular, that the existing rates are not out of compliance with the provisions of ch. 36 and associated regulations simply because a deficit exists;

- To refrain from extending this proceeding beyond its statutory purpose, and the limits of administrative practicality, by attempting to resolve in it issues already pending in the "benchmark" rulemaking, Docket RM2009-3; and

- To approach with great caution the novel and insufficiently explained Presort demand elasticity estimate submitted by the Postal Service in the course of this proceeding.

February 23, 2010

Respectfully submitted,

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