

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

Notice of Price Adjustment) Docket No. R2010-3
Standard Mail Incentive Pricing Program)

COMMENTS OF THE PUBLIC REPRESENTATIVES
(March 22, 2010)

On February 26, 2010, the Postal Service filed a Notice of Price Adjustment, proposing a 2010 “Standard Mail Volume Incentive Pricing Program pursuant to 39 U.S.C § 3622 and 39 C.F.R. 3010.”¹ The proposed program is similar to the “Summer Sale” approved by the Commission in R2009-3 Order No. 219. Commission Order No. 416 established Docket No. R2010-3, and appointed the undersigned as Public Representatives.² Commission Order No. 422 established the comment deadline of March 22, 2010.³ Pursuant to Order No. 416, the Public Representatives hereby file the following comments.

I. Introduction

In its proposal, the Postal Service states that “like its predecessor, the objective of Summer Sale 2010 is to increase incremental Standard Mail volume and revenue” Notice at 2. The Postal Service points to the importance of using pricing incentives to counteract the decline in volume due to the current economic climate. It states that by offering discounts during a typically low-volume period, the proposal sends the signal to mailers that the Postal Service is taking steps to promote the health of the mailing industry and aggressively compete for advertising budget dollars in a highly competitive

¹ United States Postal Service Notice of Market-Dominant Price Adjustment (Notice), February 26, 2010.

² Order No. 416 Notice and Order Concerning Standard Mail Volume Incentive Pricing Program. (March 2, 2010)

³ Order No. 422 Order Concerning Comment Deadline. (March 16, 2010)

marketplace. As in R2009-3, the Postal Service also points to the value of using pricing incentives “to improve postal data systems in addition to fine tun(ing) future offerings and enhance(ing) existing relationships with customers.” Id. at 3.

II. Program Summary

- Summer Sale 2010 will run from July 1, 2010 until September 30, 2010.
- The Postal Service will provide a 30 percent rebate to eligible mailers on Standard Mail letters and flats volume above the predetermined threshold to be agreed upon by both the mailer and the Postal Service.
- The threshold is the amount of Standard Mail for each participating company sent through their Permit(s) or Ghost Permit(s) (or through their Mail Service Provider) from July 1 to September 30, 2009 (SPLY) plus five percent (SPLY + 5%).
- An additional volume threshold will be established for the months of June 2010 and October 2010 using the same SPLY +5% formula. If June 2010 or October 2010 actual volumes do not meet the respective month’s threshold (SPLY +5%), the difference will be deducted from their Summer Sale 2010 rebate-qualifying volume. The June threshold is a new feature of the 2010 Summer Sale. Summer Sale 2009 had only an October threshold.
- Eligibility for participating in Summer Sale 2010 requires a qualifying customer to have mailed 350,000 or more Standard Mail letters and flats between July 1 and September 30, 2009, through one or more permit imprint advance deposit accounts owned by the company or through permits set up on behalf of the company by a Mail Service Provider (MSP). This is a lower threshold than the 2009 Summer Sale, which had a threshold of 1 million pieces.
- The Postal Service estimates that approximately 3,525 customers will be eligible to participate in the sale, representing 67 percent of Standard volume. As with the prior Summer Sale, MSP’s are not eligible for the program. Id. at 3. The

Postal Service estimates 400 additional mailers will be eligible to participate due to the lowered threshold.

- The Postal Service believes that there is currently some excess capacity, similar to the Summer Sale in 2009. Thus, the Postal Service asserts that it will be employing unused or underutilized capacity to handle increases in volume. However, unlike the previous Summer Sale, the Postal Service assumes that additional carrier cost will be incurred to deliver the incremental volumes.
- The Postal Service notes that there are inherent risks that may affect the outcome of the program. Specifically, it is noted that an overestimate of the additional volume generated by the Sale or an underestimate of the administrative effort required could unfavorably affect the expected financial performance of the Sale. Further, there is risk that a portion of the rebates would be paid on volumes that customers would have mailed anyway.
- Finally, the Postal Service expects the financial effect of the program to be a net contribution change of between -\$3.5 million and \$25.4 million. Expected administrative costs for the Summer Sale are estimated to be \$930,000.

III. Comment

In evaluating the current Incentive Pricing Program, the Public Representatives believe that two components of the proposal merit purposeful consideration: how it maximizes the net contribution to Postal Service finances and how it encourages equitable competition in the marketplace. Both issues should be straightforward in a proposal of this nature. The Postal Service is provided pricing flexibility and the ability to retain earnings in an attempt to incent businesslike behavior, the pursuit of profit. However, the profit incentive is balanced by the requirement that rates be “fair and equitable,” and the requirement that special classifications not cause “undue discrimination to the marketplace.” The current proposal is lacking on both counts. The

Public Representatives propose the following improvements to the 2010 Standard Mail Incentive Pricing Program:

1. Limiting “Anyhow Volumes” by Setting More Accurate Discount Thresholds
2. Excluding Standard Mail Products That Do Not Cover Attributable Costs
3. Requiring a Registration Fee to Cover Administrative Costs
4. Allowing All Mailers to Register

The experience with the 2009 Summer Sale provides valuable insight into the importance of accurate thresholds. Mailers who received discounts had thresholds significantly below SPLY volumes, leading to at least 38% of discounted volume receiving anyhow discounts. Further, mailers who did not receive discounts had thresholds of nearly SPLY volume, suggesting that more accurate thresholds could have increased the opportunity for both the Postal Service and Mailers to participate profitably.

Of the six products eligible for discounts through the 2009 Summer Sale, one product (Standard Mail Flats) did not cover its Long-Run or Short-Run attributable costs. This product will not cover costs in 2010, and should not be eligible for discounted rates. Few mailers participating in the 2009 Summer Sale mailed exclusively Flats, and by removing this product from the 2010 Summer Sale the Postal Service will encourage volume growth in products that are profitable to the Postal Service with minimal harm to mailers.

Setting an arbitrary cut-off for program eligibility creates discrimination. By requiring all mailers to pay a minimal (\$1,000) fee for enrollment in the Incentive Program, the Postal Service will ensure that the cost of implementing the program is paid for by each participating mailer. By allowing all mailers to pay the registration fee and enroll, the Postal Service will ensure that there is no discrimination.

a. Trend analysis

The volume threshold is the primary driver of mailer participation, incremental volume eligible for a discount, and ultimately the profitability of a volume incentive program. When the discount threshold is set too high, mailers cannot respond to the

discount. When the threshold is set too low, the value of the incremental mail is reduced (or possibly overwhelmed) by the cost of giving discounts to mail that would have been sent regardless of the program. Approximating the volume that would have been sent without a discount is a difficult task. Fortunately, the Postal Service has provided a large amount of data on the mailers who are eligible for the 2010 Summer Sale.

The 2009 Summer Sale was designed, proposed, and implemented during the worst economic climate since World War II. With this environment in mind, the Commission approved the 2009 Summer Sale, stating “Postal Service is to be commended for its response to current market conditions. Much can be learned from what, in essence, is a short-term pricing experiment. However, the program is not without risks. Thus, development and use of appropriate metrics in evaluating the program are critical in determining whether the program is successful, and also for assessing the long-term implications of such an approach.”⁴

Analyzing the results of the 2009 Summer Sale is the first step in evaluating the potential for success of the 2010 Summer Sale. This experiment has provided valuable insight on how mailers react, both individually and collectively, to an incentive pricing program.

The formula used to calculate the discount-eligible volume threshold in the 2009 Summer Sale was:

$$\frac{(\text{October 2008} - \text{March 2009})}{(\text{October 2007} - \text{March 2008})} \times (\text{July 2008} - \text{September 2008})$$

The intent of this formula was to customize the threshold for each mailer to account for the recent trend in Standard Mail Volume. If a mailer had declining volumes in the first two quarters of FY 2009 compared to SPLY, then the discount threshold was below SLPY volume. If a mailer had increasing volumes in the first two quarters of FY 2009 compared to SPLY, then the discount threshold was above SLPY volume. This formula was intended to allow all mailers to participate, providing they could increase their volumes above the trend.

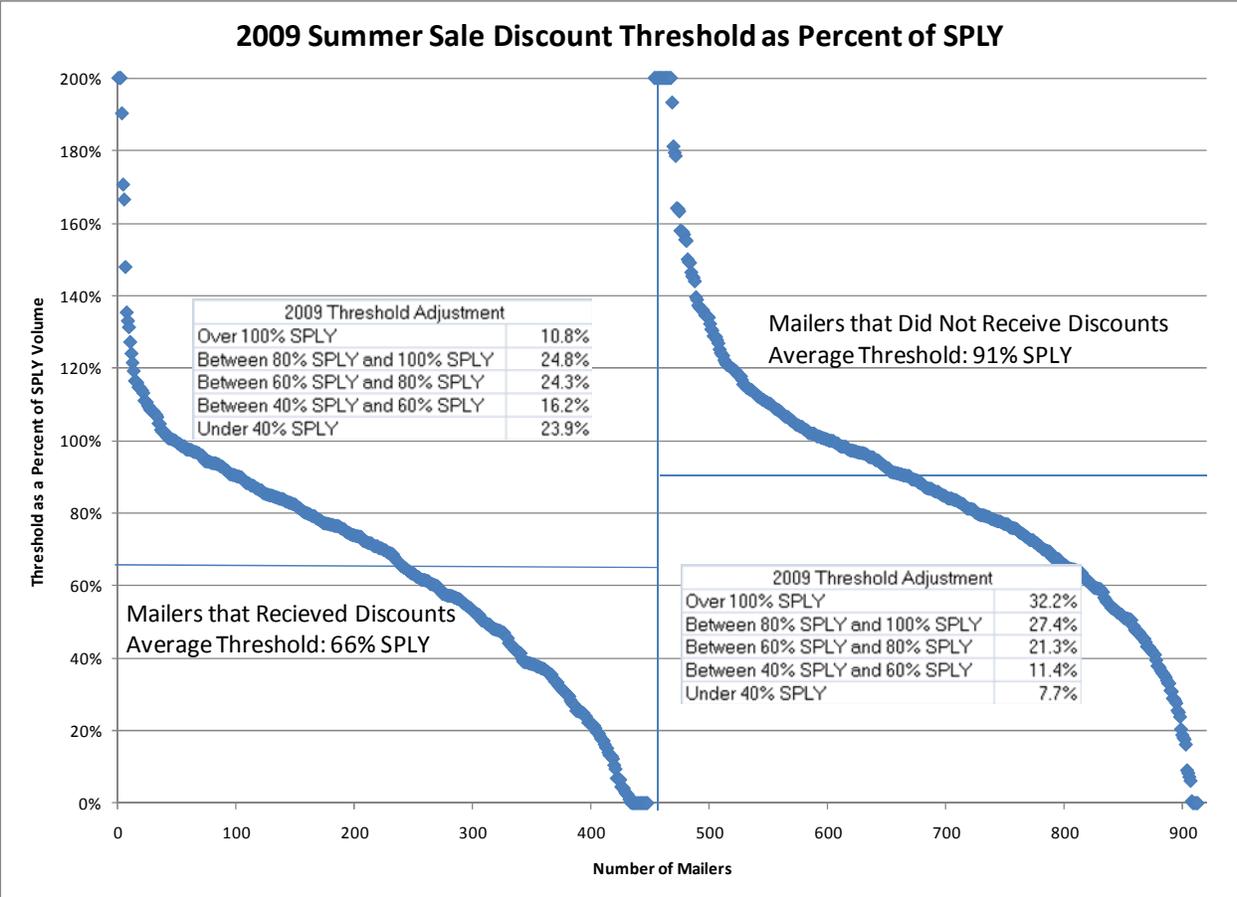
⁴ Order No. 219 at 2.

The results suggest that this is not what occurred. The following chart contains the last three years of volumes for Standard Mail as a whole, Participating Mailers who received a rebate, Participating Mailers who did not receive a rebate, and Mailers not participating.

	Standard Mail	% of SPLY	Eligible Mailers With Discount	% of SPLY	Eligible Mailers Without Discount	% of SPLY	Mailers Not Participating	% of SPLY
2007 Q1	28,410,608,000		4,875,251,358		3,650,972,028		19,884,384,614	
2007 Q2	25,291,072,000		4,801,927,488		3,348,808,037		17,140,336,475	
2007 Q3	24,584,387,000		4,908,935,314		3,365,350,933		16,310,100,753	
2007 Q4	25,230,045,000		5,539,208,370		3,597,641,479		16,093,195,151	
2008 Q1	27,634,215,000	97.3%	6,208,971,167	127.4%	4,211,240,607	115.3%	17,214,003,226	86.6%
2008 Q2	24,530,722,000	97.0%	5,311,324,186	110.6%	3,811,198,454	113.8%	15,408,199,360	89.9%
2008 Q3	23,216,603,000	94.4%	4,609,139,415	93.9%	3,598,804,784	106.9%	15,008,658,801	92.0%
2008 Q4	23,702,615,000	93.9%	4,505,859,518	81.3%	3,864,451,225	107.4%	15,332,304,257	95.3%
2009 Q1	24,599,242,000	89.0%	4,024,253,238	64.8%	3,807,476,356	90.4%	16,767,512,406	97.4%
2009 Q2	19,759,308,000	80.5%	3,332,396,349	62.7%	2,960,050,168	77.7%	13,466,861,483	87.4%
2009 Q3	18,761,285,000	80.8%	3,336,484,921	72.4%	2,659,303,426	73.9%	12,765,496,653	85.1%
2009 Q4	19,586,376,000	82.6%	4,169,973,043	92.5%	2,539,820,361	65.7%	12,876,582,596	84.0%
2010 Q1	21,916,722,000	89.1%	4,035,052,555	100.3%	2,862,110,527	75.2%	15,019,558,918	89.6%

There are two quarters that deserve close scrutiny, the final two quarters used in the threshold calculation. For mailers that received a discount, FY2009 Q1 and Q2 were the very lowest volume periods, with declines of 35.2% and 37.3% compared to SPLY. This decline is worse than the comparative decline for Standard Mail by 24.2% and 17.8%. The Mailers who did not receive a discount closely track the trend of Standard Mail as a whole for FY09 Q1 and Q2. The aggregate volumes indicate that the recessionary business cycle has hit all Standard mailers in a similar fashion, but not in the exact same fiscal quarters. Some mailers (those who received discounts) experienced their lowest volumes in FY 2009 Q2, the final quarter of the threshold calculation. Those mailers began to increase volumes (in absolute terms) in FY2009 Q3, and by FY2010 Q1, their volumes increase by .3% over SPLY. Another set of mailers, those who were not able to respond to the discount, did not experience their lowest volumes until FY2009 Q4, the period of the Summer Sale incentive. It appears the same business cycle declines hit some mailers two to three Fiscal Quarters after it hit others. Mailers that had their lowest volumes over the last 3 years in FY09 Q1 and Q2 were able to rebound and take advantage of the 2009 Summer Sale, and continue that growth beyond the 2009 Summer Sale.

It is important to evaluate the success not just on an aggregate basis, where the spikes in individual mailer behavior become much smoother curves, but also for individual mailers. The following chart shows the 2009 discount threshold for each mailer as a percentage of SPLY. For each mailer, the FY2009 Q1 and Q2 volumes are divided by the FY2008 Q1 and Q2 volumes. This “Threshold factor” is analogous to the +5% adjustment applied to each mailer in the 2010 Incentive Program, as it is the adjustment to SPLY volumes to calculate the discount threshold. The same chart for the 2010 Summer Sale would be a horizontal line at 105%. The following chart shows that the 2009 Summer Sale threshold used a SPLY adjustment that varied significantly from mailer to mailer, compared with the uniform 2010 adjustment that will be applied equally to each and every mailer. The Participating Mailers are divided into two groups, those who qualified for a discount and those who did not.



The data provided in “Revised Summer Sale PRC Report-Workbook 1.xls” show that mailers who received discounts had lower thresholds by 25%, on average. Mailers with Thresholds of over 100% SPLY (those who had to increase volume) were likely not to qualify for discounts, and mailers with thresholds under 60% of SPLY (Mailers who had to mail roughly half of Summer 2008 volume) were very likely to mail enough volume to qualify for discounts. The large dispersion in thresholds also signifies how much mailer behavior differs from year to year and from business to business. Some mailers were unable to reverse downward trends to qualify for discounts, while others were able to increase volumes even though their thresholds required growth.

b. Anyhow Volume

In the data collection report submitted by the Postal Service for R2009-3, the anyhow volume was estimated to be 38.2% of the discounted volume.⁵ The Postal Service developed this figure by comparing the Spring 2009 Growth to threshold Volumes estimated using the Summer Sale 2009 Formula. For all participating mailers, the following formula was used to estimate Spring 2009 threshold volume:

$$\frac{(\text{October 2008} - \text{March 2009})}{(\text{October 2007} - \text{March 2008})} \times (\text{April 2008} - \text{June 2008})$$

Comparing this estimate to the actual Spring 2009 volume, the Postal Service calculated that there was 7.07% volume growth for participating mailers in FY2009Q3 over the threshold. The Public Representatives commend the Postal Service for developing an empirical model to approximate anyhow growth. Evaluating the volume growth during the period that preceded the incentive program uses sound logic; if a mailer were growing before the incentive began, and the mailer continued to grow during the incentive, then the growth that preceded the discounts was not caused by the discounts. This methodology reinforces the notion that, for many mailers, the discount threshold was set based on historically low volumes, a trend which had already begun to reverse (for some mailers) before the 2009 Summer Sale began. Since the Postal Service did not submit this methodology during the last summer sale, or as a change in

⁵ R2009-3 Data Collection Report (2/26/10).

methodology prior to the ACD or this docket, the methodology has not undergone the rigor of intervenor or Commission review.

The volume growth using the spring threshold method is calculated for each mailer, and then applied to the participating volume to estimate anyhow volume. Mailers who grew their volumes in the spring, but were not able to grow their volumes during the 2009 Summer Sale have their spring growth included in the calculation of anyhow discounts. Each mailer's anyhow growth percentage should be applied to the individual mailer's growth during the Summer Sale, and only the summer growth above the spring growth should be counted as incremental growth in response to the discount. This was the subject of a motion for issuance of an Information Request.⁶ The data used in that question have subsequently been updated, and the methodology has been explained and the calculations shown. Applying the Spring Threshold method to each mailer that qualified for discounts leads to a dramatically different calculation of Anyhow Volume.⁷ The following chart details the anyhow volume for Rebate Eligible Mailers

	Total Summer Volume	Discounted Volume	Anyhow Volume
Rebate Eligible Volume Only	4,169,973,043	987,977,741	465,495,588
		23.7%	47.1%

The incremental volume qualifying for discounts in the 2009 Summer Sale was 23.7% of participating volume. Anyhow growth of 47.1% threatens the profitability of the program.

The Public Representatives also note that mailers who received discounts increased their FY 2010 Q1 volumes as compared to SPLY. If the Spring Method is applied to the winter volumes, the resulting calculations produce an estimate of 100% anyhow volume, since the increase after the sale, as compared to SPLY, was greater than the increase during the sale. The Summer Sale provided valuable benefits to some mailers, and their increased financial health will have an ongoing benefit to the Postal Service. Some of this success can, and should, be attributed to the Summer Sale. However, much of it should be attributed to the business cycle that affects all

⁶ Public Representative Motion for Issuance of Information Request (March 10, 2010) question no. 2.

⁷ The Postal Service provided the file "(2010-01-21) Summer Sale 2 loyalty analysis.xls" with hardcoded data on 3/8/2010 in response to ACR CHIR #8. It provided the file with linked cells, showing all formulas on 3/16/2010 in response to R2010-3 CHIR #1. Further, the data by mailer in this file does not precisely match the data in "Revised Summer Sale PRC Report- Workbook 1.xls" for every mailer. The Public Representatives use the file "Revised Summer Sale PRC Report- Workbook 1.xls" in their calculations.

mailers differently. If the Postal Service had the ability to gather information instantly so it could have updated the thresholds to adjust for Spring 2009 growth, the anyhow volume using this method would be zero.

c. Was the 2009 Summer Sale Profitable?

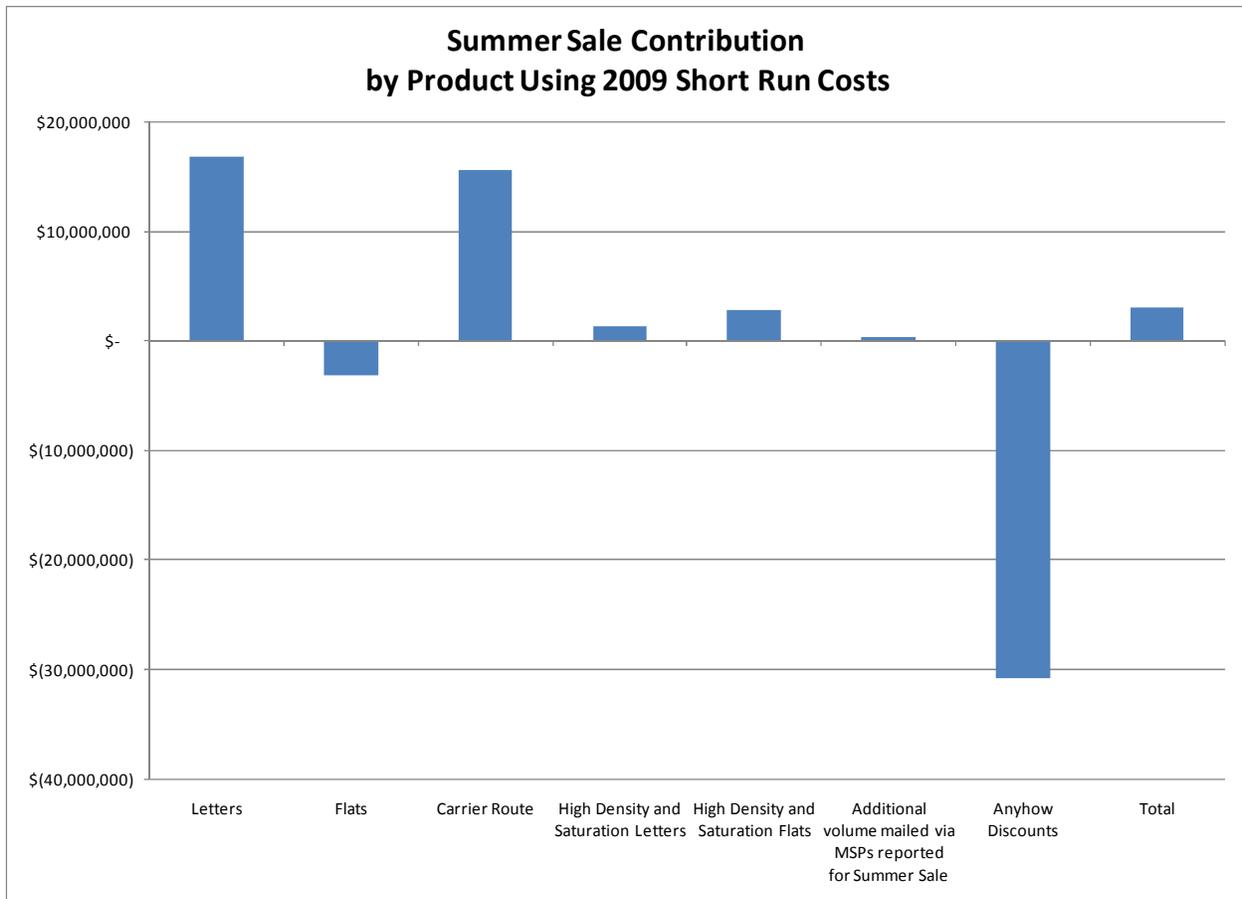
Using the data provided by the Postal Service, specifically “Revised Summer Sale PRC – Workbook 1.xls,” the Public Representatives are able to apply product level costs and anyhow growth by mailer to develop mailer revenue, cost, and contribution. The Postal Service calculates cost and anyhow volumes on aggregate in the file “(2010-03-05) Summer Sale Financials as of Round 4.xls”⁸. The following chart uses the mailer specific anyhow volume discussed in section B of these comments, the short run variable costs by product provided in “Calc SR Attributable Costs for Summer Sale.xls”⁹ applied to each mailer, and the mailer specific revenue.

	PR Analysis	USPS
Incremental Revenue	\$ 85,063,490	\$98,141,641
Anyhow Discounts	\$ 30,758,526	\$25,833,944
SR Total Cost	\$ 51,266,181	\$48,206,665
Contribution	\$ 3,038,783	\$24,101,033

This analysis estimates that the Postal Service increased contribution \$3 Million by giving over \$67 Million in discounts to nearly 1 billion pieces. The Postal Service estimates administrative costs at \$972,000. The profitability was threatened by two major sources: anyhow discounts and incremental Standard Flat volume. In its proposal for Docket R2009-3, the Postal Service estimated that the revenue from incremental Standard Flat volume would cover the short run attributable costs of that volume. In the Post-hoc evaluation, the Postal Service estimated short run attributable cost for Standard Mail Flats that was more than incremental revenue, leading to a loss in contribution on incremental Standard Flats of roughly -\$3 Million. The following chart shows the 2009 Summer Sale Contribution by Product.

⁸ Filed in response to ACR 2009 CHIR #8 on 3/8/2010.

⁹ Filed on 2/25/2010.

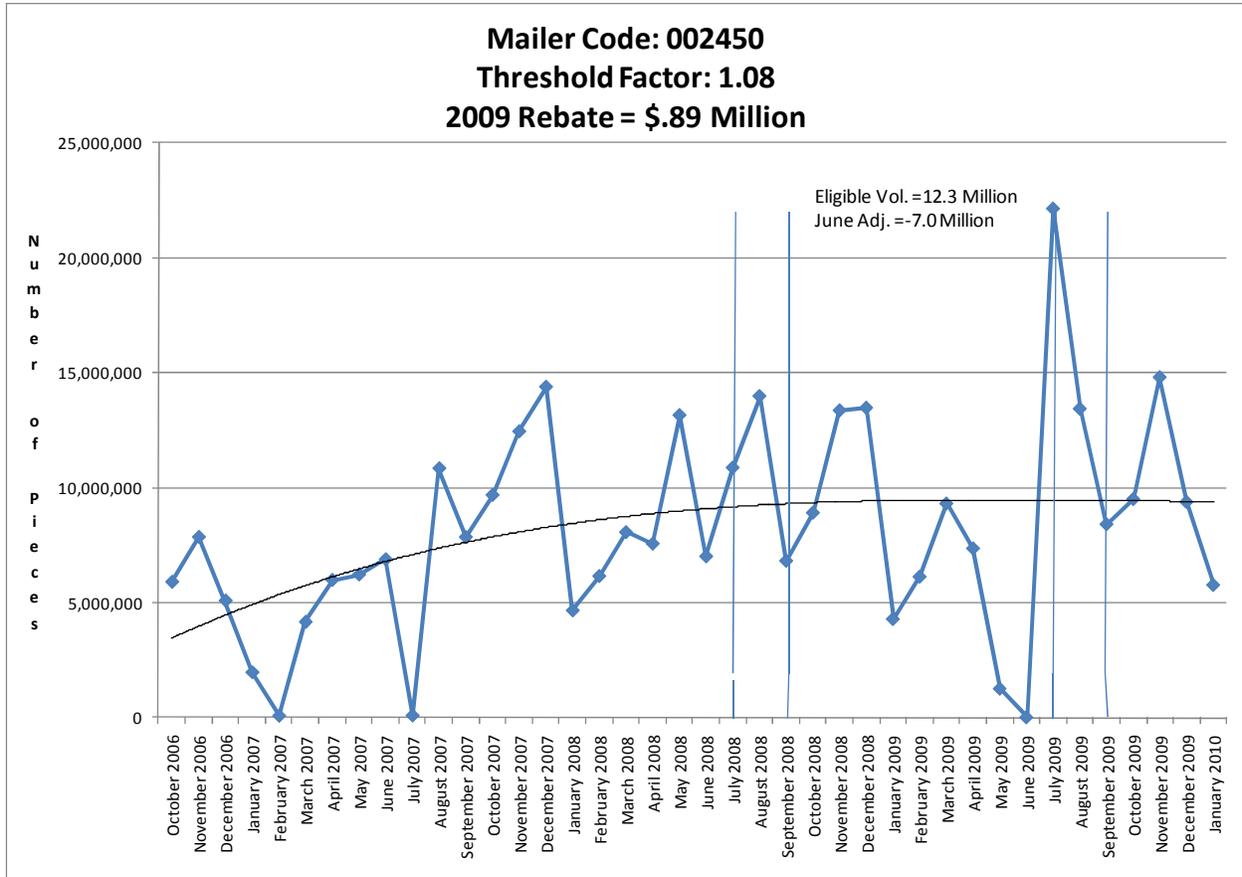


This estimate is developed using methodologies for anyhow volume not approved by the Commission. Using the Commission approved methodology of applying the current period elasticity to estimate anyhow volume, the 2009 Summer Sale produced a considerable loss of -\$39.6 Million dollars, as shown in the table below.

Summer Sale Volume from Mailers with Rebates			
Total Volume	Original Revenue/ Discounted Revenue	Elasticity	Before Rates Volume
4,169,973,043	1.428571429	-0.150182822	3,952,479,572
Incremental Volume	Discounted Volume	Anyhow Volume	
217,493,471	987,977,741	770,484,270	
Average Revenue per piece	Average Discounted Revenue Per Piece	Average Cost Per Piece	Average Anyhow Discount
\$ 0.233	\$ 0.163	\$ 0.098	\$ 0.070
Incremental Revenue	Incremental Cost	Anyhow Discounts	Contribution
35,409,350.53	21,340,556.10	53,759,934.10	(39,691,139.66)

Given the uncertain economic climate during the implementation of the Summer Sale, it may not be proper to apply this methodology. Two commenters in this Docket, DMA and ACMA, state that “there is no “anyhow” mail. It is gone, and policies established based upon “anyhow” mail will harm the Postal Service and its paying customers. It is time to face the reality of a significantly smaller Postal Service and significantly diminished demand for mail services. We ask that the “anyhow” mail policy driver be buried.” This statement argues that all volume sent under a price incentive is incremental. Taken to the extreme, no mail would be sent without discounts. This argument does not discuss the apparent anomaly of mailers who did not participate in the Summer Sale that were able to grow their volumes. It does not discuss the fact that mailers who participated in the Summer Sale grew their volumes more after the Summer Sale ended than during the discount period. This is a policy position that is not intended to maximize the contribution from the incentive pricing program, and should not be regarded as grounded in economic reality. These mailers may have been hinting at the fact that the mailers who qualified for discount in the 2009 Summer Sale were able to grow their volumes in the most recent quarter, and while the 2009 Summer Sale may not have been profitable in and of itself, the success of the 2009 Summer Sale could be measured on the longer term industry health.

The June Threshold Adjustment is a notable area where the Postal Service appears to have learned from its 2009 Summer Sale experience. The following chart highlights an apparent shift in volume, from June to July.

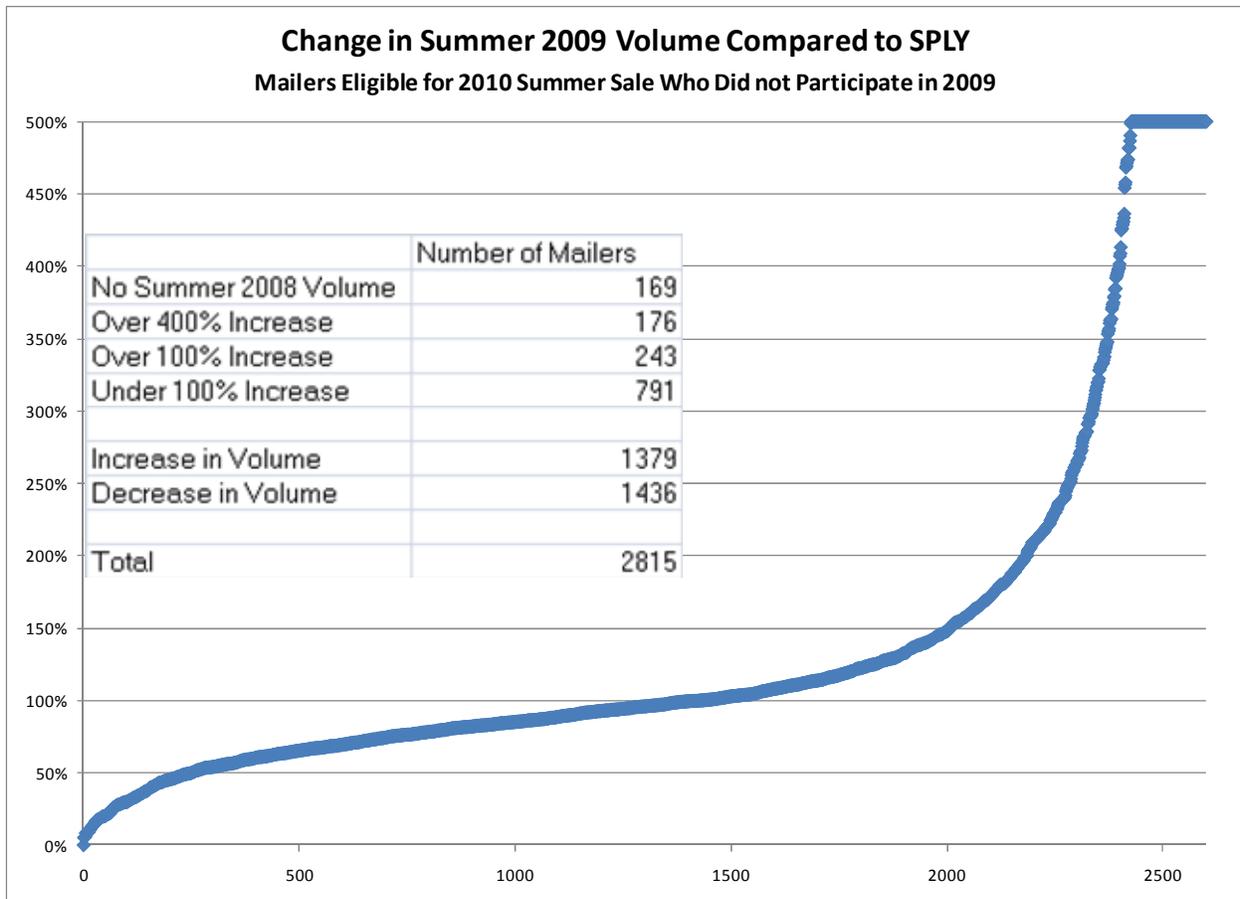


This mailer would have received a significantly smaller discount had the additional protection from volume shifting been in place in 2009.

d. Data Concerning Mailers that did not Participate in 2009 Summer Sale

On March 16, 2009, In response to CHIR #1, the Postal Service provided a database with historical volume data for the 3,525 mailers who are eligible for the 2010 Summer Sale. This database highlights the difficulties of measuring anyhow volume, and the dangers of applying a discount threshold to all mailers equally. The following chart contains the volume growth of each mailer eligible for the 2010 Summer Sale who did not participate in the 2009 Summer Sale for July to September of 2009, as compared with July to September of 2008. None of these mailers received discounts.¹⁰

¹⁰ The file "(2010-03-15) Customer list for latest summer sale 2 analysis_redacted.xls" contains 729 mailer IDs that can be matched with the 2009 Summer Sale participants. The 2009 Summer Sale had 958 participants, of which



Similar to the analysis of the 2009 Summer Sale participants, mailers who did not participate were, on average, slightly more likely to decrease volume than increase volume. This data shows that mailer growth does not occur on a uniform basis. Standard mail volume did not decrease because every mailer experienced slight volume declines. Standard mail volume decreased because the number of mailers who were able to increase their volume was more than offset by the number of mailers who decreased their volumes. Mailers who did not participate in the summer sale had an overall decline in volume from summer of 2008 to summer of 2009 of nearly 1.5 Billion pieces. The 1379 mailers that increased their volumes added over 1.6 Billion pieces in FY09. That additional volume was far outweighed by the 1436 mailers with decreasing volume, who had a SPLY change of negative 3.1 Billion. On average, smaller mailers grew their volumes and larger mailers decreased their volumes.

the volume of 229 cannot be identified in this file using the same mailer ID. It is unclear if these mailers are included. Some mailers participating in the 2009 Summer Sale mailed fewer than the 350,000 pieces needed to qualify for the 2010 program.

The historical volumes since October of 2007 can be used to calculate the 2009 Summer Sale mailer threshold, and the growth compared to that threshold. Volumes above 100% would have been eligible for the discount if the mailers had participated.¹¹ Had these mailers participated in the 2009 Summer Sale, they would have received over \$54 Million dollars in discounts for growth that occurred without a discount. Since these mailers will be eligible for the 2010 Incentive Pricing Program, it may be instructive to estimate the discounts that would have been paid using the 2010 discount threshold, SPLY +5%. That hypothetical discount would have been \$56 Million dollars.¹²

e. Alternative Method for Evaluating Profitability of the 2010 Incentive Program

The Postal Service provided its estimate (according to the file, as of January 24th 2010) of anyhow volume and contribution in response to Docket No. R2010-3 CHIR 1, filed March, 16 2010. Much of this analysis has been provided for the first time, and does not use any methodology previously presented to the Commission. The Public Representatives have provided a workbook that may offer a more logically consistent model to analyze the 2010 Summer Sale.

The Postal Service expects that eligible participants will experience anyhow growth of 7.07% over SPLY, the same anyhow growth that occurred in the 2009 Summer Sale (as measured using the threshold estimate of Spring 2009 Volume). As discussed in section B, that value understates the anyhow growth because it does not account for the fact that each mailer grows differently depending where they fall in the business cycle. The Summer Sale 2009 experience suggests that the growth rates between FY2009 Q4 and FY2010 Q4 will vary widely, and that by applying a uniform threshold there will be significant anyhow volume. There is no way to remove anyhow discounts from a volume incentive program, but they can be minimized. The chart on

¹¹ No volume data for October of 2009 is provided, so mitigation of discounts due to the October adjustment cannot be calculated.

¹² Calculated using the SPLY+5% formula and the 2009 Summer Sale formula applied to the file "(2010-03-15) Customer list for latest summer sale 2 analysis_redacted.xls" without 2009 Summer Sale participants.

Page 13 titled “Change in Summer 2009 Volume Compared to SPLY” contained the following distribution of growth rates.¹³

Change in Volume	Change in Summer 2009 Volume Compared to SPLY					
	under 60%	60-80%	80-100%	100-120%	120-140%	over 140%
Number of Mailers	390	443	584	356	174	653
Volume	711,305,740	2,245,851,271	1,763,162,898	973,441,672	268,845,376	928,016,879
Percent of Volume	10%	33%	26%	14%	4%	13%

The model produced by the Public Representatives uses the distribution from mailers that did not receive discounts in 2009 to estimate the before rates volume after the anyhow growth is estimated. It assumes that the volume after the business cycle growth will be the same as before the business cycle growth. Using the above distribution, the value of the 2010 Pricing Incentive is estimated as follows:

Percent Increase In Volume	Value
20%	\$ (25,882,885)
30%	\$ (13,338,138)
40%	\$ (793,391)

This model suggests the following:

- If 50% of mailers participate, and they have Before Rates changes in volume with the same distribution as occurred in 2009, there will be significantly more anyhow volume than the Postal Service estimates (787.6 Million Pieces compared to 187 Million), due largely to the 13% of mailers (by volume) that increased volumes by more than 140% in 2009 without discounts.
- The unprofitability is largely caused by a low incremental contribution per piece, compared to a high cost of anyhow discounts. This is due to Standard Mail Flats, the cost of which are estimated in the following table

Standard Flats as a Percent of Volume	9.5%		
	Volume	Unit Cost	Total Cost
Anyhow Volume	72,183,105.71	\$ (0.113)	\$ (8,142,254)
20% Growth	76,884,803.32	(0.119)	\$ (9,149,234)
30% Growth	120,993,147.03	(0.119)	\$ (14,398,095)
40% Growth	165,101,490.75	(0.119)	\$ (19,646,955)

¹³ This distribution does not include mailers with no summer 2008 Volume.

If Standard Flats are removed from the model, and no conversion is assumed, the value of the 2010 Incentive Pricing Program is estimated as follows:

Percent Increase In Volume	Value
20%	\$ (7,772,915)
30%	\$ 8,325,539
40%	\$ 24,423,992

f. Proposed Improvements

In section E, there were two aspects of the 2010 Summer Sale that were shown to be contribution negative: anyhow volume, and inclusion of Standard Flats. The Postal Service analysis states that with a 20% growth from participating mailers, the 2010 Incentive Pricing Program will lose \$3.4 Million, highlighting the minimum dangers of both of these financial risks.

The Postal Service estimates anyhow volume at 7%, and the discount threshold should, at a minimum, be set at this estimate of anyhow growth. The model “PR Growth Model” provided suggests anyhow growth will be much higher. Further, that model suggests that a flat threshold will exclude many mailers, and allow for significant anyhow volumes. A threshold tailored to mailer trends would increase the potential value of the program, while decreasing the risks.

While the specter of anyhow discounts cannot be removed altogether, the prospect of discounting flats that do not cover costs can be removed. While the catalog industry repeatedly voices its concerns that it needs relief from burdensome rates, the fact that their rates do not cover cost is evidence of the relief they receive on a daily basis from covering their attributable costs. Analysis of the 2009 Summer Sale data shows that 85% of mailers of Standard Mail Flats also mail at least 30% Carrier Route Flats. By not including Standard Mail Flats in the 2010 Incentive program, these pieces would not be part of the discount threshold. Any Standard Flat that converted to Carrier Route as a result of the incentive program would therefore be eligible to count as new volume, giving the mailer an opportunity to receive a sizable discount for shifting their volume to a product that produces contribution to the Postal Service, even when the discounted revenue is compared to the long run cost. This would greatly increase the profitability of

the 2010 Summer Sale, producing at least \$10 Million in additional contribution (up to \$28 Million in the estimates in section E). It does not make financial sense to discount a product that is already losing money in an attempt to encourage more volume.

The final proposed improvement to the Summer Sale would be to include all mailers, regardless historical volume. In response to PRIR 1, the Postal Service stated that the average cost of registering each mailer was \$1,014. This is a mailer-specific cost, and as such each mailer should have to pay an up-front fee to register for the sale. Further, all mailers, regardless of size, should be able to register and pay the registration fee. That would allow any mailer that felt it could increase its volume through the incentive program to participate. It would reduce the administrative risk for an unsuccessful program by producing revenue for the registration costs up front. It would allow the Postal Service to hire more employees and increase capacity as dictated by the market. Most importantly of all, it would eliminate the concern of discrimination.

g. Data Collection Report

The learning experience of the 2009 Summer Sale provides the Commission with important lessons concerning the Data Report for the 2010 Summer Sale. The following list contains some potential improvements

- Additional volume sent by MSPs should be identified by product
- The Anyhow Volume, using the established commission methodology, should be calculated for each mailer
- The cost and contribution should be calculated for each mailer
- The Postal Service should explain, in a narrative, what industries responded the strongest and weakest
- The Mailer Identification should include an industry identification
- The Postal Service should explain, in a narrative, the relative success of the volume threshold in estimating before rates volumes.

IV. Conclusion

The 2010 Incentive Pricing Program has the potential to be a valuable pricing experiment. The experience with the 2009 Summer Sale has shown that inaccurate thresholds lead to some mailers being unable to participate, while others are granted anyhow discounts. Further, the inclusion of products unprofitable to the Postal Service threatens the value of the Incentive Program as a whole. Finally, the exclusion of mailers based on historical volume creates discrimination. In these comments, the Public Representatives have outlined measures that can, and should, be undertaken to improve the Incentive Program. They are:

1. Limiting “Anyhow Volumes” by Setting More Accurate Discount Thresholds
2. Excluding Standard Mail Products That Do Not Cover Attributable Costs
3. Requiring a Registration Fee to Cover Administrative Costs
4. Allowing All Mailers to Register

Respectfully submitted,

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