

Before the  
**POSTAL REGULATORY COMMISSION**  
Washington, DC 20268-0001

**Rate Adjustment Due to Extraordinary  
Or Exceptional Circumstances**

**Docket No. R2010-4**

**REPLY COMMENTS  
OF  
MAIL ORDER ASSOCIATION OF AMERICA**

These Reply Comments are submitted by the Mail Order Association of America (MOAA) pursuant to Commission Order No. 485.

**Introduction**

The issue of principal concern to MOAA is the relative overpricing of “Standard Mail High Density Flats and Parcels” and “Carrier Route” products proposed in the Postal Service’s Request compared to the prices proposed for Standard Mail “Flats”.

Under the Request, Standard Mail “Flats” would fail by a large margin to meet attributable costs and the Postal Service has also stated that under its Flats Strategy and anticipated future pricing, Flats would not reach break even status for five years subsequent to the anticipated January 2011 implementation of the exigent rates. See Response of the United States Postal Service to Oral Request at the Hearing on August 12, 2010 (Kiefer). Tr.3/462. Response filed August 19, 2010. That is a facially unacceptable timetable. The time to remedy the situation is now.

**The Commission has Unambiguously Concluded that the Rates for Standard Mail Flats are Too Low**

The Commission has unambiguously found that the rates for Standard Mail “Flats” are too low:

The revenues for Standard Mail Flats in FY 2009 failed to satisfy section 3622(c)(2), which requires that each class of mail or type of mail service cover attributable costs and make a reasonable contribution to institutional costs. For the Postal Service to benefit from additional volume, unit costs and unit revenues need to be realigned. For flats to have covered FY 2009 costs, the rates of flats would have needed to be 21 percent higher, ignoring elasticity effects. The lack of a sufficiently high cost coverage directly implicates the requirement of section 101(d), which directs the Postal Service to apportion the costs of the Postal Service on a fair and equitable basis and section 3622(b)(5), which requires that rates must be set to ensure adequate revenues to maintain financial stability.

ACD FY 2009 at 86.

This followed similar findings about FY 2008 results:

In the future, the Postal Service should either reduce the costs of handling flats [referring to “Flats”] or develop a pricing strategy which increases prices sufficiently to recover costs within a reasonable timeframe. The justification for the lower-than-average pricing increases provided by the Postal Service may be applicable for a limited period of time. The Postal Service should provide a long-term strategy to address continued pricing preferences for a product line that lost \$218 million.

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The Commission is concerned with the \$218 million loss for Standard Mail flats [referring to the “Flats” product]

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The revenues for Standard Mail flats (referring to “Flats”) in FY 2008 failed to satisfy 39 U.S.C. § 3622 (c)(2), which requires that each class of mail or type of mail service cover attributable costs and make a reasonable contribution to institutional costs.

Commission ACD FY 2008 at 5.

The lack of a sufficiently high cost coverage may be inconsistent with the policy set forth in 39 U.S.C. § 101(d) ft. nt. Omitted, which directs the Postal Service to apportion the costs of the Postal Service on a fair and equitable basis and 39. U.S.C. § 3622(b)(5), which states that rates must be set to ensure adequate revenues to maintain financial stability.

*Ibid* at 61.

### **The American Catalog Mailers Association Plea to Continue to Under Price Standard Mail Flats Should be Rejected by the Commission**

The American Catalog Mailers Association (ACMA) claims that the record would not support an above-average increase for Standard Mail Flats. ACMA Comments, at 3. To the contrary, the “record” before the Commission not only supports an “above-average” increase for Flats, but provides no support for the less than average increase that the Service has inexplicably proposed. The Service has proposed average increases of 5.6 percent, but an increase of only 5.1 percent for “Flats”<sup>1</sup>. The Service’s and ACMA’s attempts to justify a rate that will leave “Flats” severely underwater are unconvincing.

ACMA’s attempts to raise doubts about the validity of the costs determined by the Commission in its FY 2008 Compliance Determination. ACMA Comments at 4. The costs there approved were based upon improved costing methodologies including improvement in the IOCS that permitted the attribution of mixed mail tallies to the correct shape. Additionally, shape information was collected from the Remote Encoding Centers.

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<sup>1</sup> Throughout ACMA’s comments, there is a lack of consistency in distinguishing between “Flats” as a Standard Mail “product” and “flats” as a description of a mail piece within Standard Mail (and other) products.

In sum, the Commission has approved the Service's costing methodologies and ACMA's complaints should be given no credence in the absence of data showing that the results are in error. ACMA's comments are devoid of any supporting data. Instead, the comments merely rely on unsupported assertions to support rates for Standard "Flats" that will appreciably worsen the Postal Service's already severe financial problems. ACMA Comments at 3-6.

**ACMA concedes that the Flats Strategy does not provide a "plan" to reduce "Flats" costs within a reasonable period, and instead proposes to obscure and ignore the failure of "Flats" to cover costs.**

ACMA concedes that the Flats Strategy presented by the Postal Service fails to show that costs have been or will be reduced. ACMA Comments at 6 – 8. MOAA concurs. See MOAA Initial Comments at 2-3 and VALPAK Initial Comments at 29-32. As VALPAK correctly concludes:

At some unknown time in the future, some of the various initiatives listed in the Flats Strategy hopefully will provide the Postal Service with greater efficiency and a reduction in the cost of Standard Flats, but the current arrangement, whereby the Postal Service subsidizes the prospecting by catalogers, is not tenable. At such time as unit costs are proven to have declined, then in light of their accumulated deficit Standard Flats should start contributing significantly to institutional costs. Until then, responsible rate adjustments should be based on "what is," not speculation about "what might be," with no timelines or targets for profitability.

Valpak Initial Comments at 32.

A question was addressed to Witness Kiefer at the August 12 hearing about a "reasonable" timeline for addressing the Commission's concern about the failure of Flats to cover costs, as expressed in the FY 2009 Annual Compliance Determination. The Postal Service's response is wholly unsatisfactory. The Response acknowledges that "all products should cover their costs". Response of the United States Postal Service to oral Request from the Bench at the Hearing on August 12, 2010 (Kiefer) Tr. 3/462. (The Responses

were filed on August 19, 2010.) The Response also claims that the Service's "pricing proposal makes substantial progress toward that goal." *Ibid.*

The subsequent portions of the Response, however, destroy the claim of "substantial progress". The Service acknowledges that operational improvements "are unlikely on their own to be sufficient to advance Standard Mail [F]lats to full cost coverage." The Service then asserts that Flats would have "a positive cost coverage approximately 5 years after the proposed 5.1 percent exigent increase would take effect" in January 2011. And this five year period is premised upon Postal costs increasing at no more than the CPI, a dubious proposition.

A pricing strategy for "Flats" that will, at best, result in a continuing failure to meet costs for an additional five years is unacceptable. A plan that provides that "Flats" cover attributable costs for what, at the end of another five years, will have been eight years of losses is far too long and should be rejected by the Commission.

After acknowledging that the Flats Strategy cannot be relied upon to lower the costs of Standard Flats, ACMA speculates about whether, when implemented, the Flats Strategy might result in the costs of "5-digit FSS-scheme" flats to be "lower than the cost of Carrier Route flats." ACMA comments at 9. From this speculation, ACMA argues that it would be "more reasonable ... to announce ... the 5-digit rate will be reduced toward the Carrier Route rate." *Ibid* at 10, n.9. Unfortunately, under the Service's proposed rates, that is what would occur, despite any rational support for doing so. The Service has proposed excessive rates for High Density flats and Carrier Route products in order to propose a rate for "Flats" that is clearly too low. There is, however, no basis in the record for either the Service's or ACMA's approach.

## **Standard Mail Flats are Subject to § 3622 (c)(2)**

ACMA argues that the § 3622 (c)(2) “requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable” to such class or type does not apply to Standard Mail Flats. ACMA Comments at 13. That is a perverse reading. The “requirement” factor clearly applies to Flats as a product, *i.e.* the Flats “product” is a “type of mail service” as the Commission has already determined. ACD FY 2009 at 86.

## **ACMA’s Claim that the Use of Standard Mail Flats is Residual to the Use of Carrier Route Provides No Basis for Pricing the Two Products as One, And Destroys its Argument that Mailers Would be Unduly Harmed by Pricing Flats to Cover Attributable Costs**

ACMA contends “that much of the usage of Standard Regular Flats (one product) is residual to the use of Carrier Route (another product)”. ACMA Comments at 13. From this ACMA argues, with no attempt to provide supporting data, that the “product definitions at issue are not well aligned with what is happening in the market ....” ACMA Comments at 13. The Comments of the Users of Flat-Shaped Mail make the same argument, *i.e.* that “the contribution of catalogs is best measured by summing the contribution of” Standard Mail “Flats” and Carrier Route. Comments at 27. The argument is entirely specious. The approach would merely ignore the wide cost coverage disparities between the two established “products”; not eliminate them. It represents a head-in-the-sand approach which would result in large Postal Service losses by the simple, and foolish, expedient of pretending that they do not exist.

Just as important, accepting its accuracy, the claim that mailers’ use of Standard Flats is residual to the use of Carrier Route, undercuts the ACMA claim that a remunerative Flats rate will severely harm mailers. To the extent that mailers use both the Standard Mail Flats and Carrier Route products, the proposed rates for both must be considered in assessing claims of harm. ACMA has made no attempt to do so.

In any event, the established Standard Mail “products” must serve as the basis of the rates established by the Commission in this proceeding. The extensive speculation by ACMA of what could have been in the past, or perhaps should be in the future, cannot change the fact that the Standard Mail “Flats” product has long failed to produce sufficient revenues to cover its attributable costs. This continuing, and severe, drain upon Postal Service finances should not be allowed to continue.

**The Commission Must Act on the Basis of the Record Before it and Without Consideration of Possible Congressional Action or Claimed “Multiplier Effects”**

ACMA contends that better information on elasticity is needed. ACMA Comments at 14-16. That may be the case, but rates must be set on the basis of the record before the Commission. ACMA’s argument that the elasticity calculated by the Postal Service is “well below ... what most catalogers believe they exhibit” does not constitute a basis for relying, on what ACMA characterizes as “informed judgment,” but which are, instead, obviously self-serving contentions by mailers attempting to avoid rates that cover costs. ACMA has offered at best only anecdotal information on the volume effects of a rate increase. ACMA Comments at 5. Such information provides no basis for a Commission decision. The record is the record and ACMA has presented no basis for ignoring costs or demand as presented in the Postal Service’s Request.

ACMA arguments about “multiplier effects” provides no support for continuing to tolerate underwater rates for Standard Mail “Flats”. Whatever the effect, which ACMA has made no attempt to quantify, it exists equally for those Standard Mail products that have high cost coverages, *i.e.* multiplier effects should act as an equal downward pressure on the Standard Mail products that fully cover attributable costs and make a large contribution to institutional costs.

In its conclusion, ACMA argues Congress “should rectify the situation” by the appropriation of CSRS funds. ACMA Comments at 17-18. First, whatever the effect that possible Congressional funding may have upon the Postal Service’s

Request can have no effect upon the Commission's decision unless and until it occurs. More important, whatever relief that Congress may grant would not change the stark reality that Standard Mail "Flats" are not generating sufficient revenue to cover attributable costs. The rates are too low and possible Congressional funding would not alter that reality. The underwater "Flats" rates should be corrected regardless of possible Congressional funding relief.

### **The Proposed Rates for Standard Mail Fail to Comply With the Requirement for "Efficient and Economic Management"**

Much controversy in this proceeding has revolved around the issue of whether the Postal Service is in compliance with the provisions of 39 U.S.C. § 3622 (d)(1)(E) which authorize rate increases in excess of the price cap only in the event that the "adjustment is reasonable and equitable and necessary to enable the Postal Service, under best practices of honest, efficient, and economic management, to maintain and continue postal services."

Whatever the Commission may decide about whether an exigent increase is authorized under that provision, it is clear that the rates proposed by the Postal Service for Standard Mail Flats are not "reasonable and equitable" and do not reflect either "efficient" or "economic" management. The Service has proposed below average increases for the money losing Flats product, rate increases that are only minimally higher than those proposed for the profitable Carrier Route product. The unreasonable and inequitable rate relationship between Flats and Carrier Route should be remedied.

ACMA has joined in the Comments of the Affordable Mail Alliance. Those Comments argue in part the Service has not complied with best practices of "honest, efficient and economic management", a debatable proposition. Clearly, however, the Postal Service has not met that standard in the rates that it has in the past set and is now proposing for Standard Mail Flats. Instead, the rates have served to increase volumes from the money losing "Flats" product and reduce volumes from the profitable Saturation/High Density and Carrier Route products. As set forth in the Initial Comments of MOAA, the failure of the Postal

Service to set rates for Standard Mail Flats that cover attributable costs has resulted in a shortfall of \$622 million for FY 2009 with an estimated additional shortfall of \$764 million in FY 2010-2011. The Commission cannot assume the management of the Postal Service, but it can prevent the Service from continuing the self-destructive pattern of setting rates for Standard Mail “Flats” that have severely worsened its financial position.

### **The Rates for Standard Mail Flats Should be Increased Well Above the 5.1 Percent Proposed by the Postal Service**

The Comments of the Public Representative contend that the Commission should “mandate at least a 7.0 percent increase for Standard Mail Flats.” Comments at 48-49. The recognition by the Public Representative that the proposed rate increase is too low is welcome. A rate increase of 7 percent, however, would result in continuing large losses and would offer no chance of Flats reaching break even in the two to three year period suggested by the Commission. Tr. 3/462.

An increase of 16 percent would be required just to bring Flats to break even, an increase which should result from the record before the Commission. Neither the Postal Service nor ACMA have provided record support for not increasing rates by the 16 percent that would be necessary to cover attributable costs. At absolute minimum the rate increase for Standard Mail Flats should be a multiple of the proposed rate increase. The abscess in Postal finances represented by the drastic under pricing of Standard Mail “Flats” should at least begin to be closed before doing further damage to the Postal Service and mailers.

### **Conclusion**

During this proceeding, despite being pressed by the Commission, the Postal Service has failed to advance a credible explanation for a pricing policy that encourages the growth of “Flats” a money losing product that has resulted in the loss of hundreds of millions of dollars and will continue to lose hundreds of

millions of dollars under the rates proposed by the Service. In its Compliance Determination for FY 2009, the Commission afforded the Service a possible out in continuing to under price Flats, i.e. a “plan” including a “specific timeline” for achieving a “positive contribution” for Flats. Determination at 86-87. The Postal Service has conspicuously failed to supply such a plan. Even ACMA in supporting an apparently indefinite continuation of prices for Flats that are far below attributable cost levels has concluded that the Flats Strategy “plan” fails to provide any hope within a reasonable time that Flats will recover at least attributable costs, let alone make a reasonable contribution to institutional costs.

In sum, the Postal Service’s proposed rates for Standard Mail Flats do not comply with the policies of the PAEA and represent a defiance of the Commission’s Compliance Determinations. The Commission should ensure that Standard Mail rates for Flats are raised and the resulting revenue used to provide more reasonable rates for the Saturation/High Density and Carrier Route products.

Respectfully submitted,

DAVID C. TODD  
Patton Boggs LLP  
2550 M Street, NW  
Washington, DC 20037  
dtodd@pattonboggs.com  
Counsel for Mail Order Association of America

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