Postal Regulatory Commission
Submitted 2/17/2011 2:29:53 PM
Filing ID: 72001
Accepted 2/17/2011

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON DC 20268-0001

ANNUAL COMPLIANCE REPORT, 2010	))	Docket No. ACR2010

REPLY COMMENTS OF
MAGAZINE PUBLISHERS OF AMERICA, INC.,
ALLIANCE OF NONPROFIT MAILERS
AND AMERICAN BUSINESS MEDIA

David M. Levy
Matthew D. Field
VENABLE LLP
575 Seventh Street, N.W.
Washington DC 20004
(202) 344-4732

Counsel for Magazine Publishers of America, Inc., and Alliance of Nonprofit Mailers

Clark Pettit
President/CEO
AMERICAN BUSINESS MEDIA
675 Third Avenue
New York, NY 10017-5704
(212) 661-6360

For American Business Media

February 17, 2011

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON DC 20268-0001

ANNUAL COMPLIANCE REPORT, 2010	))	Docket No. ACR2010

REPLY COMMENTS OF
MAGAZINE PUBLISHERS OF AMERICA, INC.,
ALLIANCE OF NONPROFIT MAILERS
AND AMERICAN BUSINESS MEDIA

Pursuant to Order No. 636, Magazine Publishers of America, Inc. ("MPA"), Alliance of Nonprofit Mailers ("ANM") and American Business Media ("ABM") respectfully submit these reply comments. These comments respond to the portions of the initial comments of Valpak Direct Marketing Systems, Inc., and Valpak Dealers Association, Inc. ("Valpak") concerning Periodicals mail. As in many previous dockets since the enactment of the Postal Accountability and Enhancement Act ("PAEA"), Valpak requests that the Commission raise periodical rates above the CPI cap. Valpak at 23-39, 49-55. MPA *et al*. have explained repeatedly why Valpak's position is without merit.[1] Valpak's latest rehash of these arguments has no more merit than its predecessors.

---

[1] *See* Docket No. RM2007-1, Comments of ANM and MPA (April 6, 2007) at 2-12; *id*., ABM comments (April 6, 2007) at 3-4; *id*., NNA comments (April 6, 2007) at 3-10; USPS comments (April 6, 2007) at 22-23; *id*., Reply Comments of ANM and MPA (May 7, 2007) at 2-6; *id*., ANM-MPA Reply Comments (July 3, 2007) at 6-7; *id*., Reply Comments (Oct. 9, 2007) at 6-7; Docket No. ACR2007, ANM-MPA Comments (Jan. 30, 2008) at 9-10; *id*., ANM-ABM-Dow Jones-MPA-McGraw Hill Reply Comments (February 23, 2008) at 9-23; Docket No. RM2008-4, Reply Comments of MPA, ANM and ABM (Nov. 14, 2008); Docket No. ACR2008, Reply Comments of MPA and ANM (Feb. 13, 2009), *passim*; Docket No. ACR2009, Reply Comments of MPA and ANM (Feb. 23, 2010), *passim;* Docket No. ACR2010, Comments of MPA-ANM-ABM (Feb. 2, 2011) at 3-7, Appendix A.

COMMENTS

I. THE FAILURE OF A CLASS OF MAIL TO COVER ITS REPORTED COSTS GIVES THE COMMISSION NO AUTHORITY TO IMPOSE OR APPROVE ABOVE-CPI RATE INCREASES FOR THE CLASS.

The basic defect in Valpak's position is that the failure of a class of mail to cover its attributable costs does not give the Commission authority to impose or approve above-CPI rate increases for the class. The "requirement" of 39 U.S.C. § 3622(c)(2) that each class cover its attributable is codified only as one of the “factors” of section 3622(c), not as an absolute requirement. *Cf*. Valpak at 49-50. Like the other “factors” and “objectives” of sections 3622(b) and (c), section 3622(c)(2) is subordinate to the CPI-based price cap and the two other quantitative pricing standards established by PAEA. As the PRC recently held in Docket No. RM2009-3:

> These differences necessarily lead to differences in how the quantitative and the qualitative standards are to be applied in the modern system of ratemaking. Quantitative pricing standards are at the top of the statutory hierarchy. Next in the hierarchy are the qualitative “objectives” listed in section 3622(b), followed by the qualitative “factors” listed in section 3622(c). Under this hierarchy, violations of the three quantitative pricing requirements are “out of bounds.” The Postal Service has broad flexibility to develop prices to achieve the qualitative objectives and factors of sections 3622(b) and (c) so long as its prices are “in bounds” because they satisfy these quantitative requirements.

Order No. 536 at 36.[2] Hence, if the CPI cap of section 3622(d) is at odds with the attributable cost floor of section 3622(c)(2), the cap trumps the floor.

[2] Apart from the CPI cap, the other two “quantitative pricing requirements” are the limit on workshare discounts (39 U.S.C. § 3622(e)), and the revenue ceilings for the various categories of preferred mail (39 U.S.C. § 3626).

Nor can a substantive ratemaking standard be bootstrapped from the remedial provisions of 39 U.S.C. §§ 3653 and 3662 (Valpak at 24-25). Section 3653 is merely an enforcement mechanism, and does not establish substantive ratemaking standards in its own right. The Commission may take action against a rate under section 3653 only if the rate was in noncompliance with the "applicable provisions *of this chapter* [i.e., chapter 36 of Title 39] (or regulations promulgated thereunder)."[3] 39 U.S.C. § 3653(b)(1) (emphasis added). The remedial provisions of 39 U.S.C. § 3662 in turn may be invoked in an annual compliance review proceeding only upon such a finding of noncompliance. *Id*., § 3653(c). Without any independent basis for a finding of noncompliance, no remedial action by the Commission under § 3653 or 3662 is "appropriate" under § 3653(c).

Valpak cannot plug this hole by invoking 39 U.S.C. § 101(d). *Cf*. Valpak at 23, 30, 31 and 49. Section 101(d), which was added to Title 39 by the Postal Reorganization Act of 1970, establishes a "policy" that postal rates "shall be established to apportion of the costs of all postal operations to all users of the mail on a fair and equitable basis." Whatever the meaning and significance of this general policy statement vis-à-vis the more specific provisions of section 3622,[4] section 101(d) is part of chapter 1 of Title 39, not chapter 36, and thus cannot provide the basis for a finding of noncompliance under section 3653. *Id*., § 3653(b)(1).

[3] Docket No ACR2010, MPA-ANM-ABM Comments (Feb. 2, 2010) at A-6 to A-7; Docket No. ACR2008, ANM-ABM-Dow Jones-MPA-McGraw Hill Reply Comments (Feb. 23, 2008) at 14-15; Docket No. R2008-1, Comments of ANM-ABM-Dow Jones-MPA-NNA (March 3, 2008) at 13; Docket No. RM2008-4, MPA-ANM-ABM Reply Comments (Nov. 14, 2008) at A-7; Docket No. ACR2009, PostCom-ANM-DMA-MPA-NPPC Reply Comments (February 23, 2009) at 17-18.

[4] *See Mail Order Ass'n of America v. USPS*, 986 F.2d 509, 515 (D.C. Cir. 1993) (specific provision preferred over general one).

In sum, the Commission has no authority to order an increase of "16.0 percent"—or any other rate increase that exceeds the CPI-based cap—on periodicals rates. *Cf*. Valpak at 54-55.

II. VALPAK'S QUANTIFICATION OF LOSSES FROM PERIODICALS ARE INACCURATE. FURTHERMORE, THE MAIL SENT BY PUBLISHERS BENEFIT THE POSTAL SERVICE AND OTHER MAILERS.

Valpak's elaborate calculation of the losses supposedly suffered by the USPS from Periodicals Mail (Valpak at 26-27, 34-39) begs the question of whether the calculated losses were based on economically sound benchmarks. They were not.

As explained in our initial comments, revenues for Periodicals Mail in FY 2010 failed to cover estimated long-run attributable costs (as estimated using PRC methods) only because the Postal Service has failed to limit its costs to efficient and economical levels. From FY 1996 (the last year in which Periodicals revenues covered reported costs) to FY 2010, the estimated unit costs of Periodicals have increased by more than double the rate of inflation during the same period. Had the increase in Periodicals unit costs been held to the rate of inflation, FY 2010 Periodicals revenues would have covered reported costs. Particularly troubling is that limiting increases in Periodicals unit costs to inflation during this period should not have been difficult. During this period, both automation of the flats mailstream and the amount of worksharing increased substantially, and there were no offsetting trends that should have increased costs. MPA-ANM-ABM Comments at 7-14

Furthermore, Valpak conveniently ignores that in the presence of excess capacity (the presence of which the Postal Service repeatedly acknowledged in Docket

No. R2010-4 and other recent proceedings),[5] the marginal or incremental costs of output in the short run—i.e., the period until the excess capacity can be productively disposed of or redeployed—are well below the long-run marginal or incremental costs measured by USPS costing systems. Despite the troubling trends in Periodicals reported costs, Periodicals revenues covered short-run attributable costs in FY 2010. *Id.* at 15-18.

Instead of confronting these issues, Valpak tries to brush them off on the theory that "Periodicals costing has been found accurate" by the Office of Inspector General ("OIG").[6] Valpak at 40. The actual finding of the OIG, however, was much more modest: "data collection systems and procedures accurately attribute costs to Periodicals *based on the existing cost attribution models*." OIG Report at 2 (emphasis added). The OIG made no attempt to verify the soundness and accuracy of the "existing cost attribution models" themselves, and whether those models produce accurate estimates of Periodicals costs. Rather, the OIG simply noted that the Commission reviews data and changes in costing systems. *Id*.

Furthermore, the OIG report provides additional evidence of the Postal Service inability to control its costs for handling Periodicals:

> Increases in manual processing costs attributed to Periodicals require further investigation. For example, manual processing costs attributed to Periodicals increased by 4.5 percent ($10.4 million) and 3.6 percent ($8.6 million) in fiscal years (FYs) 2008 and 2009, respectively, even though Periodicals Outside County flats volume declined by 3.6 percent and 8.6

[5] In its Initial Comments (at 4), the American Postal Workers Union also admits to the presence of "underutilized capacity."

[6] USPS OIG, Periodicals Cost Report (Report No. CRR-AR-11-001) (December 7, 2010) ("OIG Report").

> percent in FYs 2008 and 2009, respectively. In addition, Periodicals mail is now being prepared more efficiently (co-mailing, co-binding, copalletization, and sack reduction) and mailers have increased the percentage of presorted Periodicals volume to levels that should require little to no automated or manual processing.

Id. at 2. The OIG also found examples of Postal Service practices—the Hot 2C program (in which selected publications are provided with expedited mail processing) and manual processing of pieces entered after critical entry times ("CETs") —that needlessly increase Periodicals costs. OIG Report at 3-4. As explained in our initial comments as well as comments submitted by individual publishers, publishers have not asked for, and do not expect, manual processing in these circumstances. These practices should be discontinued and their associated costs eliminated. MPA-ANM-ABM at 12-13 n. 10; Time Inc. at 7-9.

Finally, Valpak's claim that the purported losses from Periodicals Mail hurt other mailers (Valpak at 50-51) is factually untrue. Studies performed by MPA, CDS Global (the largest provider of fulfillment services for the magazine publishing industry), and the Postal Service have all found that Periodicals publishers make significant use of high-contribution First-Class Mail and Standard Mail products. The contribution from these higher-markup complements to Periodicals Mail more than offsets any conceivable losses to the Postal Service from Periodicals Mail itself. MPA-ANM-ABM Comments at 19-21.

III. THE SUPREMACY OF THE CPI CAP IS NOT A "GRIEVOUS MISTAKE" IN NEED OF REPAIR, BUT THE LINCHPIN OF PAEA.

Valpak requests in the alternative that if the Commission determines that PAEA does not authorize it to order above-inflation rate increases in situations where attributable costs for a class of mail exceed revenues, the Commission should "urge that Congress act immediately to correct such a grievous mistake." Valpak at 55. The Commission should reject this fallback request as well.

The current statutory hierarchy—in which the CPI-based price cap trumps cost coverage factors and the attributable cost floor—is necessary to promote efficiency because a hard CPI cap forces the Postal Service to deal with its cost problems not through rate increases, but through improved cost control. As the Commission found in Docket No. R2010-4, the

> modern system of regulation adopted by the PAEA . . . imposes a price cap on rates tied to inflation. It is designed to incent the Postal Service to reduce its costs and improve efficiency, while creating predictable and stable rates.

Order No. 547, Docket No. R2010-4 (Sept. 30, 2010) at 64, petition for review pending, *USPS v. PRC*, No. 10-1343 (D.C. Cir.). Preserving this incentive for efficiency is especially critical for Periodicals Mail, whose reported costs exceed revenues only because of the Postal Service's chronic failure to control its costs for handling flat-shaped mail.

CONCLUSION

For the reasons explained above, and in the February 2 initial comments of the undersigned parties, the remedies proposed by Valpak for Periodicals Mail should be denied.

Respectfully submitted,

David M. Levy
Matthew D. Field
VENABLE LLP
575 Seventh Street, N.W.
Washington DC 20004
(202) 344-4732

Counsel for Magazine Publishers of America, Inc., and Alliance of Nonprofit Mailers

Clark Pettit
President/CEO
AMERICAN BUSINESS MEDIA
675 Third Avenue
New York, NY 10017-5704
(212) 661-6360

For American Business Media

February 17, 2011