

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Annual Compliance Report, 2010

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Docket No. ACR2010

**VALPAK DIRECT MARKETING SYSTEMS, INC. AND
VALPAK DEALERS' ASSOCIATION, INC.
REPLY COMMENTS ON THE UNITED STATES POSTAL SERVICE
FY 2010 ANNUAL COMPLIANCE REPORT
(February 17, 2011)**

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TABLE OF CONTENTS

Page

Introduction. 2

I. The American Catalog Mailers Association Unpersuasively Grasps at Every Straw to Justify the Continued Subsidy of Underwater Flats by Other Mailers. 2

II. The Attempt by MPA *et al.* to Ask the Commission to Denigrate the Entire Postal Cost Attribution System in Order to Present Periodicals as Being a Profitable Class of Mail and Prevent Strong Remedial Action Designed to Improve Coverage Now Should Be Rejected. 13

III. Time, Inc. Correctly Criticizes Intra-Class Periodicals Pricing, but Fails to Analyze Properly the Commission’s Power under Section 3662(c). 21

IV. The Rate Cap Required by 39 U.S.C. Section 3622(d)(1)(A) Does Not Apply to the Commission’s Remedial Powers under 39 U.S.C. Section 3662(c). 26

Conclusion. 32

Appendix A

INTRODUCTION

On December 29, 2010, the Postal Service filed its Annual Compliance Report for FY 2010. The Commission issued Order No. 636 on January 4, 2011, setting February 2, 2011 as the deadline for initial comments and setting February 17, 2011 as the deadline for reply comments. Valpak Direct Marketing Systems, Inc. and Valpak Dealers’ Association, Inc. (“Valpak”) submitted initial comments and submit the following reply comments.

REPLY COMMENTS

I. The American Catalog Mailers Association Unpersuasively Grasps at Every Straw to Justify the Continued Subsidy of Underwater Flats by Other Mailers.

Comments of the American Catalog Mailers Association (“ACMA”) raised many issues, but few were grounded in recognizable legal principles. On the one hand, ACMA

admits that coverage for Standard Flats “for FY2010 is 81.59 percent” — a coverage with which they are “disappointed.” ACMA Comments, p. 2. However, it claims “the situation ... is not as bad as the ... cost coverage figures suggest.” *Id.* ACMA seems to argue, *inter alia*, that: (a) the Commission should disregard its current definition of products to evaluate hypothetical products (ACMA Comments, section II); (b) the current practice applying the Postal Accountability and Enhancement Act’s (“PAEA”) “preferred category” rules is incorrect (*id.*, section III); (c) Commission-approved postal costing is wholly unreliable and cannot be used to evaluate when products are underwater (*id.*, section IV); and (d) desired policy outcomes should govern legal considerations (*id.*, section V). These arguments are addressed, *infra*.

A. The Commission’s Designations of Postal Products Cannot Be Disregarded When It Suits Users of Standard Flats.

ACMA states:

The Postal Service has chosen to designate Regular Standard Flats, inclusive of Nonprofit, as a product, for which a traditional cost coverage is estimated. [ACMA Comments, p. 2 (footnote omitted).]

Title 39 does not say how products should be defined. [*Id.*, p. 3.]

One approach would be ... Carrier Route would not be separated from 5-digit.... [*Id.*, pp. 3-4.]

ACMA seems to believe that the current product list can be disregarded by the Commission, and that the Commission should “reassembl[e] the revenue and cost information” so as to

evaluate the coverage of a new, hypothetical, non-existent, hybrid product which it labels

“Commercial Standard Flats”¹:

- (i) taking part of the Standard Flats Product (excluding nonprofit mail);
- (ii) combining it with part of the Carrier Route Flats Product (excluding nonprofit mail); and
- (iii) possibly including High Density Flats (from the High/Density and Saturation Flats Product). [ACMA Comments, p. 4.]

ACMA finds that coverage of its hypothetical product would be 109.57 percent, or higher if High Density Flats were included. Even if nonprofit mail were included, it states that coverage would be “slightly higher than 100 percent” according to the Postal Service. ACMA Comments, p. 4, n.2.

ACMA overlooks the fact that the Postal Service did not establish postal products unilaterally, but submitted its proposed product list to the Commission (U.S. Postal Service Submission of Initial Mail Classification Schedule in Response to Order No. 26 (Sept. 24, 2007) in Docket No. RM2007-1), and, in response, the Commission published the initial Mail Classification Schedule (“MCS”) in Order No. 43 (“Order Establishing Ratemaking Regulations for Market Dominant and Competitive Products”) (Oct. 29, 2007). Should ACMA believe that the Commission’s postal product lines need revision, it should file comments in pending Docket No. RM2011-8 (“Mail Classification Schedule”) which is considering establishing details of the MCS. *See* Order No. 666 (Feb. 7, 2011). Changes in

¹ L.L. Bean criticizes the Postal Service for suggesting regrouping Carrier Route and Standard Flats together as a way to “disguise the problem so as to perpetuate the cross subsidy, at the expense of profitable Standard Mail products.” Initial Comments of L.L. Bean, Inc., p. 9, n.2. Valpak agrees.

the MCS must be made pursuant to 39 C.F.R. sections 3020.90, *et seq.* — not in the context of an annual compliance review.

However, even if the Commission were to disregard the definition of products in the established Mail Classification Schedule, prices for the hypothetical ACMA product of Standard Flats/Carrier Route Flats are much too low.² As demonstrated in Table 1, *infra*, the losses from 7 billion Standard Flats are so huge that they almost swallow up all the contribution provided by 9.4 billion Carrier Route Flats. Put another way, the 8.3 cents of per-piece losses from Standard Flats about offsets the 7.0 cents of per-piece gains from Carrier Route Flats. It may be true that the contribution of this ACMA hypothetical product (less its other proposed nonprofit adjustment) is more than breakeven — but barely so, at 101.72 percent.

² For purposes of this analysis, we set aside the ACMA's creative idea of disregarding the accepted application of 39 U.S.C. section 3626 with respect to nonprofit rates, but discuss that proposal briefly in section I.B below.

Table 1
Profitability of Current Standard Mail Products Contrasted with
ACMA Hypothetical Combined Carrier Route/Flats Product

	Revenue (\$, millions)	Attributable Cost (\$, millions)	Cost Coverage
All Standard Mail	17,330.4	11,818.4	146.64%
Carrier Route Product	2,223.0	1,559.8	142.51%
Flats Product	2,579.4	3,161.3	81.59%
ACMA Hypothetical “Commercial Standard Flats” Product	4,802.4	4,721.1	101.72%
Target Revenue	6,923.09		146.64%
Average Price Increase to Achieve Target	44.16%		

Surely, ACMA could not believe that the Postal Service can survive as an institution with **16.4 billion pieces of Standard Mail** — overwhelmingly advertising, mostly catalogs — making virtually **no contribution to institutional costs**. These pieces are 10 percent of all market dominant mail. If these 16.4 billion pieces of Standard Mail were given a pass on making a contribution to institutional costs, from whence would the revenue to cover such substantial costs be otherwise derived? The truth is that these institutional costs are being paid currently by other mailers whose burden is not even acknowledged in ACMA’s comments. (Among the mailers subsidizing ACMA’s Standard Flats are High Density/Saturation Flats and Parcels with a high coverage of 223.81 percent, and High Density/Saturation Letters with a high coverage of 211.44 percent, as well as high coverages for most First-Class Mail products.)

In this docket, one large mailer of Carrier Route Flats, L.L. Bean, has apparently reached the breaking point in watching the Postal Service allow its brother cataloguers to be subsidized, and urges a Commission response to the unsustainable status quo. L.L. Bean Initial Comments, p. 12 (“Instead of postponing the day of reckoning, the process of transitioning those rates to full cost coverage and **a reasonable contribution should begin now**, allowing a graduated and predictable phasing toward that objective.”) (emphasis added). Likewise, the Public Representative also urges that the Commission act now. Public Representative Comments, pp. 5-6 (“The economy has improved since the Postal Service has proposed a 5 percent increase for flats. There is, thus, no reason why a price increase approaching five-percent could not be borne by the users of the standard flats product.”).

When the Postal Service is losing billions of dollars each year, it is a simple financial imperative that these 16.4 billion pieces of Standard Mail Carrier Route and Flats be called upon to make a reasonable contribution to institutional costs. What would constitute a reasonable contribution? The systemwide coverage for all market dominant products is 165.17 percent. The average coverage of Carrier Route Flats is 142.51 percent. Including the losses on Standard Flats (and Standard Parcels/NFMs), the average coverage for all Standard Mail is 146.16 percent. (All of these coverages are well less than the coverage for either saturation mail product.) Any of these coverages could be used. If ACMA’s hypothetical product were asked to provide the average Standard Mail coverage of 146.16 percent, it would require a rate increase of **44.16 percent** on all Standard Flats and all Carrier Route mail. With this percentage price increase spread evenly over the ACMA hypothetical product, the unit revenue per piece for Carrier Route would need to be increased from 23.6 cents to 34.0 cents, and the

unit revenue per piece for Standard Flats would need to be increased from 36.6 cents to 52.7 cents.

In this way, the hypothetical product posited by ACMA provides a useful device to demonstrate how far under-priced Standard Flats truly are. As against the ACMA hypothetical discussed *supra*, requiring a 44.16 percent increase, the price increase of **11 percent** proposed by Valpak (as the first of two steps toward attaining 100 percent cost coverage) for Standard Mail Flats appears quite reasonable. *See* Valpak Initial Comments, pp. 54 (revised), 71.

B. The Postal Service Cannot Disregard the Provisions of Title 39 Governing Nonprofit Mail Rates.

We will leave it to others to defend the interests of nonprofit mail, but would note in passing that ACMA would seek to change the established manner in which 39 U.S.C. section 3626(a)(6) has been applied by the Commission and the Postal Service. *See* ACMA Comments, pp. 5-6. It claims it is not making “an attack on the Nonprofit subsidy” (*id.*, p. 6), but simply wants to reverse well-established practice³ in order to shift the burden of that “subsidy” to other mailers. ACMA’s position reflects its persistent desire to make any argument necessary to continue the subsidy to its own mail at any cost, consistent with the core of Senator Russell Long’s famous maxim — “Don’t tax me ... tax the man behind the tree.”

³ *See, e.g.*, Docket No. RM2009-3, Commission Order No. 536 (Sept. 14, 2010), which states “Preferred categories revenues are restricted to specified percentages of corresponding regular-rate category revenues (section 3626)” (p. 18). (Note that this docket was limited to issues relating to worksharing.)

C. The System by which Attributable Costs Are Determined Cannot Be Disregarded or Wished Away.

ACMA posits the existence of “excess capacity” in the postal system, created “by the difficulty of reining in costs when volumes decline.” *Id.*, p. 10. ACMA believes that “excess capacity” creates a situation where certain pools of costs are not 100 percent volume variable. *Id.* For this reason, ACMA asserts, “[t]he costs available are **not robust enough** to allow valid conclusions concerning the cost coverage of flats.” *Id.* (emphasis added). ACMA believes that “the current cost system is **not sufficiently refined** to reflect current postal operations or volume loading...” and “the costs are **invalid**” and “**not robust enough** to support a finding of noncompliance....” *Id.*, p. 13 (emphasis added).

ACMA believes that “the Postal Service has made progress in [cost cutting], but more is needed.” ACMA, p. 12. ACMA now gives slight praise to the Postal Service, terming its cost-cutting as “progress.” Of course, this position must be read alongside ACMA’s position of only seven months ago, when it asserted that the Postal Service’s response to volume declines is tantamount to malfeasance — a position rejected by the Commission⁴:

The Postal Service’s recent cost cutting initiatives represent progress only by comparison with the Postal Service’s own past record. By the standards of efficient private enterprises, they **do not begin to approach** the “best practices of **honest, efficient, and economical management**” required by 39 U.S.C. § 3622(d)(1)(E) as a condition for any exigent rate increase.

⁴ Docket No. R2010-4, Order No. 547, pp. 81-86.

[Motion of Affordable Mail Alliance to Dismiss Request⁵ (Jul. 26, 2010), p. 72 (emphasis added).]

In fact, the Postal Service has demonstrated astonishingly effective cost-cutting efforts in recent years. The remarkable efficacy of Postal Service cost-cutting in addressing declining volumes is detailed in Valpak Initial Comments, Docket No. ACR2010, pp. 4-6. Putting aside the artificial burdens imposed on the Postal Service by PAEA, over the past four fiscal years, in the face of volume declines of unprecedented proportions, the Postal Service made an operating profit of \$604 million.

Moreover, the measure of attributable costs is not just something developed by the Postal Service; it is the combined effort of many talented regulatory economists and government officials over four decades. It is the best costing available. The fact that costing continues to need tweaking⁶ is not sufficient reason for the Commission to repudiate its results because it reveals a product that is deeply underwater. Indeed, if and when costing is improved, it is possible that it would demonstrate that Standard Flats are even further underwater than they are. Until improvements are made, the Commission must consistently apply established costs based on established costing and make such conclusions as required by PAEA.

⁵ The American Catalog Mailers Association, Inc. was a member of and signatory to all filings of the Affordable Mailers Alliance.
<http://www.prc.gov/Docs/69/69286/10-07-26%20AMA%20et%20al.%20motion.pdf>

⁶ See, e.g., Valpak Initial Comments, pp. 61-65.

D. Catalogs Are, after All, Just Another Form of Commercial Advertising Mail.

ACMA concludes with a string of old canards, unsupported by any evidence, to justify its continued subsidy.

1. “Catalogs enhance the value of mail to the recipient.” ACMA Comments, p. 13. This appears to be an effort to invoke the concept of the “mail moment.” ACMA cites no authority to demonstrate that the mail recipient of a commercial advertising catalog values that mail any more than a Valpak envelope with a coverage over 2.5 times higher than the coverage of Standard Flats⁷ — or any other piece of advertising mail, for that matter. Moreover, the value of mail to the recipient applies to the pricing of a product once it covers its attributable costs — not whether it should cover its costs.

2. “Catalogs provide significant social and cultural benefits to America.” ACMA Comments, p. 14. This effort to invoke 39 U.S.C. section 3622(c)(11) is unsupported, but, again, even if true, it is irrelevant to whether catalogs should pay their costs.

3. “Catalog companies originate considerable mail in a variety of products....” ACMA Comments, p. 14. This argument was rebutted by Valpak in Docket No. R2010-4, Reply Comments, pp. 29-35.

4. “The catalog industry remains financially troubled.” ACMA Comments, p. 14. Of course, many industries in America are financially troubled — and the Postal Service more than most of them. Yet, ACMA would have the Postal Service jeopardize its own financial

⁷ Standard Flats coverage of 81.59 percent x 2.59 = High Density/Saturation Letter coverage of 211.44 percent.

health so that the commercial mailers of catalogs may save postage and have greater net profits. This is not an acceptable rationale for below-cost pricing.

Catalogs may be nice, and they have their place, but even a lily⁸ can only be gilded to a limited degree. At the end of the day, catalogs are Standard Mail advertising.

At some point we must return to the requirements of PAEA. The Commission determined two years ago that “[t]he revenues for Standard Mail flats in FY2008 failed to satisfy 39 U.S.C. 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 [and] may be inconsistent with the policy set forth in 39 U.S.C. section 3622(b)(5), which directs the Postal Service to apportion the costs of the Postal Service on a fair and equitable basis and 39 U.S.C. section 3622(b)(5), which states that rates must be set to ensure adequate revenues to maintain financial stability.” FY 2008 Annual Compliance Determination (“ACD”), p. 61 (footnote omitted). The time for Commission action to remedy rates for underwater Standard Flats has arrived.

⁸ “[T]o paint the lily, To throw a perfume on the violet, To smooth the ice, or add another hue, Unto the rainbow, or with taper-light, To seek the beauteous eye of heaven to garnish, Is wasteful and ridiculous excess.” Shakespeare, King John, 1594.

II. The Attempt by MPA *et al.* to Ask the Commission to Denigrate the Entire Postal Cost Attribution System in Order to Present Periodicals as Being a Profitable Class of Mail and Prevent Strong Remedial Action Designed to Improve Coverage Now Should Be Rejected.

A. MPA *et al.*'s Claim that Periodicals Publishers Cover the Long-Run Attributable Cost of the Mail They Enter Is a Red Herring.

In response to the pressing problem of huge annual, recurring losses on Periodicals, Magazine Publishers of America, Inc., Alliance of Nonprofit Mailers, and American Business Media (“MPA *et al.*”) state that:

The notion that Periodicals **publishers** are being subsidized by other users of other products founders on a further and independent ground.... The contribution from higher-markup **complements** to periodicals more than offsets any conceivable losses to the Postal Service from the periodicals themselves. [MPA *et al.* Initial Comments, p. 19 (emphasis added).]

Almost needless to say, publishers are not a class of mail. Nothing contained in the PAEA — the factors, objectives, or elsewhere — provides for assessing profitability by industry or user group. Efforts to divert attention from problems with the Periodicals Class of mail and instead focus on publishers should be viewed as nothing more than a red herring, designed to obscure red ink.

Asserting complementarity among postal products is a common ploy. Postal products are rife with complementarity — mailers use more than one class of mail whenever it suits their purpose. It is not uncommon to observe many types of mailers using multiple classes of mail — to name just a few, (i) banks and credit card companies, (ii) catalog firms, (iii) book clubs, and (iv) continuity shippers. Those that use more than one class sometime seek to receive reductions on some of their mail, and attempt to justify any reduction by invoking

other mail they send with a higher contribution. The legal problem with this argument is that it involves double counting. The contribution from a piece of mail can count only once — not twice — and it properly counts toward the contribution of the class of mail to which it belongs.

In its effort to show that publishers are paying their fair share, MPA *et al.* cite a study of “the postage expenditures of 460 business-to-consumer and business-to-business publications that spend a total of approximately \$1 billion in postage annually.” *Id.*, p. 20. They produce a table which purports to show that those publishers who spent a total of \$1 billion on postage made a grand contribution to institutional costs of only \$16 million, or 1.6 percent. *See* MPA *et al.*, Table 4, p. 21. This 1.6 percent contribution compares with a Postal Service overhead equal to 42 percent of total revenue excluding contribution to the Postal Service Retiree Health Benefits Fund (“PSRHBF”), and 50 percent of revenue when the \$5.6 billion payment to PSRHBF is included. USPS-FY10-1, FY 2010 Public Cost and Revenue Analysis (PCRA) Report, p. 3. In the face of such institutional costs, a contribution that amounts to only 1.6 percent of the total publishing industry postage is negligible, and in no sense is it a fair share of overhead. Of course, the Periodicals Class of mail has made no contribution to the Postal Service’s institutional costs for over 14 years with the Postal Service losing an aggregate \$4.3 billion. *See* Valpak Initial Comments, Table II-2, p. 34. And MPA *et al.* do not explain how prices of the other products publishers use would be increased once the contribution now used to justify low Periodicals Class prices is removed.

Moreover, major differences exist among periodicals mailed. Some publications, especially those with a relatively high percentage of advertising and a large circulation, have a coverage comfortably in excess of 100 percent, while coverage for the entire Periodicals Class

in FY 2010 was only 75.46 percent. This means that some publications, those pulling the average down to 75.46 percent, have a coverage that is much, much lower, perhaps as low as 25-50 percent. Those publications not only fail to pay a fair or reasonable share of the costs which they cause the Postal Service to incur, they do not pay even half of those costs. Collectively, these deeply underwater publications might be referred to as the “Nautilus group.”

If it ever were to be accepted that publishers’ use of other postal products with high coverage should be regarded as offsetting the loss from periodicals, as *MPA et al.* would prefer, it then would follow that the substantial subsidy received by those publications in the Nautilus group would meet the technical definition of a cross-subsidy. Such a cross-subsidy to the Nautilus group would come not from other mailers generally, but from other publications within the Periodicals Class.⁹ It also means that the Postal Service, as well as those publishers providing the cross-subsidy, would be better off if publications in the Nautilus group were to continue to use the mail to solicit subscriptions, while switching to an all-electronic publishing format. That readily available alternative is being used increasingly by publishers.

B. MPA et al. Assert that the Postal Service’s Continuing Losses on Periodicals, which Exceeded \$600 Million in FY2010 and Now Aggregate to Over \$4 Billion, Are “Within Bounds” under PAEA, but Their Implication that the Commission Has No Power to Rectify this Egregious Situation Is Clearly Wrong.

MPA et al. state that “[t]he language, legislative history, and economic policies of Section 3622(d) preclude the Commission from allowing the attributable cost floor to trump the

⁹ *MPA et al.* fail to mention, much less protest, that those cross-subsidies, like any subsidy, tend to protect and promote inefficiency.

rate cap for individual classes of mail” (p. 3). Then, invoking the Commission’s decision in Docket No. RM2009-3, they state, “[t]he Commission has agreed. . . . [holding]¹⁰ that the CPI price cap is one of only three ‘out-of-bounds’ lines established by the PAEA that cannot be violated.” *Id.*, p. 4. The flaws in this legal argument are discussed in section IV, *infra*. But such an argument does great damage to the Postal Service. MPA *et al.*’s implication is that no matter how large the annual or cumulative loss on Periodicals, the PAEA cap leaves the Commission powerless to do anything to reduce those recurring losses from Periodicals.¹¹ Assuming, *arguendo*, the cap trumps everything (a proposition rebutted in section IV, *infra*), the Commission still enjoys two remedies.

The Commission can dramatically restructure rates within the Periodicals Class so as to reduce, and in some cases eliminate altogether, the cross-subsidy to publications in the Nautilus group — *e.g.*, by increasing to 100 percent the passthrough of costs into rates for bundles, sacks, and pallets, along lines the Commission has previously prodded the Postal Service to take. It is long past time that publications in the Nautilus group began to pay a larger and fairer share of the costs which they cause the Postal Service to incur. Until this occurs, publications in the Nautilus group will provide an increasing drag on the more economically healthy publications. *See* discussion in section III.A, *infra*.

¹⁰ In no way could the Commission’s statement in the workshare docket be called a holding as to matters other than worksharing. *See* discussion, *infra*, section III.B.

¹¹ As Valpak noted in its Initial Comments (p. 55), if both the Postal Service and the Commission are as powerless to remedy the large, continuing losses in the Periodicals Class as MPA *et al.* contend, then the Commission, in its forthcoming report to Congress, should cite this problem as a fatal flaw in PAEA.

Second, PAEA clearly states that the Commission can “order the Postal Service to **discontinue** providing **loss-making** products.” 39 U.S.C. § 3662(c) (emphasis added). *See* discussion in section IV, *infra*.

C. MPA *et al.*'s Assertions that Managerial Ineptness and Excess Capacity Co-Exist throughout the Entire Year, and throughout the Entire Postal Service Network, Are Unsupported.

MPA *et al.* make sweeping assertions concerning (i) managerial ineptness within the Postal Service, and (ii) the widespread existence of excess capacity throughout the postal network. For instance:

The excess costs are attributable not to Periodicals mail but to the **actions of Postal Service management** and labor that have made the processing of flat-shaped mail a **disguised relief program for surplus mail processing capacity** that would otherwise be unemployed. ... until the **excess capacity** is eliminated, the Commission needs to treat the costs of the surviving **excess capacity** as institutional rather than attributable to the mail classes where the excess capacity is dumped. [*Id.*, pp. 2-3 (emphasis added).]

MPA *et al.* further assert that pervasive problems of managerial ineptness and excess capacity are both long-standing, extending back many years prior to FY 2010:

major contributors to this problem are **chronic excess capacity** in mail processing facilities, above-inflation compensation increases ... and the Postal Service's **failure to manage its workforce effectively** and reduce its size sufficiently.... This **excess capacity**, and the resulting deployment of underused workers to perform manual processing, are **not new**. [*Id.*, pp. 12-13 (emphasis added).]

As if to give some credibility to their sweeping charges, MPA *et al.* then point to a Postal Service statement in Docket No. R2009-3, claiming that:

In the last **several years**, even the Postal Service has conceded the presence of excess labor. In May, 2009, the Postal Service acknowledged that “there will be **some excess capacity** in virtually all areas of operations” in the **summer of 2009**. [*Id.*, p. 13 (emphasis added).]

MPA *et al.* contend that the statement by the Postal Service concerning excess labor during the **summer of 2009** is an admission of excess labor during the **last several years**. Clearly though, any excess capacity during the summer of 2009 does not establish excess capacity throughout “the last several years.”

MPA *et al.* assume widespread existence of excess capacity over many years based on their concern about the Postal Service’s increased cost of handling and delivering periodicals. Those increased costs are the principal circumstantial evidence offered by MPA *et al.* for the existence of excess capacity during periods other than the summer months.

There could be other reasons for increased costs.¹² A number of years ago, manual handling was a far more predominant method of sorting flats. Since that time, the unit cost of Periodicals has increased at a rate faster than costs in other classes of mail, or the rate of inflation. MPA *et al.* now complain that the unit cost of Periodicals has increased because a high percentage of publications continue to be sorted manually, rather than on newer automation equipment that was not available when manual sortation was more predominant. Although one would expect sortation on the newer flat sorting machines (*e.g.*, the AFSM100 or FSS) to decrease unit cost, the cost of continued manual sortation should not have unduly

¹² See also Office of the Inspector General (“OIG”) Report Number CRR-AR-110001, Audit Report — Periodicals Mail Costs (Dec. 7, 2010). Among other factors, that study found excessive bundle breakage, shrink-wrapping that obscured readability of barcodes, and pieces not machinable.

increased costs over what they were when manual sortation was even more prevalent. Within manual sortation units, higher unit cost should reflect (i) increases in the hourly wage rate, and (ii) the rate at which publications (flats) are sorted. Almost by definition, any increase in unit cost beyond increases in the hourly wage rate and the cost of new equipment reflects a diminution in the sortation rate. Handling flats individually can be an expensive proposition. Could difficulty in reading small print on the address labels now in use by most publications be part of the problem? Could there be other problems sorting the flats submitted by Periodicals? MPA *et al.* refuse to consider any other reason why their costs may have increased. *See also* discussion in section I.C, *supra*.

D. MPA *et al.* Make an Unwarranted Frontal Assault on the Postal Service’s Costing System, Proposing to Use Short-Run Marginal Costs in lieu of Attributable Costs for Periodicals.

Having accurate knowledge about costs is important to operating a profitable business and setting prices. Costs have been the cornerstone of Postal Service pricing under both the Postal Reorganization Act and PAEA. *See* Appendix A. The Commission and the Postal Service have spent the last 40 years developing and refining the costing and attribution system now in place.¹³ In a self-serving effort to avoid proper remedial efforts to improve coverage of the Periodicals Class, MPA *et al.* would jettison the entire costing and attribution system in favor of using short-run marginal costs throughout the year, every year (not just the summer months of 2009 and 2010) — but, apparently, only for the Periodicals Class.

¹³ The Commission has convened Docket No. RM2011-3 to consider, among other things, refinements and updates to the costing system.

In FY 2010, Periodicals mail covered its **short-run attributable costs**, which, during periods of excess capacity, are much lower than the attributable costs reported in the Cost and Revenue Analysis (“CRA”). [*Id.*, p. 3 (emphasis added).¹⁴]

Whatever the actual cause(s), however, the excess costs were **not caused by Periodicals mail**, and hence **cannot be attributed to it**. [*Id.*, p. 7 (emphasis added).]

In addition to resulting in costs bloated above those that would be incurred under “best practices of honest, efficient, and economical management,” the presence of excess capacity has a substantial impact on how costs vary with changes in mail volume and thus **the attributable costs that should be used to estimate cost coverage**. [*Id.*, p. 14 (emphasis added).]

The **presence of excess capacity** that cannot be sold or productively redeployed until the proposed rates next can be increased has major implications on how costs vary with changes in mail volume, and thus **what costs should be attributed to each class and product**. [*Id.*, p. 15 (emphasis added).]

As indicated by the 31 percent increase in unit delivery costs for Periodicals flats between FY 2007 and FY 2010, the delivery network clearly had **excess capacity** throughout FY 2010 and—until these costs are dramatically reduced—will continue to have **excess capacity** into the future. [*Id.*, p. 17 (emphasis added).]

MPA *et al.* would dismiss out of hand the recent finding by the OIG concerning cost attribution in its audit report on Periodicals mail costs:

Postal Service data collection systems and procedures **accurately attribute costs to Periodicals** based on the existing cost attribution models. Specifically, the **costs** used in this process are **reconciled to the financial statements** and the data obtained

¹⁴ MPA *et al.*’s attempt to demonstrate that use of short-run marginal costs would result in coverage exceeding 100 percent is contained in Table 2 on page 18. A critical number in that table is “66.2 %” which in footnote 2 is attributed generally to Appendix B. However, that figure could not be found anywhere in Appendix B.

from the IOCS is consistent with prior year results.

Additionally, the data and any system changes are submitted to the PRC for review and approval. [OIG Report Number CRR-AR-11-001, Audit Report — Periodicals Mail Costs, p. 8 (Dec. 7, 2010) (emphasis added).]

The OIG’s report alone is sufficient reason to reject the self-serving assertion by MPA *et al.* that the existing cost attribution system be jettisoned in favor of one designed explicitly to reduce the attributable costs of periodicals. It also reinforces the view that the Periodicals Class is a big money loser, for the Postal Service and for other mailers as well.

Adopting a new, untried and untested system for cost attribution would be a huge mistake. Moreover, the Annual Compliance Review is not the time or place for such a proposal. If and when any new system for cost attribution were ever adopted, it must be applied uniformly to all classes of mail, not just to Periodicals. Further, if a new system were to reduce substantially the level of cost attribution, procedures for allocating overhead costs would need to be reviewed critically because, ultimately, prices must produce revenues sufficient to cover total costs, not just short-run marginal costs. The merits of every overhead allocation factor, including the “educational, cultural, scientific, and informational” provision, would have to be examined anew.

III. Time, Inc. Correctly Criticizes Intra-Class Periodicals Pricing, but Fails to Analyze Properly the Commission’s Power under Section 3662(c).

A. Time, Inc. Correctly Identifies the Postal Service’s Failure to Recognize Less Efficient Mail Preparation in Its Pricing.

Time, Inc. (“Time”) again raises the issue of the Postal Service not responding to Commission admonitions to increase the passthroughs of less efficient container and bundle preparation and to recognize those costs in its pricing. Specifically, Time criticizes the Postal

Service's intra-class pricing decisions which have not given mailers the correct price signals to enter low-cost mail and eschew high-cost mail:

In its FY 2009 ACD (issued March 29, 2010), the Commission stated (at 76) that “[t]here are ... current opportunities for the Postal Service to improve Periodicals cost coverage by **modifying container and bundle passthroughs**.” It gave detailed examples of such opportunities “to improve efficiency and to offer mailers appropriate pricing incentives” and stated that “[t]he Postal Service should implement such changes as soon as practicable.” *Id.* at 86. The Postal Service in its FY 2010 ACR chooses to mention only the Commission's instruction to “develop and present a plan explaining how it intends to increase Periodicals cost coverage to a reasonable level in its next notice of general price adjustments for market dominant products, or its next annual compliance report,” *id.* at 76, which it now claims is impossible to carry out. FY 2010 ACR at 8. As to the Commission's instructions concerning bundle and container passthroughs, the need to reduce manual sorting of Periodicals, to improve cost modeling, to consider “administrative solutions to processing decisions that currently elevate service decisions over cost considerations”-- none of which require increasing Periodicals rates above the statutory price caps or face any legal impediment that we are aware of -- the Postal Service has nothing to say. [Time Initial Comments, pp. 9-10 (emphasis added).]

Time concludes with a request that the Commission:

Assure at least an (80%?) passthrough of the costs identified with each rate element in the Periodicals rate structure, including costs associated with each category of bundle, sack and pallet, as well as costs associated with piece sorting machinability.... [*Id.*, p. 22.]

Valpak agrees. Valpak has also been encouraging the Postal Service to take action by properly incentivizing more efficient Periodicals preparation through cost passthroughs. *See, e.g.*, Docket No. ACR2009, Valpak Reply Comments, pp. 22-24; Docket No. ACR2010, Valpak Initial Comments, pp. 37-38.

Once the Commission makes a determination of noncompliance **in this docket**, in crafting a remedy adjusting Periodicals prices, the Commission can require the Postal Service to structure prices to reflect adequately the additional costs of less efficient mailer preparation in this docket. As Valpak urged earlier, “To the extent possible, these price increases should be focused on the least profitable components of Periodicals.” Valpak Initial Comments, p. 55. *See also* Docket No. R2011-2, Order No. 675, p. 47.

B. Time, Inc. Interprets PAEA as Mandating Unlimited and Unchecked Subsidies of Underwater Classes, Irrespective of the Harm Done to the Postal Service.

Time’s Initial Comments make two legal arguments requiring response — one with respect to the cap as a limitation upon the power of the Commission under 39 U.S.C. section 3662(c) (an issue addressed further in section IV, *infra*) and the other with respect to the Commission’s supposed resolution of the supremacy of the cap.¹⁵

1. 39 U.S.C. Section 3662(c). Time sets out its understanding of the Commission’s powers where, during an annual compliance review, it makes a “written determination of noncompliance” under 39 U.S.C. section 3653(c). Time accurately states that in such circumstance, the Commission’s remedial powers are those that it has under the complaint provision, 39 U.S.C. section 3653(c). Time Initial Comments, pp. 17-18. Time states:

Rates for a market-dominant class that are above the applicable § 3622(d) annual limitation, and that have not been authorized under either the exigency provision of § 3622(d)(1)(E) or the banking provision of § 3622(d)(2)(C), are made unlawful

¹⁵ In its legal analysis in this docket, Time pulls back significantly from the creative legal positions taken in the last Annual Compliance Determination which were roundly rejected by the Commission. *See, e.g.*, FY 2009 ACD, pp. 14-16.

by the plain language of § 3622(d)(1)(A) and § 3622(d)(2)(A)....
[Time Initial Comments, p. 18.]

Of course, Time focuses attention on the general rule — the cap on price increases under 39 U.S.C. section 3622(d). And section 3622(d) has the two exceptions that Time accurately ascribes to it, neither of which is applicable here.

Time observes:

the nature of “noncompliance” under § 3653 and the scope of the Commission’s **remedial authority** under § 3662(c) remain a source of much **confusion**, misdirected effort, and concern....
[Time Initial Comments, p. 19 (emphasis added).]

Into this confusion, Time asserts:

Section 3662(c)’s statement of remedial authority to “order[] unlawful rates to be adjusted to lawful levels” does not transubstantiate rate levels that exceed the statutory caps into “lawful levels.” [Time Initial Comments, p. 17.]

Time does little to help the Commission with this confusion. Never in Time’s analysis, does it set out a careful analysis of the complete text of section 3662(c)’s remedial authority, based on the text of that section. Valpak analyzes that statute in section IV, *infra*.

2. Commission Order No. 536. Time takes great comfort in the Commission’s Order No. 536 in Docket No. RM2009-3, as evidence that the Commission has “clarified some of the issues surrounding the ratemaking provisions of the PAEA” in recognizing a “statutory hierarchy” in 39 U.S.C. section 3622. Time Initial Comments, p. 21. At no time does Time acknowledge that the purpose of Docket No. RM2009-3 was workshare discounts — in no way related to the proposition which Time believes it has demonstrated.

Docket No. RM2009-3 had a very different purpose indeed. Order No. 192 established the docket “to develop a full record on issues concerning the proper interpretation, scope, and application of section 3622(e).” Order No. 536, p. 1. It was a follow-up docket to Docket Nos. R2009-2 and ACR2008, where issues of workshare cost avoidance were raised but there was insufficient time to address them in the context of a pricing review or annual compliance review. *See* Order No. 192, p. 2. The Commission specifically offered “the Postal Service (and interested persons supporting its rationales) an opportunity to address the legal, factual, and economic underpinnings of the methodologies used by the Postal Service to develop its proposed First-Class Mail and Standard Mail discount rates in Docket No. R2009-2.” *Id.*, p. 3.

Order No. 192 never asked for comment on the meaning and application of 39 U.S.C. section 3622(c)(2) and certainly never asked for comment on the Commission’s powers under 39 U.S.C. section 3662(c). Nevertheless, the Commission took the opportunity to expound generally on PAEA’s structure of the pricing system. It categorized the objectives and factors of section 3622(b) and (c) as “qualitative” and the price cap, workshare discount limitation, and preferred categories as “quantitative.”¹⁶ It never addressed its powers under section 3662(c), and even what it said on matters unrelated to worksharing was *dicta*, not related to the

¹⁶ For example, in Order No. 536, the Commission stated that “PAEA characterizes the quantitative standards as ‘requirements’” (pp. 35-36), but categorizes the requirement in section 3622(c)(2) as qualitative. If the Commission had requested the input of parties on these issues, Valpak might have taken the position that the “requirement” of section 3622(c)(2) makes it a quantitative standard, and thus higher in the “statutory hierarchy.” This demonstrates the danger of Time relying on *dicta*, from a docket where matters now being decided were not before the Commission.

issue in that docket, and certainly not fully briefed and argued by the parties.¹⁷ Therefore, it cannot be considered a binding resolution of the issue now under consideration in Docket No. ACR2010.

IV. The Rate Cap Required by 39 U.S.C. Section 3622(d)(1)(A) Does Not Apply to the Commission’s Remedial Powers under 39 U.S.C. Section 3662(c).

Without any statutory analysis, MPA *et al.* mistakenly assumes that the price cap of 39 U.S.C. section 3622(d)(1)(A) limits the Commission’s remedial powers for noncompliance during annual compliance reviews established by 39 U.S.C. sections 3653(c) and set out in section 3662(c). *See* MPA *et al.*’s Comments, p. 3. Time makes the same mistaken assumption. *See* Time Initial Comments, p. 17. Having made this erroneous assumption, both MPA *et al.* and Time contend that the Commission has no authority “to remedy the effects of noncompliance” by requiring the Postal Service to raise the rates for periodicals above the rate cap set by the Commission in accordance with 39 U.S.C. section 3622(d)(1)(A). Indeed, Time incorrectly argues that such remedial action would be “unlawful,” within the meaning of 39 U.S.C. section 3662(c), because such action does not fit within the parameters of the only two exceptions to the rate cap, as provided in 39 U.S.C. sections 3622(d)(1)(E) and 3622(d)(2)(C). *See id.*, pp. 17-18.

However, in this ACR, the Commission has the full powers under section 3662(c) which states, in full:

¹⁷ MPA *et al.*’s claim that the Commission’s discussion was part of what it supposedly “held” also puts too much reliance on such discussion and overstates the purpose of the discussion and inappropriately relies on it as precedent. *See* MPA *et al.* Initial Comments, pp. 4-5, A-3, A-4.

(c) Action Required if Complaint Found To Be Justified.— If the Postal Regulatory Commission finds the complaint to be justified, it shall order that the Postal Service take such action as the Commission considers appropriate in order to achieve compliance with the applicable requirements and to remedy the effects of any noncompliance (such as ordering **unlawful rates** to be **adjusted** to **lawful levels**, ordering the cancellation of market tests, ordering the Postal Service to **discontinue** providing **loss-making products**, or requiring the Postal Service to make up for revenue shortfalls in competitive products).

For the reasons set out below, these powers are not constrained by the price cap.

A. The Rate Cap Set by the Commission Applies Only to Postal Rate Adjustments Initiated by the Postal Service for Market Dominant Products.

39 U.S.C. section 3622(a) authorizes the Commission “by regulation [to] establish (and from time to time thereafter by regulation revise) a modern system for regulating rates and classes for market-dominant products.” Pursuant to that authority, the Commission has established a system that requires the Postal Service to set a rate for each class of mail, including Periodicals, *inter alia*, to bear the direct and indirect postal costs attributable to each class. *See* 39 U.S.C. section 3622)(c)(2). Before the Postal Service makes any adjustments in those rates, the Postal Service is required to provide public notice of the adjustment and an opportunity for the Commission to review any proposed rate increase to determine whether the proposed increase complies with the rate cap set by the Commission according to a statutorily-prescribed formula. *See* 39 U.S.C. section 3622(d)(1). In its conduct of this review, the Postal Service has the opportunity to justify an increase in excess of the price cap under only two exceptions set forth in sections 3622(d)(1)(E) and 3622(d)(2)(C). If the Postal Service cannot justify an increase according to the limitations of the two exceptions, then Postal

Service may not “adjust rates ... in excess of the annual limitations” set by the Commission pursuant to 39 U.S.C. section 3622(d)(1)(A).

To implement this statutory scheme, the Commission promulgated detailed regulations “establishing **ratesetting policies and procedures** for market dominant products.” *See* 39 C.F.R. section 3010.1 (emphasis added). 39 C.F.R. section 3010.10 recognized that it is the Postal Service, not the Commission, that has the “statutory authority to make ... rate adjustments for a market dominant postal product.” And 39 C.F.R. section 3010.11 states that the Postal Service’s authority to make those rate adjustments is subject to “an inflation-based limitation using CPI-U values as detailed in [39 C.F.R. section 3010.12],” subject to specified exceptions. There is nothing in this regulatory scheme to indicate that the “inflation-based” rate cap applies to any activity other than (i) “ratesetting” initiated by the Postal Service, and (ii) the Commission’s limited review authority to set the price cap and to review a Postal Service proposed price adjustment to determine whether that adjustment complies with the price cap or fits within one or the other exceptions to that cap. *See generally* 39 C.F.R. section 3010.1, *et seq.*

B. The Rate Cap Set by the Commission under 39 U.S.C. Section 3622(d)(1) Does Not Apply to the Commission’s Authority to Remedy the Effects of the Postal Services Noncompliance with the Commission’s Rule of 100 Percent Attributable Costs.

MPA *et al.* has argued that the price cap limits the authority of the Commission to remedy the effects of the Postal Service’s failure to set rates to cover 100 percent of attributable costs to the mailing of periodicals because “PAEA does not allow the Commission to **impose rate increases** that exceed the CPI-based cap on rate adjustments imposed by 39

U.S.C. § 3622(d).” *See* MPA *et al.* Comments, p. 3 (emphasis added). As demonstrated above, the price cap required by 39 U.S.C. section 3622(d) to be set by the Commission does not grant any power to the Commission to propose price increases, much less impose such increases. Indeed, section 3622, read in its entirety, confers upon the Postal Service, not the Commission, the power to set the rates for market-dominant products, limiting the role of the Commission only to review the rate-making process to ensure that the Postal Service complies with applicable statutory and regulatory standards.

Time has argued that the price cap provision in 39 U.S.C. section 3622(d) limits the authority of the Commission to remedy the effects of the Postal Services failure respecting Periodicals mail, because the Commission’s remedial power under 39 U.S.C. section 3662(c) — to “order[] unlawful rates to be adjusted to lawful levels” — is no greater than its reviewing power under 39 U.S.C. section 3622(d). *See* Time Comments, pp. 17-22. As demonstrated above, however, the price cap set by the Commission is an “inflation-based limitation” upon the power of the Postal Service to raise rates for its market-dominant products, **not** a limitation on the power of the Commission to enforce compliance with the policies of Title 39 or to remedy the effects of noncompliance.

C. In 39 U.S.C. Section 3662(c), Congress Granted Broad Remedial Powers to the Commission.

Contrary to the contentions of both MPA *et al.* and Time, 39 U.S.C. section 3662(c), by its plain language, grants to the Commission broad discretion to formulate an “**appropriate** [remedy] to achieve compliance with the applicable requirements **and to remedy the effects** of any noncompliance.” Unlike the Commission’s limited review power under 39 U.S.C. section

3622(d), and the regulations promulgated thereunder, the remedial examples set forth in 39 U.S.C. section 3662(c) represent a range of corrective actions designed, not to limit the Commission, but to illustrate the kinds of remedies that would not only (i) to stop the Postal Service from continuing an activity that the Commission found to be noncompliant, but also (ii) to remedy the effects of noncompliance. Such orders could require the Postal Service “to **discontinue providing loss-making products**” or “to **make up for revenue shortfalls in competitive products.**”¹⁸ (Emphasis added.)

MPA *et al.* would have the Commission believe that “the CPI-based cap on rate adjustments imposed by 39 U.S.C. § 3622(d)” must limit the Commission’s remedial powers in this matter because, otherwise, “the attributable cost floor [would] trump the rate cap for individual classes of mail.” *See* MPA *et al.* Comments, p. 3. This claim overlooks, however, the broad discretionary authority conferred upon the Commission by 39 U.S.C. section 3662(c), which states that the Commission may order the Postal Service take such action as “the Commission considers appropriate.” This language gives the Commission ample authority to consider violation of the policies of Title 39, including the objectives and factors set forth in 39 U.S.C. section 3622(b) and (c), in fashioning a remedy “appropriate” to each case. Such remedial powers are in no way limited by 39 U.S.C. section 3622(d), which applies only to Postal Service-noticed price increases.

Time would have the Commission believe that the parenthetical phrase in 39 U.S.C. section 3662 (c) — “ordering unlawful rates to be adjusted to lawful levels” — somehow

¹⁸ Over 14 years, Periodicals has lost \$4.3 billion. *See* Valpak Initial Comments, p. 34.

incorporates the price cap as a limit beyond which Commission would not be permitted to go in fashioning a remedy for failure to adhere to the policies of Title 39. *See* Time Initial Comments, pp. 17-20. In support of this position, Time quotes the Commission’s brief filed in the pending appeal from the exigent rate case (U.S. Postal Service v. Postal Regulatory Commission (D.C. Cir. 2010)), where the Commission stated that “Congress ... conferred no **general** authority ... to **authorize price increases** above the rate of inflation.” (Emphasis added.) But the **Commission’s general oversight authority** to review Postal Service proposed price increases is quite different from the Commission’s exercise of **remedial authority** in a case involving Postal Service **violation of the provisions and policies of Title 39**.

While the Commission’s authority to review pricing adjustments is restricted, hemmed in by a number of statutory and regulatory provisions, the Commission’s remedial authority is expressed in expansive terms, including the remarkable power “to **discontinue** providing **loss-making products**.” (Emphasis added.) Congress’ choice of the phrase “loss-making products” is an implicit reference to 39 U.S.C. section 3622(c)(2)’s requirement “that each class of mail or type of mail service bear the direct and indirect postal costs attributable to each class or type of mail service through reliably identified casual relationships....” as well as the other provisions of Title 39 which reinforce this same principle. *See* Valpak Initial Comments, pp. 23-24, 49-50.

This aspect of the remedial statute to discontinue “loss-making products” is not analyzed by MPA *et al.* or Time. The term “**loss-making products**” illumines the meaning of “**unlawful**” as it appears in that same section. If the Commission has the power to order an entire market-dominant product discontinued for failure to cover its attributable costs, it

certainly has the power to consider as an appropriate remedy that the product be priced at a level to pay its own way. It would make no sense for Congress to have vested in the Commission the death penalty over “loss-making” products, while withholding from the Commission the power to impose a price increase designed to ensure that the product moves, over two years, to paying its own way, and thereafter making a positive contribution to institutional costs.

CONCLUSION

On February 16, 2011, the Commission issued its decision in Docket No. R2011-2 (“Notice of Price Adjustment”), Order No. 675. Although the Commission limited its review to the price cap and took no action with respect to underwater products in that docket, it did address the problem.

With respect to Standard Mail Flats, the Commission advised the Postal Service to consider comments submitted in that docket critical of underwater Flats:

Commenters raise significant concerns about Standard Mail Flats pricing similar to previous views offered by the Commission. The Postal Service may not have had the benefit of those opinions prior to submitting its Notice. Upon consideration of them, it may wish to amend its filing to address those concerns. [Order No. 675, p. 4.]

With respect to Periodicals, the Commission advised the Postal Service as follows:

The Commission recognizes that the Periodicals class has not covered attributable costs over the past year, and will not do so under the Postal Service’s planned adjustments. The Commission also recognizes, as stated in connection with the worksharing discussion, that the Postal Service’s stated pricing objectives of keeping increases “around the average” impedes

progress toward full cost coverage as it fails to more fully realize the efficiencies in the revised Periodicals structure. [Order No. 675, p. 47.]

Both statements by the Commission are true, and Valpak understands that the short period of time allowed for review of rate adjustments under PAEA does not permit of significant modifications. The time and place to change rates that are not in compliance with PAEA is the Annual Compliance Determination. The Commission must (i) make a formal finding of noncompliance and (ii) take remedial action **in this docket**, and Valpak believes the changes necessarily include bringing Standard Mail Flats and Periodicals at least halfway toward covering their attributable costs.

Respectfully submitted,

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APPENDIX A

It is often stated that PAEA rejected the old and antiquated concept of “cost-based” rates and replaced it with “market-based” pricing. However, it is a mistake to believe that PAEA rejected the importance of costs. A careful examination of provisions in PAEA reveals the importance of costs, expressly, or lurking just below the surface, as demonstrated by the following PAEA provisions.

39 U.S.C. Chapter 1 (Postal Policy and Definitions)

- (1) **39 U.S.C. section 101(a)**: “The **costs** of establishing and maintaining the Postal Service shall not be apportioned to impair the over-all value of such service to the people.” (Emphasis added.)
- (2) **39 U.S.C. section 101(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.” (Emphasis added.)
- (3) **39 U.S.C. section 102(6)** defines a “product” as “a postal service with a **distinct cost** or market characteristic for which a rate or rates are, or may reasonably be, applied.” (Emphasis added.)

39 U.S.C. Chapter 4 (General Authority)

- (4) **39 U.S.C. section 403(a)** requires that postal services be offered “at fair and reasonable rates and fees.” (Although opinions differ as to what is “fair and reasonable,” costs are usually the baseline for such fairness.)
- (5) **39 U.S.C. section 403(c)** prohibits “undue or unreasonable discrimination among users” in “establishing classifications, rates, and fees....” (Notions of discrimination can focus on matters other than costs, but costs are always a primary consideration.)
- (6) **39 U.S.C. section 404(b)** authorizes the “Governors ... to establish reasonable and equitable classes of mail and reasonable and equitable rates of postage and fees for postal services in accordance with the provisions of chapter 36.” (Again, some understanding of costs is unavoidable in determining what is “reasonable” and “equitable.”)

39 U.S.C. Chapter 36 (Postal Rates, Classes and Services)

- (7) **39 U.S.C. section 3622(b)(1)** establishes an objective of the ratemaking system “[t]o maximize incentives to reduce **costs** and increase efficiency.” (Emphasis added.)
- (8) **39 U.S.C. section 3622(b)(6)** states an objective of increasing “the transparency of the ratemaking process.” (Key parts of transparency should be knowing the reasoning, costs, and other evidence on which rates are based.)
- (9) **39 U.S.C. section 3622(b)(8)** points to the importance of “just and reasonable ... rates and classifications.” (Whatever “just” and “reasonable” are taken to mean, costs are the key reference point and they should be transparent.)
- (10) **39 U.S.C. section 3622(c)(2)** requires “that each class of mail or type of mail service bear the direct and indirect postal **costs** attributable to” it. (Emphasis added.) (This provision continues the concept of cost-based rates present under PRA in former 39 U.S.C. section 3622(b)(3).)
- (11) **39 U.S.C. section 3622(c)(5)** requires that consideration be given to “the degree of preparation of mail for delivery into the postal system performed by the mailers and its effect upon reducing **costs** to the Postal Service.” (Emphasis added.)
- (12) **39 U.S.C. section 3622(c)(10)(A)(i)**, in establishing criteria for NSAs, provides one basis for an NSA being to “improve the net financial position of the Postal Service through reducing Postal Service **costs**....” (Emphasis added.)
- (13) **39 U.S.C. section 3622(c)(12)** identifies “the need for the Postal Service to increase its efficiency and reduce its **costs**, including infrastructure **costs**, to help maintain high quality, affordable postal services.” (Emphasis added.)
- (14) **39 U.S.C. section 3622(e)** provides the entire basis for the regulation of workshare discounts and specifically ties them to **costs**, and in particular to the notion of an avoided **cost**.
- (15) **39 U.S.C. section 3633(a)(1)** “prohibit[s] the subsidization of competitive products by market-dominant products.” (The entire basis for a determination of cross-subsidization requires a knowledge of the costs of the respective groups of products.)
- (16) **39 U.S.C. section 3633(a)(2)** requires that “each competitive product covers its **costs** attributable.”

- (17) **39 U.S.C. section 3642(b)(1)** defines the market-dominant products as those “which the Postal Service exercises sufficient market power that it can effectively set the price of such product substantially above **costs**, raise prices significantly, decrease quality, or decrease output, without risk of losing a significant level of business to other firms offering similar products.” (Emphasis added.)
- (18) **39 U.S.C. section 3651(b)** requires the Commission’s annual report to the President and Congress to provide “an estimate of the **costs** incurred by the Postal Service” for providing universal service, free or reduced rates, and any other statutorily mandated services or activities. (Emphasis added.) Furthermore, the Commission is required to “detail the basis for its estimates and the statutory requirement giving rise to the costs identified....”
- (19) **39 U.S.C. section 3652(a)** requires **cost** information be provided in annual reports to the Commission.
- (20) **39 U.S.C. section 3652(b)** confirms that the **cost** information in the annual reports must include detailed information on workshare discounts.
- (21) **39 U.S.C. section 3652(e)(2)** permits the Commission “to improve the quality, accuracy, or completeness of Postal Service data ... whenever it shall appear that ... the attribution of costs or revenues to products has become significantly inaccurate or can be significantly improved.”
- (22) **39 U.S.C. section 3662(c)** allows the Commission to order remedies for noncompliance with statutory requirements, including ordering “the Postal Service to discontinue providing loss-making products.” (The concept of loss-making products implies knowledge of costs.)