

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

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**Consideration of Technical Methods to be  
Applied in Workshare Discount Design**

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**Docket No. RM2010-13**

**COMMENTS OF PITNEY BOWES INC.**

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## **I. INTRODUCTION**

By Order No. 537, dated September 14, 2010, the Postal Regulatory Commission (Commission) established a proposed rulemaking to consider technical issues that relate to the design of First-Class Mail workshare discounts.<sup>1</sup> The proposed rulemaking has two primary purposes: to “solicit comments on the appropriate base group for measuring First-Class Mail workshare discounts”; and to serve as a vehicle for the Commission to “consider technical proposals to revise or refine the manner in which avoided costs are modeled.” Notice at 2.

Pitney Bowes Inc. (Pitney Bowes) respectfully submits these comments in response to Order 537. These comments discuss: (1) Pitney Bowes’ support for the adoption of “Metered” mail as the appropriate base group for First-Class Mail, and (2) Pitney Bowes’ proposed costing methodology change to the existing First-Class Mail and Standard Regular mail processing cost models to more accurately reflect costs by performing a separate or “two-part” CRA adjustment for incoming secondary and non-incoming secondary operations.

## **II. DISCUSSION**

### **A. The Commission Should Adopt “Metered” Mail as the Based Group for Measuring First-Class Mail Workshare Discounts.**

The genesis of the instant rulemaking is the Commission’s finding in Docket No. R2009-2 that the Postal Service improperly “delinked” the costs of Single- Piece and Presort First-Class Mail Letters.<sup>2</sup> Following that determination the Commission initiated Docket No. RM2009-3 to develop a full record on the issues concerning the proper interpretation, scope and application of section 3622(e) of the Postal Accountability and Enhancement Act.<sup>3</sup>

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<sup>1</sup> See Dkt. No. RM2010-13, Order No. 537, Notice of Proposed Rulemaking Concerning the Technical Methods to be Applied in Designing Workshare Discounts (Notice)(Sept. 14, 2010).

<sup>2</sup> See Dkt. No. R2009-2, Order No. 191, Review of Market Dominant Price Adjustments (Mar. 16, 2009) at 4-5.

<sup>3</sup> See Dkt. No. RM2009-3, Order No. 192, Notice of Proposed Rulemaking on Application of Workshare Discount Rate Design Principles (Mar. 16, 2009); 39 U.S.C. § 3622(e); Pub. L. No. 109-435, 120 Stat. 3198 (Dec. 20, 2006).

Pitney Bowes filed comments in Docket No. RM2009-3 in support of the Postal Service's view that a delinked rate design was appropriate because Single-Piece and Presort First-Class Mail Letters are separate products under the PAEA and because the limitations of section 3622(e) only apply within, but not across, separate products.<sup>4</sup> Pitney Bowes further argued that to the extent the Commission required the Postal Service to "link" Presort and Single-Piece letters for purposes of the First-Class Mail rate design, that BMM, as a low-cost subset of Single-Piece First-Class Mail, was not a suitable benchmark.<sup>5</sup>

Order No. 536, issued September 14, 2010, resolved the legal and policy debate.<sup>6</sup> The Commission concluded that the pricing constraint on workshare discounts under section 3622(e) may apply within or across products. The Commission further concluded that a worksharing relationship exists between First-Class Mail Presort Letters and Single-Piece First-Class Mail Letters, but that the established BMM benchmark that was previously used to measure presort First-Class Mail avoided costs is "obsolete" and, therefore, no longer valid.<sup>7</sup> The Commission stated that a "factual inquiry to identify an appropriate base group" is required, and requested that interested parties provide information on "specific cost characteristics" of the base group of First-Class Mail.<sup>8</sup>

In response to the Commission's call for a fact-based inquiry, Pitney Bowes commissioned a survey by the Center for Social Research at George Mason University (GMU) to

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The PAEA amends various sections of title 39 of the United States Code. Unless otherwise noted, section references in these comments are to sections of title 39.

<sup>4</sup> See Dkt. No. RM2009-3, Initial Comments of Pitney Bowes Inc. (May 26, 2009); Dkt. No. RM2009-3, Comments of Pitney Bowes Inc. (Sept. 11, 2009).

<sup>5</sup> See Dkt. No. RM2009-3, Initial Comments of Pitney Bowes Inc. (May 26, 2009) at 8-9.

<sup>6</sup> On October 13, 2010, the Postal Service filed a petition for review of Order No. 536 with the United States Court of Appeals for the District of Columbia Circuit. See *United States Postal Service v. Postal Regulatory Commission*, Case No. 10-1324 (Oct. 13, 2010)(D.C. Cir.). These comments presume the validity of Order No. 536.

<sup>7</sup> See Order No. 536, at 40.

<sup>8</sup> See *id.* at 21.

develop empirical data regarding the mailing practices of small-to-medium-sized businesses.<sup>9</sup>

The purpose of the GMU survey was to identify the characteristics of non-household mail that is currently being sent as Single-Piece First-Class Mail. This is the mail that is most likely to convert to presort First-Class Mail.

The empirical analysis derived from the GMU survey results is part of the empirical analysis presented by the Joint Comments which combined the GMU survey results with the results of the survey performed by the National Association of Presort Mailers (NAPM) and another by the National Postal Policy Council and the Major Mailers Association. The combined analysis confirms that the characteristics and cost profile of the mail that is most likely to convert next (as derived from the GMU data) are similar to the characteristics and cost profile of the mail that most recently converted (as derived from the NAPM data). The GMU survey corroborates the NAPM survey and vice versa.

The Commission correctly held that BMM is “obsolete” and no longer a valid base group. By volume, the GMU data confirm that only 20 percent of the undiscounted non-household mail is being entered as BMM.<sup>10</sup> Based on the available data, undiscounted non-household mail is being generated in relatively small quantities with wide variations in mail preparation and some variation in payment evidencing (10 percent of the mail is stamped). Sixty percent of the undiscounted non-household mail needed to be collected. Therefore, the

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<sup>9</sup> The GMU survey results are also included in the Joint Comments of the American Bankers Association, the Bank of America Corporation, the Direct Marketing Association, Discover Financial Services, the Major Mailers Association, the National Association of Presort Mailers, and the National Postal Policy Council (Joint Comments)(Feb. 18, 2011).

<sup>10</sup> BMM was a composite proxy for a low-cost subset of Single-Piece First Class Mail Letters which was assumed to consist of machinable, homogenous, non-barcoded pieces with machine-printed addresses, properly trayed and faced, and delivered to the Postal Service in bulk. See Dkt. No. R2005-1, Response of United States Postal Service of Witness Abdirahman to Interrogatories of American Postal Workers Union, AFL-CIO, June 24, 2005, at responses to APWU/USPS-T21-8 (APWU/USPS-T21-8).

data confirm that the typical Single-Piece mail piece at the margin of conversion is more like collection mail, not BMM.

Accordingly, Pitney Bowes joins with the Joint Comments in recommending that the Commission adopt “Metered” mail as the new base group for purposes of measuring workshare-related cost avoidances for First-Class Mail Presort Letters.<sup>11</sup> For the reasons discussed in the Joint Comments “Metered” mail is an appropriate base group. The costs of “Metered” mail most closely approximate the identified cost characteristics of the mail at the margin of converting to presort; reducing inefficiencies caused by heterogeneity in Single-Piece mail.<sup>12</sup> The use of “Metered” mail as a proxy is also advantageous because its costs are directly identifiable from the Postal Service’s existing cost systems and, thus, will avoid problems faced by a composite cost proxy due to data limitations.

**B. The Commission Should Consider Improving the CRA Adjustment Process in the First-Class Mail Presort Letter and Standard Mail Regular Presort Letter Cost Models.**

The Commission specifically invited comments on the use of two Cost and Revenue Analysis (CRA) adjustment factors to develop workshare discounts as a technical proposal to consider in this proceeding. *See* Notice at 2-3. Pitney Bowes has raised this issue previously and continues to believe that by using a single adjustment factor to tie modeled costs back to actual costs reported in the CRA,<sup>13</sup> the letter cost models filed in Docket No. ACR2010, USPS-

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<sup>11</sup> “Metered” mail as defined in the Postal Service’s existing cost systems includes metered mail, information based indicia mail (IBI mail) and PVI mail. *See* Dkt No. RM2010-13, Response to CHIR No. 1 (Jan. 18, 2011) at 4 (IBI mail as discussed in the Postal Service’s response to CHIR No. 1 includes costs for digital meters and PC Postage solutions that use an information based indicia).

<sup>12</sup> *See* Dkt. No. RM2009-3, Initial Comments of Pitney Bowes Inc. (May 26, 2009), at 8-9 (discussing effects of mail heterogeneity and limitations of BMM as low-cost, composite benchmark); Dkt. No. RM2009-3, Comments of Pitney Bowes Inc. (Sept. 11, 2009), at 13 (same).

<sup>13</sup> Because the letter cost models serve only to deaverage the cost of presort letters by presort level, this problem does not affect the average cost avoidance between Single-Piece and Presort letters. Thus, adjusting the CRA adjustment process should have no effect on the average rate difference between Single-Piece and Presort letters.

FY10-10 may understate the cost avoided by improving the presort level of First-Class Mail and Standard Mail Regular letters.

Specifically, PB has compared modeled and CRA letter-sorting costs in Docket Nos. ACR2010 First-Class Mail Presort Letter and Standard Mail Regular Presort Letter cost models. As shown in Table 1 below, the ratio of CRA-to-modeled costs is much higher for non-incoming secondary (non-IS) sorting, i.e., sorting pieces by facility and 5-Digit, than for incoming secondary (IS) sorting, i.e., sorting pieces from 5-Digit ZIP to carrier route and delivery point sequence (DPS).<sup>14</sup>

**Table 1. FY 2010 Ratio of CRA-to-Modeled Letter Sorting Costs<sup>15</sup>**

<b>Mail Class</b>	<b>IS</b>	<b>Non-IS</b>
First-Class Mail	0.984	1.681
Standard Mail	0.843	1.396

As suggested by the Public Representative in Docket No. RM2009-1 and particularly in instances where the ratios of CRA-to-modeled costs differ substantially across operations and sort schemes, it may be preferable to use two separate adjustment factors to tie modeled costs back to CRA costs, rather than just one.

One can imagine that if all rate categories used resources by cost producing activity in the same proportions, then a system level adjustment...would be justified.

However, this is hardly the case. Rate categories use activity level resources in different proportions....Under these circumstances, use of one system level

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<sup>14</sup> This finding is consistent with PB analyses of prior-year letter cost models. See Docket No. RM2009-3, Initial Comments of Pitney Bowes (filed May 26, 2009) at 12; Docket No. ACR2009, Initial Comments of Pitney Bowes (filed February 1, 2010) at 4-5.

<sup>15</sup> PB-2, PB-2.xls, "2Pt CRA - PRESORT LETTERS SUM", cells L30-M30, PB-3, PB-3.xls, "2Pt CRA - PRESORT LETTERS SUM", cells L30-M30.

adjustment factor would distort unit costs and, more importantly, unit cost differences for purposes of setting worksharing discounts.<sup>16</sup>

Because the ratio of CRA-to-modeled costs in the letter cost models is much higher for non-IS than IS sorting, using a single, system level adjustment appears to adjust non-IS costs insufficiently and IS costs too much. This likely biases downward the estimated cost avoided by improving presort because non-IS sorting costs for letters are much more affected by presorting than are IS sorting costs.<sup>17</sup> Specifically, non-IS sorts can be avoided by presorting, but even the most highly presorted letters in First-Class Mail and Standard Mail Regular require IS sorting. For example, 5-Digit letters avoid all non-IS sorts, but still must be sorted – generally into delivery point sequence – in an incoming secondary operation.

One way to remedy this problem is to perform separate CRA adjustments for IS and non-IS costs. Pitney Bowes has developed modified versions of the letter cost models filed in Docket No. ACR2010 that do that. Attached are three appendices, PB-1 through PB-3. Appendix 1 (PB-1) describes the methodology used to separately identify and adjust IS and non-IS sorting costs for consistency with the CRA. PB-2 and PB-3 contain the SAS files used to disaggregate FY 2010 CRA letter sorting costs into IS and non-IS costs, and modified versions of the PRC's Docket No. ACR2010 letter cost models that separately adjust modeled IS and non-IS costs.<sup>18</sup>

Pitney Bowes respectfully requests that the Commission consider adopting First-Class Mail Presort and Standard Mail Regular Presort letter cost models that use separate CRA adjustment factors for IS and non-IS costs for use in the FY 2011 Annual Compliance Report.

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<sup>16</sup> Dkt No. RM2009-1, Public Representative Initial Comments (Dec. 1, 2008) at 4-5.

<sup>17</sup> IS sorting costs are not completely unaffected by presorting. Presort level does affect IS sorting costs indirectly by affecting the likelihood that a piece is sorted manually.

<sup>18</sup> PB filed modified versions of the PRC's Docket Nos. R2006-1 and ACR2007 letter cost models (and the associated SAS files) as appendices to its reply comments in Docket No. RM2009-1, modified versions of the USPS Docket No. ACR2008 letter cost models (and the associated SAS files) as appendices to its Docket No. ACR2008 comments, and modified versions of the PRC's Docket No. ACR2008 letter cost models (and the associated SAS files) as appendices to its Docket No. RM2009-3 comments.

### III. CONCLUSION

For the reasons state above, Pitney Bowes respectfully requests that the Commission establish “Metered” mail as the base group for purposes of measuring First-Class Mail workshare discounts and adopt a two-part CRA adjustment for First-Class Mail Presort and Standard Mail Regular Letters to improve the accuracy of the reported mail processing costs.

Respectfully submitted:

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/s/

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