



## BACKGROUND

On April 19, 2011, the Public Representative filed a Motion for Issuance of Information Request requesting about, *inter alia*, how application of the mobile barcode discount to Standard Mail Flats is consistent with the Commission's finding of noncompliance in its FY 2010 Annual Compliance Determination.

On April 22, 2011, the Chairman issued Chairman's Information Request ("ChIR") No. 1, asking the above question posed by the Public Representative and also asking "how the proposed Docket No. R2011-5 price adjustment would move the Standard Mail Flats product toward compliance with 39 U.S.C. § 101(d)." The Postal Service responded to ChIR No. 1 on April 29, 2011.

## COMMENTS

The Public Representative has raised an important issue, and the Chairman has posed important questions to the Postal Service. Valpak would like to comment with respect to the problem of the ongoing Standard Mail Flats subsidy.

In Docket No. ACR2010, Valpak addressed at length the failure of Standard Mail Flats to cover its attributable costs. *See* Docket No. ACR2010, Valpak Initial Comments, pp. 40-49; Valpak Reply Comments, pp. 2-12. While not wanting to reiterate those lengthy comments, Valpak's position could be summarized by the following points.

First, Valpak discussed the serious financial hemorrhage that the Standard Flats product has been for the Postal Service.

In the **three years** since [the Postal Service began reporting Flats as a separate product], revenues from the Standard Mail Flats product have failed to cover attributable cost by a cumulative

total of **\$1.4 billion.**” [Valpak Initial Comments, p. 42 (emphasis added).]

Second, Valpak discussed that these losses were being subsidized by other mailers, particularly those with high coverages, such as the saturation mail products. Further, Valpak warned that:

[w]ithout **Commission-directed price increases**, continued large losses on Flats can be anticipated by the Postal Service, as well as by mailers of other profitable products who subsidize those losses.” [*Id.*, p. 44.]

Third, Valpak explained that all prior efforts to address the problem have been inadequate, including the failure of the so-called “Flats Strategy” offered by the Postal Service in Docket No. R2010-4. Without Commission direction, the Postal Service seemed unwilling to provide even a glimmer of hope for the eventual profitability of the Standard Flats product. *See id.*, pp. 45-46. In fact, making matters worse, the Postal Service had given Standard Flats back-to-back, below-average price increases, thereby exacerbating the continued substantial losses on the product. *See id.*, pp. 47-49.

Based in part on the thoughtful analysis provided by the Public Representative and L.L. Bean, as well as Valpak’s comments, in its FY 2010 Annual Compliance Determination the Commission recognized its responsibility to act, and made its first-ever finding of noncompliance under the Postal Accountability and Enhancement Act (“PAEA”), finding that pricing for Standard Flats violated 39 U.S.C. section 101(d). *See* FY 2010 Annual Compliance Determination, p. 106. As a corrective action, the Commission ordered the Postal Service to provide a plan for future above-average (albeit below the class-wide cap) pricing increases:

Pursuant to section 3653(c), the Commission directs the Postal Service to increase the cost coverage of the Standard Mail Flats product through a combination of above-average price adjustments, consistent with the price cap requirements, and cost reductions until such time that the revenues for this product exceed attributable costs. [*Id.*]

Within 90 days of the issuance of the FY 2010 ACD, the Postal Service shall present a schedule of future above-CPI price increases for Standard Mail Flats. [*Id.*, p. 107.]

The deadline for this plan is June 27, 2011 — still approximately two months in the future. Therefore, the Commission must assess the Postal Service's proposal to offer certain Standard Flats mailers a 3 percent discount in this docket without the benefit of the Postal Service's plan to price Standard Flats to achieve cost coverage. However, no matter what that plan may be, the decision to reduce prices by 3 percent now would not only be inconsistent with the Commission's direction, but also any plan that the Postal Service possibly could conceive. As a result, the Standard Flats product, that was found to be in violation of PAEA with a cost coverage of 81.6 percent in FY 2010, will be moved toward even greater violation of PAEA in FY 2011 (even though the program in question would only last two months of FY 2011). *Id.*, p. 103.

The Postal Service's general representations regarding the instant program are inapplicable to the Standard Mail Flats product:

- The Postal Service's proposal asserts that it is compliance with PAEA Objective 5 ("To assure adequate revenues, including retained earnings, to maintain financial stability.") because "the program will provide an **incentive for profitable new mail** will enhance the financial position of the Postal Service." Postal Service Proposal, p. 5. However, to the extent that the discount program provides an incentive for new Standard Mail Flats volume, it actually provides an **incentive for unprofitable new mail** which further erodes the financial position of the Postal Service in violation of PAEA Objective 5.

- The Postal Service claims that it is in compliance with the cost coverage requirement (section 3622(c)(2)), as “it will not imperil the ability of either First-Class Mail or Standard Mail to cover its attributable costs.” *Id.*, p. 7. However, the Commission has determined that section 3622(c)(2) applies at the product level as well as the class level. *See* FY 2010 Annual Compliance Determination, pp. 17-18. The Postal Service’s filing failed to explain how the discount would affect products, including Standard Mail Flats, which would obviously have its ability to cover its costs further imperiled.
- The Postal Service provided a response to ChIR No. 1, question 1 which acknowledge problems, but provided nothing persuasive to what it admits will be a reduction of Standard Mail Flats postage revenues. Response of USPS to ChIR No. 1 (Apr. 29, 2011), pp. 1-3. For various reasons, the Postal Service excluded from the program nonprofit mailers (*id.*, p. 9) and mailers of parcels (*id.*, p. 10), and for the reasons set out above, it also should exclude Standard Mail Flats.

The Postal Service recently file a Petition to Review to challenge the Commission’s finding of noncompliance in FY 2010 Annual Compliance Determination. Nevertheless, while that case is pending, it would be unconscionable to provide new discounts to a product which has been found by the Commission to be in violation of PAEA and is hemorrhaging money, especially with the prospect of the Postal Service not being able to pay its statutory obligations at the end of FY 2011.

Respectfully submitted,

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