DOCKET SECTION

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

RECEIVED
JUN 30 4 35 PM '98

POSTAL RATE AND FEE CHANGES, 1997

Docket No. R97-1

NOTICE OF THE UNITED STATES POSTAL SERVICE
OF DECISION OF THE GOVERNORS

The following Decision of the Governors has been mailed to the service list in Docket No. R97-1:

Decision of the Governors of the United States Postal Service on the Recommended Decision of the Postal Rate Commission on Prepaid Reply Mail and Courtesy Envelope Mail, Docket No. R97-1 (June 29, 1998)

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorney:

Daniel J. Foucheaux, Jr.

Daniel J. Foucheaux, Jr.
Chief Counsel, Ratemaking

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1137
(202) 268-2989; Fax -5402
June 30, 1998

Decision of the Governors of the United States Postal Service on the Recommended Decisions of the Postal Rate Commission on Prepaid Reply Mail and Courtesy Envelope Mail, Docket No. R97-1

June 29, 1998

Statement of Explanation and Justification

The Postal Rate Commission included in its Recommended Decision of May 11, 1998, two mail classification recommendations which the Governors consider separately in this Decision. These classifications are Prepaid Reply Mail (PRM) and Courtesy Envelope Mail (CEM). Our independent assessment and review of the record lead us to exercise our statutory option to reject these two recommendations. We discuss them below.

Prepaid Reply Mail

PRM was one of two First-Class Mail classifications proposed by the Postal Service to recognize the cost savings associated with processing prebarcoded automation-compatible reply mail letters and cards. The other classification was Qualified Business Reply Mail (QBRM). Reply mail, which is printed in bulk for the ultimate recipient, lends itself to prebarcoding and the accompanying savings made possible through automated processing. Under both PRM and QBRM, the account holder would pay a rate of postage lower than the basic rate for First-Class Mail letters and cards, plus accounting and permit fees. Under QBRM, the recipient will have an advanced deposit account, and the Postal Service will deduct postage for reply pieces after the pieces enter the reply mail stream and are ready for tender to the recipient. The recipient also will pay a per-piece service fee, recommended by the Commission at 5 cents per piece. The PRM provider, on the other hand, would be required to pay postage prior to distribution, based on anticipated returns, and the provider would assume primary responsibility for related accounting functions, subject to USPS audit. The provider would pay a monthly accounting fee of $1,000.00, but there would be no per-piece service fee. In a separate decision today, we approved the Commission's QBRM recommendation along with most of the other rate and classification changes recommended. We now turn to the PRM recommendation.

Preliminarily, we acknowledge that we have received numerous formal comments from Docket No. R97-1 intervenors and others pertaining to the Commission's PRM recommendation. Many of the commenters opposed to the establishment of PRM make factual assertions concerning adverse consequences which could result if we were to approve the PRM recommendation. In this regard, we observe that the evidentiary record upon which the Commission was required to rely, and to which we refer for guidance, does not include a number of these factual assertions.

After careful deliberation, we have determined that we will exercise our authority to reject the PRM recommendation. In doing so, we acknowledge that we are rejecting a recommendation that was originally proposed by the Postal Service. We commend the Commission for its thoughtful analysis and consideration of the PRM proposal. We note that the Commission's opinion reflects its own reservations about PRM. As the Commission's partner in the ratemaking process, we believe that the public interest is served by rejecting PRM so that the Postal Service can re-examine the feasibility of its PRM proposal in the context of the Commission's reservations and our principal Decision today.

We have rejected PRM because we consider that critical questions about the establishment of PRM as a discrete classification remain unanswered at this time. Although we have accepted the QBRM recommendation, we expect the Postal Service will explore possible refinements to QBRM. These refinements might diminish significantly the basis for some of the material distinctions between the two categories, and the necessity of maintaining separate First-Class Mail and special service classifications for each.

As proposed and recommended, both PRM and QBRM would require the customers who would pay for this mail to maintain advance deposit accounts with the Postal Service from which postage and fees would be deducted. The PRM classification would include a postage prepayment requirement, under which postage would be deducted from the account when the reply piece was mailed to the potential sender by the PRM envelope or card provider. In contrast, QBRM -- like current BRM -- will not require that postage for the reply pieces be deducted from the account until after the pieces have entered the reply mailstream and are ready for tender to the recipient. While open to persuasion, we are not yet satisfied that such a distinction is necessary.

In our principal Decision today, which approves the recommended QBRM classifications and fees, we express reservations about long-term retention of a requirement that all QBRM recipients pay the same per-piece accounting fee. Accordingly, we are encouraging management to review potential alternatives to the QBRM per-piece accounting fee we have approved, and to explore further such matters as the extent to which reply mail volume should influence fees charged to different recipients.

PRM would allow for accounting by the reply mail recipient to determine postage (subject to postal audit). Under QBRM, Postal Service accounting will perform the same task. Again, we question whether the mutual exclusivity of these options is a compelling basis for the establishment of separate mail classifications for what appears to be one distinct mailstream.

In summary, we reject PRM at this time because we do not consider that the record placed before the Commission in this docket is sufficiently persuasive on establishing a distinct mail classification. We consider this conclusion appropriate in light of our belief that the Postal Service should examine potential improvements to QBRM. We look forward to consideration of refinements to the prebarcoded automation-compatible First-Class Mail stream and the opportunity to resolve these and other related issues. Current reply mail recipients who may be anticipating the establishment of PRM still have an incentive to work with the Postal Service in exploring possible improvements to QBRM, which reflect operationally feasible accounting options, and which meet appropriate revenue protection standards.

COURTESY ENVELOPE MAIL

The Commission has recommended the creation, within First-Class Mail, of a Courtesy Envelope Mail (CEM) classification for prebarcoded, single-piece reply letters. The primary feature which distinguishes CEM from both QBRM and PRM is the necessity for the sender of a CEM piece to affix First-Class Mail postage at a discounted rate before entering it into the mailstream.

As it has in past cases, the Commission decided not to recommend a specific CEM rate or discount from the basic First-Class Mail rate in Docket No. R97-1. A grouping of mail identified for discrete rate treatment, but without any particular current rate level recommended, has come to be known as a "shell classification." Thus, in this instance, the CEM classification language the Commission recommends, if approved by us, would create a shell classification, appearing as DMCS § 221.25. In earlier Decisions, we have had the opportunity to address recommended shell classifications. For example, in Docket No. R87–1, in addition to the shell classification recommended for CEM, the Commission also recommended shell classifications for palletized second-class and third-class mail. In Docket No. MC96-3, the Commission recommended a shell classification for stamped cards.

Our observations in addressing the Docket No. R87-1 shell classification recommendations are applicable to almost any recommended shell classification. There, we noted:

> The Act establishes an elaborate process for adding provisions to the mail classification schedule, and contemplates precisely the same process for removing them. If, in examining the rate question that the Commission postpones for the future, reliable data disclose that cost-based incentives ... *are not justified, or if, for compelling reasons,* the Postal Service finds that ...

> other operating policies must be adjusted to properly and efficiently serve customers, had we accepted the changes recommended here we would then be required under the Act to burden the Commission and the parties with additional proceedings to remove these changes. If upon that examination, reliable data disclose that additional rate incentives are warranted . . ., the Act requires that additional proceedings be had before the Commission to establish those rate incentives; in that circumstance the task is not made more difficult if the classification schedule language emerges from those proceedings at that time.

Decision of the Governors on Commission's Recommended Decision on Mail Classification Changes, Docket No. R87–1, at 5 (May 2, 1988). In rejecting the shell classifications recommended in that proceeding, we concluded that "[u]ntil the questions posed ... can be answered with confidence, however, we believe the better practice is to leave the classification schedule silent on them." *Id.* at 6.

One consequence of the Commission's decision to recommend a shell classification for CEM is that it avoids complication of our consideration of the entire range of other Docket No. R97-1 rate and classification recommendations which are before us in this proceeding. By refraining from making its other rate recommendations contingent upon our acceptance of a specific CEM discount, with associated financial consequences that could directly affect many other rate levels, the Commission has enhanced our ability to review and evaluate the recommended CEM classification on its own merits. We continue to find this to be a worthwhile approach. Nevertheless, the substantial questions raised on the record regarding discrete rate treatment for prebarcoded CEM lead us to reject the recommended classification change.

As we observed above, a significant distinction between CEM, on the one hand, and QBRM and PRM, on the other, is that only the first one would require the sender to affix postage to the discounted mail piece. Thus, for instance, our decision to approve QBRM does not generate the significant administrative and enforcement concerns which discourage us from approving the CEM shell classification.

An advantage of CEM perceived by its proponents is that it would permit a much broader base of First-Class Mail users to benefit from automation through the reduced postage they would pay on some of their qualified CEM letters. However, the record suggests that, even if given the option of using a reduced rate CEM stamp on qualifying letters, a substantial majority of household mailers (the principal intended beneficiaries of CEM) prefer the current "one-stamp" system, instead of having to administer two different denominations of postage stamps for their most common postal transaction, the mailing of one-ounce First-Class Mail letters. At page 326 of its opinion, the Commission states that "it finds it is troubling that the [Postal] Service emphasizes concerns about manipulation of the 'two-stamp' system by CEM users." However, we read the Postal Service's testimony on this issue to focus on the potential for public confusion from a "two-stamp" system, and the adverse consequences from the return to sender of short-paid mail pieces on which CEM postage was improperly affixed. Caution is required in matters affecting the goodwill of the general mailing public. We respectfully consider that postal management should be accorded deference on this issue.

Moreover, as was the case in Docket Nos. MC95-1 and R87-1, the Postal Service in Docket No. R97-1 has demonstrated to our satisfaction that the perceived benefits of CEM are accompanied by significant and nettlesome administrative and enforcement concerns which would result from the application of different denominations of postage stamps on basic one-ounce First-Class Mail letters. The evidence suggests that the costs of CEM could outweigh the relatively modest automation benefits intended to be distributed more directly to single-piece First-Class Mail users. We believe this evidence deserves consideration.

Although CEM was described by its proponents as a means of allowing household mailers to obtain a direct and tangible rate benefit from the postal automation program, the record shows that household mailers already appropriately benefit from automation. The savings realized from automated processing of household mail, averaged with the other costs of First-Class Mail, mitigate overall First-Class Mail rate increases. Given the cost profile of typical household mail, we consider this to be fair and equitable. As we noted in our discussion of this topic in Docket No. MC95-1:

> When households use the CEM envelope provided by others to pay a bill (or for some other return correspondence), the letter they mail has relatively low-cost. For the rest of their letters, however, sent in their own envelopes, often with hand-written addresses, the households continue to deposit relatively high-cost mail. Each of these two disparate types of mail constitutes approximately one-half of the typical household's mail. Under the current rate and classification structure, the costs of all household r. ail are averaged with the generally low costs of business mail, to create one base letter rate applicable to both.

Decision of the Governors of the United States Postal Service on the Recommended Decisions of the Postal Rate Commission on Courtesy Envelope Mail and Bulk Parcel Post, Docket No. MC95–1, at 5 (March 4, 1996). As we further observed then:

> CEM would offer to households the new advantages of deaveraging for their low-cost mail, and the continuing advantages of averaging for their high-cost mail. We are not convinced that such a ratemaking scheme is either fair or equitable. Unless households were called upon to pay higher rates which reflect the higher costs of their mail that is not sent in reply envelopes (an approach advocated by no one in this case), a proposal such as CEM that would nevertheless allow them to pay lower rates which reflect the lower costs of their reply mail seems distinctly one-sided.

Id. at 5-6. Based upon the Docket No. R97-1 record, we find the same principles to apply to the CEM recommendation before us. Accordingly, we reject the recommendation to establish a "shell" rate category for prebarcoded CEM in this case.

As part of its review of QBRM, we encourage postal management to determine whether there are ways in which it can encourage more widespread use of prebarcoded automation-compatible reply letters and cards which enjoy reduced postage paid by the recipient, in accordance with methods satisfying appropriate revenue protection standards. We believe that if reduced reply mail postage lowers the cost of conducting transactions with a reply mail recipient, then regardless of whether the postage savings are realized directly by the sender or the recipient, the Postal Service may benefit from retaining business reply transactions in the face of inroads being made by competitive technologies.

ESTIMATE OF ANTICIPATED REVENUE

The Postal Reorganization Act requires that our Decision include an estimate of the estimated revenue impact. 39 U.S.C. § 3625(e). In this Decision, we are rejecting two recommended classification changes. Even if we had accepted those recommendations, however, only PRM would have been a classification change with rate consequences, since CEM was recommended as a "shell" classification. Accordingly, we estimate that our rejection of PRM has the effect of increasing test year revenues by approximately $27 million, which is comprised of $15 million in additional postage and $12 million in additional fees. Since the increased fee revenue is largely offset by increased costs, our rejection of PRM means that the revenue needed from all other mail is reduced by approximately $15 million. While our rejection of CEM has no impact on revenues, it does reduce our costs by the $33 million the Commission assumed to be set aside for CEM consumer education.

ORDER

In accordance with the foregoing Decision of the Governors, changes in the Domestic Mail Classification Schedule to include new sections recommended by the Commission on May 11, 1998, to appear as DMCS § 221.23, 221.25 and 934 are rejected, as are any corresponding cross-references to those sections.

The foregoing was adopted by the Governors on June 29, 1998.

By The Governors

Sam Winters

Chairman