

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

Annual Compliance Report, 2011

Docket No. ACR2011

COMMENTS OF THE DIRECT MARKETING ASSOCIATION, INC.,
THE NATIONAL ASSOCIATION OF PRESORT MAILERS, AND
THE PARCEL SHIPPERS ASSOCIATION
(February 3, 2012)

Pursuant to Order No. 1095, the Direct Marketing Association, Inc., the National Association of Presort Mailers, and the Parcel Shippers Association (Joint Commenters) respectfully submits these comments on the Annual Compliance Report for Fiscal Year 2011 filed by the Postal Service on December 29, 2011 (FY2011 ACR). These comments focus on the Postal Service's statements about First-Class Mail.

The Postal Service expresses concern about the implications of the growing disparity in the cost coverage and unit contribution of First-Class Mail Single-Piece and Presort Letters/Cards,

The cost coverage for First-Class Mail Presorted Letters/Cards was 298.8 percent; as discussed in footnote 21, the increasing differential between the unit contributions of the presorted and single-piece products is becoming a cause for concern. In FY 2011, product volume declined 3.7 percent. While it is the largest product within First-Class Mail, continued presort volume declines create significant financial concerns.

FY2011 ACR at 17. The Postal Service expanded on these concerns, as follows,

In the FY 2010 ACD, the Commission noted presort customers' concern that the presort cost coverages were too high and could soon be not "just and reasonable." FY 2010 ACD, at 85. In response, the Commission stated that it would continue to monitor these cost coverages to ensure compliance with the law. *Id.* Unfortunately, in FY 2011, the difference between the unit contributions of presorted First-Class Mail letters and single-piece First-Class Mail Letters increased (from 5.2 cents in FY 2010 to 6.1 cents in FY 2011). Under the Commission's workshare rules, this difference in unit contribution is almost certain to grow. Thus, the Commission's current interpretation and application of

the workshare provision appears to be on a collision course with the clear statutory objective of a just and reasonable rate schedule.

FY2011 ACR at 50, n.21. The Joint Commenters shares these concerns. Minimizing the disparity in unit contributions between First-Class Mail Single-Piece Letters/Cards and Presort Letters/Cards would create a more equitable price schedule and would improve the Postal Service’s financial position.

The Postal Service has reported costs and revenues on a product basis for the past four years. As shown in Table 1, below, over that same time period the unit attributable cost of Presort Letters/Cards has been relatively stable compared to that of Single-Piece Letters/Cards. Unit attributable cost of Presort Letters/Cards has increased by only .7 cents while the cost of Single-Piece Letters/Cards has increased by 2.7 cents. Over this same time period the unit revenue of Single-Piece Letters/Cards has increased by 2.8 cents, the unit revenue for Presort Letters/Cards increased by 2 cents.

		Unit Attributable Cost (\$)		Unit Attributable Revenue (\$)		Unit Contribution (\$)		
		Single-Piece	Presort	Single-Piece	Presort	Single-Piece	Presort	Difference [a]
FY 2011	[1]	.278	.116	.448	.348	.170	.232	.062
FY 2010	[2]	.272	.117	.446	.346	.174	.229	.055
FY 2009	[3]	.264	.117	.435	.340	.171	.223	.052
FY 2008	[4]	.251	.110	.420	.328	.169	.218	.049

[1] FY2011 ACR at 16, Table 1.
 [2] FY2010 ACR at 18, Table 1.
 [3] FY2009 ACR at 22, Table 1.
 [4] FY2008 ACR at 18, Table 1.
 [a] Difference calculated as Presort Unit Contribution minus Single-Piece Unit Contribution

As a consequence of these unit cost and revenue increases, the unit contribution of Single-Piece Letters/Cards has increased by a scant .1 cents from FY 2008 to FY 2011. In contrast, the unit contribution of Presort Letters/Cards has increased by a far more robust 1.4 cents. Thus, the difference in unit contribution grew by 1.2 cents per piece (almost) 25 percent, from 4.9 cents in FY 2008 to 6.2 cents in FY 2011.

Under the Commission’s methodology for measuring workshare discounts, these trends will likely be exacerbated. This growing disparity in the cost coverage and unit contribution between First-Class Mail Single-Piece Letters/Cards and Presort Letters/Cards cannot be

justified. See 39 U.S.C. § 101(d) (“[p]ostal rates shall be established to apportion the costs of all postal operations to all users of the mail on a fair and equitable basis.”); 39 U.S.C. § 3622(b)(8)(modern rate system “shall be designed . . . [t]o establish and maintain a just and reasonable schedule for rates”). It is inexplicable that the Postal Service’s pricing schedule would be biased against its largest and most profitable customers.

Minimizing the disparity in unit contributions between First-Class Mail Single-Piece Letters/Cards and Presort Letters/Cards would also improve the financial position of the Postal Service, as shown in Table 2, below. The model used to generate this table is described in the Appendix to these comments and attached to them in the workbook.

Change in Single-Piece from Current (\$)	Price (\$)		Unit Contribution (\$)		Change in Total Contribution from Contribution at Current Prices (\$ millions)
	Single-Piece	Presort	Single-Piece	Presort	
-.02	.428	.360	.150	.244	-120
-.01	.438	.354	.160	.238	-58
0	.448	.348	.170	.232	0
.01	.458	.342	.180	.226	55
.02	.468	.336	.190	.220	106
.03	.478	.331	.200	.215	153
.04	.488	.325	.210	.209	197
.05	.498	.319	.220	.203	237

Under the PAEA price cap, increases in the price of Single-Piece Letters/Cards must be offset with decreases in the price of Presort Letters/Cards. This is reflected in Table 2. However, because of the differences in volume responses to price increases (Presort Letters/Cards are more price sensitive than Single-Piece Letters/Cards) total contribution increases monotonically. At the point unit contribution is roughly the same - a 4-cent increase for Single-Piece and a 2.3-cent decrease for Presort, equalizing contribution at about 21 cents for each - total contribution is increased by \$197 million over the contribution at ACR average prices. And as shown in the underlying model, total contribution continues to rise far past the point of unit contribution equalization, reaching its point of maximum increase of \$424 million

at a price increase of 14 cents for Single-Piece.¹ The converse also holds; a two cent decrease in Single-Piece would cost the Postal Service \$120 million.

The Commission should allow the Postal Service to immediately begin taking incremental steps to minimize the disparity in unit contributions between First-Class Mail Single-Piece Letters/Cards and Presort Letters/Cards. This is necessary to create more equitable price schedule and to improve the Postal Service's financial position.

Respectfully submitted,

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¹ The Joint Commenters are not advocating this maximum increase. A disparity in the cost coverage and unit contribution between First-Class Mail Single-Piece Letters and Presort Letters would be inequitable in either direction. But a bias in favor of Presort Letters would significantly improve the Postal Service's financial position.

APPENDIX

The attached Excel workbook produced the entries in Table 2, using the most recent own-price elasticity provided by the Postal Service, along with volumes, average prices, and average attributable costs for Fiscal Year 2011. ACR2011 at 16, Table 1.

There are two tabs in the attached workbook. The first tab, labeled “Max Contribution,” is a tool to calculate unit and total contribution at various cap-compliant sets of prices for Single-Piece and Presort First-Class Letters/Cards. Rather than calculating the maximum contribution analytically or the total contribution implications of equalizing unit contribution, values are calculated “by hand” – substituting different values for the prices. This is straightforward to do because only one of the two prices – for Single-Piece and Presort – can be independently set if we assume the price cap continues to apply since the price cap will determine the second price once the first one has been set. For the worksheet, the formulae are set up to determine Presort price and all other values once the Single- Piece price is set.

The second tab, labeled “Results,” shows the results of varying these prices by one cent increments for Single-Piece and can be used to find the change in total contribution from equalizing unit contributions or the effect on contribution possible given any set of prices given the cap and the applicable price elasticities of demand.