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

ANNUAL COMPLIANCE REPORT, 2011	Docket No. ACR2011

REPLY COMMENTS OF
THE NATIONAL POSTAL POLICY COUNCIL
(February 17, 2012)

The National Postal Policy Council ("NPPC") respectfully submits this reply to certain comments on the Postal Service's Annual Compliance Report for Fiscal Year 2011 ("*ACR*").

Several parties filed comments that contain useful discussions of the Postal Service's financial predicament.[1] NPPC agrees that those parties properly assigned the lion's share of responsibility for the Postal Service's dire balance sheet and cash flow to the Congress, and particularly the obligation imposed by the Postal Accountability and Enhancements Act to prefund future retiree health benefits. Although those comments are informed contributions to the ongoing policy debate and place the Service's fiscal deficit in perspective, the Commission lacks any authority to amend the statute.

In this proceeding, however, the Commission can only evaluate the Postal Service's operating performance under the statute as it exists. Towards that end, NPPC will address two issues in these reply comments:

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[1] *Public Representative Comments*, Docket No. ACR2011 at 1-5 (Feb. 3, 2012); *Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc., Initial Comments on the United States Postal Service FY 2011 Annual Compliance Report*, Docket No. ACR2011 at 2-23 (Feb. 3, 2012).

- The need to reduce the excessive burden on First-Class Presort letters by adopting a new, realistic benchmark (as long as First-Class Presort mail is considered a mere worksharing derivative of Single-Piece mail[2]) without driving mail out of the system through raising rates; and
- The (related) need for accurate, operationally-based benchmarks when considering discounts in First-Class Presort mail.

I. THE EXCESSIVE CONTRIBUTION PAID BY FIRST-CLASS PRESORT MAIL MUST BE ADDRESSED

In its opening comments, NPPC noted that rates for the First-Class Automation and Presort Letters and Cards mail product greatly exceeded attributable costs and, for yet another year, paid an excessive – and increasing – cost coverage. These excessive rates increasingly conflict with the Section 3622(b)(1) & (b)(8) objectives to maximize incentives to reduce costs and maintain a just and reasonable rate schedule.[3]

In joint comments, several parties purported to calculate what rates would be required for First-Class Single-Piece and Presort Mail to pay equal unit contributions.[4] Whatever the merits of that calculation, those were not the rates in effect in FY2011. Moreover, NPPC – whose members use Presort letters, Presort cards, and some

[2] NPPC's position is that the Commission's ruling that a worksharing relationship exists between Single-Piece mail and Automation and Presorted mail is incorrect as a matter of law. The Postal Service's petition for review of the Commission's conclusion to that effect in Order No. 536 was dismissed as not ripe by the U.S. Court of Appeals for the District of Columbia Circuit. *United States Postal Service v. Postal Regulatory Commission*, Docket No. 10-1324 (mandate issued Oct. 21, 2011). NPPC intervened in that proceeding in support of the Postal Service.

[3] *Comments of the National Postal Policy Council*, Docket No. ACR2011 at 2 (Feb. 3, 2012).

[4] *Comments of the Direct Marketing Association, Inc., the National Association of Presort Mailers, and the Parcel Shippers Association*, Docket No. ACR2011 at 2 (Feb. 3, 2012).

Single-Piece mail -- does not agree that the Postal Service would be better off were significant rate increases imposed on any particular product within First-Class Mail. At a time when volumes are declining rapidly for both Single-Piece and Presort mail and economic factors appear to be driving mail demand more than price, the Postal Service and Commission should not be raising rates. Instead, they should be acting swiftly to fix the First-Class Mail rate schedule by reducing rates in order to preserve and stabilize volumes.

NPPC agrees with the joint commenters that Presort mailers and Presort Mail volumes suffer each day that Presort rates are held at excessive levels. Those rates are excessive because of an erroneous "linking" policy effectuated by an unrealistic and admittedly "obsolete" benchmark.[5] To relieve the burden on Presort mailers without triggering an accelerated decline in other mail volumes during a difficult economy, NPPC believes that the Postal Service would be best off reducing Presort rates to the full extent allowed by the new benchmark without any attempt to "offset" that reduction with increases in rates for other products.

II. THE COMMISSION SHOULD APPLY ACCURATE BENCHMARKS WHEN EVALUATING FIRST-CLASS PRESORT DISCOUNTS

Several parties submitted comments addressing worksharing discounts. In considering Section 3622(e), the Commission must pay careful attention to the

[5] In Docket No. RM2010-13, NPPC joined several other parties in recommending that the Commission adopt as the new benchmark Metered Mail, including collection costs. *See Joint Comments of the American Bankers Association, the Bank of America Corporation, the Direct Marketing Association, Discover Financial Services, the Major Mailers Association, and the National Postal Policy Council*, Docket No. RM2010-13 (February 18, 2011)

benchmarks used. In the particular case of Presort discounts, two of the opening comments raise issues that highlight the importance of using accurate benchmarks that recognizes market and operational activities.

First, the Public Representative criticizes the appropriateness of the apparent pass-through of 147 percent for the First-Class Automation Mixed AADC letter discount, and urges the Commission to inquire whether that "significantly reduces efficiency incentives" and is a factor in "negative contributions."[6] The short answer is that the Public Representative's criticism has no factual basis.

What the Public Representative overlooks is that the 147 percent figure is based on the "Bulk Metered Mail" ("BMM") benchmark. *See* Library Reference USPS-FY11-3 Workshare Discounts and Benchmarks-Tab FCM Bulk Letters, Cards. The Commission ruled in Order No. 536 that BMM is obsolete and no longer valid as a benchmark. *Order Adopting Analytical Principles Regarding Workshare Discount Methodology*, Docket No. RM2010-13 (Sept. 14, 2010) (Order No. 536). Consequently, and as the Postal Service correctly stated in the ACR (at 52), the calculation of the Automation Mixed AADC Letters pass-through is "no longer meaningful." The Public Representative's entire contention is based on a measure that has no validity, and thus has no merit.

As NPPC has explained both in this proceeding and in its comments on the recent adjustments of market-dominant prices, there is no justification for the Postal

[6] *Public Representative Comments*, Docket No. ACR2011 at 22-23 (Feb. 3, 2012).

Service's continued use of the admittedly obsolete BMM construct as a guide in rate design. The Public Representative's misguided criticism illustrates the errors that can arise from its continuing to do so. Indeed, as NPPC stated in its opening comments, a more accurate pass-through calculation would be available had the Postal Service compared the Automation discounts to the costs of Metered Mail, and would have shown a much smaller pass-through, perhaps even less than 100 percent. Such a measure would also have provided a better indication of whether the Mixed AADC discount provides the proper efficiency incentive.

Second, the largest and most important category within Presort letters is the 5-digit Automation discount, and its relationship to the AADC Automation discount is now becoming increasingly important. Pitney Bowes points out in its comments that the recently implemented adjustments to market-dominant rates eliminate any rate difference between the AADC letter discount and the 3-digit Automation letter discount. The Postal Service set the two rates equal in anticipation of possible changes in sortation levels stemming from the network rationalization process.[7]

Of course, discount rate design affects the efficiency signals given by the discounts. As Pitney Bowes notes, a consequence of setting the AADC rate equal to the 3-digit rate is that the proper reference point for assessing the 5-digit Automation rate logically becomes the AADC rate. This is because there is no mailer discount

[7] *Comments of Pitney Bowes Inc*., Docket No. ACR2011 at 8 (Feb. 3, 2012). *See United States Postal Service Notice of Market-Dominant Price Adjustment*, Docket No. R2012-3 at 14 (Oct. 18, 2011).

incentive or preparation requirement to use the 3-digit rate (which is equal to the AADC rate).

Using the AADC rate as the benchmark for the 5-digit rate has clear implications. For instance, the FY 2011 *ACR* reports that the pass-through between the *3-digit* and *5-digit* levels slightly exceeded 100 percent because the cost difference declined by 0.2 cents. But, at the same time, the *ACR* indicates that the difference between the *AADC* and 5-digit discounts in FY 2011was smaller than the 2.8 cents per piece cost savings between those two levels. In other words, in FY 2011, the 5-digit discount did not reflect all of the cost difference between the 5-digit and Automation AADC levels.

Although changes caused by the Postal Service's network rationalization process were not implemented in FY 2011, they are expected to begin in FY 2012. Accordingly, the ACR for Fiscal Year 2012 should compare the 5-digit Automation discount to the AADC discount, not to the 3-digit discount. At this time, NPPC will note only that the Postal Service's most recent rate adjustment passed through less than 100 percent of the 5-digit cost savings in the discount – whether compared to AADC Automation or to 3-digit Automation costs. That suggests that the 5-digit discount is too small and will generate inefficient signals in FY 2012.

III. CONCLUSION

For the reasons stated herein and in its opening comments, the National Postal Policy Council urges the Commission to work towards reducing the excessive cost contributions made by First-Class Presort mail without accelerating the departure of other mail, and to apply Section 3622(e) in a manner that reflects operational realities.

Respectfully submitted,

NATIONAL POSTAL POLICY COUNCIL

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