

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

VALASSIS NSA

Docket No. MC2012-14

VALASSIS NSA

Docket No. R2012-8

RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO CHAIRMAN'S INFORMATION REQUEST NO. 3
(MAY 21, 2012)

Chairman's Information Request (CHIR) No. 3 was issued on May 15, 2012.

The request sought answers no later than May 21, 2012. Attached are the Postal Service's responses to questions 1 - 9.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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1. At various places in its Notice and attachments, the Postal Service identifies various factors as key aspects of this contract, some of which appear to bear on its understanding of the requirement that the Valassis NSA be made “available on public and reasonable terms to similarly situated mailers.” 39 U.S.C. § 3622(c)(10). Does the Postal Service consider all of the following objectives, elements, principles, or terms of the Valassis NSA to be required in determining whether another mailer is deemed to be similarly situated?
 - a. “The **objective** of this Standard Mail market dominant agreement is to maintain the total contribution the Postal Service receives from Valassis Saturation Mail postage, and to provide an incentive for Valassis to find innovative ways to expand its use of Standard Mail.” Notice at 2. (Emphasis added.)
 - b. “The **basic agreement** consists of four key components: mailer eligibility, mail eligibility, mailing and volume commitments, and rebates on Standard Mail Saturation Flats Mail.... The Postal Service regards each of the four main elements described above...to be an essential component of this agreement...” Id. at 4, 6. (Emphasis added.)
 - c. “Th[e] **design imperative**—to generate additional contribution—and the basic structure of the agreement with Valassis...will guide the Postal Service in the negotiation of similar agreements....” Id. at 6. (Emphasis added.)
 - d. “[T]he Postal Service believes that the **defining characteristics** of Valassis are its size, its nationwide distribution network, and its significant volume of Saturation Mail. These characteristics enable Valassis to provide a new opportunity to durable and semi-durable good retail advertisers that is scalable across multiple media markets.” Id. at 7. (Emphasis added.)
 - e. “The **primary justification** for a Negotiated Service Agreement that will facilitate the new shared mail advertising offered by Valassis is the dynamic nature of how durable goods retailers are reaching the consumer.” Attachment E at 5. (Emphasis added.)
 - f. If there are any aspects of the Valassis NSA that the Postal Service will require for an NSA with a similarly situated mailer not stated in subparts a through e, please identify those aspects.

RESPONSE:

a–f. The Valassis NSA is a specific contract with a particular mailer. Neither the contract itself nor the Postal Service’s Notice were intended to interpret “similarly situated” for any hypothetical purpose. As noted in the Postal Service’s Notice, the Postal Service believes that mailer eligibility, mail eligibility, mailing and volume

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commitments, and rebates are main elements of the contract with Valassis. Notice at 6. The “design imperative” of additional contribution mentioned in the Notice reflects the substantive standard in 39 U.S.C. § 3622(c)(10)(A)(i) that agreements improve the net financial position of the Postal Service. Beyond that, it would be premature to speculate on how each of the elements of this specific agreement with Valassis would be interpreted in assessing whether a comparable agreement would be available to another, similarly situated mailer.

The terms of the Valassis NSA outline circumstances and conditions that both the Postal Service and Valassis have agreed would result in pricing incentives that would be beneficial to both parties. In particular, the NSA is aimed at enabling a right-priced saturation shared mail program for national durable and semi-durable goods retail advertisers that are not currently using the mail for their general-distribution advertising. The terms reflect the mutual conclusion that the conditions in the NSA are designed to account for the market characteristics of a particular advertising segment in a manner that will foster the new mailing programs and generate incremental contribution for the Postal Service.

The Postal Service is always willing to explore NSA opportunities with other mailers. As with the Valassis contract, the circumstances and factors that might condition such agreements will be assessed on a case-by-case basis.

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2. Will the mailpieces under the Valassis NSA be entered in envelopes or will they be wraps? If wraps, can FSS machines process those wraps?
 - a. Does the Postal Service anticipate that any or all of the mailpieces entered at SCFs under this contract will be processed on FSS machines? If not, please explain the rationale for the Valassis NSA requiring that qualifying mailpieces be at least 1/4 inch thick.

RESPONSE:

It is the Postal Service's understanding that the advertising inserts will be placed inside a wrap.

- a. The Postal Service does not anticipate that any of the mailpieces will be processed on FSS equipment.

The ¼ inch specification was agreed to as a condition that would define eligible mailpieces under the NSA. As a practical matter, this specification is subsumed within the other required physical attributes of the eligible mailpieces, including the three advertising insert minimum and the four-ounce weight threshold. See section II and section V.B. of the NSA agreement. Those two criteria, particularly the 4-ounce weight threshold, are expected to result in all qualifying pieces meeting or exceeding 1/4-inch thickness. The mailpieces will qualify as Standard Mail flats under the DMM.

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3. The Postal Service states that "Valassis must initiate new shared saturation mail programs in markets where it has maintained an existing Standard Mail Saturation mailing program on at least a monthly basis during the two years preceding execution of this NSA." Notice at 4. Further, "Valassis...must maintain its preexisting shared mail program for the duration of this agreement." Id. As to geographical areas where Valassis is already mailing on a weekly basis:
- a. Please explain how the Postal Service will handle a new mailing under the agreement assuming it is also on a weekly basis, addressing the following issues.
 - b. Is there any requirement that Valassis spread out these two shared saturation mailings so that they do not arrive on the same day?
 - c. Will mailings under the agreement be taken to the street as a third bundle?
 - d. How much excess capacity does the Postal Service have to take additional third bundles before manual collating of such third bundles or other costly delivery-related processing will be required?
 - e. Will this agreement increase Valassis' volume of mail to be delivered on Saturday? If so, what effect would the elimination of Saturday delivery have on the NSA, both from the standpoint of Valassis' ability to market the product, and the ability of the Postal Service to deliver the product?

RESPONSE:

a-e. Decisions on operational treatment of mail are made locally, based on local conditions. Processing and delivery of mailpieces qualifying under the NSA will be conducted in accordance with all procedures and regulations applicable to saturation mailings. The NSA does not specifically prescribe the days on which mailings must be presented, although the Postal Service has been informed that, for production reasons, Valassis plans to enter its current mailings and mailings under the NSA on different days. Beyond that, decisions on delivery practices and capacity considerations must be addressed with specific reference to the operational contexts in which they might arise. These will include any decisions concerning Saturday delivery. In this regard, Valassis has represented that there would be no impact to marketability, if Saturday were not available as a delivery option. Generally, the Postal Service does not anticipate major problems that would interfere with mailings under this NSA.

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4. In Attachment E, the Postal Service response to the requirement to “provide a description of the likely impact of the proposed modification on small business concerns” (p. 4) discusses only the effect on small businesses which deliver hard-copy advertising.
- a. Does this limitation on the Postal Service required response indicate that the Postal Service believes that no other small business concerns would be materially implicated?
 - b. Will the Valassis NSA have a positive effect or a negative effect on small businesses that currently compete with those national retailers who would be able to advertise at discounted rates under this NSA?
 - c. To the extent that any newspapers are considered small businesses, what could be the effect on them, as relates to their financial survival?

RESPONSE:

- a. Yes.
- b. The discounts the Postal Service is offering apply to Valassis, not to its advertisers. The Postal Service does not control the prices Valassis would charge to its advertisers. Small businesses across the nation already have options to join shared mail programs.

Further, it is unlikely to have much impact on small business currently competing with the national retailers that are eligible for this program. Due to their size and scope, those national retailers currently have lower cost advertising alternatives than do most small businesses. This is true regardless of the type of distribution: private delivery, newspaper delivery, broadcast or other electronic delivery. The rate structure offered by Valassis to retailers will not necessarily be discounted but will likely be competitive.

- c. Valassis' existing shared mail programs are primarily located in large to mid-size metropolitan markets where the primary newspaper competitors would not be considered small businesses. The NSA agreement restricts the new mailing program to

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those existing markets, so that small newspapers in markets outside Valassis' existing shared mail markets would not be affected.

Moreover, to the extent that there are newspapers that would qualify as small businesses in Valassis' existing markets, the NSA restricts Valassis to the carriage of advertising from national durable and semi-durable goods retailers. This excludes advertising from local and regional retailers that operate in fewer than 30 states, as well as all non-durable goods retailers such as grocery and drug stores, fast food and restaurants, and service businesses that likely account for a substantial portion of the advertising carried by small newspapers that would qualify as small businesses. Such newspapers can distribute their products – and any national retailer circulars they may include with their editorial content – either through low-priced Periodicals rates or through low-cost private delivery arrangements. Thus, they appear positioned to compete effectively, even under these contract rates.

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5. In its Notice, the Postal Service states that: "Private delivery alternatives to the mail are becoming technologically more sophisticated, offering prices substantially below the current prices of mail distribution, and aggressively marketing their services to saturation mailers, newspapers, and retail advertisers. Saturation mailers are increasingly looking to private delivery options, and newspapers are extending their reach through Total Market Coverage and Sunday Select (distribution to non-subscribers) delivered via nonpostal carriers." Notice at 3.
- a. Please explain the extent to which this reference to "private delivery alternatives" includes electronic delivery.
 - b. Please explain the ways in which the Postal Service believes that "private delivery alternatives" for hard-copy materials, such as retail advertising circulars, are becoming technologically more sophisticated.
 - c. Please provide any surveys, studies, or other information that the Postal Service has in its possession supporting its representations concerning:
 - i. the extent and growth of private sector delivery competition for hardcopy advertising circulars, and
 - ii. the extent to which prices offered by such private sector competitors for hard-copy delivery are "substantially below the current prices of mail distribution."
 - d. Please describe the extent to which existing Postal Service volume of Saturation Mail is challenged or threatened by those developments discussed or alluded to in the above-quoted statement in the Notice, as well as in the responses to preceding parts a, b, and c.

RESPONSE:

- a. It does not. Private delivery alternatives refer to non-postal general distribution print channels, which may include private carriers or newspaper delivery. However, it is clear that such advertisers are actively pursuing electronic delivery and broadcast options.
- b. In addition to independent private delivery companies, newspapers continue to invest and own affiliated companies that have focused on all aspects of private carrier delivery through the use of technology such as GPS, delivery routing software, and other computer-enabled devices, which better enable their capabilities to plan, track, monitor and measure results. Some of these technologies equal or exceed those

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currently used by the Postal Service. Additionally, newspapers are able to piggy-back their existing carrier route and labor efficiencies. The combination of improved technology and rapid migration to private delivery has provided a capital surplus for these companies to invest in further technological advancements related to the delivery of advertising. These combined elements present a formidable threat to this class of mail and, in turn, Postal Service mail volume.

c.

i. The U.S. Census Bureau's most recent Economic Census report revealed the Advertising Material Distribution Services industry (NAICS 54187) had dramatic growth across many of the measured key industry statistics including the increase of number of establishments, 646 to 931 (+44.1%), Receipts (\$ Millions) 1,488 to 4,171 (+180%) and Annual payroll (\$ Millions) 356 to 1,031 (+188%) – Source: U.S Economic Census: Industry Snapshot – Advertising material distribution services (NAICS 54187).

In addition, the Postal Service also reviewed numerous alternate delivery company, association, and industry websites. The review of leading alternative delivery company's CIPS Marketing and ADS posted 2011 press releases and product offerings provided many examples of the movement of Total Market Coverage programs from the mail to their services. The Newspaper Association of America website (www.naa.org) includes references to the migration of Total Market Coverage programs from the mail to alternate or private delivery companies. The NAA site includes the reference to a NAA commissioned study by Mather Economics entitled "How Are USPS Rates

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Affecting the Preprint Advertising Market?" which details the movement or planned movement of TMC programs to alternate delivery.

ii. The Postal Service used a variety of sources to determine private sector distribution prices, including review of industry reports and discussion with industry leaders. A survey conducted by the Saturation Mail Coalition (SMC) and documented in a 2009 article estimated a private delivery rate between \$0.08 and \$0.11 regardless of weight. See Free Paper INK Magazine, October 2009, pgs 7-10 and 20.

d. In addition to technology, private delivery companies, including those affiliated with newspapers, are more aggressively marketing this product to potential customers across the full saturation advertising mail distribution spectrum. Newspapers have filled this exact void by creating privately-delivered "Sunday Select" programs in over 110 markets, reaching 4.4 million households. (Valassis Internal Study) In addition, the Postal Service is aware that a number of saturation shared mailers of various sizes have been approached by private delivery companies to switch out of mail delivery. Some mailers have recently shifted portions of their distribution to private delivery or are testing such distribution. Many mailers have told the Postal Service that they are considering such changes.

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6. The Valassis NSA states: "The new mail programs covered by this agreement are limited to the carriage of advertising of national retail advertisers, defined as retail providers primarily offering durable and semi-durable goods and having a physical retail outlet presence in 30 or more states." Attachment B, Paragraph IV.D.
- a. What is the rationale for limiting qualifying mailers in this way?
 - b. Would any retail provider which advertises under this contract need to apply to be certified by the Postal Service to ensure that sales revenues from durable and semi-durable goods sold by the advertiser are their primary product lines, and they have not previously engaged in impermissible solo mailings?
 - c. Will the Postal Service and Valassis develop a list of qualifying retailers?

RESPONSE:

- a. The purpose is to segment the market by usage and needs. Saturation shared mail has been a reasonably attractive distribution channel for non-durable goods businesses, such as grocery and drug stores, fast food and restaurants, and service businesses. However, for many national durable and semi-durable goods retailers that have a need to reach a general audience on a regular and frequent basis, the distribution cost at current postal prices is an impediment to their usage of the mail.
- b. No.
- c. No.

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7. Under the Valassis NSA:

- a. Would each and every individual piece in the qualifying mailing be required to come from a qualifying retailer?
- b. If so, would the presence of one piece of mail from a non-qualifying retailer render the entire mailing ineligible for the discount? If not, what share of mail must come from qualifying retailers?

RESPONSE:

- a. Yes.
- b. Yes.

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8. As to mailers who had previously sent solo mail, the NSA provides for a specific "penalty in the form of a surcharge equal to the published solo mail price for such individual circular at the time of mailing." Attachment B, section IV.F. Since there is no similar penalty for mailpieces containing advertisements for retailers which do not meet the test of national retailers of durable and semi-durable goods and services, would inclusion of any one such advertisement disqualify the entire mailing from the rebate program?

RESPONSE:

Yes.

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9. To the extent that the Postal Service is aware, please explain:
- a. Whether private delivery alternatives, marketing their services to Saturation mailers, are focused exclusively on those who mail Saturation flats, or whether they also are marketing their services to mailers of Saturation letters.
 - b. Whether these private delivery alternatives are only marketing to national durable and semi-durable goods retail chains.

RESPONSE:

- a. The Postal Service is aware that this is occurring with respect to Saturation flats, but does not have information with respect to Saturation letters. However, we would assume private delivery alternatives would provide whatever is in the best interest of the market and best suits their businesses.
- b. The Postal Service is not aware of such limitations on marketing by private delivery alternatives.