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

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| NOTICE OF MARKET-DOMINANT PRICE ADJUSTMENT | Docket No. R2013-1 |

**COMMENTS OF THE**
**<u>NATIONAL POSTAL POLICY COUNCIL</u>**
(November 1, 2012)

The National Postal Policy Council[1] hereby respectfully submits these comments on the Postal Service's notice of rate adjustments for market-dominant products.[2]

NPPC believes that the Postal Service's rate adjustments miss several opportunities to price First-Class Presort letters – particularly 5-digit Presort letters, the Postal Service's most profitable category – more attractively to mailers and thus missed an opportunity to increase revenues and profits. Although the noticed adjustments do not appear on their face to violate prevailing law, several aspects of the changes affecting the First-Class and Standard letter prices paid by NPPC members are troubling, counter-productive to the Postal

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1 The National Postal Policy Council is an association of large business users of letter mail, primarily Bulk First-Class Mail using the Automation rate category, with member companies from the telecommunications, banking and financial services, insurance, and mail services industries. Comprised of 36 of the largest customers of the Postal Service with aggregated mailings of nearly 30 billion pieces and pivotal suppliers, NPPC supports a robust postal system as a key to its members' business success and to the health of the economy generally.

2 *United States Postal Service Notice of Market-Dominant Price Adjustment*, Docket No. R2013-1 (October 11, 2012) ("*USPS Notice*"). The Commission gave notice of these adjustments in Order No. 1501, 77 *Fed. Reg*. 64362 (Oct. 19, 2012). *See also* Order No. 1522 (Oct. 31, 2012) (extending comment period).

Service's asserted goals, and if perpetuated could eventually violate legal standards.

In particular:

- For yet another year, the rate increase for 5-Digit Presort Letters is the largest in First-Class Letters. Repeatedly imposing above-average increases does not encourage retention and growth of its largest and most profitable rate category;

- The Postal Service has unaccountably failed to make use of the pricing flexibility that it has, even under current legal interpretations, for First-Class Presort Letter discounts;

- The modest increase in Presort Postcard rates is undermined by the elimination of the 3-Digit discount, the largest volume category in Cards, which sends inefficient pricing signals;

- The excessive increase for additional ounces in First-Class Automation Flats – up to a 15 percent increase at heavier weights – raises an issue of just and reasonableness when compared to the rates for Standard Carrier Route flats, which pay about 1/5$^{th}$ the postage;

- The above-average increase in prices for Standard Letters will discourage letter volume growth;

- The new 48-cent Single-Piece rate for residual 1- and 2-ounce machinable letters, although presumably well-intentioned, will not benefit mailers but rather will increase costs for the vast majority of Presort mailers' residual pieces. Instead, the Postal Service should, consistent with the Presort rate design, set the price at 46 cents for the first two ounces of residual letters;

- Although commending the Postal Service for presenting its planned promotional discounts for 2013, NPPC recommends even earlier notice in the future. Also, NPPC is concerned that "baking" promotions into current prices may enable the Postal Service to exceed the rate cap;

- The Postal Service's insistence in charging for Picture Permit Imprint Indicia is ill-advised; and

- The Commission should continue to monitor the effect of service reductions stemming from network rationalization on the rate cap, as service reductions are tantamount to a rate increase.

## I. THE RATE ADJUSTMENTS FOR FIRST-CLASS AUTOMATION PRESORT LETTERS CONTINUE TO PENALIZE, NOT ENCOURAGE, THE POSTAL SERVICE's MOST PROFITABLE MAIL

First-Class Presort Letters and Postcards receive a 2.55 percent increase (*USPS Notice* at 14). Focusing on this average creates a misleading picture of the impact. A glance at the Presort rate categories makes evident that 5-Digit letters – by far the largest and most profitable category -- will experience a 2.9 percent increase and 3-Digit letters – by far the second largest and most profitable rate category[3] -- a 2.7 percent increase. Put differently, the two largest categories in Presort letters both receive an above-cap (2.57 percent) and an above-average increase. In comparison, the Single Piece rate will rise a below-average 2.2 percent.[4]

This is the second consecutive case in which the Postal Service has imposed an above-average increase on 5-Digit Presort letters. In last year's adjustment (Docket No. R2012-3), as in the one now under review, the Postal Service increased 5-Digit Presort Automation letter prices by 2.9 percent, more than 40 percent higher than the class cap 2.133 percent increase.[5] Such repeated disproportionate increases for 5-Digit Presort letters are not required by

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[3] *See* USPS-LR-201301/1, USPS_CAPCALC-FCM-R2013-1 (Tab Hybrid Yr. Billing Determinants).

[4] NPPC has difficulty understanding how, at a time when members of Congress of both parties in both Houses are urging the Postal Service to reduce costs and staffing levels, and approving bills to do just that, the Postal Service intends to drive costs out of the system by giving the smallest increases to the most costly mail, and the largest increases to the most efficient mail.

[5] In 2011, the Postal Service raised the 5-Digit Letter rate by less than inflation, although Presort Letters as a product rose more than inflation. *United States Postal Service Notice of Market-Dominant Price Adjustment*, Docket No. R2011-2 (Jan. 13, 2011).

law, by regulation, or by policy.  They discourage mail use and only encourage migration to electronic alternatives.  .

The Postal Service could have avoided this problem had it proposed more economically-sound prices that would encourage retention and growth of 5-Digit mail.  NPPC sets forth below some specific suggestions as to how the Postal Service could improve its proposals and the reasonableness of the rate schedule.

### A. The Postal Service Missed An Opportunity To Establish A Presort Benchmark That Would Establish Efficient Incentives To Encourage Volume Growth

Although the noticed First-Class Presort Letter workshare discounts do not appear to violate the statute on their face, the Postal Service has failed to take advantage of opportunities to encourage retention and growth of Presort mail. NPPC urges the Postal Service to seize these opportunities in the future.

One missed opportunity was the Postal Service's selection of the worksharing "benchmark" for Presort rates.  Although the Postal Service (consistent with the Commission's interpretation in Order No. 1320 now under judicial review, pursuant to which Presort discounts are "linked" to Single-Piece rates)[6] used Metered Mail as the benchmark for calculating workshare-related cost differences in order to set the discount for Mixed AADC Presort letters, it regrettably did not create a corresponding new Metered letter price in Single-

[6] *Consideration of Technical Methods to Be Applied in Workshare Discount Design*, Docket No.RM2010-13 (April 20, 2012) (Order No. 1320), *appeal pending sub nom. United States Postal Service v. Postal Regulatory Commission*, No.12-1221 (Respondent Brief filed Oct. 15, 2012).

Piece, as the Commission has twice suggested.[7] Instead, the Postal Service, despite the substantial differences between much of Single-Piece letter volume and metered mail, as if by habit once again took the discount from the full Single-Piece stamp. It stated merely that it is "considering" a new Metered mail price in Single-Piece in the future. *USPS Notice* at 37.[8]

NPPC regrets the Postal Service's failure to establish a Single-Piece Metered letter price at this time. Such a step would have allowed the Postal Service to price Presort letters in ways that could encourage retention and growth and would have benefitted many Single Piece mailers that use meters.

### B. The Postal Service's Proposed Workshare Pass-throughs Within First-Class Presort Letters Are Inefficient

The Postal Service also missed an opportunity to improve operational efficiency by passing through the full amount of avoided costs in its new Presort letter workshare discounts. The prevailing costs avoided and corresponding pass-throughs presented by the Postal Service are as follows:

| Category | Costs Avoided | P/T |
|---|---|---|
| Mixed AADC Automation | $0.059 | 93.2% |
| AADC Automation | $0.021 | 100.0% |
| 3-Digit Automation | $0.004 | 0.0% |
| 5-Digit Automation | $0.025 | 96.0% |

[7] *See* Order No. 1320 at n.20. *See also Annual Compliance Determination, Fiscal Year 2009* at 73 (Mar. 29, 2010) ("It should also be noted that the [former] benchmark for automation mixed AADC presort letters is currently BMM, not single-piece letters. With adequate justification, a separate rate for BMM could be introduced, further increasing the rate design flexibility of the Postal Service").

[8] The Postal Service recently published advance notice that it is considering proposing next year a separate price category for Single-Piece metered mail. 77 *Fed. Reg*. 64775, 64777 (Oct. 23, 2012).

For economically efficient pricing signals and to advance the principle of lowest combined cost, the discounts should be larger at the Mixed AADC, 3-Digit, and 5-Digit levels. It is also important to note that the Postal Service has significantly overstated the actual pass-through at the 5-Digit tier.

### 1. The Mixed AADC Presort level pass-through is unexplained

First, as the table indicates, the Postal Service will passthrough 93.2% of the difference between the Single Piece 46 cent stamp and the Mixed AADC Automation price. The Postal Service does not appear to have offered an explanation for this economically inefficient pass-through.

### 2. The 0 percent pass-through at the 3-Digit level continues the inefficient and costly policy of "pricing to excess capacity" rather than decreasing costs

Second, although it proposes a full discount to the AADC level, the Postal Service, as it did last year, has not passed through any of the cost differences at the 3-Digit level. Last year, the Postal Service justified the refusal to recognize 3-Digit cost savings on the grounds that it wanted (1) to preserve the AADC/3-Digit presortation options as it plans sortation levels as part of the network realignment process; and (2) to encourage the preparation of AADC/3-Digit presorted mail to improve operational efficiency because it then had excess capacity in incoming mail processing.

In its comments on last year's proposal, NPPC acknowledged that temporary dislocations in staffing levels are likely to occur during a network restructuring. However, it expressed concern about the dangers of "pricing to excess capacity" and that the failure to recognize any pass-through at the 3-Digit level would signal mailers to perform less efficient sortation and would not serve the system's long-term interest.

NPPC's warning has proven accurate. The billing determinants show a dramatic reduction in the volume of 3-Digit Automation Presort letters of about 1 billion pieces (or more than 1/3) between Q3 of FY11, when a 100 percent pass-through was in effect, and Q3 of FY12, when the pass-through was zero. Between the same two periods, the AADC letter volume nearly doubled, rising by nearly 1 billion pieces. *See* USPS-LR-2013-1/1 USSP_CAPCALC-FCM-R2013-1 (Tab Quarterly BDs). In other words, the Postal Service's failure to offer any discount for 3-Digit Presort letters has resulted in inefficient increased work for the Postal Service, because mailers have had no discount incentive to prepare mailings to the 3-Digit level. While this may have helped the Postal Service's goal of creating unnecessary make-work for excessive staffing levels, it has increased postal costs for no real benefit.

This policy of pricing to excess capacity is misguided and is inefficient. Moreover, it strongly suggests that the Postal Service is not serious about attempting to drive costs out of the system. The Postal Service makes its priorities most clear not through speeches but through its pricing proposals, and it appears that postal management is seeking to manipulate rates in order to avoid having to make further needed cost reductions. This is a course destined for failure.

NPPC is concerned that there is no end in sight for this undesirable rate design. The network rationalization process, assuming it stays on its current plan, will not be complete until 2014, and the Postal Service has not indicated when it will determine the most efficient sortation schemes for the post-realigned environment. Instead of setting a sunset for this inefficient policy, the Postal Service is now compounding the problem by *extending* the zero pass-through to 3-Digit Postcards.

The Postal Service merely states that sometime "[i]n the future" it will "have one, yet to be determined, sortation level between Mixed AADC and 5-digit." *USPS Notice* at n.25. This is small solace. At this point, the Postal Service is well into the implementation of Phase I of its network rationalization restructuring. The Commission should ask the Postal Service to present more clearly its future plans for Presort sortation levels.

### 3. The pass-through at the 5-Digit letter rate is less than the Postal Service asserts and gives inappropriate pricing signals

The newly noticed price for 5-Digit Presort letters is 36 cents. The Postal Service asserts that this reflects a 96 percent pass-through of the cost savings between the 3-Digit and 5-Digit tiers. It also states that the discount "has remained at 10 cents" compared to the Single Piece stamp. *USPS Notice* at 50. Neither is a sufficient justification for an inefficiently high price.

First, the Postal Service's claim that the pass-through is 96 percent is misleading. As the Commission has recognized, a consequence of the Postal Service's setting the 3-Digit price equal to the AADC price is that the "benchmark" price facing Presort mailers deciding whether to sort to the 5-Digit level is the AADC rate, not the 3-Digit rate. *See* PRC Order No. 987 at 12-13 (expressing concern about the pricing signals implied by pricing to excess capacity); *Annual Compliance Determination* FY2011 at 99. Accordingly, the relevant pricing signal for mailers considering whether to presort to the 5-Digit level is the pass-through of the cumulative cost savings between the AADC and the 5-Digit level.[9] On this more accurate basis, the avoided costs equal $0.029, and the pass-through seen by 5-Digit mailers from the AADC tier is only 82.75 percent, not 96 percent.[10] The Commission should require a better justification for this inefficient pass-through at the most important rate tier within Presort Letters, or order a reduction.

It is no justification that the difference between the 5-Digit price and the full Single-Piece stamp is 10 cents or any other number. Neither the statute, nor the Commission's regulations, nor any recognized rate design policy requires that there be any particular relationship between the full Single Piece rate and the 5-Digit Presort letter rate. That relationship is legally meaningless, irrelevant to business mailers, and lulls the USPS into ill-advised rates.

In fact, any insistence that the total rate difference remains unchanged guarantees, as a matter of mathematics, that the 5-Digit rate will always receive a higher percentage increase than the Single Piece rate. NPPC is concerned

[9] The Commission just initiated a rulemaking proceeding to consider changing as a formal matter the benchmark for 5-Digit Presort letters to AADC letters. *Notice of Proposed Rulemaking on Analytical Principle Used In Periodic Reporting (Pitney Bowes Inc. Proposal One*, Docket No. RM2012-6 (Oct. 23, 2012) (Order No. 1510).

[10] The costs avoided between the AADC and 5-Digit tiers are $0.025 plus $0.004, a total of $0.029. The discount is $0.024, which equals a pass-through is 82.75 percent.

that the Postal Service appears content to condemn the most-highly presorted, efficient, and profitable mail in the system perpetually to above-average price increases.

Furthermore, from the perspective of mail service providers, the "spread" between the Mixed AADC price and the 5-Digit price has significant business importance. Under the prices in effect today, that spread is $0.054, but the noticed prices would reduce it to $0.045. That is a reduction of $0.009 per piece for work done to co-mingle and barcode these pieces, which will cause smaller volume mailing services providers, for whom margins are vital, to suffer.

Had the Postal Service instead passed through the full amount of avoided costs between the 3-Digit and 5-Digit levels, the 5-Digit price would be $0.355 (assuming no other changes).[11] Passing through the full amount of avoided costs between the AADC and 5-Digit levels would result in a more moderate increase for the Postal Service's most profitable mail (and increase the "spread" seen by mailing service providers compared to the noticed rates). And as noted above, had the Postal Service used a new Single Piece Metered Mail price as the starting point for the Presort discounts, the 5-digit price would have been still more reasonable.

[11] As NPPC noted in its comments last year, had the Postal Service given 5-Digit a full pass-through at that time, the price would have been $0.346. If that were the price today, a 100 percent pass-through would again result in a new price of $0.355, but the change would be merely 2.6 percent, very close to average. The Postal Service's failure to set the price properly last year affects the new prices this year, perpetuating an excessive price for 5-Digit Letters.

## II. THE POSTAL SERVICE SHOULD NOT ELIMINATE THE DIFFERENCE BETWEEN THE FIRST-CLASS POSTCARD AADC AND 3-DIGIT LEVELS

NPPC, some of whose members use the Presort Postcard rate extensively, is pleased that the Automation Card rates increase is modest. This is welcome after the grossly excessive 9.63% increase in R2012-3.

However, NPPC is concerned about the Postal Service's extension to Postcards of the "temporary" economically undesirable practice of setting the AADC and 3-Digit Presort price at the same level. Within Postcards, the 3-Digit rate tier has the largest volume, accounting for approximately 50 percent of Presort Postcard volume. *See* USPS-LR-2013-1/1 USSP_CAPCALC-FCM-R2013-1 (Tab Quarterly BDs). That tier should be priced commensurate with its size and importance.

The Postal Service justifies its elimination of any recognition of 3-Digit presort cost savings on the basis of operational issues arising from network realignment, and for the convenience of mailers that combine Cards and Letters into the same trays. *USPS Notice* at 39.[12] NPPC's members do not believe that the logistical issue caused by two different Postcard price applicable to one tray is as big a concern as the Postal Service asserts. Nor does NPPC believe that effectively eliminating the 3-Digit price will promote efficiency, as it will merely remove a signal that would shift sortation work to the most efficient provider.

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12 The Postal Service states that if AADC and 3-Digit letters pay the same price, but Card rates differ at the same two levels, mailers encounter problems calculating the postage correctly. *USPS Notice* at 39-40.

In addition, just as in the case of Presort letters, because the Postal Service has set the AADC Card price equal to that of 5-Digit Cards, the relevant measure for calculating the 5-Digit pass-through is the AADC price. The discount at the 5-digit tier passes through only 85.7 percent of the total costs avoided between the AADC and 5-digit levels. The Postal Service should, as a matter of policy, set 100 percent pass-throughs at the largest volume tiers.

Finally, the Postal Service is passing through more than 100 percent of the costs avoided at the Postcard Mixed AADC tier. In addition to the reasons cited by the Postal Service (*USPS Notice* at 39), which NPPC supports, NPPC would further note that the Mixed AADC tier is one of the two smallest within Presort Postcards. The comparatively minor volumes at that tier mean that a modestly excessive discount will not lead to significant uneconomic presortation activity by Postcard mailers.

## III. THE ALARMINGLY LARGE INCREASE IN FIRST-CLASS PRESORT FLATS RATES IS UNEXPLAINED AND HARMFUL

The Postal Service describes the increase for Presort Flats as 2.675 percent, which it acknowledges exceeds slightly the CPI-U cap. *USPS Notice* at 9. It also asserts that the increases for 3-Digit and 5-Digit Automation flats are 3.5 percent and 1.5 percent, respectively. *Id.* However, these percentages severely understate the increases for heavy 3-Digit and 5-Digit Automation flats, which exceed 10 percent by the 4 ounce weight increment and reach 15 percent at 13 ounces.

The Postal Service does acknowledge the large increase on heavier flats when discussing Nonautomation flats, which it attributes to the increase in the price of additional ounces from 17 cents to 20 cents. *USPS Notice* at 17. But the increase in the additional ounce charge produces very large increases in the prices for extra ounce Automation flats as well. These increases inflict the most pronounced effect at the 3-Digit and 5-Digit tiers, which account for more than 72 percent of the extra ounces in Automation flats. *See* USPS-LR-2013-1/1 USSP_CAPCALC-FCM-R2013-1 (Tab Quarterly BDs).

These increases will prove particularly damaging to financial services and insurance companies, among others, that must mail documents to consumers to satisfy regulatory requirements. A number of NPPC members will be impacted in the 6-figure range, and at least one NPPC member estimates that the excessive rate increase for heavy flats will cost it nearly $1 million.

What these excessive increases demonstrate is that the rate design for heavy First-Class flats needs to be revisited. The increase hits heavier weights so severely because the 3-cent increase in the extra ounce rate applies to each ounce increment. As a result, although the maximum weight of a First-Class Flat is 13 ounces, the new rate design is tantamount to a pound rate of $3.772. By comparison, the pound charge in Standard Flats is rising to $0.699 (Carrier Route Flats at Origin entry) with a $0.135-cent piece charge.

NPPC is unaware of any cost analyses that would suggest that First-Class Automation Flats impose anything close to five times the costs of Standard Carrier Route flats, or of any pricing analyses that would explain why they should pay approximately five times more. Such discriminatory pricing between First-Class Automation and Standard Carrier Route flats, if unaddressed, could pose a substantial issue of whether this aspect of the rate schedule is just and reasonable.

## IV. THE ABOVE-AVERAGE INCREASE IN STANDARD LETTER PRICES DISCOURAGES VOLUME GROWTH

Standard Letter rates rise 2.722 percent, above the class average. NPPC members use a considerable amount of Standard letter mail for their marketing initiatives. NPPC is troubled that this above-cap and above-average increase comes while the increase proposed for Standard Flats – which as the Commission is well aware do not even recover their costs at current rates – is only a system-wide average 2.57 percent.

Disproportionate price increases on Standard letters relative to Standard Flats is a recurring problem. The Commission is well aware of this history[13] and NPPC need not repeat it here. While NPPC is sensitive to the Postal Service's concerns about the health of the catalog industry and so is hesitant to recommend steep price increases for Standard Flats,[14] the noticed Standard Flats prices fail to comply with the Commission's remedial orders and will continue the current intra-class cross-subsidy.

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[13] *Annual Compliance Determination*, Docket No. ACR2010, at 106 (Mar. 29, 2011), *affirmed in part and remanded in part United States Postal Service v. Postal Regulatory Commission*, 676 F.3d 1108 D.C. Cir. 2012).

[14] In the past, low catalog rates have been justified on the basis of a strong "multiplier effect" by which the advertising led to increased mail volume in other classes. NPPC has not seen a clear factual predicate for such a justification. If accurate, the benefit for all who use the system, provided it outweighed the costs of intra-Standard subsidization for Flats, could offer a basis for moderation in price increases for Standard Flats. Absent such a factual predicate, NPPC members support the Commission's direction on gradually increasing Standard Flats prices due to the intra-class subsidy.

NPPC members are among the many Standard Letter mailers that are disadvantaged by the current and proposed Standard Letter prices. And NPPC is rather concerned that the Postal Service is relying upon unproven future cost savings from network rationalization as a justification for below-cost rates for Standard Flats. It would be preferable to set prices on the basis of known, current costs, and moderate future prices in the future should anticipated cost savings, in fact, be realized.

The above-average rate increases for Standard letters, coupled with little apparent reason to believe that this situation will change in the foreseeable future, will tend to discourage significantly the use of that type of mail in marketing initiatives. NPPC urges the Commission and Postal Service to alleviate the excessive rates for Standard letters.

## V. THE NEW 48-CENT SINGLE-PIECE PRICE FOR RESIDUAL 2-OUNCE LETTERS WILL NOT BENEFIT MAILERS

Last year, the Postal Service successfully introduced into First-Class Presort Letters a zero cent charge for the second ounce of a 2-ounce letter. The goal of this "free second-ounce"[15] rate design, which has now been made permanent, is to provide Presort mailers with an incentive to make creative use of the extra allowed weight, thereby encouraging Presort mail volume. NPPC supported that proposal last year, and continues to support it now. Some NPPC members that were unable to take advantage of the "second-ounce free" last

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[15] The Postal Service refers to this as "free second ounce" in its *Notice*. *USPS Notice* at 9. This means that the second-ounce should truly be free and is not a blended rate.

year expect to do so this year, and NPPC commends the Postal Service for a successful rate design innovation.

This year, the Postal Service has attempted to address an unfortunate quirk in the pricing structure facing mailers that use the "second-ounce free" in Presort mail. As the Postal Service notes, residual 2-ounce First-Class letters that do not qualify for Presort prices pay the much-higher Single Piece first and second ounce postage, *and* mailers have to perform additional work "to separate out the 1 and 2 ounce pieces to accurately calculate the postage." *USPS Notice* at 16. The Postal Service proposes to address this problem by introducing a new "Single-Piece Residual Machinable Letters" price which would not increase with a second ounce.

NPPC accepts that this proposal is well-intentioned, and that the Postal Service believes that this proposal will help Presort mailers. Unfortunately, NPPC members are advising that the proposal in fact will harm, rather than help. NPPC asks that the Postal Service withdraw or revise this proposal.

If the Postal Service had simply extended "second-ounce free" to residual Single Piece mail, NPPC would have been as supportive as it has in the successful Presort offering. Unfortunately, that is *not* what the Postal Service has done. Instead, the Postal Service intends to charge a "blended" rate of 48 cents for all 1 and 2 ounce residual pieces that is *higher* than the 1-ounce Single-Piece rate. *USPS Notice* at 16. That means that a residual 1-ounce letter would pay 48 cents, not 46 cents. In other words, despite the cost saving mail preparation done by the mailer of the residual 1-ounce piece, that piece would be charged a higher rate than a hand-addressed greeting card mailed in a colorful envelope deposited in a blue box.  For one-ounce letters, the new blended 48-cent price is a three-cent, or 6.7 percent, increase over the current price, nearly triple the inflation rate.

Although NPPC has not conducted a formal membership survey, it appears that the extra two-cent charge built into the blended rate for 1-ounce pieces will, in total, cost mailers more than they will save by paying, in effect, 2-cents for the second-ounce rather than the normal 20 cents.  NPPC members anecdotally have indicated that the vast majority (over 95 percent) of their residual Single-Piece mail weighs less than two ounces.  And billing determinant data suggest that the percentage of Single-Piece letters that weigh more than one ounce is easily less than ten percent of the Single-Piece letter volume.  *See* USPS-LR-2013-1/1 USSP_CAPCALC-FCM-R2013-1 (Tab Quarterly BDs).

So it appears that the vast majority of Presort mailers with residual pieces will have a choice between: (1) paying 48 cents for all residual pieces; or (2) separating the 2-ounce pieces, paying 48 cents for them, and mailing the 1-ounce pieces separately at the normal 46 cent First-Class Single-Piece rate.  But separating the pieces by weight would require an additional run through the mailing equipment, which itself incurs an additional cost.

If the Postal Service wants to help Presort mailers in this area, a better design would be simply to charge 46 cents for both ounces, which would apply the established “free second ounce” design to residual Single-Piece mailings instead of the new, higher blended charge (which cannot be marketed as a "second-ounce free."[16] That would avoid imposing a larger-than-advertised increase on one-ounce pieces while providing some relief for the relatively small number of residual 2-ounce letters.

## VI. THE POSTAL SERVICE's PROVIDING A SCHEDULE OF PLANNED PROMOTIONAL RATES IS COMMENDABLE, BUT COULD BE IMPROVED AND PRESENTS A RISK OF CIRCUMVENTING THE CAP

NPPC is pleased that the Postal Service has met its goal of providing, for the first time, a schedule of planned price promotion for the next year. NPPC members are evaluating whether they will be able to make use of any of the promotions. However, at this point NPPC is able to note several concerns.

### A. NPPC Urges The Postal Service To Provide Even Earlier Notice Next Year

One fact that NPPC has been advised by numerous members, however, is that many of those and other members have already been assigned a fixed postage budget for the year 2013 as part of their corporate budgeting process, and the Postal Service's announcement of the promotions came too late to be taken into account in the budgeting process. That means either: (1) those members simply will not have any budget that will enable them to take advantage of these promotions; or (2) they would have to rearrange their mailings (especially their promotional campaigns) and possibly reduce or eliminate a proven mailing in order to free budget space for the (untested) new promotion. Few are likely to do so.

[16] The Federal Trade Commission regards the practice of raising the price of one component of a composite product, which a two-ounce letter is, in order to offer another part for "free" as an unfair trade practice.

Although it may sound almost ungrateful, NPPC urges the Postal Service to consider providing even more advance notice of planned promotions in the future. A year's advance notice may seem sufficient for many mailers, and it is. However, it is not for some of the largest potential customers whose mailing budgets for the upcoming year have already been fixed by October as part of larger corporate budget-setting process. In most cases, they simply cannot reopen their budgets now in an effort to obtain additional funds to use one of the scheduled promotions. Thus, despite this advance, NPPC hopes that the USPS will work with mailers in order to identify ways to provide even earlier advance notice in a way that can make a difference in large mailers' internal budget planning.

### B. The Commission Should Examine The Practice Of "Baking" Estimated "Leakage" From Promotions Into Prices Paid By All Mailers

Announcing the promotions as part of the annual adjustment has enabled the Postal Service to estimate the likely revenue "leakage" due to promotions and recover those losses by offsetting rate increases under the rate cap calculation. In this case, the amount affecting First-Class Mail as a class is relatively small -- about $13.8 million (and another $15 million in Standard Mail) – and accordingly does not seem to present a substantial material issue this time. However, if the amount of the promotional discounts were large, and were "baked" into general class rates, the outcome potentially could be unfair to mailers that cannot participate in the promotion.

In addition, “baking” estimates of promotional discounts into the rate adjustments opens a door to breaking the rate cap. In the future, the Postal Service conceivably could overestimate the extent to which mailers will use promotions, thus building excessive “offsetting” rate increases into the general rates. When the promotional discounts turn out to be used less than estimated, the result would be an above-cap rate adjustment.

In the past, other mailers have not had to pay for promotional discounts. The current *Notice* shifts the risk of failed discounts and overestimates of usage from the Postal Service to other mailers. It is, in fact, a troubling precedent, and one for which NPPC believes some reconsideration is in order.

## VII. THE POSTAL SERVICE’S INSISTENCE ON CHARGING FOR PICTURE PERMIT IMPRINT INDICIA WILL DETER THE USE OF AN OTHERWISE PROMISING INITIATIVE

NPPC members like Picture Permit Indicia. They add interest to mail pieces, and their use in lieu of pre-canceled presort stamps saves the Postal Service money. Therefore, NPPC remains perplexed over the Postal Service’s apparent zeal to discourage the use of such indicia by charging a fee for their use, and extending the fee in the *Notice* to flat pieces as well.

The Postal Service’s desire to charge a fee, which it began to do earlier this year as a result of Docket No. R2012-7, is self-defeating as it discourages mailers. NPPC is struck by the Postal Service’s plan to offer such indicia for free in one of its 2013 promotions, which seems an admission that charging for the fee is a mistake. Perhaps the Postal Service believes that mailers will become so addicted to the indicia that they will be willing to pay the fee in the future. This is unlikely, because the fee simply adds an additional cost to the investment necessary if one is to use Picture Permit Indicia.

Mailers, including NPPC members, will probably use Picture Permit Imprint Indicia to a limited extent even with the fee. But the Postal Service is missing an opportunity to add excitement and interest to the mail by treating Picture Permit Imprint Indicia themselves as a revenue source, rather than as a reason to use the mail. NPPC recommends that the Postal Service eliminate any fees for the use of Picture Permit Imprint Indicia on a permanent basis, not merely as a temporary promotion.

## VIII. SERVICE REDUCTIONS ASSOCIATED WITH NETWORK RATIONALIZATION SHOULD AFFECT THE RATE CAP

In its Advisory Opinion regarding the Postal Service's network rationalization proposal in Docket No. N2012-1, the Commission noted approvingly testimony to the effect that service quality reductions could be tantamount to rate increases. *Advisory Opinion on Mail Processing Network Rationalization Service Changes*, Docket No. N2012-1 at 151-155 (Sept. 28, 2012). To date, the Postal Service has not yet fully implemented Phase I of the plant closings, and currently intends to preserve overnight delivery for approximately 80 percent of First-Class Mail until January 31, 2014. *Id*. at 47. After that date, the new service rules premised on Phase II would take effect, and under current plans overnight delivery will be substantially reduced. *Id*.

The Postal Service contends that speed of delivery is not particularly important, and is of less importance than consistency. NPPC is not so sure. Many NPPC members face statutory requirements to provide legally-mandated notices within specific narrow time intervals; the statutes require speed, not "consistency." Others value speed for business purposes. In any event, economic theory recognizes that a classic tactic of a regulated entity operating under a price cap is to reduce costs by degrading service quality. *See Mail Processing Network Rationalization Service Changes, 2012*, Docket No. N2012-1, at 151-153 (Sept. 28, 2012) (Advisory Opinion) (summarizing testimony of Public Representative witness Neels and NALC witness Crew).

First Class Mail service standards are partially reduced from those that were in effect when the current rate cap regulations were adopted. NPPC believes that this reduction may reduce service quality, which has implications for the rate cap. In this instance, however, the degradation is of relatively recent vintage and may not yet be felt throughout the postal system. More substantial service reductions may not occur until 2014. Accordingly, it may be premature at this time to reduce the rate cap applicable to First-Class and Periodicals Mail – the classes whose service stands in the greatest jeopardy. However, the Commission should continue to monitor service quality, and considering initiating a formal proceeding to consider the effects of network realignment on the rate cap.

## IX. CONCLUSION

For the foregoing reasons, the National Postal Policy Council respectfully urges the Commission and Postal Service to take these comments into consideration and work towards prices that provide the proper incentives for First-Class Letter/Postcards mailers to use, and increase their usage of, the Postal Service's most profitable products.

Respectfully submitted,

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