

Before The
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

RATE ADJUSTMENT DUE TO EXTRAORDINARY
OR EXCEPTIONAL CIRCUMSTANCES

Docket No. R2013-11

**REPLY COMMENTS OF THE UNITED STATES POSTAL SERVICE RELATED
TO EXIGENT SURCHARGE REMOVAL PLAN**

(August 26, 2014)

In Order No. 1926, the Commission sought a report “providing a proposed plan for removing the surcharge for postage rates with a complete explanation of how the plan will operate.” Order No. 1926 (Dec. 24, 2013) at 193. The Postal Service submitted its report on June 2, 2014. Subsequently, Order No. 2089 (June 11, 2014) solicited comments addressing specific topics relating to that report. Six sets of comments were filed on July 28, 2014. The Postal Service hereby responds, but reiterates our earlier position that these comments are only relevant in the event that the requirement to implement a plan for removing the exigent surcharge withstands appellate scrutiny. The Postal Service continues to believe that rescission of the exigent surcharge as required by Order No 1926 is contrary to law and that therefore a plan to remove the exigent surcharge should be unnecessary.

Analysis of Workshare Discounts in Prior CPI Case

The National Postal Policy Council (NPPC) suggests that, if the Postal Service files for a CPI price adjustment before the exigent surcharge revenue limit is reached, then the resulting workshare discounts should be evaluated using both the resulting CPI prices, and also the prices after the exigent surcharge is added back in. NPPC Comments at 9. The Postal Service believes that, in a separate CPI filing, the statutory factors should apply to only the base rate plus the CPI increase. In Docket No. R2013-11, the Commission approved a fixed set of exigent surcharges intended to generate a fixed amount of revenue. As such, only the CPI prices (absent the surcharge) need to be subject to a workshare analysis in any CPI case that we might file before that fixed amount is reached. Keeping the passthroughs for both sets of workshare discounts under 100 percent would lead to lower discounts than necessary, and remove legitimate pricing flexibility from the Postal Service. Nonetheless, in any CPI case that is filed before the exigent surcharge revenue limit is reached, the Postal Service will present the actual prices that will result for its customers (including the exigent surcharges).

One or Two Filings

Some mailers argue that separate filings are needed if a roll-back is required and the Postal Service decides to do a contemporaneous CPI price change in conjunction with the Exigent surcharge removal. NPPC Comments at 6-8; MPA, ANM, PostComm, and DMA Comments at 3-4 (hereinafter MPA

Comments). The Postal Service disagrees. One filing would be sufficient both to remove the surcharge if it becomes necessary to do so, and to make concurrent CPI price changes. In fact, as explained below, the CPI case incorporates the surcharge removal under the procedures established by the Commission in Order No. 1926. Order No. 1926, at 178-81. CPI cases during the exigent surcharge period require the Postal Service to apply CPI to the base rates (without the surcharge). Then, the exigent surcharge is added back in to determine the actual prices that would be charged. But at the time of the exigent surcharge removal, the Postal Service would simply omit the step of adding the surcharge back in. The resulting rates would accomplish the surcharge removal.

Not only would that single case be simpler for the mailers, the Commission, and the Postal Service, but also it would more effectively allow for review of the actual prices that result from the two changes. A separate case in which the exigent surcharge is removed from the old prices (either the Docket No. R2013-11 prices or prices resulting from an interim CPI price change), would result in a set of prices that would never take effect, which would be inefficient and unnecessary.

GCA on Across-the-Board Surcharge Removal

The Greeting Card Association (GCA), advancing an additional argument made by no other party, advocates “independent” rescission of the surcharge, with no concurrent CPI adjustment allowed. GCA claims this is necessary to preserve the “across-the-board” nature of the exigent increase. GCA, however,

fails to identify any valid reason why the across-the-board nature of the exigent increase must be carried over to any subsequent actions removing the exigent increase.

GCA's argument that the Postal Service should be afforded no flexibility in rolling back the surcharge if it becomes necessary to do so is transparently hollow. In offering its exigent proposal, the Postal Service certainly did not commit to a perpetual across-the-board framework for rate changes. Before the surcharge was allowed, the Postal Service was limited to CPI-based rates, and after the surcharge is removed, the same limitation applies. The Postal Service is entitled to move to any new set of CPI-based rates that are allowed under the CPI rules. GCA essentially admits as much at the bottom of page 9 of its comments. The interim imposition of a temporary exigent surcharge in no way changes that, or can reduce the flexibility inherent in a class-based CPI regime. The Commission lacks statutory authority – at least on the grounds advanced by GCA – to withhold its approval of otherwise appropriate rate changes that simultaneously remove the surcharge and implement new prices within the CPI cap.

90-Days' Notice

In Order No. 2089, the PRC sought mailer input on whether the details of the Postal Service's surcharge removal plan, in the event one is ultimately necessary, would affect the desirable amount of notice. Order No. 2089, at 4 (June 11, 2014). In response to this inquiry, NPPC and

MPA, et al. support requiring the Postal Service to provide 90-days' notice before the effective date of the exigent surcharge removal. These commenters primarily argue that the 90-day notice period is needed to provide rate certainty, so that necessary programming changes can be completed. NPPC Comments, at 3-4; MPA Comments, at 2. In contrast, the Public Representative (PR) believes that 45 days should provide sufficient notice regardless of how the Postal Service chooses to remove the surcharge. PR Comments, at 14. The Postal Service agrees with the PR, and believes that the 45-day notice period prescribed in Order No. 1926 is the most appropriate.

While the Postal Service intends to provide as much notice of the surcharge removal (and any concurrent market-dominant price adjustment) as possible, 39 U.S.C. § 3622(d)(1)(C) and 39 C.F.R. § 3010.10(a)(1) clearly state that the Postal Service need only provide notice of CPI price adjustments “not later than 45 days” before implementation, and 45 days is the longest notice period provided for price changes in the PAEA. The Commission lacks the statutory authority to change such requirements in the context of this proceeding. Moreover, as NPPC recognizes in its own comments, the statute and rules pertaining to exigent rate cases are silent as to the amount of notice required for removing an exigent price increase. NPPC Comments, at 3. Outside the context of a rulemaking proceeding, the Commission cannot now mandate a minimum notice requirement. To do so would be completely contrary to the Commission’s historic reluctance to change its procedural rules in the middle of ongoing rate or

classification cases. See, e.g., Docket No. R2013-10, Order No. 1890 - Order on Price Adjustments for Market Dominant Products and Related Mail Classification Changes, at 18 n.30. Accordingly, despite mailers' arguments to the contrary, the Postal Service would be legally permitted to announce the removal of the surcharge (and any associated CPI changes) 45-days prior to implementation.

Moreover, putting statutory arguments aside, the Postal Service believes that there are additional reasons that militate against requiring that a notice of surcharge removal be filed more than 45 days prior to implementation. First, the Commission and mailers must recognize that it will be difficult for the Postal Service to project exactly when it will hit the surcharge revenue limit of \$3.2 billion. While such predictions could be made with some precision under perfect conditions (e.g. if future volume patterns were known), the Postal Service must instead forecast when it will reach the approved revenue limit using imperfect knowledge about future events and trends. Complicating matters further, the Postal Service must forecast when the exigent surcharge should be removed using lagging quarterly data that does not become available for analysis until several weeks after the close of each quarter. In that regard, if the Commission adopts a 90-day notice requirement, the Postal Service could be required to forecast the date of the surcharge rollback without the benefit of up to two quarters of revenue/volume data.¹ Given such inherent uncertainties, requiring

¹ For instance, if the surcharge needed to be removed effective July 1, 2015, the Postal Service would have to forecast the date of the surcharge rollback using data from Q1 of FY2015, since it would be the newest revenue data available on April 2nd (90-days prior to the expected removal date, but several weeks before data for Q2 becomes available). This extreme data lag could result in the Postal Service prematurely announcing the date of the surcharge removal, especially if substantially different volume trends become apparent in the finalized data for subsequent quarters.

that the effective date of the surcharge removal be announced 90 days in advance would greatly increase the risk of the Postal Service collecting more (or less) revenue than the approved limit.

Second, the Commission should consider the possibility that a standalone surcharge removal case is likely to be simpler than a typical CPI price change. Indeed, during such a case prices would simply be reduced by amounts that are already known. For example, if the Postal Service were to remove the exigent surcharge without having implemented an intervening CPI price adjustment, then market-dominant rates would return to those approved in Docket No. R2013-10. Similarly, if the Postal Service were to implement its annual CPI price adjustment in January of 2015, rates would revert to those approved in that docket. In either instance, mailers would know (many months in advance) what the market-dominant rates would be when the exigent surcharge was rescinded. Consequently, the need for an extended 90-day notice period is greatly reduced, as mailers would not have to wait until a surcharge removal notice was filed to begin preliminary programming efforts if that was the approach taken by the Postal Service.

Finally, while the Postal Service opposes the implementation of a 90-day notice requirement, it does not take mailers' programming concerns lightly. Indeed, the Postal Service itself faces equal, if not greater, pressures to develop and implement software changes across its nationwide network. Accordingly, the Postal Service has a vested interest in ensuring that mailers are well informed and prepared for any price adjustments that occur. NPPC, it should be noted, in

its Comments recognizes the Postal Service's efforts to communicate with mailers well in advance of regular CPI price changes. NPPC Comments at 3. The Postal Service intends to provide as much information and coordination with the mailing community as practicable in advance of any surcharge rollback that may be required. For example, the Postal Service will make postage statements and other materials available in user-friendly formats on *Postal Explorer*. In addition, price files (and other associated changes) will be discussed with the mailing industry through existing channels such as the Mailers Technical Advisory Committee, workgroups, webinars, and other mediums. As a result of these (and other) efforts, the mailing community will be in a position to begin their programming implementation far in advance of any necessary filing with the Commission.

In summary, while firmly opposed to any required extension beyond the 45 days specified for minimum notice in the statute, the Postal Service is committed to providing as much notice as it reasonably can. The unique challenges faced in this situation come from the inherent tension between setting any required expiration date as accurately as possible, and providing details on the what and when of any new rates as early as possible. The first objective is best achieved by delaying any decisions in order to evaluate (and fine tune the response to) new data, while the second objective pushes in the exact opposite direction. A deadline in excess of 45 days could seriously complicate the need to balance the two.

Valpak's Argument for Restoration of Unused Price Authority Has Already Been Rejected.

Valpak repeats its earlier argument that the unused rate authority that existed prior to the Exigent case (Docket No. R2013-11) needs to be restored when the Postal Service files to remove the exigent surcharge. Valpak Comments at 3-5. The Commission already rejected this argument when it determined that the Exigent price change exhausted all unused rate authority for each class, resulting in zero unused rate authority after Docket No. R2013-11. Order No. 1926 at 190-91 (December 24, 2013).

Forever Stamp PIHOP Adjustment

In contemplating an appropriate methodology for calculating the amount of exigent surcharge revenue as directed by Order No. 1926, the Postal Service realized that, compared with the more customary 1-cent and 2-cent (and zero) stamp price increases of the last decade, the 3-cent January increase (from 46-cents to 49-cents) created a much more significant incentive for mailers to stock up on 46-cent Forever stamps before the change, and then run down that inventory over the 49-cent surcharge period. Without some recognition of these circumstances, the Postal Service would be including 2 cents as surcharge revenue on letters for which 46 cents was paid, and no surcharge revenue was actually received. Therefore, the Postal Service estimated the amount of PIHOP revenue relating to Forever stamps as of the January change, and used that amount as an offset against surcharge revenues otherwise calculated (by

application of the 2-cent surcharge to the entire billing determinant volume of stamped letters) as if Forever stamps were not an issue.

This PIHOP adjustment was questioned in initial comments filed by the Public Representative and by MPA. These comments largely follow up on the issue raised by the Commission in POIR No. 13, Question 1, and addressed in the Postal Service's June 6, 2014 response to the question. That issue, in a nutshell, is whether Forever stamps purchased (but not yet used) during the surcharge period will likely offset Forever stamps purchased before the surcharge period and used during the surcharge period. The Public Representative, for example, questions whether there will be any asymmetry in the mailers' response, suggesting that under certain scenarios at the end of the surcharge period, mailers using stamps "may have little incentive to change their buying habits." PR Comments at 15. Therefore, it is necessary to examine mailer incentives in some detail.

To begin, there are at least two reasons why mailers can logically have been expected to significantly increase Forever stamp purchases prior to implementation of the surcharge. First, as noted above, the 3-cent increase was significantly larger than previous increases during the Forever stamp era, automatically creating above-normal incentives to increase the inventory of Forever stamps. Second, when the increase was announced, mailers also were put on notice that the surcharge was of limited duration, and the increase could be partially rolled back in a year or two. Mailers thus had the additional incentive that, with an adequate number of Forever stamp purchases before

implementation of the surcharge, the effects of the surcharge could be substantially mitigated or even entirely avoided. In particular, these circumstances would also thus increase the proclivity of mailers, during the surcharge period, to seek out and use any existing inventory of Forever stamps they might have tucked away, in order to postpone stamp purchases until after what they might expect would be a price rollback.

The PR Comments do not appear to question the extraordinary incentives created at the front end of the surcharge period. Instead, the PR Comments focus on the back end, highlighting the potential scenario in which subsequent CPI adjustments implemented at the end of the surcharge period result in little or no actual change in stamp prices, and postulate that this may result in “little to no change in buying habits.” PR Comments at 15. In essence, the Public Representative is merely acknowledging that the direction and magnitude of stamp price changes will drive Forever stamp price purchases in a period leading up to new rates. As explained above, if the changes will result in higher stamp prices, Forever stamp purchases should naturally increase, with the amount of the purchase increase greater as the stamp price increase rises. If, on the other hand, the change would result in lower stamp prices (i.e., a rollback), common sense dictates that customers will, if possible, postpone all stamp purchases until the lower rates are available. Alternatively, in the neutral scenario of most interest to the Public Representative, if broader rate changes result in no change in stamp prices, Forever stamp purchases would seem likely to be unaffected, and continue at the pace exhibited during normal periods when no price changes

are on the horizon. But expecting “no change in buying habits,” compared with a benchmark period of no anticipated stamp price changes, is in no way equivalent with expecting “no change in buying habits” compared with the exclusive benchmark period of interest here – the period prior to the January 2014 rate change, when a very substantial stamp price increase was scheduled. The Public Representative is engaging in the wrong comparison. Whether stamp prices remain the same when the surcharge period ends, or actually decline, there is simply no reason to expect the level of Forever stamp purchases during the period leading up to the end of the surcharge to equal the level of purchases in the period leading up to implementation of the surcharge. In other words, the Public Representative has identified no valid reason to question the asymmetry postulated by the Postal Service.

One additional argument advanced by the Public Representative merits special comment. The PR Comments suggest on page 15 that “mailers may not care,” apparently with reference to circumstances in which immediate purchase of Forever stamps saves them money on future stamp use, or contrasting circumstances in which postponed purchase of Forever stamps likewise offers the opportunity for savings. It is difficult to respond to such a baffling suggestion. Certainly, there may be *some* mailers for whom a penny or two either way on the price of a stamp is of little or no consequence, but, if that attitude were the prevailing one, then the Public Representative should have no qualms whatsoever about extending the surcharge period to account for a PIHOP adjustment. It seems much more likely, though, that many other mailers will

respond to the incentives inherent in a Forever stamp regime under circumstances of relatively large stamp increases, followed by at least the potential for a stamp rollback. Those circumstances establish a compelling case for the PIHOP adjustment adopted by the Postal Service.

In contrast with the PR Comments, the MPA Comments focus less on mailer incentives in the abstract, and more on quantification based on empirical data and analysis. MPA Comments at 5-6. Of course, those parties know that, while the challenges of untangling stamp purchases and stamp usage are daunting enough looking backward, the ability to satisfactorily do so prospectively, under varying scenarios with details that have yet to be determined, is even less likely. One suspects that, whatever amount of analysis the Postal Service provided, these parties would deem it insufficient. In this regard, the Postal Service is inclined to agree with a comment appearing on page 10 of the PR Comments on the more general topic of rescinding the surcharge: "Perfection will be elusive." That basic tautology, however, provides no legitimate basis to omit any PIHOP adjustment at all, which would clearly be wrong. The Public Representative is misguided to urge that resolution, and, to the extent that they indirectly seek the same result, the MPA Comments are equally misguided as well. The PIHOP adjustment advanced by the Postal Service properly takes into account reasonable expectations of customer behavior and should be accepted by the Commission.

Respectfully submitted,

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