

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Annual Compliance Report, 2014

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Docket No. ACR2014

**REPLY COMMENTS OF THE
AMERICAN CATALOG MAILERS ASSOCIATION**

(February 13, 2015)

Pursuant to Commission Order No. 2313 (Dec. 31, 2014), the American Catalog Mailers Association (“ACMA”) is pleased to submit these comments, which reply to the Initial Comments of Valpak Direct Marketing Systems, Inc. and Valpak Dealers’ Association, Inc. (“Valpak”) in this docket.

At great length, Valpak presents a pedantic discussion of product profitability and net income, drawing along the way on summary figures reported for various Standard Mail products. Valpak’s focus is unwaveringly on obtaining an increase in rates for Standard Flats and a decrease in rates for its Saturation Letters, consistent with price-cap constraints. Its principal argument is that the cost coverage reported for Standard Flats is below 100 percent, that the cost coverage reported for its Saturation Letters is unduly high, and that Postal Service profits would increase if associated adjustments in

rates were made. Throughout, Valpak professes interest in getting the cost coverage of Standard Flats to a level of 100 percent, which may be above the level that the Commission has found necessary to satisfy section 101(d).

At the outset, the magnitude of the changes Valpak supports should be noted. The loss shown in the FY 2014 CRA for Standard Flats is \$469.7 million. Before volume effects, reducing this to zero would require a rate increase for Standard Flats of about 22.6 percent and would result in an average rate reduction for other Standard mail of about 3.1 percent, a relatively small amount.

Determining the net effect of such an adjustment on the Postal Service would be difficult. It would require knowing the effects of any rate changes on the volumes, something that could be estimated only roughly, and knowing how the costs would actually change in the face of those volume changes. The volume effects would extend to First-Class, Carrier Route, High-Density, and parcels, through cross effects, relations which are understood to exist but which cannot be quantified. If volume effects *were* estimated, perhaps acknowledging limitations and high imprecision, the costs of record could be applied, but, as explained further below, substantial questions exist about these costs. In any case, contrary to the confident but baseless suppositions of Valpak, the net effect of the package of adjustments on the Postal Service would be a small fraction of \$469.7 million, and could be negative. Further, the adjustments sought by Valpak would virtually eliminate the Standard Flats product, decimate Carrier Route volume, and likely depress other categories, and thereby require the dismantling of large segments of the Postal Service's processing and distribution network, for a gain

that may well be a pipe dream. Valpak argues that the law requires such changes, a position repeatedly rejected by the Commission.¹

The difficulties with Valpak's prescriptions, however, go to much more than relative magnitudes and uncertainty of outcomes. They go to the imperative that theoretical frameworks must be tailored to the realities of the situation being analyzed. Valpak makes no attempt to do so. The following sections discuss some of the realities that Valpak fails to address or otherwise recognize. These realities are completely relevant and cannot be assumed away, as schoolroom economists are wont to do. ACMA has explained all of them before, to the end of neglect by Valpak. They are all part of going from theory to reality.²

1. Valpak fails to consider whether the Standard Flats category is a meaningful one for pointed cost coverage consideration. ACMA has explained that Standard Flats is a declining category that supports a range of flats mailings: (a) it is a category for small mailings and non-Carrier-Route portions of co-mail pools, and (b) it is

¹ See Docket No. ACR2010-R, Order On Remand (Order No. 1427), Aug. 9, 2012, at 4 ("The totality of circumstances presented is critical to Commission evaluations under section 3653"); see also FY 2013 Annual Compliance Determination, at 53-54, and FY 2012 Annual Compliance Determination at 115-116 (rejecting further finding of noncompliance against Standard Flats mail).

It is the Commission that evaluates the "totality of circumstances." In this regard, it may be noted that Valpak, in its comments, twice (at II-11 and VII-3), inaccurately attributes to the D.C. Circuit Court the statement that: "[T]he persistent losses incurred by Standard Flats amounted to a subsidy of Flats." Valpak omitted the Court's immediately preceding words: "In the Commission's view." *USPS v. PRC*, 676 F.3d 1105, 1106 (D.C. Cir. 2012).

² The issues summarized in the following paragraphs of these comments were presented and discussed in ACMA's initial comments in this proceeding. Further support for them is contained in ACMA's comments (initial, sometimes reply, and in one case surreply) and accompanying workpapers in Docket Nos. ACR2013, ACR2012, ACR2011, ACR2010, R2013-10, R2013-1, R2012-3, and R2011-2, which are incorporated herein by reference.

a companion to mailings that are partly or mainly Carrier Route. Today, nearly all bulk mailers, whether sending locally or nationwide, qualify as much of their mail as possible for Carrier Route, and count on Standard Flats for the remainder. Indeed the quantities sent by most mailers are dependent on the average rate for the two categories. Rate relationships between Standard Flats and Carrier Route must be coordinated. It makes no sense to review Standard Flats and Carrier Route separately.

2. Valpak fails to consider current work relating to the provision of FSS rates. The FSS is a very large and forward-looking investment of the Postal Service. It is important to both Carrier Route and Standard Flats. It has been clear for several years that the Postal Service needs to design rates that support the FSS and that guide mailers to efficient practices. The Postal Service has been working with mailers on this matter and questions surrounding it. In Docket No. R2015-4, which overlaps the instant one, the Postal Service is taking significant steps toward FSS rates. Those steps move a considerable portion of Carrier Route volume (as well as some High-Density volume) into the Standard Flats category, and present a uniform rate for the two, on the assumption that they will be intermeshed. This blurs further, and perhaps destroys, the distinctions between Standard Flats and Carrier Route, and makes it even clearer that it is not sensible to attempt to focus separately on the cost coverages of each.

3. Valpak fails to recognize that the costs available are not robust enough to support the prescriptions it writes. ACMA has analyzed pertinent costs over a period beginning in 1998, a period long enough to be unaffected by short-term

adjustment effects. ACMA has presented strong evidence that sufficiently serious questions exist concerning the available costs to warrant the conclusion that they are unreliable. We have shown that, overall, the costs of flats have risen inordinately and inexplicably. We have shown startling increases and unexplained behavior in mail processing costs, city carrier street costs, and city carrier in-office costs. It may be that a costing algorithm has assigned these costs to the respective categories, but it certainly is not the case that anyone can count on the costs being good estimates of how costs actually would change in the face of volume changes. Until these questions are answered, there is no reliable support for Valpak's prescriptions.

4. Valpak fails to recognize issues presented by the Nonprofit rates, which are included in Standard Flats. For the Nonprofit categories of Standard Mail, section 3622(a)(6)(A) requires that “[t]he estimated average revenue per piece to be received ... from each subclass of mail ... shall be equal, as nearly as practicable, to 60 percent of the estimated average revenue per piece to be received from the most closely corresponding regular-rate subclass of mail.” Under the PAEA, the Postal Service has interpreted the “most closely corresponding regular-rate subclass” to be, and the 60-percent requirement to apply to, the Standard class as a whole. See USPS Notice, Doc. No. R2015-4, Jan. 15, 2015 at 40. Therefore, the rates for the Nonprofit category within Standard Flats are tied to the Standard class rather than to the Standard Flats product. Under these conditions, it is inconsistent and illogical on its face to allow the low rates of Nonprofit mail to hold down the cost coverage of Standard Flats. The cost coverage of all Nonprofit mail should be estimated separately, and viewed as a

component of the class. The analysis required to do this has been provided by the Postal Service in Library Reference 27.

CONCLUSION

In view of the considerations outlined above, the only coverage that has meaning in regard to non-Nonprofit flats in Standard Flats is the cost coverage for the combined category consisting of Commercial Standard Flats and Commercial Carrier Route. ACMA showed in its initial comments that this coverage, using costs as reported despite the questions that exist about them, is in excess of 114.6 percent, passing handsomely the test set out by Valpak.

Respectfully submitted,

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