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POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Periodic Reporting (UPS Proposals One, Two, and Three) — Docket No. RM2016-2

REPLY COMMENTS OF NATIONAL NEWSPAPER ASSOCIATION
(March 25, 2016)

Pursuant to Commission Order No. 2793, National Newspaper Association (NNA) offers the following comments in reply to initial comments of various parties to this rulemaking.

NNA did not participate in the initial round of comments, but finds that its interests in the outcome of the proceeding have been affected by comments of the participants to date. NNA's members are about 2,400 community newspapers and their affiliated operations, which use all classes of mail, particularly Within County and Outside County Periodicals and Saturation and High Density Standard Flats.

1. **The impact of the changes in costing methodology proposed by United Parcel Service (UPS) could be profoundly negative for community newspapers, which are already under pricing pressure.**

United Parcel Service competes with the United States Postal Service's (USPS) offerings in various competitive product lines. In the instant rulemaking proposal, UPS alleges that the Postal Service's pricing of products in the competitive marketplace is subsidized by USPS's ability to cover certain costs through market dominant products. It suggests fundamental changes in the Postal Service's pricing methodology.

UPS proposes three changes: 1) to alter the way the Postal Service attributes certain variable costs to market dominant products by reclassifying some $13 billion in "inframarginal costs"; 2) to reclassify costs that USPS considers institutional or overhead costs so that a greater portion of those costs would be attributed to the individual products or classes; and 3) to reassess the contribution required in lieu of income taxes in the competitive products line. The Commission is holding the third proposal in abeyance pending the outcome of its deliberations in the first two proposals.

A. Newspapers already face fearsome pressure for price increases.

The comments of American Catalog Mailers Association (ACMA) et al, filed January 25, 2016, make clear what a dramatic impact the two proposals under consideration would have upon market dominant products. The combined new cost assignments to the products used primarily by NNA's members would result in the following cost increases:

Within County Periodicals	43%
Outside County Periodicals	33%
Standard HD and SAT flats	55%[1]

If adopted these cost increases portend devastating price consequences for newspapers.

The Commission and Postal Service continue to seek compliance with 39 USC 3622(b)(3), which requires all classes of mail to bear their own costs. Resulting pressure for prices to increase dramatically already exists for mail products that

[1] Calculated by ACMA, et al, in Attachment 1 to its comments.

currently fail to cover costs, a general category that includes Periodicals and Standard Flat mail, among others.

In the most recent full USPS fiscal year, Within County Periodicals achieved only a 74.49% cost coverage; Outside County Periodicals a 75.3% cost coverage. The Postal Service admits that this cost coverage continues to deteriorate because its costs are rising faster than revenues. Last year, costs increased by 2%. The overall price cap was 1.9%. The previous year, the Commission noted that while revenue per piece for Periodicals had increased by .8 cents, the costs had increased by a full cent. [2]

Mailers, the Postal Service and regulators have faced this situation for much of the last decade, with no clear demonstration that the rising costs are the result of changes in mail makeup, mailer behavior or anything else mailers can control. In fact, one Periodicals association insists the mail itself is more efficient and that the problem is a direct result of failures to achieve processing efficiencies.

> "The persistence of the less-than-100 percent reported cost coverages is the direct result of the Postal Service's failure to increase its efficiency in handling Periodicals mail despite "large investments in automation equipment by the Postal Service, and large increases in work-sharing by periodical publishers and their mail services providers." [3]

NNA is inclined to view the cost coverage problem somewhat differently. NNA believes the sinking cost coverage is primarily a consequence of overall rising USPS costs that most unfortunately affects a product whose cost coverage requirement was long ago set

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[2] Annual Compliance Determination Report, Postal Regulatory Commission, Fiscal Year 2014, at 34 et seq. (March 15, 2015).

[3] Reply Comments of Magazine Publishers of America, Inc., and Alliance of Nonprofit Mailers filed February 13, 2015 ("MPA-ANM Reply Comments") Docket No. ACR2014, at 2.

low to recognize the educational, cultural, scientific and informational value (ECSI) embodied in 39 USC 3622(c)(11). [4] The value of this mail is unchanged over the past decade. No one has suggested its mail makeup or characteristics have substantially changed either. So, if overall costs rise faster than inflation and prices are capped at inflation, cost coverage is guaranteed to deteriorate, through no fault of the mailers. Yet the Commission and USPS continue to examine issues specific to Periodicals in hopes of improving cost coverage without creating undue damage to the industry. NNA has supported many of those efforts and has recently engaged in intensive studies through the Postal Service's Kaizen projects focusing on handling and delivery efficiencies of newspaper mail. The Postal Service explains these efforts in its Annual Compliance report at page 27 et seq. [5]

The outcome of this protracted discussion about Periodicals cost coverage is yet to be determined, despite the multiple efforts of many parties to address the problem through rate changes, legislation, mail preparation, pricing design and other hopeful possibilities. If the Commission were to adopt either or both of UPS's proposals, it would either consign any hope of achieving cost coverage in the Periodicals products to the scrap heap or pass along devastating price increases to our members. Neither result

[4] In the benchmarking case of R2006-1, the Commission engaged in a lengthy examination of Periodicals costs and pricing incentives. It examined multiple proposals from industry to incentivize mailers' cost-saving behaviors and apply unusually detailed pricing governed by rate cell costs that are rarely even considered for the similar flats product line: standard mail. In the end the Commission recommended certain structural changes, a container and bundle charge and a revision in the method of calculating contribution to institutional costs. The resulting cost coverages were 100.2% for Outside County and 100.1% for Within County. [4] See extensive discussion of Periodicals costs and pricing incentives. Opinion and Recommended Decision of the Postal Regulatory Commission, Docket No. R2006-1 At 299 et seq. (February 26, 2007).

[5] United States Postal Service FY 2015 ANNUAL COMPLIANCE REPORT, (December 29, 2015).

particularly helps UPS. It certainly would damage the Postal Service. It would be the end of a lot of newspapers in the mail.

B. Declining service is a form of postal cost to industry.

Speaking solely for community newspapers in the mail, NNA urges the Commission to recognize the damage already done from the Postal Service's half-decade of cost-cutting in the form of service deterioration.

NNA President Chip Hutcheson, publisher of the Times-Leader in Princeton, KY, testified on January 21 before the Senate Committee on Homeland Security and Governmental Affairs about the substantial losses to community newspapers caused by the erosion of the Postal Service's delivery network. Because the link to the official Senate committee website has itself deteriorated, NNA provides a portion of Hutcheson's testimony here:

> The Postal Service has closed more than half of its mail processing centers in the past eight years. The centers that were closest to most of small town America are now gone or have had key functions downsized and removed to larger cities.
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> Just in my home state of Kentucky, we have lost processing operations in Somerset, Bowling Green, Owensboro, Paducah, Elizabethtown, Campton, Ashland, Pikeville and London. Mail that was handled in the state is now going to Louisville, Nashville, Huntington WV, Evansville IN, or beyond.
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> Just getting to the processing center can add an additional day to delivery. But it can add more than that if mail arrives just a bit too late to get on a critical truck taking processed mail back to a town we are trying to reach. If something else also goes wrong—for example, handling our mail is deferred because the plant is now focused on the growing package business—the delays can multiply.

Speaking for the Times-Leader, I can tell you that complaints to our circulation department increase every time a mail processing plant downsizes or closes. I can also say that we experience a slow-down in our own first-class mail, which we depend upon because it has invoices and checks in it. And I am told by publishers across the country that even Priority Mail has become a problem, which many small town publishers use to deliver payroll to their own staffs in news bureaus outside their headquarters. One publisher friend in Blackshear, GA, knowing I was preparing for this hearing told me on January 8, he had just received a Christmas card postmarked Dec. 21 in Fargo, ND. We were not surprised.

To validate my perceptions, I asked our members last week to update me on their experiences with newspaper delivery. Here is what our member survey told me:

- 92.5 percent have experienced problems reaching readers on time with their Periodicals newspaper;
- 40.3 percent report delivery problems with First-Class or Priority Mail;
- 49.2 percent attribute the problem to a closed or downsized plant; 44 percent say they don't know where the problem arose;
- 53 percent experienced a problem reaching core-market readers on time—either within their county or within the market but outside the county;
- 79 percent describe the Postal Service as critical to their survival.

It is difficult to assess how UPS would be helped in its competitive stance by forcing higher costs and resulting higher rates for NNA's vulnerable market-dominant products, in light of the problems the industry already faces. But it is clear that the industry is in no condition to absorb the blows either of the UPS proposals would create.

II. There is no perfect world in rate-setting, but rate stability is valuable.

Many commenters noted that there is no perfect solution for rate-setting. The National Postal Policy Council believes costs should be charged accurately, but takes no position on many of UPS's specific proposals. The National Association of Letter Carriers

(NALC) objects that the UPS has tried to advance its theory of fully-allocated costs before as a ploy to undermine the Postal Service. The ACMA coalition notes that many of its members have raised objections to cost attribution, cost coverage and other issues and probably would continue to do so.

Interestingly, the body whose intellectual process led to the current price-cap regime made a number of comments pertinent to this discussion, along with its belief that the Postal Service should not be able to use monopoly revenues to unfairly compete. The President's Commission on the Postal Service was established by President George W. Bush in 2002 to figure out how to save the Postal Service. After extensive hearings, consultant reports and conversations with stakeholders, workers and management, it recommended the rate cap concept in place today, and also offered these guideposts:

> The Postal Service should not be able to pass on the costs of substantial inefficiencies to mailers captured by the postal monopoly, and the quality of services provided in monopoly markets should be held to strict accounting. "Embracing the Future: Making the Tough Choices to Preserve Universal Mail Service, Report of the President's Commission on the United States Postal Service (July 31, 2003) at 53.
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> ***"***Of almost equal concern to frequent mailers as the *cost* of postal Services is the *predictability* of prices. Rate ceilings would permit mailers to factor rate increases into their business plans with greater predictability. They also would benefit Postal Service managers by giving the Postal Service a ceiling under which management knows they need to control costs. Report at 59

And finally,

> The Commission recommends that the Postal Regulatory Board, over the next two years, undertake an extensive process to design the most appropriate, workable and beneficial mechanism. While the Commission believes the Postal Regulatory Board should have broad

> latitude in doing so, it should generally strive to develop a mechanism that promotes: reduced costs and increased efficiency, rate predictability and stability, reasonable pricing flexibility, adequate revenues and a reduced administrative burden for the rate-setting process. Report at 62.

In short, the "regulatory board" (now the Commission) should do it all. Make it efficient, create incentives, design predictable and stable rates and fund universal service. It was a tall order—and an impossible one to achieve with unblemished perfection.

What is important about this modern history is that the President's Commission did not give a priority to protecting competitors over all other values that it considered necessary to the mission of universal service.

Nor did the Congress give competitors priority over all other values when it enacted PAEA. As the ACMA coalition has already noted, Congress set up multiple values in section 3622 that both USPS and the Commission must grapple with. The Commission has largely done so by adhering to the costing theories of Dr. John Panzar, who has relied upon measures of marginal costs as the starting point in cost attribution, but not the ending point in pricing. Many forces have affected the costs and prices in the system today.

One value both USPS and the Commission have kept as a priority, however, is price stability. With a few aberrations—the recently contested exigency rate being one--both the Service and the regulator have tried to avoid rate shocks. It is unclear whether UPS has fully weighed the scope of the rate shock it would pass to market dominant mail users and whether it has assessed the risk to the entire institution from that rate shock but the size of cost increases its proposals would support would suggest it has not. As

NALC has pointed out, UPS does rely upon the stability of the postal system itself, as it uses Postal Service carriers for a portion of its own delivery.

It is notable that the Commission in a recent case addressed competitive concerns in the newspaper industry's own objections to a USPS Negotiated Service Agreement. Newspapers believed they would be harmed by the NSA. The Commission relied on the timeworn antitrust doctrine: "It is competition, not competitors, which the antitrust laws protect." *Brown Shoe Company v. U.S.,* 370 U.S. 294, 320 (1962). In the review of the proposed Valassis, Inc., Negotiated Service Agreement, the Commission found that pricing that was in excess of attributable costs was not anti-competitive. Order 1448, Valassis NSA, Docket No MC2012-14, R2012-8 at 28.

UPS would say the statement begs the question because it does not consider the costs that lead to competitive rates to be fairly measured. NNA has no knowledge of the costing of competitive parcel and Priority Mail rates, but it observes that if UPS is right, and system-wide reattribution is undertaken, NSAs in the market dominant products would be far more difficult to create. NNA doesn't necessarily think a higher hurdle for these NSAs is bad, but the Commission must take the impact upon them into consideration.

III. Now is not the time

In 2017, the Commission will embark upon a major reassessment of the workings of the rate-setting system created under PAEA. NNA agrees with the ACMA coalition, NALC and others who point out that the exhaustive review will absorb much of the Commission's limited resources. It will have a similar impact upon the stakeholders, including UPS, who rely upon universal service and have developed their businesses in reliance upon the pricing and costing systems the Commission has developed, tweaked and sanctioned over the years. The parties could expect that UPS will bring its theory of fully-distributed costs to the 2017 rate review. If its objections to the systems in place have merit, the Commission has the opportunity to create a process that will allow all affected parties to examine them, recommend changes or object to new proposals. It would be unwise for the Commission to begin the 2017 process here. Rather it should consider the arguments of the parties as it designs the rate review and engage in the open and transparent process this Commission is known for providing all stakeholders.

Respectfully submitted,

Tonda F. Rush
CNLC, LLC
Counsel to National Newspaper Association
200 Little Falls Street, Suite 405
Falls Church, VA 22046
(703) 237-9801
tonda@nna.org