

Testimony of
The Honorable Edward J. Gleiman, Chairman
Postal Rate Commission
Before the
Subcommittee on the Postal Service
Committee on Government Reform and Oversight
U.S. House of Representatives

July 10, 1996

Mr. Chairman and Members of the Subcommittee,

Good afternoon. I am accompanied today by my fellow Commissioners-- W. H. "Trey" LeBlanc, George W. Haley, and H. Edward Quick. They have been very involved in our analysis of this legislation. Vice Chairman LeBlanc has submitted individual views for the record.

When I testified here 15 months ago, I closed my testimony by urging the Congress to address a fundamental public policy question: What should be the role of the Postal Service in the future? Mr. Chairman, 15 days ago, after months of hearings and careful consideration, you moved forward and addressed that question. H.R. 3717, the Postal Reform Act of 1996, would revolutionize the way postal rates are set and free the Postal Service to compete in many product areas.

My purpose today, is neither to endorse nor reject the economic premise on which the legislation is founded. You have developed a new, complex structure and I have not fully evaluated the variety of potential ramifications of implementing all of these changes. Hopefully we will have the opportunity to provide additional thoughts in the coming weeks.

In preparing this testimony I recalled a passage from John Steinbeck's *Travels with Charlie* which I think is apt:

A long time ago I was in the ancient city of Prague and at the same time Joseph Alsop, the justly famous critic of places and event, was there. He talked to informed people, officials, ambassadors; he read reports, even the fine print and figures, while I in my slipshod manner roved about with actors, gypsies, vagabonds. Joe and I flew home to America on the same plane, and on the way he told me about Prague, and his Prague had no relation to the city I had seen and heard. It just wasn't the same place, and yet each of us was honest, neither one a liar, both pretty good observers by any standard, and we brought home two cities, two truths.

We may ultimately differ on what is best from a public policy standpoint. Ultimately, however, in my role as a regulator I will work with you to ensure that

whatever the legislative output, this new paradigm is workable, with minimal confusion and dislocation.

So, today I have some questions, and some suggestions intended to clarify and strengthen your bill.

Among matters on which we definitely agree is your commitment to “maintain universal postal service to our citizens at a uniform, affordable rate” and your emphasis on the need to increase Postal Service efficiency (142 CONG. REC. E1159 (daily ed. June 25, 1996)). These policies should be the bedrock of any postal reform legislation.

My testimony focuses primarily on the proposed ratemaking reform. It presents a brief overview of how I think the new system is intended to work, and discusses several areas on which you may wish to focus particular attention. There are many other important issues which, given the limited time to prepare for this hearing, are not addressed in this testimony; and, we may have many more questions and, hopefully, constructive suggestions.

Mr. Chairman, I thank you and your staff for the courtesies you have shown the Commission during the drafting of H.R. 3717. While the actual proposal was a tightly held document, your staff has kept us apprised of your progress, and several provisions we suggested are in your bill. This cooperation continues. Last week our staffs met and clarified many matters of concern including: (1) the Commission’s subpoena authority is intended to extend to its audit responsibilities under proposed sections 3781, 3782, and 3783, and to consideration of complaints under revised section 3662; (2) in fulfilling its audit responsibilities, the Commission will determine whether prices for competitive products “cover direct and indirect costs” and “make a reasonable contribution” to overhead; (3) the Commission will determine both what costs are attributable and the costing methodology employed in the reporting and auditing process; and (4) the proposed amendment to the third sentence of section 3625(d) of title 39 (see, H.R. 3717, §1002(d)(1)) is not intended to change the conditions which under existing law apply to the Governors’ (Directors’) ability to modify Commission recommended decisions.

We look forward to continuing to work with the Subcommittee and will provide whatever assistance we can.

Following a brief overview of the bill, my testimony addresses the following issues:

RESPONSIBILITIES OF THE DIRECTORS

COMMISSION RESPONSIBILITIES

THE BASELINE CASE

NONCOMPETITIVE AND COMPETITIVE CATEGORIES

FLEXIBILITY

LEVEL PLAYING FIELD

VOLUME DISCOUNTS

EXPERIMENTAL PRODUCTS

FINALITY

PRICE CAP REGULATION

OVERVIEW

H.R. 3717 would divide postal “products” into two categories: Competitive and Noncompetitive. It would provide separate pricing mechanisms for these two categories.

Competitive products, initially, would include Priority, Expedited (Express Mail), Mailgrams, International, Parcel Post, and Special Services. The Postal Service would be free to price competitive products as it saw fit, subject only to the constraints of the anti-trust laws and the requirement that rates cover “direct and indirect costs” and make “a reasonable contribution” to overhead.

For Noncompetitive products, H.R. 3717 would replace the existing rate setting system, a “cost-of-service” system, with a form of incentive regulation which, to the extent it can be characterized, would be considered “price-cap” regulation. The bill

establishes five-year cycles for setting price caps, and annual rate adjustment authority for the Postal Service.

Noncompetitive products would be divided into four “baskets” as follows:

--First basket: single piece First Class letters, parcels, and cards (domestic and international).

--Second basket: all other First Class (domestic only).

--Third basket: Periodicals (regular rate, within county, nonprofit, classroom).

--Fourth basket: Standard (single piece, regular, enhanced carrier route, nonprofit, bound printed matter, special rate, library rate).

Every five years the Commission would conduct a proceeding to establish separate price caps for each of the Noncompetitive baskets. These price caps would be based on the percentage change in the Gross Domestic Product Chain-Type Price Index (GDPPI) modified by an “adjustment factor” which the Commission, after hearings, would determine for each basket.

The Postal Service could price Noncompetitive products as it saw fit, subject only to the requirement that prices, generally, could not exceed the price caps.

Interestingly, it appears that at today’s rates Competitive products would constitute only about one percent of total postal volume and generate 14 percent of total postal revenues. The volumes, revenues, and contributions to overhead of Noncompetitive and Competitive products under current classifications and rates are set forth in Attachment A.

Following enactment, one last omnibus rate case (the baseline case) would be conducted under, generally, existing procedures and rules. The rates from this case would, forever, serve as the foundation for future rate adjustments. This would be an especially important case for Noncompetitive products, which would never again have their cost base reviewed.

The Commission annually would audit the Postal Service to ensure it was acting in compliance with the law, with respect to both Noncompetitive and Competitive products.

A matter not directly related to rate setting, but which could nevertheless have a significant effect on the financial viability of the Postal Service, is the bill's narrowing of the postal monopoly. Section 703 of the bill would amend the Private Express statutes to allow private carriage of letters outside the Postal Service when the amount charged is at least \$2. This would replace the existing "double the postage rule." At current First-Class rates, the \$2 minimum would effectively exempt any letter weighing more than 8 ounces. Also, because the \$2 minimum would be a statutory limitation which is not indexed, more mail matter might qualify for this exemption as postal rates increase with the passage of time.

One feature of current law that could complicate application of the \$2 minimum is section 601(b) of title 39, which allows the Postal Service to "suspend the operation of any part of this section"—which would include the \$2 provision—"upon any mail route where the public interest requires the suspension." The bill does not repeal or alter the quoted language. Consequently, section 601(b) could be read to authorize the Postal Service to suspend and subsequently increase the \$2 minimum in selected service areas based on its assessment of what the public interest requires. The Postal Service may need this escape hatch. A 1992 General Accounting Office report concluded that Priority Mail would be immediately at risk to competition if the double the postage rule were suspended (*U.S. Postal Service: Priority Mail at Risk to Competition if Double Postage Rule is Suspended*, GAO/GGD-92-68 (May 1992)).

RESPONSIBILITIES OF THE DIRECTORS

H.R. 3717 greatly increases the responsibilities of the Postal Service Directors (now, Governors). It is the Directors who will set the rates for both Competitive and Noncompetitive products. Under the existing system, they adjust rates, generally, every

three or four years, and, at that, against a backdrop of an extensive body of public input. Under the bill, they would be adjusting many rates as often as annually. It is not clear, but perhaps they would also be required to pass on experimental market tests and volume discounts. Also unclear is the extent to which the Directors' deliberations would be governed by the Government in the Sunshine Act (5 U.S.C. §552b). Thus, it appears the Directors' responsibilities will increase substantially; and so will their liability. They will be subject to civil and criminal penalties under the anti trust laws (see, section 3744).

The bill would triple Directors' compensation, from \$10,000 per year to \$30,000. The salary increase is the first since postal reorganization 25 years ago and really amounts to little more than a cost-of-living adjustment. The bill contemplates that Directors will continue to serve part time. The 42-day per year statutory service limitation, which would be unchanged, may not be sufficient given their increased authority and responsibility (see, 39 U.S.C. §202(a)).

COMMISSION RESPONSIBILITIES

Mr. Chairman, I want to thank you for the confidence you have expressed in the Postal Rate Commission. You have pointed out that “[t]he bill enacts stringent reporting requirements to the Congress and to the U.S. Postal Rate Commission by providing the Commission with the ability to issue subpoenas, manage proprietary documentation and procure necessary information. This legislation places significant responsibilities on the Commission . . .” (142 CONG. REC. E1159 (daily ed. June 25, 1996)). Section 3723 gives the Commission final decision making authority in determining price caps. Under section 3783 the Commission would be given oversight responsibilities, not just with respect to Postal Service ratesetting and classification, but also with respect to determining whether the Service is meeting its performance goals, and, importantly, whether it is meeting its service standards. The Commission would determine if the Postal Service was truly delivering. An additional area of review should be Postal Service productivity, and the extent to which the Service is meeting reasonable productivity standards or targets it has established. Given the absence of residual stakeholders, i.e., stockholders, to hold the

Postal Service accountable for inefficiencies, some review of productivity is warranted. The absence of total factor productivity as a major consideration would permit huge and unwarranted rewards in the face of declining productivity. For example, postal officials are currently touting record “profits” for the second straight year and each of these years has seen a drop in productivity. Productivity also declined in 1994. In that year however, there were no profits. The difference: rates *and* profits increased in 1995.

Our initial reading of the bill suggests the Commission may need additional guidance as to how Congress intends it to meet these new responsibilities.

Determining the Adjustment Factor.

The ratemaking provisions (proposed 39 U.S.C. §3723) require the Commission to commence proceedings every five years to establish adjustment factors for the four baskets of products in the Noncompetitive category. These adjustment factors, coupled with percentage changes in the GDPPI, determine the “price caps” which apply to all Noncompetitive postal products. Proposed section 3723(c) lists six factors the Commission must consider in determining appropriate adjustment factors. These factors are similar to, but not identical to, the nine factors currently used to set rates (see, 39 U.S.C. 3622(b)). Proposed section 3723(c) also requires the Commission to take into account other “policies of this title” (i.e., the Postal Reorganization Act) in determining adjustment factors. I expect this is intended to include policies such as:

--“[t]he Postal Service shall have as its basic function the obligation to provide postal service to bind the Nation together through the personal, educational, literary, and business correspondence of the people” (39 U.S.C. §101(a));

--“[t]he Postal Service shall plan, develop, promote, and provide adequate and efficient postal services at fair and reasonable rates and fees . . .” (39 U.S.C. §403(a));

--“[t]he Postal Service shall provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining” (39 U.S.C. §101(b));

--“the Postal Service shall give highest consideration to the requirement for the most expeditious collection, transportation, and delivery of important letter mail” (39 U.S.C. §101(e));

--“[n]o small post office shall be closed solely for operating at a deficit, it being the intent of the Congress that effective postal services be insured to residents of both urban and rural communities . . .” (39 U.S.C. §101(a)); and

--“[a]s an employer, the Postal Service shall achieve and maintain compensation for its officers and employees comparable to rates and types of compensation paid in the private sector of the economy of the United States” (39 U.S.C. §101(c)).

The bill repeals the policy added by the 1976 amendments, that when setting rates recognition should be given to the educational, cultural, scientific, and informational value to the recipient of mail matter and relegates the concept of fairness and equity--- previously the first criterion for both ratemaking and classification---to an “also ran” status.

The explanatory material circulated June 24 with the draft bill sets forth examples where the adjustment factor is applied to *offset* increases in inflation as measured by the GDPPI. This is consistent with practice in other price cap regulatory regimens where the adjustment factor is typically a productivity offset. Subtracting an adjustment factor from an inflation index brings pressure to bear on management to control costs and operate efficiently. Proposed section 3723(e)(2), however, provides that “the adjustment factor shall be *added to* or subtracted from such change in the GDPPI, as the case may be” (emphasis added).

The second factor the Commission is required to consider in setting an adjustment factor is “[c]ost to the Postal Service of providing the product” (proposed section 3723(c)(2)). Is the Commission supposed to set the adjustment factors to ensure that the Postal Service may recover all of its costs? This question is critical.

Labor costs constitute approximately 82 percent of total Postal Service costs. While H.R. 3717 establishes a Postal Employee-Management Commission to study and

report on labor matters, it leaves the existing collective-bargaining system intact. I do not advocate changes in this area. However, the facts of the past and the expectations for the future may well clash when the adjusted GDPPI meets an arbitration decision.

Attachment B compares increases in postal labor costs since postal reorganization (as measured by the Postal Service's productive hourly wage rate for clerks, mailhandlers, city carriers, rural carriers, and vehicle service drivers) with two inflation factors, the CPI-U and the GDPPI, over the same period. Using 1971 as the base period, labor costs have increased by 340 percent, while the GDPPI and the CPI-U have increased by only 241 percent and 281 percent, respectively. If this trend continues, should the Commission establish adjustment factors which are *added to* the GDPPI, thereby permitting Noncompetitive postal rates to increase faster than general inflation? Or should it establish adjustment factors which are *subtracted from* the GDPPI, thereby forcing Postal Service management to operate more efficiently, and perhaps, indirectly, bringing substantial pressure to bear on the collective-bargaining process? It appears the latter is contemplated since the existing requirement that rates be set to permit the Postal Service to "break even" is repealed by section 1002(a) of the bill. Additional congressional guidance on this question would be helpful.

Audit Responsibilities and Authority.

H.R. 3717 creates a new, extremely important responsibility for the Commission -- annually reviewing Postal Service data and information to assure compliance with the Service's obligations under the law. This audit plays a central role in assuring that mailers continue to receive the kinds and quality of postal services envisioned in section 101 of title 39.

Fortunately, data collection systems and cost analysis methodologies which will be integral to audit efforts already exist. The bill allows the Commission to develop regulations so that data will be available in a form and detail to enable it to meet its new

responsibilities. At the same time, the bill directs the Commission to give due consideration to avoiding unnecessary effort and expense for the Postal Service. Over the years the Commission has been very responsive to Postal Service concerns of this nature. Current reporting requirements reflect a cooperative, continuing open dialogue between the agencies. This will continue. It seems, however, that the Postal Service would have no basis for withholding or objecting to the availability of any and all data pertaining to Noncompetitive products, since such information if disclosed could not, by definition, result in competitive harm.

The Commission is directed to make a written determination that all rates or fees placed in effect were in compliance with law.

In the area of Noncompetitive rates, the Commission would be responsible for assuring that the Service does not obtain revenues in excess of the maximum allowable for any product. This is the type of analysis the Commission has performed continuously during the past 25 years. It would have no difficulty in making such determinations.

For Competitive products, compliance with the law would mean rates which recover attributable costs and make a reasonable contribution as required by proposed section 3742(b). It is my understanding that the Commission would continue to exercise its current responsibility for determining what costs are attributable to the various types of mail. For the system to work, I view this role as self-evidently essential. In the past, the Postal Service contended that even service-specific advertising costs should not be attributed, a position rejected by the Commission. If, for example, the Postal Service could initiate a multi-million dollar advertising campaign to support a new, discounted Express Mail service or a nation-wide Priority Mail service, and unilaterally determine that those advertising expenses should not be attributed when evaluating whether the new service recovered costs, the annual audit would become meaningless.

Similarly, the Commission would be expected to exercise independent, unbiased judgment to determine that a product made a "reasonable" contribution to other postal costs. With respect to the reasonableness of the contribution to overhead made by Postal

Service competitive products, “reasonable” for a private sector competitor means recovery of all overhead costs.

There is some ambiguity in the language of proposed section 3783(b)(1). The Commission is to identify when “rates or fees were *placed in effect* . . . which were not in compliance with applicable provisions of this title” (emphasis added). The clause “placed in effect” is ambiguous: does it mean rates which are *offered* to the public, or does it mean only rates which are *changed*? This is an important distinction, because rates for competitive products which comply with the Act one year, might come to be below cost in a subsequent year if extensive additional resources are applied in providing service during a period when rates remain unchanged. Presumably, Congress and the public would like to know whenever the Service fails to adhere to the standards of the law.

THE BASELINE CASE

Proposed section 3701 requires the establishment of baseline rates and fees. In essence, it provides for “The Last Great Omnibus Rate Case.” Proposed section 3701 appears to contemplate a proceeding analogous to those conducted under existing law, although if the case is initiated after the enactment of the bill, pricing factors different from those required under existing law would be used to allocate institutional costs (*compare*, proposed section 3701(c), 39 U.S.C. §3622(b)). This baseline case is critical because it establishes the foundation for establishing price caps for Noncompetitive products. It will have long-lasting influence on the extent to which the Postal Service can recover institutional (overhead) costs from Competitive versus Noncompetitive products. I have two primary concerns: who establishes the revenue requirement, and the appropriateness of new pricing factors for this next and last omnibus rate case.

The Revenue Requirement.

Judicial precedents under the Postal Reorganization Act have established that the Postal Service has broad discretion to determine how much revenue must be generated by a rate case (*Newsweek, Inc. v. U.S. Postal Service*, 663 F.2d 1186 (2d Cir. 1981); *Time, Inc. v. U.S. Postal Service*, 710 F.2d 34 (2d Cir. 1983)). The bill appears to contemplate a

price cap system where the regulator would encourage the regulated entity to perform efficiently by limiting its ability to increase revenues simply to cover costs. Yet in the proceeding which sets the baseline for this new system, the regulated entity would have every incentive and, indeed, virtually unfettered authority, to pad its revenue at least for the short term.

A related issue is whether the revenue requirement for the baseline case should include amounts for contingencies and for prior years' losses. Proposed section 3723(f) provides a mechanism for the Postal Service to request relief from the price caps if it faces "severe financial exigencies." This is the type of emergency the contingency was intended for, so it seems inappropriate to include an amount for contingencies in the baseline case.

Another area where Congressional guidance would be helpful is the treatment of the provision for prior years' losses. This convention was established in the late 1970s by the Commission to help the Postal Service retire the substantial losses it had accumulated earlier in that decade. In recent cases, the Commission has allowed the Service to add one-ninth of its cumulative losses to the revenue requirement, with the intention of bringing the Postal Service's book equity back to its 1970 level in nine years. This practice substantially increases the revenue requirement. In the last omnibus rate case, Docket No. R94-1, \$936 million over and above expected operating expenses was allowed for this purpose.

While this convention was justifiable in the context of "break-even" ratemaking, should it be allowed to inflate the rates which will be the basis for the profit-oriented, price-cap ratemaking called for by H.R. 3717? The Postal Service Directors will be expected to use market-based rates to build and maintain sufficient equity over time, without regard to the figure which happened to be on the books when the 1970 legislation became effective. Inflating base rates over expected costs by hundreds of millions of dollars seems inconsistent with the new system, which is designed to limit rate increases to reflect an index of the economy as a whole.

The New Pricing Factors.

For almost 25 years omnibus rate cases have been conducted in accordance with the pricing factors set forth in section 3622(b) of title 39, United States Code. Section 3622(b) directs how institutional (overhead) costs shall be assigned to the various classes of mail and types of mail service. These criteria have been examined and applied in nine omnibus rate cases and numerous other proceedings. They have been interpreted repeatedly by the courts, including the Supreme Court in *National Association of Greeting Card Publishers v. U.S. Postal Service* (462 U.S. 810 (1983)). I suggest that rewriting them for one last omnibus case could raise uncertainties and might unnecessarily generate judicial appeals, which could frustrate the attempts to avoid administrative delays in establishing the new system which are built into the bill. Moreover, demand, which is identified as second most important of the proposed new factors, is among the existing factors and has been given substantial weight in recent Commission proceedings. For example, formulative measures of demand, i.e., elasticities, were significant factors leading to the establishment of an Enhanced Carrier Route subclass in the recent reclassification case (Docket No. MC95-1).

NONCOMPETITIVE AND COMPETITIVE CATEGORIES

While one might expect that the term “Noncompetitive” would equate with “monopoly” and “Competitive” would equate with “nonmonopoly,” this appears not to be the case under the bill. The Noncompetitive product category includes some products which are not subject to the monopoly, such as catalogs and magazines, for which little competition exists; and others, such as addressed saturation mail, which is subject to the monopoly *but* for which substantial competition exists.

Under the bill, the only constraint on the Directors’ pricing authority for Noncompetitive products is that prices, generally, may not exceed the price caps (proposed section 3724). This is a ceiling. There appears to be no floor. It appears that rates for Noncompetitive products could be set below cost, and that the Directors’ pricing activities in this area are not covered by the anti trust laws (proposed section 3744).

Thus, it appears the Directors could engage in predatory pricing with a Noncompetitive product such as saturation mail which, in essence, is a highly competitive product. I am not suggesting that they would; but, if their primary goal were to increase market share in the advertising market and eliminate competition from newspapers and others, they could (see e.g., *The Federal Times*, September 1993, quoting Chief Operating Officer William Henderson: “Henderson predicted, ‘ . . . the Postal Service, by the year 2000, will be the advertising medium of choice.’ . . . Two-day Priority Mail is a gold waiting to be mined, he added. ‘If we can make it two days, we could drive everybody out of business.’”).

There also appear to be some anomalies in the Competitive category, particularly in the Special Services area. Many special services such as post office boxes in rural areas and certificates of mailing and delivery may be available only from the Postal Service. Is there really competition for these services?

FLEXIBILITY

A principal feature of the bill is increased flexibility for Postal Service management in pricing products. What is the extent of this flexibility?

In the Competitive category, the only constraint is that rates must cover “direct and indirect” costs and make “a reasonable contribution” toward paying overhead (proposed section 3742). In the Noncompetitive category, generally, the only constraint is the price caps (proposed section 3724), although in many instances it appears numerous rate elements could be averaged to determine compliance with the caps.

Proposed section 3721 sets forth a rather complicated classification mechanism, consisting of “subordinate units,” “further subordinate units,” and, perhaps, even “further, further subordinate units.” The existing mail classification structure is incredibly complex. It consists not just of classes, subclasses, and rate categories. It also includes rate elements, discounts, pound and piece rates, surcharges, and zones. The drafters of H.R. 3717 have tried diligently to capture and address this complexity; but, the new, complex terminology raises new questions.

Under proposed section 3724 rates for products in the First Basket may not be averaged. For the other baskets, as we interpret the bill, rates at the subclass level could not be averaged, but rates at lower levels, e.g., rate categories and discounts, could. Attachment C attempts to classify existing “products” as subordinate units (not subject to averaging) and further subordinate units (subject to averaging). If this is correct, what does it mean? What is the true extent of pricing flexibility?

Three contentious proposals arose during the last decade in the Regular Periodicals subclass, formerly called second class. The Periodicals rates apply to more than 12,000 magazines and newspapers. They range from very small to very large, from local to nationwide, from light to heavy, and from bound to unbound. Some carry large portions of advertising and some carry none.

The first proposal was to give a discount to periodicals submitted to the Postal Service on pallets instead of in sacks or in some other container. To the degree that that discount depends on the minimum weight of the pallet and on the geographical make-up required for the pallets, it would have decreased rates for the larger mailers and increased them for the smaller mailers. The second proposal was to make pound rates for non-advertising material (commonly referred to as editorial material) vary with the distance the mail travels. This change would have increased rates for periodicals that go long distances and that have a high proportion of editorial content. The third proposal was to split periodicals into two products, one with high density and one with low density. In this case, density is defined roughly in terms of the proportion of postal delivery points in relevant delivery areas receiving the publication.

Each of these proposals was hotly debated. Each was discussed in terms of competition and other factors. The pallet discount was, after several steps, recommended by the Commission and then rejected by the Governors. The proposal to zone the editorial content of publications was rejected by the Commission in both the 1987 case and the 1990 case. The proposal to split second class into two separate products was also

rejected, although the rates finally recommended went a long way toward recognizing the cost differences on which the Service's proposal was based.

It appears that the bill would allow the Postal Service to implement its own version of all of these changes, and then some. That is, the Postal Service, following Federal Register notice, could implement a pallet discount, a zoned rate structure for editorial matter, and a bulk discount for high-density publications. Further, it could develop discounts based on other characteristics, and it could amplify the discounts that already exist. If changes of this kind were made, the potential exists to increase the rates for many thousands of publications by 20 to 30 percent or more to offset rate reductions for a relatively few publications by percentages of similar magnitude.

The nature of such a chain of events deserves attention. If the Postal Service develops a change and finds it possible under the new bill to make the change quickly and without the substantial cost of litigating it before the Commission, this saves time and money. But, what about those times when the proposal was found wanting? Then, perhaps, the time and money were well spent. For example, the third change discussed above, splitting periodicals into two products, one high density and one low density, was the key element in the reclassification proposal for second class in the first phase of reclassification, Docket No. MC95-1. After the Postal Service worked on the proposal for several years, there was a 10-month litigation period before the Commission. More than 40 pieces of testimony focused predominantly or in substantial degree on this issue. A range of second class mailers and mailer groups undoubtedly spent hundreds of thousands of dollars analyzing the proposal. Then, based on an extensive record, which included considerable attention to testimony from several economists with expertise in the regulatory area, the Commission recommended against the split.

Under the bill, the Postal Service, on the basis of short notice and limited or no additional review, could proceed with a quantity discount or a density discount to bring about almost the exact same split it originally proposed. There would be no need to consult with customers. Equally important, it appears there is no recourse short of a

legislative remedy. This type of extensive Congressional involvement is what the Postal Reorganization Act sought to reduce.

Classifying Products.

Classifying “products,” and identifying subordinate units and further subordinate units will be very important. Under proposed section 3741, it appears that the Domestic Mail Classification Schedule will be controlling, at least initially. Who interprets and applies its provisions? The Commission and the Postal Service have disagreed on this. Perhaps the bill should address the issue more fully.

45-Day Notice; Annual Adjustments.

For both Competitive and Noncompetitive products, the Postal Service may adjust rates only once each year and only after 45 days advance notice in the Federal Register (proposed sections 3724, 3742). In the Competitive area, does this give the Postal Service sufficient flexibility? If Postal Service management designs a Priority Mail marketing campaign to increase market share at the expense of its competitors, should it be required to disclose publicly those rates 45 days before the campaign begins? If a campaign launched in February flops, should management be able to change rates again in October? Although an annual limitation on rate adjustments would probably assist the Commission in performing its annual audit function, in all fairness, given the stated goal of increased flexibility, I wonder if these limitations are appropriate for pricing products in the Competitive category.

LEVEL PLAYING FIELD

In the Competitive category, does the bill really “level the playing field”? The anti-trust laws are made applicable; but is this enough?

Under the bill, the Postal Service would continue to enjoy other cost advantages that economists might view as artificial in a competitive arena. It would not have to earn profits for investors or pay taxes, even on its competitive activities, in the communities in which it operates. Economists might view this as a failure to recognize the “true

opportunity cost” of the resources that the Postal Service diverts from other economic uses in order to provide Competitive postal products. Also, except for a proposed limited experiment, the Postal Service’s monopoly on mail box access remains in effect.

Perhaps most importantly, the Postal Service still enjoys the stature of being an entity of the United States Government. This gives it an advantage in negotiating with foreign postal administrations over matters such as customs procedures. Additionally, despite the financing changes contemplated by Title IV of the bill, it appears the Federal Government would in all likelihood still be seen as an implicit guarantor of the Postal Service’s debt. This would allow the Service to borrow on terms more favorable than commercial enterprises in the private sector and, indeed, allow it to borrow in circumstances where no private sector firm could borrow.

Other advantages continue also. The Postal Service would continue to exercise eminent domain in instances where it deemed it advantageous to build processing or delivery facilities. It would also continue to be immune from parking tickets in accessing urban delivery points.

All of these give the Postal Service a competitive advantage not earned through greater efficiency and may enable the Postal Service to displace private competitors in competitive markets, even though it may not be the least-cost provider.

VOLUME DISCOUNTS

Section 604 of the bill would allow the Postal Service to offer volume discounts in a rate or fee, as long as all users of the class or service involved would be eligible for the same discount, and as long as the discounted rate satisfies a criterion applicable to the mail’s status in the Competitive or Noncompetitive category. The “equal access” provision in this section is necessary to promote fairness, and in my view should be an essential component of any Postal Service program of discounted rates. However, the discretion to set eligibility criteria can result in discrimination, and the discounts themselves deserve very careful attention.

Under current law and Commission practice, the Postal Service must justify volume discounts by demonstrating that there will be a cost saving, which usually results from worksharing performed by the mailer. The bill in its current form does not require any assessment of costs before discounts can be offered in the Noncompetitive area. Without an estimate of cost savings as a benchmark, the net effects of volume-based discounts on the revenues and costs of particular services could be difficult to gauge. Discounts, after all, reduce revenues for mail volume that is already in the postal system, and “loss leader” discounts for new volume may not produce a net financial benefit to the Postal Service, although they could be used to take business away from competitors. These issues should be addressed before discounts are put into effect.

Both section 604 and the ratemaking provisions in Title X of the bill require that each product in the Competitive mail category recover its direct and indirect costs and make a reasonable contribution to the other costs of the Postal Service. This is a reasonable and necessary standard, because it would prohibit cross-subsidies of Competitive products by the Noncompetitive category, most notably First-Class Mail. However, without an assessment of the respective costs and revenue benefits of a program of discounts for a competitive product, it could be difficult to establish whether this requirement is being met.

EXPERIMENTAL PRODUCTS

This bill grants the Postal Service broad authority to offer new or modified products on an experimental basis. An experimental product could be offered for up to three years before the Service would have to take action to make it a permanent Competitive or Noncompetitive product. The only substantive limitation is that a market test could not be conducted if its anticipated annual revenues exceed \$100 million.

First, it should go without saying that \$100 million per year is a huge amount of money for most businesses. Gross revenues of this magnitude, if achieved by the Postal Service relative to a single product or service, could seriously disrupt many existing markets. Of even more importance to mailers, if the Postal Service spends serious money

in the expectation of obtaining this much revenue, but it in fact loses substantial sums of money, the question then arises who must bear the burden of recovering these losses.

Recently the Commission granted Postal Service requests to increase its flexibility by adopting new rules of procedure. One week ago today, the Commission received a joint Motion for Reconsideration filed on behalf of diverse parties questioning the potential financial impact of the Commission's actions with respect to expedited treatment of provisional services and multi-year test periods (which did not grant nearly as much flexibility as H.R. 3717). I can not comment on the merits of the arguments presented. The Motion is included as Attachment D so that you can understand the depth of concern of those mailers that view themselves as captive to the Postal Service.

FINALITY

One aspect of the new ratesetting process that bears a special mention is that the current extensive provisions for multiple reconsiderations and judicial reviews of rate decisions would be eliminated. The Commission previously has testified in favor of eliminating some of these reviews in order to simplify and expedite the rate process. My opinion remains that the current system of multiple checks and balances is, in some instances, too much of a good thing.

At the same time, I suggest caution about going too far in the opposite direction. For individuals and numerous diverse business interests, the Postal Service provides the only hard copy access to every American. This means that a flawed rate decision could have a devastating impact on a sector of the business community.

H.R. 3717 provides no recourse and no remedy should the Postal Service implement rates that unintentionally or unwittingly destroy small businesses, or even a whole segment of an industry. For example, if rates for publications are changed so that copies sent locally pay much less, while copies sent to distant or rural areas pay much more, on average the increase might not exceed the GDPPI. Nonetheless, such a decision might leave a substantial number of low circulation publications with national mailing lists unable to afford to have their product delivered, and they might fail. Even if the

Postal Service rationale for its decision, as published in the Federal Register, was completely arbitrary or based on an inaccurate factual predicate, those publications would have no recourse. The Directors' decisions are final. They "are not subject to judicial or administrative review" (proposed sections 3724, 3742).

The complaint procedure also provides no effective remedy. In the previous example, suppose that when the Postal Service increased the rates for publications sent to distant areas it accidentally increased the rates for publications by more than the GDPPI. If a complaint is filed and the Commission finds it justified, relief still may not prevent many of the publications harmed by those rates from being put out of business. The Commission cannot order the Postal Service to change the unlawful rate. It can only order the Postal Service to set aside profits for limited purposes. If there are no profits, a complaint case is meaningless; and even if profits exist, the Service may satisfy its obligations by claiming to delay future increases for Noncompetitive products. Deferring an increase for all Noncompetitive products would be of little benefit to these low circulation publications.

In this hypothetical situation, publications may not be the only ones adversely affected. If the Postal Service changes rates so that it becomes uneconomic to send publications longer distances, citizens living in remote rural areas may effectively be denied access to many publications.

Earlier I discussed the predatory pricing possibilities created by the fact that several postal products in the "Noncompetitive" baskets are in direct competition with products offered by private enterprises. For example, Enhanced Carrier Route saturation mail competes with newspaper inserts. There is nothing that prevents the Postal Service from exploiting some captive users of one or more further subordinate units in Enhanced Carrier Route mail, for example catalog mailers, to cross-subsidize saturation mail's direct competition with daily and weekly newspapers.

Here again, a complaint to the Commission would provide no real relief to either the exploited captive mailers or to the private enterprise facing unfair competition.

H.R. 3717 appears to allow for exploitation of one further subordinate unit to benefit others. Even if the Commission were to find a complaint justified and find that a particular product should be reclassified as “Competitive,” the Directors could reject that recommendation and their decision would not be subject to judicial review.

I believe that there should be some mechanism to allow those who are convinced that certain Postal Service rates are in direct violation of law to present their concern, and if their concern is valid, to obtain relief. I suggest that if the Commission finds that the Postal Service has implemented unlawful rates, it should be authorized simultaneously to direct the Service to implement changes to bring those rates into conformance with the standards of title 39.

I am not confident that the anti trust laws, by themselves, will provide a satisfactory solution. While the specter of an adverse treble damage award may restrain stock-owning managers of publicly-held private businesses from unfair competition, Postal Service managers would be motivated by H.R. 3717 to stretch the edge of the competitive envelope. They would benefit in profitable years and would suffer no personal harm if they inadvertently go too far. An anti trust award against the Postal Service only will reduce taxpayers’ equity. It will not depress future profits which are measured on an accrual basis.

PRICE CAP REGULATION

Price-cap regulation is a form of incentive regulation. The incentive that drives price-cap regulation is the profit incentive. Owners of a monopoly franchise are offered a deal. In return for imposing a cap on prices, the regulator or legislature allows the monopolist to keep any profits it might earn through lowering costs. In other words, the price cap places downward pressure on prices, which translates into downward pressure on costs.

In a Postal Service where 80-85 percent of costs are labor costs, downward pressure on costs means downward pressure on total wages and benefits. A reduction in total wages and benefits can only be accomplished by reducing wage rates or number of

employees. Whether significant reductions of this kind can realistically be achieved without significant changes in postal labor-management relations and/or service seems questionable.

A second problem with price-cap regulation has been identified in the economic literature. This problem relates to the inability of a regulator to make an irrevocable commitment to maintain a price-cap mechanism no matter how much profit a monopolist earns. After all, the whole point of regulation--whether old-fashioned cost-of-service regulation or modern incentive regulation--is to prevent a monopolist from exploiting its monopoly power. Large, "obscene" profits are likely to be interpreted as evidence of monopoly exploitation, which in turn could lead to reimposition of stringent price controls.

With a very real threat of more stringent regulation hanging over their heads, owners of a monopoly franchise may prefer to forgo large profits in order to retain the pricing freedom that is available under price-cap regulation. But a self-imposed limit on profits is no different than one imposed by a regulator. In the end, price-cap regulation may not be much different from cost-of-service regulation in terms of ultimate outcomes.

Mr. Chairman, as I mentioned earlier, my testimony today focuses primarily on the new pricing mechanisms. We will, undoubtedly, have additional questions, comments and suggestions about this and other aspects of H.R. 3717 as consideration of the bill proceeds. I look forward to continuing to work with you. This, however, completes testimony for today. I will try to answer questions you may have.

Attachment A

	Noncompetitive Services				Competitive Services		Total
	First Basket	Second Basket	Third Basket	Fourth Basket	A Priority Mail		
	Single Piece First Class Letters, Parcels and Cards (domestic and international)	All Other First Class (domestic)	Periodicals	Standard Mail except Parcel Post	B Expedited Mail		
					C Mailgrams		
					D International Mail (except single piece First Class)		
					E Parcel Post		
					F Special Services		
					G Any product transferred to competitive		
Current Class or Subclass	First Class: Letters and sealed parcels (partial) 1/ Cards (partial) 1/ International (partial) 1/	First Class: Letters and sealed parcels (partial) 2/ Cards (partial)2/	Periodicals: Regular Rate Within County Nonprofit Classroom	Standard: Single piece Regular Enhanced Carrier Rte Nonprofit Bound Prnt Mtr Spec Rate Library Rate			
	1/ Nonpresort portion.	2/ Presort portion.					
Volume (millions)	58,924	36,647	10,467	70,048	1,997	178,083	
% of total	33%	21%	6%	39%	1%	100%	
Revenue (\$millions)	22,032	10,334	2,059	12,387	7,344	54,156	
% of total	41%	19%	4%	23%	14%	100%	
Contribution (\$millions)	7,912	5,762	242	3,598	2,211	19,725	
% of total	40%	29%	1%	18%	11%	100%	

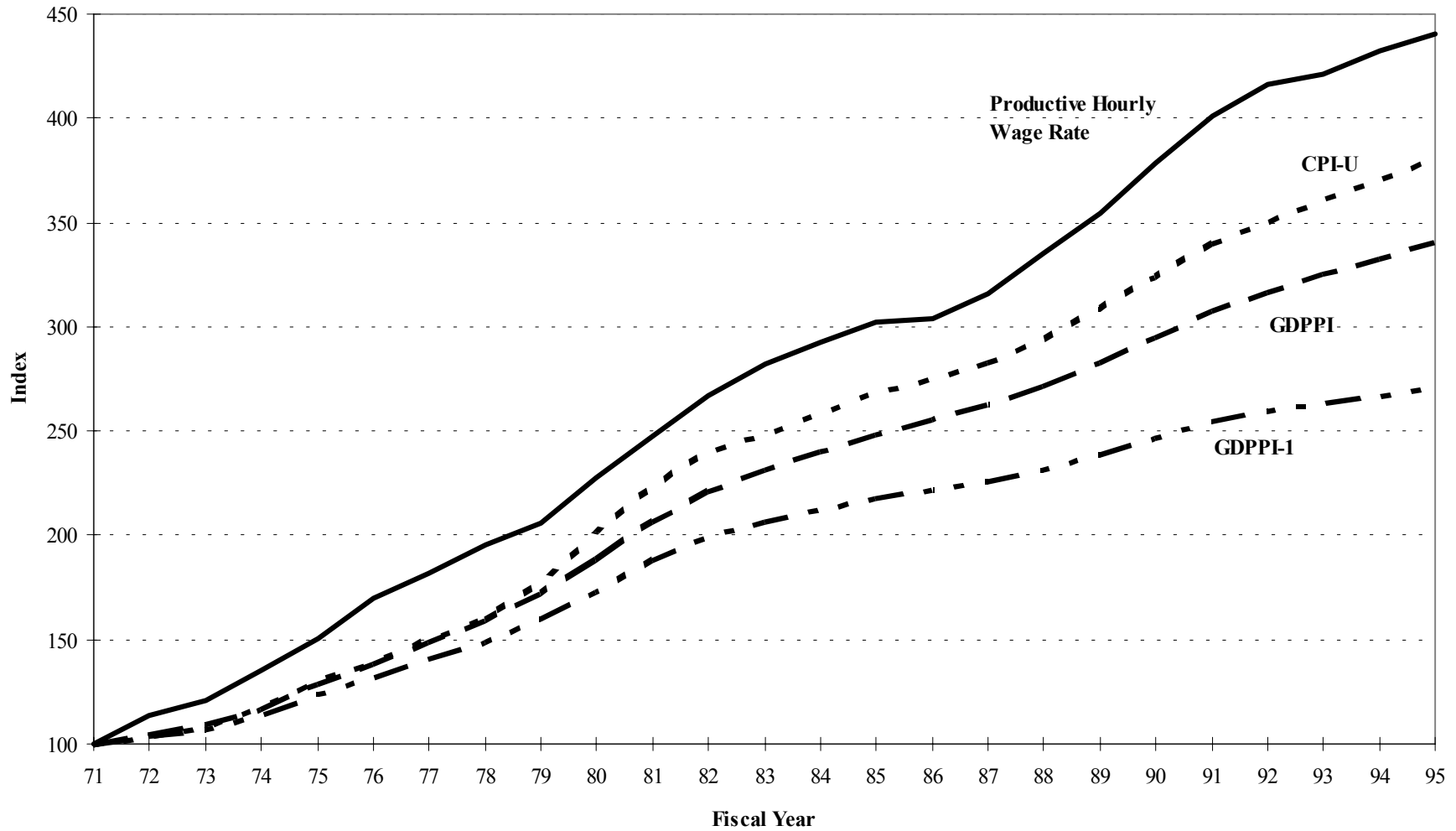
Breakdown of Competitive Services:

	Volume	Revenue	% Rev	Contrib	% Cont
Priority Mail	762	2,763	5.1%	1,362	6.9%
Expedited Mail	53	682	1.3%	108	0.5%
Mailgrams	5	8	0.0%	-	0.0%
International Mail	991	1,671	3.1%	299	1.5%
Parcel Post	186	678	1.3%	47	0.2%
Special Services		1,542	2.8%	395	2.0%
Total	1,997	7,344	13.6%	2,211	11.2%

Note: All International Mail data are included in Competitive Services figures.
Information breaking out First Class International Mail is not available.

Source: PRC R94-1 Opinion, Appendix G, Schedule 1.

**Indices for USPS Productive Hourly Wage rate, CPI-U, GDPPI, & GDPPI-1
1971 = 100**



USPS Productive Hourly Wage Rate for Clerks, Mailhandlers, City Carriers, Rural Carriers, and Vehicle Service Drivers from USPS Cost and Revenue Analysis Report and National Payroll Hours summary Report, FY 1971 - 1995
 CPI-U - Department of Labor, Bureau of Labor Statistics
 GDPPI - Department of Commerce, Bureau of Economic Analysis
 GDPPI - 1 assumes a negative one percent (1%) adjustment factor of the GDPPI each year

Subordinate Units in Bold
Further Subordinate Units in Italics

BASKET 1
(Rates for Basket 1 may not be averaged)

Single Piece First-Class Letters

Domestic
International

Single Piece First-Class Cards

Domestic
International

Single Piece First-Class Parcels

Domestic (weigh up to 12 ounces)
International (weigh up to 4 pounds)

BASKET 2

First-Class Letters (not single piece)

Presort
Automation Basic
Automation Three-digit
Automation Five-digit
Automation Carrier Route
Presort Flats
Automation Basic Flats
Automation Three- and Five-digit Flats

First-Class Cards

Presort
Automation Basic
Automation Three-digit
Automation Five-digit
Automation Carrier Route

BASKET 3

Regular Publications

Basic
Three-digit City and Five-digit
Carrier Route

Within County Publications

Nonprofit Publications

*Basic**
*Three-digit City and Five-digit**
*Carrier Route**

Classroom Publications

Science of Agriculture

[* proposed in MC96-2]

BASKET 4

Single Piece (weighing less than 16 oz.)

Basic
Keys and Identification Devices

Standard Regular (weighing less than 16 oz.)

Basic Sortation
Basic Sortation, Prebarcoded
Three- and Five-digit Presort
Three-digit Presort Letters, Prebarcoded
Five-digit Presort Letters, Prebarcoded
Three- and Five-digit Presort Flats, Prebarcoded

Enhanced Carrier Route (weighing less than 16 oz.)

Residual Basic
Basic Prebarcoded
High Density
Saturation

Nonprofit Standard (weighing less than 16 oz.)

*Basic Sortation**

*Basic Sortation, Prebarcoded**

*Three- and Five-digit Presort**

*Three-digit Presort Letters, Prebarcoded**

*Five-digit Presort Letters, Prebarcoded**

*Three- and Five-digit Presort Flats, Prebarcoded**

Nonprofit Enhanced Carrier Route (weighing less than 16 oz.)*

*Residual Basic**

*Basic Prebarcoded**

*High Density**

*Saturation**

Special

Single Piece

Level A (5-digit) Presort

Level B (Destination Bulk Mail Centers) Presort

Library

[*proposed in MC96-2]

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

Rules of Practice and Procedure)
_____))

Docket No. RM95-4

**MOTION FOR RECONSIDERATION OF
AMERICAN BANKERS ASSOCIATION, AMERICAN BUSINESS PRESS,
GREETING CARD ASSOCIATION, AND
THE NEWSPAPER ASSOCIATION OF AMERICA**

American Bankers Association ("ABA"), American Business Press ("ABP"), Greeting Card Association ("GCA"), and the Newspaper Association of America ("NAA") (collectively, "Movants"), respectfully submit this motion for reconsideration of the Commission's Order No. 1110 ("*Order*") in this proceeding.¹

In the *Order*, this Commission adopted special procedures for the expedited consideration of certain types of proceedings. Movants respectfully submit that two of these new rules -- the provisional services rule and the five year test period -- should be reconsidered. In particular, Movants urge the Commission:

- To rescind the rule (39 C.F.R. §§ 3001.171 *et seq.*) for expedited consideration of "provisional" services;² and
- Limit multiyear test periods (39 C.F.R. §§ 3001.181 *et seq.*) for new services to, at most, three years.

¹ 61 *Fed. Reg.* 24,447 (May 15, 1996).

² Alternatively, should the Commission be able to articulate exactly what a "provisional" service is and how it differs from "experimental" or "new services," the Commission should treat this motion as one for clarification.

I. INTRODUCTION AND STATEMENT OF INTEREST

Movants represent thousands of mailers that collectively use all classes of mail. While Movants represent a variety of interests, they share a deeply-held concern that the Postal Service must not use revenues generated by First Class, periodicals, and other captive mailers to support ill-advised ventures and that the Service, as a public service, must not favor some mailers at the expense of others. This motion is filed out of a strong belief that the new rules for provisional services and *five*-year test periods for new services pose a substantial risk of precisely such dangers. Accordingly, they respectfully urge the Commission to reconsider its recent *Order*.

ABA is the only national trade and professional association serving the entire banking industry, from small community banks to large bank holding companies. ABA members represent approximately 90 percent of the commercial banking industry's total assets. About 94 percent of ABA members are community banks with assets less than \$500 million.

ABP is an association of over 100 publishing companies that mail at periodical rates approximately 700 trade, professional, medical, and business periodicals to readers in every industry and profession. ABP filed comments on the proposed rules that were adopted by the Commission. In every rate and most classification cases that have come before this Commission, ABP has been the primary advocate for thousands of nationally-circulated smaller-volume periodicals.

GCA is a trade association representing many of the greeting card producers in

the United States. In 1995, an estimated 7.4 billion greeting cards were purchased by American consumers, most of which were sent by First-Class mail. GCA represents the interests of its members as well as the interests of over 95% of American households which mail greeting cards.

NAA represents approximately 1,500 newspapers in the United States and Canada. Members account for about 85 percent of the daily circulation in the United States. Many non-daily newspapers also are members of NAA. NAA members are users of all classes of mail, and spend several hundred million dollars annually with the Postal Service.

Although Movants have specific concerns, as described below in Sections III and IV, with each of the new rules for provisional services and the five years allowed for the test period for new services, they also have fundamental concerns of a more general nature that arise from the mandates of the Postal Reorganization Act, as discussed in Section II below. For these reasons, Movants submit that the new rules are inappropriate and should be rescinded (provisional services rule) or modified (multiyear test period to no more than three years).

II. THE ORDER FAILS TO CONSIDER ADEQUATELY THE CONSEQUENCES OF THE COMMISSION'S LIMITED POWERS UNDER THE ACT ON ITS ABILITY TO MONITOR PROVISIONAL SERVICES AND TEST PERIODS OF UP TO FIVE YEARS DURATION

Whatever might be the appropriateness of the expedited rules for provisional services and the five year test period for new services in the case of a private, commercial firm subject to the discipline of shareholder oversight as well as the competitive market, they are inappropriate for a large governmental institution that is required by statute to operate in the public interest. The Postal Service's status as a government service not only confers substantial benefits and powers that private businesses do not enjoy -- such as immunity from tax laws and a legal monopoly over the vast majority of its products -- but also creates incentives markedly different from those facing a private business. Unless and until these fundamental differences are changed by Congress, they have a major bearing on the propriety of the final rules, and militate in favor of reconsideration.

The Postal Service has plainly demonstrated over many years that its major motivation is the generation of increased volumes. Such a goal poses a particularly strong danger that the Postal Service will underprice "provisional" services or market tests of five-year duration in order to maximize volumes, secure in the knowledge that other mailers will pick up the tab.³

³ See *Comments of the Newspaper Association of America*, Docket No. RM95-4 (Jan. 11, 1996) ("*NAA Comments*") at 4-5, 9-12.

This danger arises under current ratemaking practice because any financial losses that the Postal Service incurs in an expedited service venture, or over a five year test period, will simply become part of the Prior Year Loss component of the revenue requirement in the next rate case. Because Prior Year Losses are apportioned in the same manner as institutional costs to be recovered, any financial losses stemming from ill-advised or underpriced "provisional" services under the new rules effectively would shift from the users of these services to First Class or other small volume mailers that lack alternatives and that cannot qualify for the provisional service.⁴ This would constitute a cross-subsidy of such services,⁵ a result specifically rejected by Congress.⁶

Although the Commission in the *Order* acknowledges the merit of this concern, it simply asserts a belief that it has fashioned rules "that will serve to limit the potential

⁴ First Class mailers currently pay approximately 69 percent of institutional costs. *See Postal Rate and Fee Changes, 1994*, Docket No. R94-1 at Appendix G, Schedule 1 (November 30, 1994) (Opinion and Recommended Decision). In the past, the Commission has declined to accept proposals that prior year losses should be recovered from subclasses of mail that can be shown to have caused the losses. *Id.* at III-60-64.

⁵ By definition, since the new or provisional service would have lost money, its rates could not have met the statutory requirement that they recover their attributable costs. *See* 39 U.S.C. § 3622(b)(3).

⁶ As the Senate Report stated: "The temptation to resolve the financial problems of the Post Office by charging the lion's share of all operational costs to first class is strong: that's where the big money is." S. Rep. No. 912, 91st Cong., 2d Sess. 13 (1970) ("*Senate Report*"). In addition, although small volume periodicals mailers pay a relatively small proportion of overall institutional costs, they might experience large percentage increases if institutional costs now paid by third-class (or, as of July 1, Standard Class) mail or large-volume periodicals were shifted to residual mail.

negative financial impact" of the new rules" and thereby "avoid this potential harm."⁷ Movants respectfully submit that the protections set forth in the *Order* are insufficient. The truncated period which intervenors will have in which to review, analyze, and critique the Postal Service's request for expedited consideration simply will not allow sufficient time to assess the quality of the Postal Service's financial projections (which one may reasonably assume will always paint a rosy financial forecast for whatever service is offered) and identify flaws (which can take weeks of discovery to uncover).⁸ Consequently, Movants urge the Commission to reconsider its conclusions.

The dangers of non-compensatory provisional services and multiyear test periods are of particular concern because the Act does not grant this Commission many of the powers commonly possessed by regulatory commissions having jurisdiction over private firms. Experience has now demonstrated that the Commission may need *more* powers, including the ability to subpoena data from the Postal Service. Certainly the Commission should not be *reducing* its regulatory oversight, and limiting its own powers, which Movants believe is exactly what it has done through these rules.

The Commission's greatest powers are the ability to say no at the outset of a Postal Service request, and to exercise its power under 39 U.S.C. § 3603 to craft clear and strong precise rules that fully protect the substantive and procedural rights of all

⁷ 61 *Fed. Reg.* at 24,448.

⁸ See *American Bankers Association Comments*, Docket No. RM95-4 (Jan. 11, 1996) ("*ABA Comments*") at 3, 4; *Comments of American Business Press*, Docket No. RM95-4 (Jan. 11, 1996) ("*ABP Comments*") at 6; *NAA Comments* at 15-17.

parties. Giving postal management a means to reprice cosmetically altered versions of existing services on an expedited basis and without a corresponding and offsetting increase in its own powers merely reduces what limited power the Commission possesses to prevent rampant cross-subsidies of "competitive" services from services used by captive mailers. It should not do so.

If Congress makes fundamental changes to the Postal Reorganization Act to authorize the types of proceedings contemplated by these rules, to grant the Commission appropriate regulatory powers, and to ensure that captive mailers will not bear any losses arising from such ventures, the situation would be different. Unless and until Congress changes the law, however, the Commission should not be weakening its oversight powers in such a sweeping manner.⁹

III. THE RULE FOR EXPEDITED CONSIDERATION OF "PROVISIONAL SERVICES" UNNECESSARY, VAGUE, AND POTENTIALLY DETRIMENTAL TO MAILERS AND SHOULD BE REPEALED OR SUBSTANTIALLY CLARIFIED

Movants urge the Commission to repeal the special rule for expedited consideration of provisional services on the grounds: (1) that it is unnecessary; (2) that it is excessively vague and broad; and (3) that it creates far too many opportunities for abuse. Alternatively, the Commission should try to clarify the rule to resolve these problems.

⁹ The Postal Service would be free, of course, to seek waivers of its procedural rules at any time.

First, the fundamental problem with the rule for expedited consideration of "provisional services" is that the concept is so grossly vague as to be meaningless. It is a basic precept of administrative law that vagueness in agency rules is undesirable: agencies should give the public clear notice of what is at stake. A vague rule is especially problematic because it is susceptible to arbitrary application; if no one knows what a rule really means, it can easily be abused. *See, e.g., Connally v. General Construction Co.*, 269 U.S. 385, 391 (1926) ("a statute which either forbids or requires the doing of an act in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application, violates the first essential of due process of law"); *Georgia Pacific Corporation v. OSHRC*, 25 F.3d 999 (11th Cir. 1994) (voiding regulation as unconstitutionally vague because of susceptibility to many plausible and inconsistent interpretations).

In particular, the difference between a "provisional" service and either a "market test" of a "new" service or an experimental service under longstanding rules remains utterly unclear.¹⁰ No one -- the Commission, the Postal Service, those supporting the proposal, or even the Joint Task Force -- has identified a single example of an offering that requires the unique designation of "provisional." Although the Commission states that the primary difference between provisional services and market tests is that the latter are intended to be "limited in scope, scale, duration, and potential adverse impact,"¹¹

¹⁰ 61 *Fed. Reg.* 24,450 ("a separate rule *may* be useful . . . ") (emphasis added).

¹¹ § 3001.161, *id.* at 24,454.

while provisional services will "supplement, but will not alter, existing mail classifications and rates for a limited and fixed duration,"¹² this distinction is meaningless. Nothing in the market test rules would limit such a test to a particular scope, scale or duration that a provisional service could not have.¹³ Virtually any service imaginable, including one subject to a market test, could "supplement, . . . but not alter" existing services. Therefore, the *Order* does not justify a separate rule for "provisional" services.

¹² § 3001.171, *id.* at 24,456.

¹³ Indeed, the market test rule expressly states that the Postal Service is not prohibited from "conducting more than one market test in support of a potential permanent change in mail classification." 61 *Fed. Reg.* at 24,455. Plainly, if the Postal Service can conduct more than one market test, each of sufficient scale, it would equate to a provisional service -- only pursuant to different rules.

Furthermore, given the vagueness of the concept of provisional services, there now appears to be two sets of different (and conflicting) rules that could apply to the same conduct.¹⁴ If the Postal Service wants to offer a "new" service in a tentative manner, the existing experimental service rules and newly adopted market test rules offer adequate latitude. The recent reclassification case was intended to simplify and streamline USPS services; overlapping special procedural rules runs directly contrary to this purpose.

Second, compounding the vagueness problem is the potential for abuse created by the potential breadth and duration of provisional services, coupled with the severe curtailment of the procedures by which they would be established.¹⁵ As shown above, virtually any proposal could qualify for two years of "provisional" service, which can be a very long time in the postal world. In particular, nothing in the provisional services and five-year test period rules prevent the Postal Service from relabelling existing services, with cosmetic differences, in order to engage in anti-competitive price discrimination or to tailor a service to the specific eligibility criteria of a particular large and influential mailer, and from attempting to recover losses from such activities through

¹⁴ See *ABP Comments* at 6; *NAA Comments* at 15.

¹⁵ See *ABA Comments* at 3, 4; *NAA Comments* at 14-18.

the Prior Year Loss cost component of the revenue requirement.¹⁶

Third, the rule as adopted is defective in another important respect. In particular, the *Order* did not adopt the proposal of Movants that the Postal Service be required to provide sufficient cost data, such as an estimate of the product incremental cost (or, in the case of a discount, avoided cost), to establish that rates for a provisional service would actually be compensatory and non-predatory.¹⁷ Given the danger that any financial losses would result in a cross-subsidy by captive mailers, the Commission should condition any such authorization on a requirement that the Postal Service provide a calculation of the incremental costs associated with a proposed provisional service.

"Provisional" services remain far too vague to deserve any form of expedited procedures. Movants respectfully request that, upon reconsideration, the Commission issue an order withdrawing the Rules 3001.171 *et seq.*

¹⁶ The Postal Service's ill-conceived "Neighborhood Mail" program, had it included a new rate, might even have met that standard. Similarly, the "supplement" standard appears so elastic that even the Publications Service and Enhanced Carrier Route subclass proposals -- so controversial in Docket No. MC95-1 -- might have qualified. *ABP Comments* at 5, *NAA Comments* at 14.

¹⁷ See *ABP Comments* at 3, 4; *NAA Comments* at 15.

IV. THE FINAL RULE FOR MULTIYEAR TEST PERIODS IS SERIOUSLY FLAWED

Although Movants are not opposed to the concept of a multiyear test period for new services, a five year period is *far* too long. Accordingly, Movants respectfully request that the Commission reconsider section 3001.181 *et seq.* of its rules of practice to shorten the maximum test year period and tighten the showing the Postal Service must make to invoke this rule.

First, a test period of five years is simply unwarranted.¹⁸ Although five years is the outer bound of the recommendation of the Joint Task Force cited in the *Order*, the Task Force's recommendations do not enjoy the force of law, nor did it ever come to grips with the problems inherent in long-range projections for new services. Neither history nor the record in this proceeding provides grounds for believing that the Postal Service is able to make reliable five-year forecasts of costs, volumes, and revenues with respect to new services.¹⁹ Movants respectfully suggest that a maximum period of three

¹⁸ The *Order* appears to attach no real significance to the five-year limit, for it states that the Postal Service "is free" to ask for an even longer period. 61 *Fed. Reg.* at 24,452.

¹⁹ Movants note that recently filed testimony of a Postal Service witness in the *Special Services* proceeding defends the selection of FY96 as the Test Year in that proceeding on the reasonable grounds that estimates for that period "are likely to be more reliable than those for future fiscal years." Direct Testimony of W. Ashley Lyons, USPS-T-1 at 7, Docket No. MC96-3 (filed June 7, 1996).

years or less is sufficient.²⁰

The problem of accurate measurements is especially pertinent to multiyear test periods because, as the Joint Task Force recognized:

The Postal Service should recognize its responsibility to minimize its losses by requesting changes or terminations when it sees expectations unfulfilled. It should anticipate that the general receptivity of the Commission and other participants to new service proposals will be affected by its record in limiting its losses as well as in building successes.²¹

This problem persists. Nothing in either the non-binding Task Force Report or in the newly-adopted rule prevents the Postal Service from shifting losses from ill-advised "provisional" services to captive mailers through the Prior Year Loss component.

Second, the *Order* compounds this danger by materially reducing the standard of proof that the Postal Service must sustain in order to support its request for a multi-year test period. The proposed rules had included a standard of "convincing substantial evidence"²² that the Postal Service would have to meet to justify a multiyear test period, which Movants believe appropriately reflected the policy, substantive and procedural concerns shared by many parties.

²⁰ *NAA Comments* at 25-26.

²¹ *Joint Task Force Report* at 52.

²² Proposed § 3001.181, *Notice* at 54,985.

Unfortunately, in the *Order* the Commission eliminated altogether the word "convincing," thus eviscerating this potentially strong safeguard, while stating that it had not intended to require a stronger showing than normally is required. On the contrary, Movants submit that the more persuasive showing required by a "convincing" standard, as proposed, would be a prudent, even necessary, prerequisite for the special privilege of a multiyear test period, especially one stretching for up to five years. The Commission should reconsider its decision to accept a weaker showing.

For all these reasons, Movants respectfully request the Commission to reconsider its approval of the five year multi-year test period, and either withdraw section 3001.181 *et seq.* of the rules or implement the modifications suggested herein.

V. CONCLUSION

For the foregoing reasons, Movants American Bankers Association, American Business Press, Greeting Card Association, and the Newspaper Association of America respectfully urge the Commission to reconsider the recently adopted rule for expedited consideration of provisional services and five year test periods for new services.

Respectfully submitted,

AMERICAN BANKERS ASSOCIATION

By: _____
Irving D. Warden
Associate General Counsel
1120 Connecticut Avenue, N.W.
Washington, D.C. 20036
(202) 663-5027

AMERICAN BUSINESS PRESS

By: _____
Stephen M. Feldman
David R. Straus
SPIEGEL & McDIARMID
1350 New York Avenue, N.W.
Washington, D.C. 20005
(202) 879-4000

GREETING CARD ASSOCIATION

By: _____

Alan R. Swendiman
JACKSON & CAMPBELL
1120 Twentieth Street, N.W.
Washington, D.C. 20036-3437
(202) 457-1600

NEWSPAPER ASSOCIATION OF AMERICA

By: _____

Robert J. Brinkmann
NEWSPAPER ASSOCIATION
OF AMERICA
National Press Building
529 14th Street, N.W.
Suite 440
Washington, D.C. 20045-1402
(202) 683-4792

William B. Baker
Leslie A. Platt
WILEY, REIN & FIELDING
1776 K Street, N.W.
Washington, D.C. 20006-2359
(202) 429-7000

July 3, 1996

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the instant document on all participants of record in this proceeding (see attached list) in accordance with section 12 of the Rules of Practice.

William B. Baker

July 3, 1996