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

EXIGENT REQUEST, 2010	Docket No. R2010-4R

COMMENTS OF THE MAJOR MAILERS ASSOCIATION AND
THE NATIONAL POSTAL POLICY COUNCIL
(August 1, 2011)

The Major Mailers Association and the National Postal Policy Council hereby reply to the opening comments in this proceeding on remand from the U.S. Court of Appeals. *U.S. Postal Service v. Postal Regulatory Commission*, 640 F.3d 1263 (D.C. Cir. 2011).

In these reply comments, MMA and NPPC respectfully submit:

- That the only interpretation of Section 3622(d)(1)(E) truly consistent with the structure and intent of the Postal Accountability and Enhancements Act and the legislative intent is that the amount of an above-cap exigent increase must be limited to that caused solely by the extraordinary or exceptional circumstance; and

- That the "reasonable and equitable and necessary" provision is unrelated to the causation issue and, in any event, provides no justification for raising rates on classes of mail whose volume continues to plummet, including First-Class Presort letters (the most profitable mail in the system).

I. THE AMOUNT OF AN ABOVE-CAP INCREASE MAY NOT EXCEED THAT DIRECTLY CAUSED BY AND DUE SOLELY TO THE EXIGENT EVENT

The issue on remand is narrow. The Court of Appeals agreed with the Commission that any rate adjustment based on "extraordinary or exceptional circumstances" pursuant to 39 U.S.C. §3622(d)(1)(E) must be "due to" – that is, caused by the extraordinary circumstances. The Court remanded the case to the Commission "to fill the statutory gap by determining how closely the amount of the adjustments must match the amount of the revenue lost as a result of the exigent circumstances." 640 F.3d at 10. Thus, the Commission is to exercise the discretion vested in it by Congress as the expert regulatory agency to interpret *how closely* the amount of an exigent rate adjustment must match the amount of revenue lost as a result of an exigent circumstances under Section 3622(e)(1)(E). 640 F.3d at 1267; *see Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc*., 467 U.S. 837, 842-43 (1984).

Several commenters used similar language to capture the causal relationship that is most consistent with the PAEA's structure and intent and that supports the primary role Congress assigned to the rate cap. MMA and NPPC agree with the Saturation Mail Coalition and Valassis that "the only reasonable and practicable interpretation that makes sense with the context of the PAEA is that the amount sought by the Postal Service must be limited to that 'due solely to' the exigent circumstance." *Comments of the Saturation Mail Coalition and Valassis Direct Mail, Inc*., at 3 (July 25, 2011).[1] Such a narrow construction would best implement the Congressional intent. *See Letter from Sen. Susan M. Collins to Ms. Shoshana Grove*, Docket No. R2010-4R, at 1 (July 25, 2011) (stating that the Postal Service must "demonstrate a distinct and close nexus between the proposed rate increase under the Postal Service's exigent rate

[1] *Accord Public Representative Comments on Remand Concerning the Exigent Request of the United States Postal Service*, at 2 (July 25, 2011) (stating "a level of financial recovery of no more than can be shown to be directly caused by the exigent circumstance").

authority and the exigent circumstance" and the Commission must "disallow above-inflation rate increases under the exigent rate authority, except when the exigent circumstance the Postal Service invoke is the only significant cause of the proposed rate increase)".

That this "due solely to" and "directly caused by" interpretation is the most consistent with the PAEA is evident when contrasted with the far less rigorous "general proportionality" interpretation now advocated by the Postal Service. *Initial Comments of the United States Postal Service Regarding Court Remand* at 6 (July 25, 2011). Furthermore, the manner in which the Postal Service proposes to apply its "general proportionality" interpretation makes clear that such a standard would be effectively meaningless – elastic, open-ended, and apparently perpetual.

Under the Postal Service's view, the exigency provision is not an exception to the price cap, to be invoked only in extraordinary or exceptional circumstances, but is essentially an option for raising rates "equally as central to the pricing system" as the price cap. *Id*. at 8. Furthermore, the Postal Service apparently still believes, despite rulings to the contrary by this Commission and the Court, that the exigency provision exists to give it an opportunity to deal with all of its financial problems, regardless of the cause.

This flows from the Postal Service's position that it is entitled under the exigency clause, apparently in perpetuity, to every penny of contribution that it received at 2007 volume and rates. USPS Comments at 27-35. Under the

Postal Service's theory, it would be entitled to an above-cap rate increase every time volume declines during a recession. Such a view is nonsense.

Although institutional costs do not vary by volume, they are certainly neither permanent nor fixed. Institutional costs are not immune from the need to economize; indeed, they can be managed more easily than volume variable costs precisely *because* they are not driven by volume.

There are many ways in which the Postal Service should be pro-active in reducing its overhead costs. The Postal Service's recent filing regarding the possible closing of more than 3,000 facilities is a commendable example of just such an action. Unfortunately, it has taken management four years since the start of the recession to respond, and that delay has caused substantial losses. But the exigent rate provision "does not provide an all purpose exception to the price cap" (Order No. 547 at 64) and mailers are not a piggybank to be tapped to pay the price when management has delayed taking necessary steps to lower overhead costs.

In any event, it is also apparent that failures to reduce overhead costs and continuing volume declines are not the Postal Service's real problem: the real problem remains the Congressional mandate to pay more than $5 billion annually for prepaid retiree health benefits. As the Commission observed only four months ago, without the retiree health benefit premium prefunding requirement, the Postal Service actually would have achieved a small net profit over the past four years. *Annual Compliance Determination, Fiscal Year 2010* at 2 (March 29, 2011). The rates that achieved that result had built in some $3.1 billion annually in retiree benefit payments, as has ever since Docket No. R2005-1.[2]

In other words, the Postal Service managed over the past four years to reduce its volume variable costs on an operating basis during these difficult times. The problem is that Congressional-imposed funding requirements have drained its funds.

As the Commission correctly stated in Order No. 547, "an exigent rate adjustment must be due to, and commensurate with, some specific extraordinary or exceptional circumstance." The Postal Service made no attempt to make this showing when it filed its exigency request in July 2010. That alone provides sufficient grounds for terminating this proceeding at this time. Its belated request now for approval of unspecified, but surely large, rate increases that would take effect in 2012, *five years* after the recession began and more than two years after it ended, should be denied outright.

II. THE "REASONABLE AND EQUITABLE AND NECESSARY" CLAUSE DOES NOT BROADEN THE "DUE TO" REQUIREMENT

In order to be allowed above-cap rate increases under the narrow statutory exigency exception, not only must the Postal Service prove the

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2 At first, the $3.1 billion added by Docket No. R2005-1 was intended to fund an escrow related to the Postal Service Civil Service Retirement System. *See generally Opinion and Recommended Decision*, Docket No. R2005-1 at ¶3001 *et seq*. (Nov. 1, 2005). The PAEA redirected those escrowed funds to be a partial prepayment of the Postal Service's retiree health benefit premiums. Those rates have never been rescinded. In FY 2009, the Postal Service *profited* by $1.7 billion from this requirement, as Congress reduced its obligation to $1.4 billion for that year.

existence of an “extraordinary or exceptional circumstance” to justify any increase, but it must also show that the requested rates are:

> reasonable and equitable and necessary to enable the Postal Service, under best practices of honest, efficient, and economical management, to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.

39 U.S.C. §3622(d)(1)(E).

The Postal Service argues that the “reasonable and equitable and necessary” language “sets forth a broad, functional inquiry” that relates to the size of the exigency increase under the “due to” standard. *USPS Comments* at 13.

MMA and NPPC submit that the Postal Service misapplies this language. The “reasonable and equitable and necessary” provision most appropriately applies to the specific rate adjustments that would result.[3] The “reasonable and equitable and necessary” clause requires the Commission to evaluate whether the actual rates proposed would reasonably and equitably recover the amount of funds needed “due to” the exigent circumstance. Thus, even if the Postal Service could show a direct causal link between an exigency and a financial loss, the “reasonable and equitable and necessary” provision would require review of the particular proposed new rates.

Even regardless of any nexus between the exigent circumstance of the 2008-2009 recession and the Postal Service’s finances, the Postal Service has completely failed to satisfy this element of Section 3622(d). It has made *no*

[3] Thus, the Postal Service errs in arguing that the “reasonable and equitable and necessary” language in the exigency clause focuses on the overall amount of the adjustment in a manner “that is not consistent with a strict offset approach”. Postal Service Comments at 13.

attempt to show that the steep rate hikes for First-Class Presort mail that it demanded last year (much less the "black box" set of rates contemplated by its comments) would satisfy the "reasonable and equitable and necessary" standard established by 39 U.S.C. §3622(d)(1)(E)).

First, MMA and NPPC – whose members are the largest First-Class mailers – are confident that any increase in Presort rates will simply accelerate still more the diversion of letter communications to electronic delivery. Mail budgets are quite tight, and even seemingly small rate increases can drive mailers to abandon a physical mailing for an electronic one. Given the unit contributions of First-Class letters, this would clearly harm the Postal Service.

Indeed, electronic conversion is an even greater risk for the Postal Service than in years before, because for most mailers the costs for moving customers to online communications – the servers, software, personnel and training – by now have been sunk. Consequently, moving an additional customer or a new messaging campaign online incurs only marginal costs that are essentially *de minimis*.

The Postal Service recognized only last year that First-Class Bulk letter volumes are at grave risk:

> Not only is this mail highly profitable and extremely important financially*, it is highly vulnerable*. Our customers are increasingly looking to nonmail alternatives to transact business with their customers, with the result that *many presort First-Class Mail customers may respond to large price increases, not by simply sending fewer pieces (the traditional elasticity effect), but by abandoning hard copy mail altogether*.

Kiefer Statement at 17 (emphasis added). Mr. Kiefer's statement, if anything, rings even more true today.

Second, and MMA and NPPC say this reluctantly and in recognition of the difficulties now facing postal management, First-Class mailers frankly are becoming hesitant about making commitments to physical mail in the year to come. This hesitation arises directly from doubts being sown by statements by senior postal management. Consider, for example, the Postmaster General's recent Senate testimony that at some point in FY2012, absent legislative relief, the mail delivery system will "grind to a halt." *Statement of Postmaster General/CEO Patrick R. Donahoe Before the Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security, United States Senate*, May 17, 2011 at 4. Consider also that when the Postal Service suspended its FERS payments, it stated that it "could run out of cash as early as October 2011." *United States Postal Service Fact Sheet: FERS Payment Suspension* (June 2011).

Statements that the Postal Service might run out of money and shut down, perhaps as early as this October, already are making mailers uncomfortable about committing to making plans that depend on the postal system. Adding a rate increase to these uncertainties would only aggravate these doubts.

Third, now is a particularly inauspicious time to be discussing rate increases. July and August is the time of the year when mailers prepare their budgets for the upcoming year. Talk of a large rate increase may well lead them to decide to shift funds away from postal plans to electronic alternatives.

Finally, MMA and NPPC continue to believe that Postal Service volume forecasts continue to understate the electronic diversion of First-Class Mail, especially Presort letters. Last year, in its initial filing, and without a rate increase, the Postal Service projected a 0.6 percent (235 million piece) Before Rates decline in First-Class Presort letter volume in 2011. Almost all of this loss was forecast to occur in the first quarter alone. The Postal Service also forecast a Before Rates 0.1 percent decline in the second quarter of FY2011, and volume *increases* in the 3d and 4th quarters of FY2011. The actual *second* quarter decline was 4.8 percent decline. *Compare* RPW Report 2Q 2011 *with* RPW Report 2Q 2010. And the April rate increase means that volume may dip still more throughout the remainder of the fiscal year. This suggests that the Postal Service has woefully underestimated electronic diversion.

The trend seems to be worsening. Figures through May show that First-Class Mail volumes overall fell 7.2 percent from last year on a SPLY basis, and are down 7 percent for the year as of May. *USPS Preliminary Financial Information (Unaudited) May 2011* at 2. A rate increase of the magnitude claimed by the Postal Service on top of these declines would be lethal.

When the problem is declining volume of the most profitable mail, it would not be "reasonable or equitable" or consistent with best business practices to accelerate the trend with another rate increase. In First-Class Mail, whose volumes continue to plummet even two years after the end of the recession, doing so plainly would be counterproductive. For Presort letters, the net result would be an accelerated and permanent loss of high-margin Automation and

Presort letters, leaving the Postal Service in an even worse position than it is today. Driving the most profitable product away is a short-sighted plan, not a "best management practice."

Accordingly, MMA and NPPC urge the Commission to rule that raising rates for First-Class Bulk letter mail would not be "reasonable and equitable" or consistent with "best practices" of management because they will cause the most profitable customers to leave the postal system at a much faster rate than the Postal Service forecasts,

III. CONCLUSION

For the foregoing reasons, the Major Mailers Association and the National Postal Policy Council respectfully urge the Commission to hold that the amount of an above-cap exigent rate increase must be quantitatively and causally linked to the threshold extraordinary or exceptional circumstances, and that raising r rates for mail whose volumes continue to decline would not be “reasonable and equitable” and would run contrary to best management practices.

Respectfully submitted,

MAJOR MAILERS ASSOCIATION
Mury Salls
DST Mailing Services
1100 Investment Blvd
El Dorado Hills, CA 95762
MLSalls@dstmailingservices.com

Arthur B. Sackler
Executive Director
NATIONAL POSTAL POLICY COUNCIL
750 National Press Building
529 14th Street, N.W.
Washington, D.C. 20004
Telephone: (202) 955-0097
E-Mail: asackler@postalcouncil.org

William B. Baker
Wiley Rein LLP
1776 K Street, N.W.
Washington, DC 20006-2304
Telephone: (202) 719-7255
E-Mail: wbaker@wileyrein.com

Counsel to NATIONAL POSTAL POLICY COUNCIL