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

MARKET-DOMINANT PRICE CHANGE	Docket No. R2021-1

COMMENTS OF THE
<u>NATIONAL POSTAL POLICY COUNCIL</u>
(October 29, 2020)

The National Postal Policy Council ("NPPC")[1] hereby respectfully submits these comments on the Postal Service's notice of market-dominant price adjustments.[2]

Although the proposed rates for First-Class Mail appear to comply with the quantitative requirements of the price cap, qualitatively both the price levels and workshare discount passthroughs are a missed opportunity. It is disappointing that the Postal Service did not continue its strategy of using its pricing flexibility to encourage efficient preparation and mail retention and growth of the lowest-cost and most profitable First-Class Mail product: Metered Mail and Presort Letters.

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1 The National Postal Policy Council is an association of large business users of letter mail, primarily First-Class Mail using the Automation rate category, with member companies from the telecommunications, banking and financial services, insurance, and mail services industries. NPPC members account for a large majority of the Presort Letters and Card (hereinafter "Presort Mail") in the postal system and work closely with the Postal Service on worksharing and many other efforts to make their mail as efficient and low cost as possible.

2 *United States Postal Service Notice of Market-Dominant Price Change*, Docket No. R2021-1 (Oct. 9, 2019) ("*USPS Notice*"). The Commission issued public notice in Order No. 5071. *Notice and Order on Price Adjustments and Classification Changes for Market Dominant Products*, Docket No. R2020-1 (Oct. 13, 2020), 85 *Fed. Reg.* 66368 (Oct. 19, 2020).

Instead, the Postal Service has apparently abandoned *sub silentio* its "strategy of incentivizing the entry of volume that would reduce the costs of the Postal Service and increase contribution to institutional costs," both steps that would improve the Postal Service's financial position. Order No. 5285, at 43-44 (Oct. 24, 2019). This is evident from, in particular:

- The above-inflation price increases for the most important Automation Letter rates, which renders those rates even more unjust and unreasonable;

- The decrease in the Metered Mail rate differential; and

- The reduced workshare discount passthroughs for Automation Mixed AADC Letters and 5-Digit Automation Letters, which set inefficient price signals and do not maximize cost reduction.

Despite this disappointing overall strategy, certain aspects of the proposed First-Class Presort Mail rates have merit. In particular, the Postal Service's renewal of its promotional incentives[3] and introduction of a Seamless Acceptance incentive[4] are commendable steps to encourage volume or improve operations, respectively. The Commission should approve those proposals.[5] NPPC also urges the Postal Service to give serious consideration to a future promotion for Seamless Destruction.

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[3] NPPC continues to commend the Postal Service for pursuing promotions. NPPC urges the Postal Service to identify and develop additional promotions that would be mutually beneficial to the Service and its customers and, in particular, take advantage of the opportunity to build a promotion around Secure Destruction.

[4] While NPPC supports the seamless discount, NPPC members that are edoc submitters are concerned that Seamless Acceptance is not being implemented efficiently either in practice or in pricing. In particular, the Postal Service must make the process easy to use by all mailers.

[5] The Postal Service "offset" the estimated cost of the promotional discounts in cap space. This action is consistent with the Commission's notice of nonenforcement in its Notice of Intent to Reconsider in Docket No. RM2020-5. Order No. 5655, at 2 (Aug. 25, 2020).

Despite these desirable initiatives, the proposed new Presort rates, as well as the increased Single-Piece Metered Mail rate, unfortunately will perpetuate uneconomic pricing for the most perennially overcharged mail while doing nothing to encourage volume growth and retention or cost efficiency.

I. THE POSTAL SERVICE HAS ABANDONED ITS STRATEGY OF USING PRICING TO ENCOURAGE VOLUME, PROMOTE EFFICIENCY, OR REDUCE COSTS

In Docket No. R2019-1, the Postal Service articulated a clear strategy of below-inflation rate increases for Presort Mail and moving discount passthroughs closer to 100 percent of avoided costs in order to encourage volume, reduce costs, and improve pricing efficiency. The Service stated that a smaller increase for Presort Letters as compared to stamped letters was deliberately designed to "help preserve volume in the category of First-Class Mal that both provides higher unit contribution and is most at risk for electronic diversion."[6]

The Commission approved that pricing strategy only last year as consistent with the PAEA, stating that the "modest increase for Presorted Letters/Postcards, sent by business mail users, reflects the Postal Service's need to retain and encourage volume for this highly profitable but price-sensitive product." The Commission also noted that increasing the volume of Presort mail "allows the Postal Service to process mailpieces at a reduced cost per piece compared to non-presorted mailpieces." Order No. 5285 at 36 (Oct. 24, 2019).

[6] *United States Postal Service Notice of Market-Dominant Price Change*, Docket No. R2019-1, at 7-8 (Oct. 10, 2019).

The First-Class Mail rates approved in Docket No. R2020-1 continued that strategy.

With the arrival of a new Postmaster General who is focused on controlling costs, the Postal Service might have been expected to continue the use of pricing to encourage efficiency and the preparation of low-cost mail. Unfortunately, despite the urgency of the current time, the prices for First-Class Mail presented in the *USPS Notice* do not reflect a continued, focused strategy to drive efficiency and retain volume. Instead, they are quite the reverse.

The Postal Service is imposing the largest increase on its lowest-cost, most profitable mail – Automation 5-Digit Letters. Instead of continuing to move workshare discount rates to more efficient passthroughs, the Postal Service is offering inefficient workshare discounts, including reducing the passthrough at the 5-Digit level by nearly 10 percentage points.

Whether the Postal Service has a coherent and sustained pricing strategy at a time when the paramount concerns are cost management and volume retention is unclear. To be sure, the Postal Service routinely discusses how it must implement its pricing strategy over a multiyear period. *E.g., USPS Notice* at 9-10. NPPC recognizes that a strategy may need more than one year to be implemented in rates.

However, a strategy must be applied consistently over that period, or it is no strategy at all. That means that any pricing justifications that the Postal Service invokes, and the Commission approves, should be applied consistently within each annual filing and across the multiyear period. Under the

Administrative Procedure Act, if a justification is applied inconsistently from year to year or a policy changed, the change must be explicit, and a reasoned explanation provided.[7] The Postal Service in this proposal does neither.

NPPC recognizes that, in Docket No. R2019-1, the Postal Service indicated that it might apply larger than average increases in future years to rate categories that received smaller increases in that docket, an assertion it has repeated in this proceeding. *USPS Notice R2019-1* at 8; *see also Response of the United States Postal Service to Chairman's Information Request No. 2*, Q. 7 (Oct. 26, 2020). But the Postal Service may not simply rely on that non-binding statement[8] in this proceeding without considering all relevant circumstances, nor may it assume that mailers' "expectations" are unaffected by subsequent economic and business developments. On the contrary, the Commission has stated that "each situation would require specific analysis when it is presented." Order No. 5285, at 40-41.

No such "specific analysis" of the impact of the above-average increases on Presort mail appears in the *USPS Notice*. The Postal Service has not explained how it has taken current price elasticity, diversion, the desirability of low-cost profitable mail, and the effect of the COVID-19 pandemic into account in these rates. It has made no effort to explain why raising Presort rates, instead of

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[7] *See, e.g, FCC v. Fox Television Stations,* 556 U.S. 502, 515-16 (2009) (agency changing standards must provide a reasoned explanation for disregarding facts and circumstances that underlay the previous action); *California v. Environmental Protection Agency*, No. 18-1114, Slip Op. at 17 (D.C. Cir. (Oct. 25, 2019).

[8] The Commission has specifically noted the nonbinding nature of that statement. Order No. 5285 at 40, n.64.

others, in this case results in a just rate schedule appropriate for today's mailing environment.

In fact, it appears that the Postal Service in fact simply is following an average-increase-for-everyone-over-time pricing strategy, spread over several years. For example, the Postal Service justifies an above-average price increase on already overpriced Presort Mail because doing so "balances the effect of prior above-average price increases to other products in First-Class Mail, thereby balancing the effect of the Postal Service's multi-year pricing strategy upon the general public and business mailers." *USPS Notice* at 11.

If the Postal Service's strategy is simply to try to give most mailers an average increase as measured over a multiyear period, one could debate whether such a course would be consistent with the Objectives and Factors set forth in the PAEA. But such a strategy is plainly different from one that aggressively uses pricing to retain and attract volume and drove costs out of the system. And at a point in the Service's history when it faces many challenges – including rising costs and declining volume – such a strategy is unlikely to prove viable in the long-term. Moreover, it suggests that the Postal Service is fundamentally unwilling to use its pricing power to pursue a consistent strategy of encouraging low-cost/high contribution mail over a multiyear period.

II. THE COMMISSION MUST CONSIDER THE SECTION 3622 OBJECTIVES AND FACTORS IN THIS PROCEEDING

In *Carlson v. Postal Regulatory Commission*, 938 F. 3d 337 (D.C. Cir. 2019), the Court of Appeals ruled that the Administrative Procedure Act requires the Commission, when administering the PAEA, to consider seriously and address arguments that particular proposed market-dominant rates are not consistent with the statutory considerations – quantitative and qualitative -- that Congress directed the ratesetting system to achieve. Despite the Postal Service's bald assertion that it was "wrongly decided" (*USPS Notice* at 2), *Carlson* remains governing law and cannot simply be ignored.

Accordingly, the Commission must consider the applicability of the statutory Objectives and Factors to specific rates, particularly those that commenters challenge. If the Postal Service has failed to justify a rate proposal sufficiently, the Commission must reject that rate and require the Postal Service either to modify it or provide a better justification.

In this case, the Postal Service has failed to provide a "specific analysis" of the rates. Instead, it devotes merely one paragraph to explain how the Presort Letters and Cards pricing purports to comply with the objectives and factors. *See USPS Notice* at 16-17. But, as discussed in the following section, that lone paragraph does not provide the specific analysis demanded by *Carlson*.

III. THE PROPOSED RATES WILL PERPETUATE UNREASONABLE FIRST-CLASS PRESORT MAIL PRICES AND REDUCE EFFICIENCY

A. The Postal Service Is Imposing Above-Average Rate Increases On Presort Mail, Which Already Bears The Highest Cost Contribution Burden

As NPPC has pointed out repeatedly, First-Class Presort Mail bears by far the greatest institutional cost coverage burden – whether measured by cost coverage, markup index or unit contribution -- not only within First-Class Mail, but also throughout the entire market-dominant product rate schedule. *See* Attachment A hereto. The Commission has acknowledged this fact as well. *See,* *e.g.*, *Order No. 4257,* at Table II-5, Docket No. RM2017-3 (Dec. 1, 2017). These persistently high Presort Mail rates continue to send an unmistakable signal to cost-conscious business mailers to consider electronic alternatives. Presort mail volume trends show that this message is being heard.

The above-average increases for Presort Mail proposed in the *USPS Notice* will aggravate this burden. Compared to the average class adjustment of 1.836 percent (*USPS Notice* at 7), the rate for:

- Mixed Automation AADC Letters increases by 2.506 percent;
- Automation AADC Letters increases by 2.148 percent; and
- 5-Digit Automation Letters, by far the largest category in the Product, increases by 2.314 percent.

Note that these increases are driven in part by a separate proposed increase: the 2 percent increase in the Single-Piece Metered Mail rate. That increase alone will adversely affect the many NPPC members that use it. But it affects all Presort Mail users as well because the Metered Mail rate serves as the benchmark for the Presort discount tree.[9] By raising the benchmark rate by 2 percent, the Postal Service simultaneously pushes up all of the Presort Automation rates that are derived from it.

Increases in the Metered Mail rate can be ameliorated in part by full passthroughs of avoided costs in workshare discounts. However, in this proceeding the Postal Service once again has failed to set Presort and Automation discounts at efficient levels, particularly for the 5-Digit Letters

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[9] Specifically, the Metered Mail rate is the benchmark for the Nonautomation Machinable Letters rate, which in turn serves as the benchmark for the Automation Mixed AADC rate.

category which has by far the largest volume. Worse, the Postal Service is *reducing* the passthroughs from the AADC to the 5-Digit tier from 88.2 percent to 78.95 percent compared to its proposals only last year in Docket No. R2020-1.

Unfortunately, the entirely predictable result of the Postal Service's failure to set efficient pricing signals and address the exorbitant overpricing of Presort Mail will be to continue to drive this profitable category of mail from the postal system, promote inefficiency, and harm the Postal Service's financial stability. As discussed below, these proposals are contrary to the PAEA.

B. The Proposed Presort Mail Rates Violate The PAEA

The proposed First-Class Presort Mail rates violate, at a minimum, Objectives 1 and 5 of the PAEA.

Under Objective 1, the ratesetting system should produce rates that "maximize incentives to reduce costs and increase efficiency." 39 U.S.C. §3622(b)(1). Above-average rate increases for Presort Letters do not maximize the incentives to reduce costs and increase efficiency. They also fail to take properly into account Factors 5 (the degree of preparation) and 12 (the need for the Postal Service to increase its efficiency and reduce its costs).

In Docket No. R2019-1, the Commission twice approved below-inflation rate increases for Presort Mail as consistent with Objective 1 "by encouraging the entry of First-Class Mali pieces that are less costly to the Postal Service to process." Order No. 5285, at 36. The Commission specifically found that a below-average price increase for less costly Presort Mail reflected "a proper incentive" to encourage entry of mailpieces that would reduce Postal Service costs. *Id*.

The Postal Service's proposed above-average increase on Presort Letters will have the opposite effect. Increasing that burden directly conflicts with the Postal Service's recent pricing strategy of incentivizing "the entry of mailpieces that would reduce the costs of the Postal Service." Order No. 5285, at 36. It offers little reason for its most profitable customers to want to remain in or increase their use of the mail and will only accelerate volume losses to the detriment of its financial position.

Objective 5 seeks to assure the Postal Service's financial stability through adequate revenues. Although rate increases would seem to promote the Postal Service's financial stability, not all increases have the same effect.

In this proceeding, the largest First-Class rate increases are being imposed on the product that, according to its own estimates, are comparatively price elastic (Presort Letters: -0.320)[10] while making almost no change in the rates for the less elastic (-0.190) Single-Piece mail.[11] That is precisely backwards as a matter of pricing economics.

The Postal Service demonstrated its understanding of the proper role of elasticity in pricing in Docket No. R2019-1. In that case, the Postal Service noticed a below-average increase on Presort Letters to "retain[] volume in a

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[10] NPPC has long believed, based on its members' business choices, that the price elasticity of Presort has been underestimated, and must be reexamined.

[11] *See* Postal Service, *Narrative Explanation of Econometric Demand Equations for Market Dominant Products Filed with Postal Regulatory Commission on January 21, 2020* at 24 & 33.

category of mail that provides higher unit contribution and slows electronic diversion." *See USPS R2019-1 Notice*, at 7-8, n.12, *quoted at* Order No. 5285, at 43. The Commission approved that strategy, noting that "retaining and encouraging volume for Presorted Letters/Postcards, which provide a greater unit contribution than Single-Piece Letters/Postcards, would improve the financial position of the Postal Service." Order No. 5285, at 54. The Commission specifically noted how that "illustrates how the price adjustments are consistent with Objective 5." Order No. 5285, at 44.

In light of that recent experience, the Postal Service's reversal of position in this proceeding requires much better explanation. Above-average rate increases on comparatively most price sensitive mail in a product is not likely to advance the financial stability of the Postal Service. That failure requires the Commission to find those increases to be arbitrary and in violation of the PAEA.

C. The Proposed First-Class Mail Automation Passthroughs Are Inefficient And Unjustified

The proposed new Presort Letter discount passthroughs are:

Rate Category	Costs Avoided	Passthrough
Nonautomation machinable letters	$0.076	65.79%
Mixed AADC	$0.067	89.55%
AADC Automation	$0.025	88.00%
5-Digit Automation	$0.038	78.95%

USPS Notice, Attachment B Tab FCM Bulk Letters, Cards. The Postal Service's *Notice* (at 18) says only that they are less than 100 percent. It does not mention that although the 5-Digit discount itself is unchanged, the passthrough is sharply reduced from last year because the costs avoided by mailer presortation to the 5-Digit level have increased.

Objective 1, supplemented by Factor 5, requires the Postal Service to maximize the price incentives to reduce costs and increase efficiency. The Commission has long recognized that passthroughs of 100 percent, consistent with Efficient Component Pricing, best advance the statutory Objective of maximizing the incentives to reduce costs and increase efficiency. *See* Order No. 5285, at 37 ("prices are most efficient when workshare discounts are set equal to avoided costs"). And it recognizes that adhering "to ECP has a positive effect on business mail users' participation in worksharing." Order No. 5285, at 54. Only earlier this year, the Commission stated that it "encourages the Postal Service to set all workshare discounts as close as possible to avoided costs in order to send efficient pricing signals." *Annual Compliance Determination Report Fiscal Year 2019*, at 15 (Mar. 25, 2020). The Commission has proposed rules in Docket No. R2017-3 that would "require the Postal Service to improve the pricing efficiency of workshare discounts." *Id*.[12] NPPC has urged the Commission in that proceeding to adopt those proposed rules, with certain modifications.[13]

Only last year, in Docket No. R2020-1, the Commission stated approvingly "that the planned workshare discounts for First-Class Mail demonstrate progress in increasing pricing efficiency, a component of Objective 1, by improving

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[12] The Postal Service's proposed reduction in the 5-Digit workshare discount would likely violate the rules that the Commission proposed in Order No. 5337.

[13] *See Comments of the National Postal Policy Council, the Major Mailers Association, the National Association of Presort Mailers, and the Association for Mail Electronic Enhancement*, Docket No. RM2017-3, at 15 *et seq*. (Feb. 3, 2020).

adherence to the principle of ECP. Order No. 5373, at 31. Regrettably, that progress has not been sustained.

As shown above, in this proceeding the relevant passthroughs range from a high of 89.55 percent to a low of 65.79 percent. That these would convey inefficient pricing signals is self-evident.

NPPC urges the Commission to reject the passthroughs for both the Nonautomation Machinable Letters and at the 5-Digit tier. The former is well below any justifiable level and should be increased.

The passthrough at the 5-Digit tier is especially egregious because the Postal Service is *reducing* the passthrough despite an *increase* in avoided costs. That reduction in the 5-Digit passthrough conflicts with Objective 1 because it results in even more inefficient pricing than the current passthrough.

Moreover, Commission Rule 3010.12(b)(6) requires the Postal Service to identify and explain worksharing passthroughs that are substantially below 100 percent. The Commission has not ruled whether a 78.95 percent passthrough, such as proposed at the 5-Digit Automation Letter category, is "substantially" below 100 percent.[14] However, a passthrough of 65.9 percent at the Nonautomation Machinable category is substantially below 100 percent by any measure. By comparison, the Commission's pending proposal in Docket No. RM2017-3 generally would require the Postal Service to passthrough at least 85

[14] When the Commission adopted rule 3012(b)(6), it refrained from defining "substantially," stating that the Postal Service "would not be required to explain reasonable passthroughs of less than 100 percent that were due to rounding, or other similar rate design goals." Order No. 43, Docket No. RM2007-1, at 41 (Oct. 29, 2007).

percent of the avoided costs, a threshold that neither the Nonautomation Machinable nor 5-Digit Letter passthroughs would satisfy.

NPPC has commented in Docket No. RM2017-3 that the proposed band is too wide; nonetheless, the proposed passthroughs for Nonautomation Machinable Letters and 5-Digit Letters fall outside even that generous band. The Postal Service has not complied with rule 3010.12(b)(6) and the proposed rates accordingly should be rejected.

IV. CONCLUSION

For the foregoing reasons, the National Postal Policy Council respectfully urges the Commission to consider these comments when evaluating the proposed new rates for First-Class Presort Letters, in particular the passthroughs proposed for the Presort Letter worksharing discounts.

Respectfully submitted,

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Attachment

Attributable cost, average price, unit contribution, and cost coverage of First-Class Presort Letters and Cards since 2008, compared to the average market-dominant cost coverage:

First-Class Presort Letters and Cards

	Attributable Cost (cents)	Average Price (cents)	Unit Contribution (cents)	Cost Coverage (%)	M-D Avg. Cost Coverage (%)	Markup Index[15]
FY2008[16]	11.023	33.023	22.000	299.6	170.8	1.75
FY2009[17]	11.704	34.152	22.448	291.8	164.5	1.77
FY2010[18]	11.679	34.739	23.060	297.4	165.2	1.80
FY2011[19]	11.65	34.982	23.332	300.3	159.1	1.89
FY2012[20]	12.15	35.64	23.49	293.3	166.6	1.76

15 Under the former law, the markup index (or cost coverage index) was calculated across all products. In Order No. 4257, the Commission chose to calculate the markup index by dividing the cost coverage of a class or product by the cost coverage of all market-dominant classes or products. Order No. 4257 at n.223.

16 PRC, *Annual Compliance Determination, Fiscal Year 2008,* at Table III-2 (Mar. 30, 2009) ("*FY08 ACD*").

17 PRC, *Annual Compliance Determination, Fiscal Year 2009,* at Tables VII-1 & B-1 (Mar. 29, 2010).

18 PRC *Annual Compliance Determination, Fiscal Year 2010,* at 84 Table VII-1 (Mar. 29, 2011, as corrected Apr. 8, 2011).

19 PRC, *Annual Compliance Determination, Fiscal Year 2011,* at 96 Table VII-1 (Mar. 28, 2012).

20 PRC, *Annual Compliance Determination Fiscal Year 2012*, at Tables VII-1 & D-1 (Mar. 28, 2013).

FY2013[21]	11.67	36.30	24.63	311.1	176.1	1.77
FY2014[22]	11.8	37.848	26.04	320.6	184.3	1.74
FY2015[23]	12.14	38.85	26.71	320.1	183.4	1.75
FY2016[24]	11.46	38.73	27.27	332.8	181.3	1.84
FY2017[25]	11.78	37.64	25.86	319.9	169.5	1.89
FY2018[26]	12.24	37.90	25.66	309.8	166.6	1.86
FY2019[27]	13.085	38.323	28.238	292.9	160.9	1.82

[21] PRC, *Financial Analysis 2013: Analysis of United States Postal Service Financial Results and 10-K Statement for Fiscal Year 2013*, at 43-44 App. A (revised Apr. 20, 2014).

[22] PRC, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2014*, Appendix A, at 73 (April 1, 2015).

[23] PRC, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2015*, Appendix A, at 88 (Mar. 29, 2016).

[24] PRC, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2016*, Appendix A-2 at 93 (Mar. 31, 2017).

[25] PRC, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2017*, Appendix B, at 85 (Apr. 5, 2018).

[26] PRC, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2018*, Appendix A, at 87 (Apr. 4, 2019).

[27] PRC, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2019*, Appendix A, at 87 (May 7, 2020).