

DOCKET SECTION

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-001

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Postal Rate and Fees Changes, 1997

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Docket No. R97-1

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Motion to Accept Late-Filed Responses and
Responses of ABA/EEI/NAPM Witness Clifton to Interrogatories of
Val-Pak Direct Marketing Systems, Inc., *et al.*
(VP-CW/ABA/EEI/NAPM-T1-1-9)

(February 13, 1998)

Pursuant to the Commission's Rules of Practice, American Bankers Association ("ABA"), Edison Electric Institute ("EEI"), and National Association of Presort Mailers ("NAPM") hereby file the responses of their witness James A. Clifton to the interrogatories of Val-Pak Direct Marketing Systems, Inc., Val-Pak Dealers' Association, Inc., and Carol Wright Promotions, Inc., VP-CW/ABA/EEI/NAPM-T1-1-9. In addition, ABA/EEI/NAPM hereby *move for acceptance of said responses two days late.* The delay was occasioned by difficulties in coordinating the various, and sometimes conflicting, schedules of the individuals concerned.

Respectfully submitted,

American Bankers Association,
Edison Electric Institute, and
National Association of Presort Mailers

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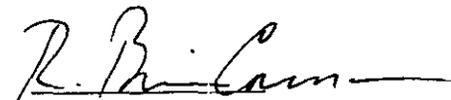
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CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the rules of practice.

February 13, 1998


R. Brian Corcoran

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-1

Please refer to you testimony at page 44, lines 22-26.

- a. Is it your view that the price elasticity between First-Class workshared mail (-0.289) and that of Standard A ECR mail (-0.598) are not that different? Please explain your answer
- b. Is it your testimony that the fact that the cost coverage of First-Class workshared mail (283 percent) is higher than the cost of coverage of Standard A ECR mail (228 percent), Exhibit USPS-30B (as revised 9/19/97), cannot be justified by a comparison of the price elasticity of each type of mail? Please explain your answer.
- c. Do you believe that the Standard A Regular and Standard A ECR subclasses should be viewed together (as Standard A Commercial) for purposes of comparison with the rate category First-Class workshared mail when coverages are considered? Please explain your answer.
- d. Would you recommend that First-class workshared mail should never be combined with First-Class single piece mail (forming the First-Class letters subclass) for purposes of comparison with other classes or subclasses when rates are proposed or recommended? Please explain your answer.
- e. Is it your testimony that the Commission should treat First-Class workshared mail as a subclass when considering rate proposals and recommending rates, even though the Commission has repeatedly rejected proposals to make First-Class workshared mail a subclass separate from First-Class letter mail? Please explain your answer.

RESPONSE

- a. In my testimony on page 44, I was comparing the elasticity for First-Class workshared mail as a whole to Standard A commercial mail as a whole. The USPS has not estimated an elasticity for Standard A commercial mail as a whole. The elasticities which are available from the USPS are for Standard A commercial regular (-0.328) and Standard A commercial ECR (-0.598). Under these circumstances, for example, if Standard A commercial had an elasticity value near the mid-point of the range (-0.463), I would characterize them as not that different. Moreover, as I note in my testimony, both are inelastic.
- b. In my testimony, I do not relate relative cost coverage levels to relative elasticities. My argument that the cost coverage for First-Class workshared mail is too high is based on the recent trend of growing First-Class cost coverage divergence from the system-wide average, the greater-than- average increase in revenue per piece for First-Class workshared mail proposed by the Postal Service in R97-1, and the disparity in contributions to institutional costs between First-Class workshared and Standard A mail. I discuss First-Class workshared cost coverage in detail at pages 36-41 of my testimony.
- c. Yes, some such comparison is appropriate since much of the volumes in the two mailstreams have similar physical characteristics and, therefore, generally similar cost characteristics.
- d. No. Generally, however, such comparisons are not as useful as comparing similarly prepared mail, e.g., First-Class workshared versus Standard A commercial mail.

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INTERROGATORIES OF VP-CW**

e. No. However, lack of formal subclass status should not preclude either the Commission from recommending or the Postal Service from proposing rates and cost coverages for First-Class workshared mail in some reasonable relationship to the corresponding rates and cost coverages for Standard A commercial mail. The Postal Service's own witness for Standard A mail, Sharon Daniel, makes comparisons of mail processing and delivery cost as between Standard A and First-Class workshared, so there is a basis in fact for doing so. Furthermore, lack of formal subclass status should not be used as an excuse by the Postal Service or the Commission to "load up" the institutional cost burden borne by First-Class workshared mail in favor of either First-Class single piece rates or Standard A commercial rates. But that is precisely the result of the Postal Service's rate proposal in this case -- First-Class workshared mailers have been saddled with an inequitable and inefficient share of institutional costs.

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-2.

Please refer to your testimony at page 44, line 29 to page 45, line 2.

- a. Is it your testimony that the Commission should only consider economic efficiency in setting First-Class and Standard A coverages?
- b. If not, what other factors of 39 U.S.C. Sec. 3622(b) support closer coverage factors?
- c. Do any factors support the Postal Service's proposal?

RESPONSE

- a. No. Equity with Standard A commercial mail rates, cost coverages, and discounts figures prominently throughout my testimony. See, especially, Section IV.
- b. Principally, §§ 3622 (b) (1), (2), and 8 but arguably 4-7, and 3 insofar as extra ounce coverages are concerned.
- c. No. My testimony describes my disagreement with the Postal Service's filing.

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-3

In your testimony, at Technical Appendix C-2, you analyze a proposal which would increase Standard A ECR's cost coverage from 228 percent to **241 percent** (*Id.*, p.2), and adds **1.2 cents** to the rates of all piece-rated Standard A ECR rate categories (*Id.*, p. 3). At Technical Appendix D, you analyze a proposal which would increase the Standard A ECR cost coverage from 228 percent to **245 percent** (*Id.*, p.2), which would add **1.6 cents** to the rates of all piece rated Standard A ECR rate categories (*Id.*, p.3).

- a. Given the price elasticity of First-Class workshared mail (-0.289) and the price elasticity of Standard A ECR mail (-0.598) (ABA/EEI/NAPM-T-1-4, p. 44), in the pursuit of economic efficiency, which postal product could better sustain an increase in rates? Please explain your answer.

RESPONSE

- a. Please see my response to VP-CW/ABA/EEI/NAPM-T1-1b.

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-4

Please refer to your testimony at page 38, lines 8-10.

- a. Please explain how the unit contribution made to postal institutional costs by First-Class workshared mail under the Postal Service's proposed rates is more than two and one half times the contribution from Standard A Regular mail.
- b. Would you recommend that the Commission look to Priority Mail's per-piece contribution to institutional costs when setting Priority Mail coverage?

RESPONSE

- a. The unit contribution of First-Class workshared mail is 2.43 times that of Standard A Regular mail; the total contribution is 2.65 times that of Standard A Regular mail. The word "over" on line 9 should read "about".
- b. While I did not consider Priority Mail in my proposal as it is different in character from workshared letter mail, per-piece contribution is a relevant factor for the Commission to consider.

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-5

- a. Please confirm that the adoption of your cost estimates, proposed coverage, and proposed rates for First-Class Mail would result in a revenue loss of \$139 million. Please explain any non-confirmation (sic).
- b. Please confirm that you propose an increase in Standard Mail A rates of \$469 million. Please explain any non-confirmation (sic).
- c. Please explain why you propose rate increases in Standard Mail A greater than the revenue loss arising from your proposal in First-Class Mail.

RESPONSE

- a. Not confirmed. In Technical Appendix C.1 (revised 2/12/98), my proposed discounts and rates are analyzed before adjusting the cost coverage for Standard A commercial mail. See also my testimony at 43 (Revised 2/12/98). In this case, the net surplus/(deficit) is (-\$117) million, although the C.1 analysis is not my formal proposal.
- b. It is not clear to which of my analyses this question is referring. Concerning my proposed discounts and rates before adjusting the cost coverage for Standard A commercial mail, the revenue for Standard A commercial mail is unchanged (see page 8 of Technical Appendix C.1) (Revised 2/12/98) Concerning my proposed discounts and rates after adjusting the cost coverage for Standard A commercial mail, the revenue from Standard A commercial mail does indeed increase by \$469 million (see Technical Appendix C.2) (Revised 2/12/98).
- c. The question appears to be based on a misreading of my testimony. It is obviously incorrect to combine the \$117 million net deficit in my analysis of my proposed discounts and rates before adjusting the cost coverage for Standard A commercial mail (Technical Appendix C.1) with the \$469 million revenue increase from Standard A commercial mail after adjusting the cost coverage for Standard A mail. The \$117 million net deficit is the difference between total Postal Service revenues and total Postal Service costs. The \$469 million is revenue from a single type of mail and does not take into account changes in revenues from other types of mail and changes in costs for all types of mail. The proper figure to look at is the \$54.0 million net postal surplus in my analysis after adjusting the cost coverage for Standard A mail (see Technical Appendix C.2, page 5) (Revised 2/12/98).

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-6

At page 26, lines 11-13, you state that "There is probably more potential conversion mail to First-Class from Standard A regular mail than from bulk metered First-Class Mail."

- a. Please provide copies of our citations to all data, studies, analysis, or reports on which you rely to support this statement.
- b. In the absence of studies or analysis, please provide all examples or anecdotal evidence of which you are aware that support this statement.

RESPONSE

a. & b. The statement is based on my recollection that the Postal Service has encouraged advertising mailers to "trade up" to First-Class mail, reflecting the position that workshared First-Class mail is a substitute for Standard A Regular mail, and that generally the mail is physically similar and prepared similarly by rate category.

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-7.

At page 44, lines 15-16, you propose to raise "the cost coverages of Standard A Mail from the USPS proposed 167 percent to 175 percent."

- a. Please specify separately your proposed coverage for each independent subclass of Standard A, including the nonprofit subclasses.
- b. Do you agree that increasing the average of the commercial rate subclasses would, under RFRA, also increase the coverage on nonprofit subclasses? Please explain fully any answer that is not an unqualified affirmative.

RESPONSE

a. & b. My testimony addresses the issues of cost coverages, discounts, and rate equity and efficiency between First-Class workshared mail and Standard A commercial mail. While I recognize that RFRA may require adjusting the cost coverage for Standard A nonprofit mail, such an adjustment was not reflected in my results since I did not develop non-profit rate category data necessary for making such an adjustment. See Technical Appendix C.2 at 2. It was not my intent that such an adjustment be ignored.

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-8.

At page 46, line 13, you state that your proposed rates and coverages are "more efficient" than those proposed by the Postal Service. Explain every sense in which you consider your rates to be more efficient, including but not limited to consideration of Ramsey Pricing (sic).

RESPONSE

To quote a widely used basic textbook:

"To economists, the concept of efficiency is related to a concern with the well-being of those in the economy For the economy to be efficient, it must meet the conditions of exchange efficiency, production efficiency, and product-mix efficiency."

Stiglitz, Joseph, Economics, W.W. Norton, 1993, pp. 380-381

As I pointed out in MC-95-1, recent USPS Household Diary Study volumes clearly indicate that at the margin, the general public finds the value of advertising mail at the margin to be zero or negative. Whereas, the value of First-Class Mail at the margin is generally found to be high. While nobody likes receiving bills as such, the ECSJ value of the First-Class workshared mail I receive is very high for its informational content -- mutual fund statements, banking statements, credit card statements from which I can discern how I am allocating my monthly budget, etc.

To be more efficient, postal prices must reflect the preferences noted above. That is, Standard A commercial rates should be higher, reflecting the public preference for less advertising mail to be sent, while First-Class Mail rates should be lower, and discounts higher, reflecting the preference of the public for the types of mail that are sent First-Class. Under the USPS proposed rates, to borrow Stiglitz's terminology, the Postal Service's product mix is inefficient, leading to too much advertising mail volume, and too little First-Class mail volume, relative to the preferences of the consuming public.

If the public could choose the type of mail it consumes from USPS delivery, clearly it would choose to receive less advertising mail and more First-Class Mail. Stated otherwise, the Postal Service's proposed rates exacerbate what Stiglitz calls "exchange inefficiency."

In general, I do not support Ramsey pricing for postal services as it would seem to legitimize (efficient) monopoly pricing, whereas a major purpose and goal of postal rate regulation is to replicate efficient competitive prices in rate design insofar as possible. USPS witness Bernstein's calculations of hypothetical Ramsey-efficient rates in R97-1 would however, lead to a 245% cost coverage for First Class workshared mail, well under the USPS proposed coverage of 283% and well under my proposed coverage of 274%. I view the Ramsey rates as being what an efficient monopolist would charge using inverse elasticity pricing. Thus, First-Class workshared rates with a cost coverage in excess of 245% are absolutely inefficient, but my proposed 274% cost coverage (269% including my extra ounce rate proposal in ABA/NAA-T1) at least moves First-Class workshared rates a small way in the direction of greater efficiency than the Postal Services's proposed rates with a 283% cost coverage.

**RESPONSES OF ABA/EEI/NAPM WITNESS CLIFTON TO
INTERROGATORIES OF VP-CW**

VP-CW/ABA/EEI/NAPM-T1-9

At page 46, lines 14-17, you state that your proposed rates reflect "what the general public finds of greatest value in the nation's postal service and what it finds of lesser, little or even negative value."

- a. Please provide copies of, or citations to, all data, studies, analysis or reports on which you rely concerning what the general public finds of greatest value in the nation's postal service.
- b. Please specify all aspects of the nation's postal service that the general public finds to be of negative value, and cite the source of all information on which you rely to support the findings of negative value.

RESPONSE

See my answer to VP-CW/ABA/EEI/NAPM-T1-8.

DECLARATION

I, James A. Clifton, declare under penalty of perjury that the answers to interrogatories VP-CW/ABA/EEI/NAPM-T-1-1-9 of Val Pak Direct Marketing Systems, Inc., Val-Pak Dealers' Association, Inc. and Carol Wright Promotions, Inc. are true and correct, to the best of my knowledge, information and belief.

Executed FEB 13, 98

A handwritten signature in cursive script, appearing to read "James A. Clifton", written over a horizontal line.

James A. Clifton