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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

April 2, 1998

The Honorable Margaret P. Crenshaw
Secretary
Postal Rate Commission
1333 H Street, N.W.
Washington, DC 20268-0001

Re: Docket No. R97-1

Dear Ms. Crenshaw:

Enclosed for filing are corrected responses of the initial brief filed by the Alliance of Nonprofit Mailers yesterday afternoon. The corrections consist of two changes: (1) a table of contents has been added, and (2) the heading on page 38 has been capitalized and renumbered as "III" rather than "E".

Very truly yours,

David M. Levy

David M. Levy

Counsel for Alliance of Nonprofit Mailers

cc: All parties of record

This document has been conditionally accepted as a late filing pending consideration of acceptance.

DOCKET SECTION

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

RECEIVED APR 2 4 5 PM '98

Docket No. R97-1

Postal Rate And Fee Changes, 1997

INITIAL BRIEF OF ALLIANCE OF NONPROFIT MAILERS

David M. Levy
SIDLEY & AUSTIN
1722 Eye Street, N.W.
Washington, D.C. 20006-3704
(202) 736-8214

Joel T. Thomas
Suite 810
1800 K Street, N.W.
Washington, D.C. 20006
(703) 476-4646

Counsel for Alliance of Nonprofit Mailers

April 1, 1998

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

Docket No. R97-1

Postal Rate And Fee Changes, 1997

INITIAL BRIEF OF
ALLIANCE OF NONPROFIT MAILERS

The Alliance of Nonprofit Mailers ("ANM") respectfully submits its initial post-hearing brief. This brief covers three issues: (1) the Postal Service's revenue requirement; (2) the attribution of mail processing costs to Standard (A) nonprofit mail—and, in particular, the mismatch of IOCS and RPW data for mail entered with nonprofit markings at commercial rates; and (3) the validity of the TRACS methodology used to attribute of transportation costs. ANM is separately filing a joint brief with other users of Periodicals class mail dealing with rates for that mail class. For the reasons stated herein, ANM believes that the rate changes proposed in this docket should be denied.[1]

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[1] ANM also continues to believe that the Postal Service's rate request should be denied for failure to satisfy the Commission's rules for documentation of rate requests. *See* ANM Pre-Hearing Brief at 3-15. Because the evidence offered during the hearing has not substantially altered the record on this issue, ANM will not repeat the same analysis here.

ARGUMENT

I. THE RECORD IS DEVOID OF CREDIBLE EVIDENCE ON THE POSTAL SERVICE'S REVENUE REQUIREMENT.

A. The Legal Standards

Postal rates and charges must be set to "provide sufficient revenues so that the total estimated income and appropriations to the Postal Service will equal as nearly as practicable total estimated costs of the Postal Service." 39 U.S.C. § 3621. Accordingly, the Commission cannot lawfully recommend rates changes without probative and reliable evidence that they will cause the Postal Service to break even during the test year it has chosen. *See* OCA Initial Brief (First Section) at 6-7. The Postal Service, as the proponent of change, bears both the initial burden of production and the ultimate burden of persuasion. 39 U.S.C. § 3624(a) (incorporating 5 U.S.C. § 556(d)); *Director OWCP v. Greenwich Collieries*, 511 U.S. 1028, 114 S.Ct. 2751 (1994).

B. The Postal Service's Actual Financial Performance Since The Beginning Of The Test Year Has Destroyed The Credibility Of The Financial Projections Underlying the Postal Service's Rate Request.

The test year chosen by the Postal Service in this case is Fiscal Year 1998—October 1, 1997 through September 30, 1998. As OCA has explained in its brief, the Postal Service's financial performance since the beginning of the test year has revealed that the financial projections underlying the Postal Service's proposed revenue requirement are grossly pessimistic. *See* OCA Initial Brief (First Section) at 4-6, 7-10. In contrast to the Postal Service's rate case projection

of approximately $1.2 billion in operating losses for the test year, the Service has achieved over $1.2 billion in net *income* through the first six Accounting Periods of FY 1998. 35 Tr. 18604:8-22 (Porras). To convert this part-year surplus of $1.2 billion into an operating loss of the same magnitude, the Postal Service USPS would have to lose over *$2 billion* in remaining accounting periods of the year. 35 Tr. 18605-07 (Porras); OCA Initial Brief (First Section) at 7-9, 21-22.

The Postal Service has offered no credible evidence that it will incur losses of this magnitude during the remaining accounting periods. The Service's track record in predicting its financial performance during the Accounting Periods 10 through 13 has been notoriously poor in recent years. In Fiscal Years 1996 and 1997, respectively, the Service's actual losses during those Account Periods were only 33 and 17 percent, respectively, of the amounts projected by the Service. OCA Br. 18-20 (citing record); 35 Tr. 18636 (chart comparing projected vs. actual earnings). The managers responsible for those loss overestimates are also responsible in significant part for the financial projections in the present rate case. 35 Tr. 18632-33 (Porras).

As the Postal Service's test year revenue requirement projections have become increasingly implausible, the Service has retreated behind a shroud of managerial discretion, asserting that any reduction in the revenue requirement would infringe on "management's goals and objectives"—more specifically, the "spending programs" that the Postal Service has "in place for capital and other types of investments." 35 Tr. 18574-76, 18607-08, 18682:20-24, 18687-92. This claim does not withstand scrutiny.

First, the outflows needed to snatch a $1 billion-plus loss from the jaws of a $1.2 billion surplus would be heroic in scale. Postal Service expenses would

have to increase by *11 percent* over the same period of the previous year—an amount greater than the Postal Service's Controller has ever experienced during his 35-year career with the Service. 35 Tr. 18684:14-17 (Porras). Moreover, the Postal Service's spending levels would have to be far higher than even the levels approved by Postal Service management in October—*after* the outset of the rate case. 35 Tr. 18731-32 (Porras). Neither Mr. Porras nor any other witness has explained why the Postal Service's projected spending needs have skyrocketed so much during this relatively brief period.

The record contains no evidence that such expenditures will actually occur during the test year. Mr. Porras, while initially insisting that the requisite sums would be spent, 35 Tr. 18607-08, ultimately conceded on cross-examination that he could not predict what management will actually do in the test year. *Id.* at 18735 ("they may carry over to '99"); *id.* at 18737:5-6 ("I don't know at this point whether they will or not."). Indeed, cross-examination revealed that many of these supposed "losses" involve projects that have yet to be approved by the Board of Governors, *id.* at 18741:4-6, let alone signed into contract, *id.* at 18607:23-24, 18701:14-15, 18709:16, let alone performed by the Postal Service's vendors and recognized on its books, *id.* at 18744:1-7, 18744:25-18745:10. For some projects, months could elapse between Board approval and the actual signing of contracts. *Id.* at 18744:14-15). For others (e.g., ADP), only a tiny fraction of the outflows projected for the test year have actually occurred. *Id.* at 18747:13-18748:7.

The discretionary and uncertain magnitude and timing of these outflows renders the Postal Service's lost projections speculative. "If you don't spend the money in 1998, the deficit would be less." 35 Tr. 18716 (Porras). And expendi-

tures booked after September 30, 1998 are irrelevant to this case: the test year chosen by the Postal Service is Fiscal Year 1998, not some later period.

There exists an even more fundamental flaw in the Postal Service's theory of deficit-by-shopping spree: regardless of their timing and magnitude, the kinds of spending projects that the Postal Service is supposedly undertaking cannot generate losses recoverable from ratepayers.

Mr. Porras testified that *all* of the expenditures on the Postal Service's shopping list are for projects whose incremental benefits—including future increases in demand for postal services, and reduced exposure to asbestos cleanup charges and similar potential liabilities, as well as immediately quantifiable cash inflows—are expected to exceed incremental costs over the life of the investment. 35 Tr. 18619:17-18620:5 (Porras). If Mr. Porras is correct, then the Postal Service's spending projects must improve, not worsen, the present value of the Postal Service's net earnings.[2] Spending money on programs with an expected payoff bigger than their expected outflow cannot turn a projected surplus into a projected loss.

For prudent and economical spending projects to generate a projected loss on the Postal Service's books during the test year, there must be a timing mismatch between recognition of the expected outflows and recognition of the expected benefits of the project. Specifically, the Postal Service must have

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[2] If the present value of the anticipated payoff (in the broad sense of all anticipated future gains in revenue and reductions in anticipated losses or outflows) of a spending project does not exceed the present value of the anticipated costs, then the expenditure is imprudent, and must be disallowed under 39 U.S.C. § 3621 as inconsistent with "honest, efficient and economical management." Not surprisingly, Mr. Porras testified that "[t]his case here, it's an investment. It's not a waste of money. It's an investment." 35 Tr. 18735.

expensed items that should have been capitalized, assumed depreciation or amortization lives that are shorter than the anticipated economic lives of the projects, or adopted a test year that includes an atypically high level of expenditures, rather than normalizing expenditures over a more representative period.[3] Significantly, Mr. Porras conceded that, while most or all of the projects at issue will have a multi-year payoff, the Postal Service is nonetheless expensing much of their cost during the test year. 35 Tr. 18611-13.

The Postal Service has failed to produce the information needed to determine whether the expense projections underlying the projected revenue requirement are properly matched to the timing of the income projections. Mr. Porras' assertion that the Service's expensing of its cash outflows is consistent with Generally Accepted Accounting Principles ("GAAP"), 35 Tr. at 18609-11, 18621:22-23, is both unverifiable and insufficient. Neither Mr. Porras nor Mr. Tayman provided sufficient information to verify this claim. In any event, GAAP is a financial accounting standard that leaves management with considerable discretion in timing the recognition of costs, and expense timing assumptions that satisfy GAAP may be too front-loaded to satisfy economic regulatory standards.

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[3] The requirement that the timing of anticipated expenditures be properly matched the with timing of the expected economic benefits from those benefits—through the capitalization of expenditures with multi-year payoffs, and the normalization of extraordinary, atypical or nonrecurring expenses—is a bedrock principle of cost of service ratemaking. *See, e.g.*, *Western Mass. Elec. Co.*, 114 P.U.R.4th 1, 23-24, 30-31 (1990); *Westmoreland Coal Sales Co. v. Denver & Rio Grande Western Railroad Co.*., 5 I.C.C.2d 1067, 1080 (1988); *Momarc Util. Corp.*, 80 P.U.R. (N.S.) 53, 56 (1949); *Picholta v. Skagway*, 78 F.Supp. 999, 1007 (D. Alaska 1948).

The overstated and unsupported nature of the Postal Service's proposed revenue requirement has been confirmed by the Commission's recent discovery of an internal strategy memorandum *acknowledging* that the Postal Service's loss projections are inflated. 35 Tr. 18730. The memorandum reveals that one or more knowledgeable individuals involved in defending the Postal Service's proposed revenue requirement (1) were aware—before the Service filed its rebuttal testimony—that the proposed revenue requirement was overstated, and (2) sought to conceal that fact from the Commission and the public. Specifically, the memorandum acknowledged that a "complete revenue requirement update would be time consuming and *would probably result in a further reduction in test year costs*." *Id.* (emphasis added). Moreover, "there is also risk in exposing the [Postal Service's] rebuttal witness to cross examination *which could result in even more impetus for updating and reducing the revenue requirement*." *Id.* (emphasis added). To counter evidence that the Postal Service's costs have declined since the outset of the rate case, the memorandum proposed, *inter alia*, that the Postal Service provide a selective updating of its cost accounts in rebuttal testimony to create the impression that cost increases had offset the cost decreases ("[p]rovide updated information on cost increases *to offset the decreases* included under number 1"). *Id.* In the context of the Postal Service's later rebuttal testimony defending the Service's original revenue requirement, the memorandum is a classic smoking gun.

Finally, brief note should be made of the Postal Service's extraordinary suggestion that reducing the Postal Service's proposed revenue requirement would infringe on the Service's general management prerogatives even if it achieved break-even earnings during the test year. 35 Tr. 18585-86 (Porras). The short

anwer is that the Commission has both the power and the duty to enforce the statutory break-even requirement. OCA Initial Brief (First Section) at 13. If the Postal Service's general management plans are inconsistent with that requirement, then those plans must give way.

In any event, the Postal Service has offered no reason why the investment expenditures could not be financed by issuing debt with a maturity equivalent to the anticipated economic life of the goods and services that the Postal Service plans to acquire. The Postal Service is $8 billion below its long-term debt ceiling of $15 billion. 35 Tr. 18613-14 (Porras). On cross-examination, Mr. Porras grudgingly admitted that he did not know whether financing the Postal Service's expenditures through debt would run afoul of any debt ceiling. 35 Tr. 18624:5-17.

C. Rejecting the Postal Service's Rate Request Is The Only Lawful Remedy Open to the Commission.

The staleness and incredibility of the Postal Service's revenue requirement projections preclude the Commission from relying on them. OCA Initial Brief (Section I) at 16-7 (citing cases); MMA Response at 2 (citing cases). *Cf.* OCA Memo in Response to Notice of Inquiry No. 5 at 3-4 (precedent for updating original rate case data). Moreover, the existing record does not enable the Commission to split the baby by approving a more modest set of rate increases based on a smaller revenue requirement. Too many key determinants of the Postal Service's revenue requirement—including the Service's actual spending plans for Fiscal Year 1998, and the portion of that outflow that is properly attributed to Fiscal Year 1998—are simply unknown. Indeed, Mr. Porras so testified for other reasons:

> While appropriations of how much revenue and expense related to the strike should or should not be rolled forward into the test year might be made, the accuracy and validity of such estimates would be questionionable.

35 Tr. 18578:11.

Rejection of the Postal Service's rate request is appropriate on several grounds. First, the Postal Service exposed itself to this remedy when it refused to acquiesce in the limited extension in the decision deadline by three months. *Cf.* Letter from Chairman Gleiman, Vice Chairman Haley, and Commissioners LeBlanc and Omas to the Honorable Sam Winters (Feb. 24, 1998); Letter from Mr. Winters to Chairman Gleiman (March 4, 1998).

Second, dismissal of the Postal Service's case is an appropriate sanction for its attempt to mislead the Commission. *Cf. Peerless Industrial Pain Coatings Co. v. Canam Steel Corp.*, 979 F.2d 685 (8th Cir. 1992); *Combs v. Rockwell Int'l Corp.*, 927 F.2d 486 (9th Cir. 1991); *Sun World Inc. v. Lizarazu Olivarria*, 144 F.R.D. 384 (D.C. Cal. 1992). Failure to respond properly to conduct of this kind would undermine public confidence in the ratemaking process.

II. THE POSTAL SERVICE HAS FAILED TO PROVIDE CREDIBLE EVIDENCE OF THE MAIL PROCESSING COSTS ATTRIBUTABLE TO STANDARD (A) NONPROFIT MAIL.

A. The Disproportionate Rate Increases Proposed For Nonprofit Regular Mail Cannot Be Explained By Any Reported Changes In Its Cost-Causing Characteristics.

In this docket, the Postal Service has proposed rates for Nonprofit Standard Mail (A) Regular (Bulk Nonprofit ("BNP") Other) mail that increase sharply, while proposing only a small overall increase in rates for the corresponding

commercial rate subclass (Standard Mail (A) Regular, former Bulk Regular Rate ("BRR") Other). The *letter* rates proposed by the Postal Service for Standard Mail (A) Regular illustrate the deviation between nonprofit and commercial rates in this docket. As can be seen from Table 1, letter rates within the Presort Category exhibit the sharpest contrast; Nonprofit Standard Mail (A) Regular letters *up 19 percent*, Standard Mail (A) Regular letters *down slightly*. On a percentage basis, the changes in rates proposed for Automation letters, a fairly homogeneous category, also deviate significantly (except for carrier route automation letters). 22 Tr. 11776-11777 (Haldi).[4]

Table 1

Standard Mail (A) Regular
Postal Service Proposed Letter Rates

	NONPROFIT RATE			COMMERCIAL RATE		
	Old Step 6	New Step 6	**Percent Change**	Existing	Proposed	**Percent Change**
PRESORT CATEGORY						
Basic Presort Letter	13.8	16.5	**19.57%**	25.6	24.7	**-3.52%**
3/5 Presort Letter	12.0	14.3	**19.17%**	20.9	20.9	**0.00%**
AUTOMATION CATEGORY						
Basic Auto Letter	10.5	12.4	**18.10%**	18.3	18.9	**3.28%**
3-digit Auto Letter	10.1	11.2	**10.89%**	17.5	17.6	**0.57%**
5-digit Auto Letter	8.8	9.5	**7.95%**	15.5	16.0	**3.23%**
Cr Rte Auto Letter	8.5	9.2	**8.24%**	14.6	15.7	**7.53%**

[4] At the same time, the Postal Service proposes downward revisions for Nonprofit ECR rates, while rates proposed for the commercial rate ECR subclass increase modestly. 22 Tr. 11776 n. 1 (Haldi).

These disproportionate rate increases are driven by disproportionate increases in the costs attributed by the Postal Service to nonprofit mail. Table 2, taken from Dr. Haldi's testimony, compares average unit costs for Standard Mail (A) and Nonprofit Standard Mail (A) Regular (formerly third-class bulk) since 1992. 22 Tr. 11778-11780 (Haldi). The most telling comparisons are between columns 1 and 2, for FY95 and FY96. From FY95 to FY96, the unit cost for Bulk Regular Rate (BRR), "other" (the predecessor to Standard Mail (A) Regular) declined modestly, by 0.1 cent. At the same time, from FY95 to FY96 the unit cost for Bulk Nonprofit (BNP) "other" (the predecessor to Nonprofit Standard Mail (A) Regular) increased by an abnormally large amount, 0.8 cent. Considered together, these two changes narrowed the difference in unit cost between BRR "other" and BNP "other" by 0.9 cent. *Id.*

FY96 was unusual in the following respect. From FY92 through FY95, whenever the average unit cost for BRR "other" increased or decreased, the unit cost of BNP "other" also increased or decreased, whereas in FY96 the unit cost for BRR "other" decreased slightly while BNP "other" skyrocketed upward. *Id.* at 11778-11779.

The unusually large increase in unit costs in FY96 carries through to Base Year 1996, which is then rolled forward to Test Year 1998. That is, the relationship between Nonprofit Standard Mail (A) Regular and Standard Mail (A)

Regular rates is preserved more or less unaltered by the transformations that take place in the Postal Service models. *Id.* at 11779-11780.

Table 2

Third Class/Standard Mail (A)
Average Unit Cost
(cents)

Fiscal Year	BRR Other (1)	BNP Other (2)	BRR Carrier Route (3)	BNP Carrier Route (4)
1992	15.3	10.8	6.9	5.0
1993	14.6	10.4	6.1	4.9
1994	14.2	10.2	6.1	4.5
1995	**14.7**	**10.4**	6.4	4.4
1996	**14.6**	**11.2**	6.4	4.8

These disproportionate increases in unit attributable costs cannot be explained by relative year-to-year changes in the cost-causing attributes of nonprofit and commercial Standard Mail (A)—including presort condition, shape, automation, dropship entry, and weight—during the same period. 22 Tr. 11781-11791. Both subclasses are handled in the same manner, and mail processing cost models assume the same productivity (or lack thereof) for both. *Id.* at 11791.

As the proponent of increases in nonprofit postal rates, the Service bears the burden of proving that these disparate increases in attributable costs for nonprofit mail have really occurred. Failure to do so requires rejection of the Postal Service's rate request, at least with respect to nonprofit rates. 39 U.S.C. § 3624(a) (incorporating 5 U.S.C. § 556(d)); 39 U.S.C. §§ 3622(b)(3), 3626(a)(3). In fact, the record contains substantial evidence identifying several specific

reasons why the Postal Service's attributable cost data for nonprofit mail are inflated.

B. The Automation Refugee Problem Has Inflated The Mail Processing Costs Attributed to Nonprofit Standard (A) Regular Mail.

Much of the apparent increase in Nonprofit Standard (A) attributable costs appears to be the byproduct an influx of "automation refugees"—workers who remain on the Postal Service payroll despite having been rendered surplus by automation of other mail processing operations—into manual mail sorting operations. While these surplus workers appear on IOCS tallies for nonprofit mail, their costs are not attributable to the subclass, for a firm operating under "honest, efficient, and economical management" (39 U.S.C. § 3621) would not process nonprofit mail with more workers than needed to handle it.

How significant is the automation refugee problem? Between Fiscal Years 1995 and 1996, the total costs attributable to Nonprofit Standard (A) Mail Regular increased by 8.7 percent, while volume increased by only 0.8 percent. The average increase in unit attributable cost was 0.81 cents, or 7.8 percent, reflecting the small increase in volume and the large increase in total attributable cost. ANM-T-1 (Haldi) at 21; 22 Tr. 11792. Two cost segments—clerks and mailhandlers and purchased transportation— and related piggybacks accounted for three-fourths of this increase. And clerks and mailhandlers (and associated piggyback costs) in turn accounted for three-fourths of this fraction. ANM-T-1 (Haldi) at 21; 22 Tr. 11792.

Nonprofit mailers barcode and drop ship a lower percentage of their mail than do regular rate mailers, and thus a larger portion of nonprofit mail must be

handled manually. In other words, a lower percentage of Nonprofit Standard Mail (A) Regular qualifies for worksharing discounts, which means that less of it bypasses the Postal Service network. ANM-T-1 (Haldi) at 11-19; 22 Tr. 11782-11790.

The increase in unit cost for Nonprofit Standard Mail (A) Regular is consistent with hypotheses that (1) the Postal Service has "automation refugees," and (2) productivity has declined and continues to decline in areas where mail is not handled by automation or mechanization. That is, the Postal Service has an excess of displaced clerks and mailhandlers who are kept busy (at reduced productivity rates) processing mail that is not automated and does not (or can not) take advantage of drop-shipment to bypass the Postal network. ANM-T-1 (Haldi) at 22-23; 22 Tr. 11793-11794; TW-T-1 (Stralberg).

In this environment, the design of the IOCS tends to produce nonsensical results. For example, mail that is handled manually, at constant productivity, will have an increasing proportion of direct handling tallies. In turn, the higher ratio of direct tallies will cause an increase in the share of "not handling" tallies and costs assigned to manually sorted mail.[5] In other words, without any cost-driving change in manually sorted mail, total costs (and unit costs) may nevertheless be deemed to have increased. TW-T-1 (Stralberg); ANM-T-1 (Haldi) at 23-24; 22 Tr. 11794-11795.

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[5] As automation has progressed, the share of "not handling" tallies has increased substantially, with a corresponding decline in the share of direct tallies. 22 Tr. 11794 n. 9 (Haldi).

The existence of an automation refugee problem also helps explain the sharp increase in mail processing costs *relative to direct carrier costs.* ANM-T-1 (Haldi) at 23; 22 Tr. 11794; TW-T-1 (Stralberg).

Finally, rates for the Basic and 3/5-Digit presort categories show the greatest rate increase, along with the Automation Basic category. These categories require the greatest amount of handling. The higher-than-average rate increases reflect higher-than-average cost increases, which reflect productivity changes below average (*i.e.*, a decline in productivity). *Id.*

C. Nonsensical IOCS Tallies Inflate The Reported Attributable Costs Of Nonprofit Standard (A) Mail And Betray A Pervasive Quality Control Problem With The IOCS.

Mail processing costs for each subclass reflect the IOCS tallies of clerks and mailhandlers recorded for that subclass. Unfortunately, scrutiny of the FY96 IOCS tallies for Nonprofit Standard Mail (A) Regular reveals a number of tallies that are nonsensical on their face.

In FY96, 2,568, IOCS tallies were recorded for Nonprofit Standard Mail (A). Of this total, 2,393 tallies were for Nonprofit Standard Mail (A) Regular, and 175 were for Nonprofit Standard Mail (A) ECR. Direct mail processing accounted for most of the tallies (2,533 out of 2,568). 2,362 of the 2,533 direct mail processing tallies were for Nonprofit Standard Mail (A) Regular. 22 Tr. 11797-11798 (Haldi).

Table 3 shows the recorded weight for each of the 2,362 Nonprofit Standard Mail (A) Regular tallies (*id.* at 11803):

Table 3

Nonprofit Standard Mail (A) Regular
Distribution of Mail Processing Tallies
By Item and Weight

	Single Piece Tallies		Item Tallies		Container Tallies
No Weight recorded	0		29		0
Up to 1oz.	940		533		12
1 up to 2 oz.	282		141		5
2 up to 3 oz.	115		65		1
3 up to 4 oz.	106		22		2
4 up to 5 oz.	0		0		0
5 up to 6 oz.	37		19		0
6 up to 7 oz.	9		2		0
7 up to 8 oz.	0		0		0
8 up to 9 oz.	9		5		0
9 up to 10 oz.	0		0		0
10 up to 11 oz.	11		2		0
11 up to 12 oz.	0		0		0
12 up to 13 oz.	4		0		0
13 up to 14 oz.	0		0		0
14 up to 15 oz.	0		1		1
15 up to 16 oz.	1		1		0
2.5 up to 3.0 lbs.	1	IPP	0		0
3.0 up to 3.5 lbs.	0		1	letter	0
4.0 up to 4.5 lbs.	0		1	flat	0
4.5 up to 5.0 lbs.	1	IPP	1	flat	0
6.0 up to 7.0 lbs.	1	flat	0		0
over 15 lbs.	0		1	parcel	0
Total	1,517		824		21

Seven of the tallies record a weight in excess of 16 ounces, the weight limit for Standard Mail (A). *Id.* Clearly, something is wrong with these 7 tallies.[6]

[6] These tallies cannot be explained on the theory that a container or item have been measured. In all instances where weight is recorded, it is supposed to be

Either the weight is in error, or the tally has been misrecorded as Nonprofit Standard Mail (A). In response to a hypothetical question about a piece of Standard Mail (A) whose weight exceeded 16 ounces, USPS witness Degen stated that:

> The F-45 handbook (LR-H-49) contains no specific instructions for the disposition of such a tally. Mail class is recorded in question 23b. The question 23b instructions indicate that the Third-Class/Standard Mail (A) categories apply to mailpieces weighing less than 16 ounces. Weight is recorded in question 23g. The instruction to question 23g (LR-H-49, p. 131) are simply to record the weight in pounds and ounces, rounded to the nearest ounce, for mailpieces weighing more than 4 ounces. *It cannot be determined from the hypothetical whether the mail class was misidentified or the weight was incorrectly entered.*[7]

In addition to the tallies that recorded weight in excess of 16 ounces, another 35 tallies recorded weight between half a pound and 16 ounces. 22 Tr. 11803 (Haldi). To have so many heavyweight tallies in a subclass with an average weight of only 1.1 ounces (22 Tr. 11791 (Table 7) (Haldi)) is unusual, especially the three letter-shaped tallies, one of which was reported to weigh between 15 and 16 ounces.

All tallies above 16 ounces are clearly in error, and should be disregarded when computing the cost of Nonprofit Standard Mail (A) Regular. This correction does not end the matter, however. The ability of these facially nonsensical tallies to survive the editing process suggests a far broader and deeper breakdown in the

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for a single piece of mail. 22 Tr. 11800-11801 (Haldi).

[7] 22 Tr. 11801-11802 (Haldi) (quoting written response of USPS witness Degen to oral questions of ANM (filed October 28, 1997) (emphasis added)).

IOCS quality controls. The errors identified here are likely to be only the tip of the iceberg. 22 Tr. 11802 (Haldi).

D. The Reported Cost Data For Nonprofit Mail Are Tainted With IOCS Tallies For Mail With Nonprofit Markings Entered At Commercial Rates.

1. Description of the problem

The attributable costs of nonprofit Standard (A) mail have been further inflated by a mismatch of the IOCS and RPW data for Standard (A) mail bearing nonprofit evidencing of postage but paying commercial rates. There are several reasons why this mismatch occurs:

(1) the Postal Service collects a revenue deficiency assessment after entry of the mail, on the ground that the mail was ineligible for nonprofit rates;

(2) the Postal Service rejects the mail for nonprofit rates at the entry point, on the ground that the mail is ineligible for nonprofit rates; or

(3) the mailer determines in advance that the Postal Service would reject the mail for entry at nonprofit rates, and voluntarily enters it at commercial rates.

22 Tr. 11808-11816 (Haldi). New eligibility restrictions for nonprofit mail taking effect shortly before and during the test year have caused nonprofit mailers to pay commercial Standard (A) rates for substantial volumes of mail bearing nonprofit indicia. *Id.* at 11811-11814, 11827-34 (Haldi).

This phenomenon has created a serious mismatch between the RPW volume data and the IOCS cost data for the nonprofit subclass during the test year. Mail volumes entered by nonprofit mailers at commercial rates, and volumes subject to back postage assessments that lead to the filing of a new Form 3602, are recorded in the RPW as commercial mail. *Id.* When such pieces bear nonprofit rather than commercial indicia (e.g., meter markings or precancelled stamps), however, the IOCS attributes their mail processing costs to the nonprofit subclass. *When entry data (Form 3602s) and envelope markings do not coincide, the IOCS will attribute costs to one subclass, while the volumes and revenues will be recorded in another subclass.*[8] The subclass that is credited with extra volumes but no extra costs (tallies) will have *an understated unit cost*, while the subclass that is assigned the extra cost (tallies) but gets no credit for the corresponding volume will have *an inflated unit cost.* *Id.* at 11806.

The initial cost and volume data are primary inputs to many other modeling efforts, most notably the roll-forward model. When these fundamental data become unsynchronized, the entire costing edifice built on the IOCS becomes unsound. *Id.* at 11811.

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[8] *Id.* at 11806. This situation occurred in Docket No. R94-1 for In-County Publications. Through a programming error, IOCS tallies distributed costs to *In-County* publications, while revenues and volumes from those same publications were recorded under *regular rate* publications. The result was a sharp increase in the unit cost of In-County publications. The Postal Service may also have problems of this nature with respect to the various rate categories of First-Class Mail. *Id.* at 11806 n. 16.

In the absence of Postal Service data shedding light on the extent to which the sharp increase in Nonprofit Standard Mail (A) Regular unit costs may have resulted from revenue and cost data being "out of sync," the Alliance of Nonprofit Mailers undertook a survey of nonprofit organizations. A summary of the results of that survey follows. Additional details are contained in Exhibit 1 ANM-T-1 (22 Tr. 11827-30). Of 108 responses received:

- 31 organizations entered mail at commercial rates and used commercial rate indicia.
- 49 organizations entered mail at commercial rates, but used nonprofit evidencing of postage.
- 28 organizations entered nonprofit mail at nonprofit rates and with nonprofit markings, but later were assessed regular rates. Of those mailers, at least 13 organizations were certain that they filed a corrected USPS Form 3602-R.

The responses come from all major geographic areas of the United States, which indicates that the phenomenon of using nonprofit evidencing on Standard Mail (A) is indeed widespread. 22 Tr. 11812 (Haldi).[9]

ANM is unable to offer a precise correction for this error, for the Postal Service has refused to produce data quantifying the full extent of the problem. The record does provide two reasonable methods of estimating its magnitude, however.

First, one may reasonably estimate the share of Standard (A) mail volume which paid commercial rates but bore nonprofit evidincing of postage. These data support a reduction of 7.85 percent in the mail processing costs (including

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[9] Entry of mail with nonprofit markings at commercial rates appears to be a continuing problem.

piggybacks) attributed to Standard (A) nonprofit mail. 22 Tr. 11812-11814 (Haldi); 30 Tr. 16390-405 (Haldi response to POIR No. 13).

In the alternative, the Commission may limit the Postal Service's proposed increase in unit attributable mail processing costs for nonprofit Standard (A) mail to the ratio of nonprofit and commercial unit attributable mail processing costs that has prevailed in recent years before FY 1996. From FY 1992 to FY 1995, the unit attributable Clerks and Mailhandlers cost for Bulk Rate Nonprofit Other mail (now called Standard (A) Nonprofit) was approximately equal to 70 percent of the unit cost for Bulk Rate Regular Other (now called Standard (A) Regular). This changed between FY 1995 and FY 1996. Specifically, the unit cost for Standard (A) Nonprofit increased by more than eight percent while the unit cost for Standard (A) Regular dropped about two percent. As the following table shows, this resulted in a ratio of the Standard (A) Nonprofit unit cost to the Standard (A) Regular unit cost of nearly 0.79:

Unit Attributable Clerks and Mailhandlers Cost (in dollars)[10]

Subclass	1992	1993	1994	1995	1996
Standard A Regular	0.0648	0.0664	0.0621	0.0617	0.0604
Standard A Nonprofit	0.0456	0.0457	0.0436	0.0439	0.0476
Ratio	0.7037	0.6883	0.7021	0.7115	0.7881

[10] Source: Dividing the costs for Clerks and Mailhandlers in ANM-T-1, Table 8 by the volumes shown at the bottom of the table results in the FY 1995 and FY 1996 unit costs for Standard (A) nonprofit mail. It is a straightforward exercise to calculate unit costs for Standard (A) Nonprofit for earlier years and Standard (A) Regular for all years. For these calculations, we divided total costs from FY 1992-1996 Cost Segments and Components reports by volumes from FY 1992-1996 Cost and Revenue Analysis reports.

Limiting the Base Year Clerks and Mailhandlers costs for Standard (A) Nonprofit mail to 0.7115 times the unit cost for Standard (A) Regular mail (the ratio in FY 1995 and the highest of the ratios between FY 1992 and FY 1995) would yield a Base Year unit Clerks and Mailhandlers cost for Standard (A) Nonprofit mail of 3.8 cents, 8.6 percent less than that proposed by the Postal Service.

The Postal Service, after initially initially dismissing the IOCS/RPW mismatch as an unproven "hypothesis"—and denying that it possessed, or could produce, any data on the subject—conceded that phenomenon could indeed occur, and could indeed result in an overattribution of costs to nonprofit mail. 36 Tr. 14594:6-9 (Schenk). In its rebuttal testimony, however, the Service sponsored a survey of 30 USPS sites purportedly showing that the effect of this mismatch is insignificant. Dr. Schenk also argued that Dr. Haldi's study should be disregarded as unsound. 36 Tr. 19587 *et seq.* (rebuttal testimony of Dr. Leslie R. Schenk). ANM responds to each contention in turn.

2. Dr. Schenk's study does not provide credible evidence of the extent of the IOCS/RPW mismatch.

(a) The study relies on guesswork and multiple hearsay.

Dr. Schenk's survey of Postal Service facilities suffers from several basic flaws. First, the study rests on multiple layers of hearsay. In many instances, the information ultimately reported in the study was recounted by one Postal Service employee to another employee, who reported the information to an employee or colleague of Dr. Schenk, who jotted down the information on the form ultimately used by Dr. Schenk. 37 Tr. 19949-50, 19953-54 (Schenk). This chain of multiple hearsay is of particular concern for several reasons.

Neither Dr. Schenk nor her two fellow survey takers had any prior experience with nonprofit mail acceptance criteria before undertaking the survey. 37 Tr. 19951:14-17 (Schenk). Moreover, at all but two sites, Postal Service on-site employees supplied their answers from sheer memory, unaided by by any review of the disqualification logs or other business records made contemporaneously with the mailings. 36 Tr. 19638; 37 Tr. 19999. Stated otherwise, Dr. Schenk's volume estimates at the vast majority of sites are based solely on the unrefreshed recollections of busy Postal Service employees about the volume and characteristics of a small subset of the mail entered between 18 months and 2 1/2 years earlier.

Moreover, at a number of sites the volume estimates (or, more precisely, guesses) provided by the Postal Service employees were for a single accounting period in FY 1998, not for FY 1996 at all. 37 Tr. 19960-61. This assumption alone ensures meaningless results unless the volume of mail with nonprofit markings entered at commercial rates in the more recent period is a good proxy for the volume of such mail during the entire year of FY 1996. In Dr. Schenk's study, however, this critical assumption is supported by unaided memory at best, and typically nothing but sheer guesswork. *See* 37 Tr. 19962-63; ANM-XE-2 at 75; 37 Tr. 19961:14-20; ANM-XE-2 at 78, Question 1 (stating that the respondent "doesn't know" how many nonprofit mailings were rejected or ruled ineligible for nonprofit rates in Accounting Period 5 of FY 1998); *id.* at 72 (stating that respondent is "not sure" whether Accounting Period 5 of FY 1998 is a good proxy for the 13 accounting periods in FY 1996, "but thinks it is as good as any"); 37 Tr. 19972 (no indication on form for Site 2 (ANM-XE-2 at 18 *et seq.*) to support assumption that FY 1997 data are a good proxy for FY 1996; instead, Dr. Schenk

relied on her recollection that that the respondents' "general comments" were that "FY '97 was representative").[11]

Dr. Schenk added additional layers of guesswork and extrapolation in interpreting the study responses. Most of the survey respondents did not provide specific volume figures for rejected mailings; rather, they stated (or guessed) where the mailings fit in volume ranges dictated by the survey itself. *See, e.g.*, 37 Tr. 19967-68; ANM-XE-2 at 77 (indicating that "most of them" fell within the range of 5,000 to 10,000 pieces). To convert these responses into specific volume data, Dr. Schenk arbitrarily assumed that the average number of pieces of each mailing within a given size range equalled the unweighted midpoint of the range. *See, e.g.*, 37 Tr. 19983-84, 19985-86, 19994-95, 19998.[12] In some instances,

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[11] The likelihood that the many of the answers were sheer guesses is heightened by the failure to include "filter" questions such as"I don't know" or "no opinion" to screen out answers from respondents who might otherwise be tempted to guess. A survey of this kind that lacks filter questions "tends to overestimate the number of respondents with opinions, because some respondents offering opinions are guessing." Shari S. Diamond, "Reference Guide on Survey Research," in Federal Judicial Center, *Reference Manual on Scientific Evidence* 245 (1994)

[12] Dr. Schenk offered several defenses for this assumption. First, she asserted that it was "conservative" because survey respondents indicated that the Postal Service had more compliance problems with "smaller-volume mailers." 37 Tr. 19984, 19995. This is a *non sequitur*: that smaller mailers that tender more non-complaint mail than bigger mailers does not explain why the unweighted midpoint is a valid proxy for the weighted average volume *within the individual size ranges* used by Dr. Schenk. Moreover, Dr. Schenk simply overlooked the 250-piece minimum for entry of any mailing. 37 Tr. 20012-13.

Second, Dr. Schenk contended that adopting a different assumption would not change the results much. *Id.* at 19985. She promptly admitted, however, that she did not know by what percentage the results would change,

where the response indicated that "most" of the mailings fell within a particular size range, Dr. Schenk simply assumed that *all* of the mailings did so. 37 Tr. 19968. This assumption can inject a significant downward bias in the result, for omitting even a handful of very large mailings can significantly understate the average piece count per mailing.

Likewise, when a mailing was reported to fall the "above-100,000" volume range of pieces, Dr. Schenk assumed that the actual piece count was 500,000. What basis did Dr. Schenk have for choosing that value rather than 101,000—or 1,000,000? None at all. She "picked" the 500,000-piece assumption "up out of thin air . . . with no basis in any factual information for choosing it." *Id.* at 19988.

In sum, the apparent precision of Dr. Schenk's survey results is misleading. While the results may be reported to the precision of single digits (*see* 37 Tr. 19996:9-12 (discussing 36 Tr. 19621)), the underlying values are the product of guesswork, heroic assumptions, and estimates multiplied by estimates.[13]

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and had never done "that particular math at any point in this process." *Id.* at 19985.

Third, Dr. Schenk allowed that "the average was a very representative number to use in this case" because "I had people giving me this information who had been there in FY '96." *Id.* at 19987. She promptly admitted, however, that the survey forms contain "nothing" that "indicates that they told you that they though that . . . the midpoint was a good representative for the weighted average." *Id.*

Dr. Schenk eventually admitted the truth: she used the midpoint "because I had no information to choose" another proxy for the weighted average number of pieces. *Id.* at 19987:8-10.

[13] Attachment A at the end of this brief lists additional defects and anomalies in the survey response forms and disqualification logs.

(b) The study suffers from respondent bias.

Dr. Schenk's survey suffers from a second major defect: respondent bias. The local Postal Service employees who answered the survey questionnaire had an obvious incentive to underreport the true extent to which they and their co-workers accepted mail with nonprofit markings at commercial rates. As Dr. Schenk notes in her own testimony, this practice is a violation of the Domestic Mail Manual. 36 Tr. 19593:8-13 (Schenk). The correspondence received by the local post office sites from Dr. Schenk's consulting firm, and from Postal Service headquarters, made clear that the survey was undertaken at the behest of headquarters. *See* 37 Tr. 19923, 19938, 20017 (Schenk/Loetscher letter); 37 Tr. 19924, 19940, 20022 (Bizzotto letter). No precautions were taken to conceal the involvement of headquarters from the postal employees who actually answered the surveys, and no promises were made to hide their identities from Postal Service headquarters personnel. 37 Tr. 20009-10 (Schenk).

(c) The study overlooked mail with nonprofit markings that was voluntarily entered at commercial rates.

The most serious flaw of all, however, was the complete failure of the survey to investigate by far the most significant cause of the IOCS/RPW mismatch identified by Dr. Haldi: the *voluntary* entry of mail with nonprofit markings at commercial rates, without any attempt by the mailer to enter the mail at nonprofit rates, and without any action by the Postal Service to disqualify the mailing for such rates.

This phenomenon can occur for a variety of reasons. For example, a nonprofit organization with a large press run of catalogs bearing nonprofit

markings may enter them in a series of mailings over a period of several weeks or months. If the first mailing is disqualified for nonprofit rates, the mailer may simply enter the remaining mailings at commercial rates. Or a major university that occasionally sends out solicitations for affinity credit cards at commercial rates may enclose them in envelopes with nonprofit markings rather than maintain a separate inventory of envelopes with commercial markings.[14] Or a postal employee who has developed a close working relationship with a nonprofit mailer (even perhaps through a plant loading arrangement) may "accommodate" a mailer by informally warning him or her to pay commercial postage for a forthcoming mailing with nonprofit markings, rather than formally disqualifying the mailing at the acceptance dock after the mailer has tendered it with nonprofit postage. *See* 36 Tr. 19593:14-19594:1 (Schenk) (noting practice of postal employees to "accommodate" mailings with mismatched indicia).

Dr. Haldi's survey found that the majority of mailings entered with nonprofit markings at commercial rates were voluntarily entered in this condition by the mailer, without any formal entry or disqualification of the mailings at nonprofit rates. 22 Tr. 11812 (Haldi). Dr. Schenk also acknowledged that voluntary entry occurred at "some sites" in lieu of formal disqualification: the employees "did mention" that "instead of formally rejecting the mail, the postal employee will hold it until the mailer comes and fixes it." 37 Tr. 19973:1-4. As "an accommodation, the sites sometimes allow mail to . . . go all the way through with a nonprofit marking even at commercial postage." 37 Tr. 20005:2-6.

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[14] Solicitations for affinity cards generally do not qualify for nonprofit Standard (A) rates. *See* 39 U.S.C. § 3626(j)(1)(A).

Dr. Schenk's survey response forms also allude to the existence of this phenomenon as widespread. At one site, the respondent indicated that no mailings were "rejected" because of content: "mostly mail will just sit there until corrected, not sent through." *See* ANM-XE-2 at 25.

At another site, the respondent stated that "[r]ecently an auditor . . . was "stunned to see how few problems [redacted] had with nonprofit mailings, esp. given the volume they have. [Name redacted] attributes this to good relations he and his clerks have with mailers & printers." *Id.* at 48.

At a third site, the Postal Service employee reponded that her facility accepts repeat mailings "still endorsed NP" for entry at commercial rates. *Id.* at 78. The volumes entered are simply recorded in "PERMIT & accounting as Regular." *Id.*

At another site, a postal employee "doesn't really keep a disqualification log because he helps mailers prepare their mail they come in for the first time." *Id.* at 312. "If something looked wrong [we] would correct it with customer. Go over w/ customer before ever mail NP what can and can't do." *Id.* at 318.

Despite observing this phenomenon, Dr. Schenk and her colleagues made no attempt to measure it. The volumes reported in her testimony are limited to mailings formally entered at nonprofit rates and then formally disqualified by the Postal Service. Thus, the table on page 2 of her prefiled testimony offers volume figures only for "disqualification after acceptance," "reversals," and "disqualification at acceptance." 36 Tr. 19592. For "disqualification during acceptance," her operative definition was expressly limited to pieces that the mailer actually tried to enter at nonprofit rates, triggering a formal Postal Service ruling on their eligibility for nonprofit rates:

> "Disqualification During Acceptance
>
> Nonprofit mailings can be disqualified *for nonprofit rates* during mail acceptance proceedures, *if a determination is made that the contents of the mailings do not follow accepted guidelines for nonprofit mailings*."

Id. at 19605:8-10 (emphasis added); *accord, id.* at 19606:18-18 ("I estimate . . . the volume of mail bearing nonprofit indicia that was *disqualified for nonprofit rates during acceptance*"); *id.* at 19616:8-10 (purpose of survey was to "determine the degree to which *nonprofit transactions disqualified during acceptance* pay regular rates but have nonprofit indicia") (emphasis added); *id.* at 19618; 36 Tr. 19621 (table) (right-hand column heading reading "volume disqualified, paid reg. Std. (A)"); 37 Tr. 19942 (column was source of Schenk's volume estimates).

During the interval between Dr. Schenk's adoption of her prefiled testimony on March 20 and her return to the witness stand on March 30, however, her recollection of the study methodology underwent a remarkable refurbishment. Soon after resuming the stand, she announced that the term "disqualified mail," as used in her survey and testimony, had included all along both disqualified mail *and mail entered voluntarily at commercial rates*. 37 Tr. 19931-34, 19942-43 (Schenk). Mail voluntarily entered "at regular rates but with nonprofit indicia," she insisted, "would be part of our survey and therefore would be included in the 30 million volume . . . recorded" (*id.* at 19933-34). Mail "described as being disqualification at acceptance" in the survey "really is *anything* that during the acceptance process was mailed at regular rates but with nonprofit indicia." *Id.* at 19934 (emphasis added).

Dr. Schenk's present recollection is unsupported by *any* document generated by her, her colleagues, or the Postal Service during the course of the study. The study documentation offers no hint that the Postal Service field employees interviewed over the telephone by Dr. Schenk or her colleagues shared her present understanding of the term "disqualified mail," or thought that they were being asked to supply volume data for mail voluntarily entered at commercial rates. Indeed, much of the documentation produced by the Postal Service for her study directly indicates the contrary.

First, the pre-survey script sent to the managers of the postal sites included in the survey made no mention of mailings voluntarily entered at nonprofit rates. *All* of the relevant questions were limited to "Nonprofit Mailings Rejected Or Ruled Ineligible During The Acceptance Process." 37 Tr. 19926-27, 20020-21.

Likewise, the preprinted forms used by the survey takers, and the handwritten notes they wrote on the forms during the survey, also contain no indication that the volumes reported "included mail that was voluntarily entered at commercial rates with nonprofit markings." 37 Tr. 19997:1-9; ANM-XE-2 (admitted into evidence at 37 Tr. 20023).[15] This means that no such indication was recorded *anywhere* during the course of the survey, because no other scripts, notes or similar documents were generated in the course of the survey. 37 Tr. 20025-26 (letter dated March 16, 1998 from Anne B. Reynolds to David M.

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[15] During cross-examination, Dr. Schenk tried to brush off this omission on the ground "the survey had been designed early in the stage when we weren't sure exactly what kind of information we were getting, so it was generally worded." 37 Tr. 19958:23-25. But Dr. Schenk and the Postal Service *continued* to use the *same* terminology throughout the course of the entire project, including the filing of Dr. Schenk's testimony and her adoption of it under oath on March 20.

Levy). Similarly, there is nothing in the study documentation to show that "the Postal Service employee who answered the questions was *told* that mail volumes that were voluntarily entered as commercial mail should be included in the total given," or that the respondents, in answering the quesion, "intended to include voluntary entries as rejected mailings." *See* 37 Tr. 19970:20-19971 (emphasis added); *accord*, 37 Tr. 19989:17-19990:4 (commenting on survey response for Site 7 (ANM-XE-2 at 86-99)); *id.* at 19997:11-21 (general admission that *none* of the survey forms contain such information).

Confronted with these facts on cross-examination, Dr. Schenk asserted that she and her colleagues had obtained this information through improvised *oral* questions and answers that she and her colleagues left unrecorded on the form. 37 Tr. 19990-91. These claims deserve little weight. Reliable survey reports state "the exact wording of the questions used"; reliance on undocumented questions or answers undermines the trustworthiness of the results. Shari S. Diamon, "Reference Guide on Survey Research," in Federal Judicial Center, *Reference Manual on Scientific Evidence* 264 (1994).[16]

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[16] Dr. Schenk's purported reliance on questions and answers not documented on the survey forms is particularly ironic in light of her criticism of Dr. Haldi for engaging in the same practice. *Compare* 36 Tr. 19600:1-3 (Schenk) (criticizing ANM study because certain of "the data recorded in [Dr. Haldi's] Exhibit ANM-T-1 did not match the answers provided on the survey forms") and *id.* at 19657 (criticizing similar omission in Haldi testimony) (". . . there is nothing indicated on those survey forms that I could tell that indicated that additional information. . . . I assume if you are following the evidence rules -- I could recreate the numbers in the exhibit from this library reference, and that's what I was going on.") with 37 Tr. 19991:17-22 ("I guess" the Commission "would also have to rely on my testimony and what I am -- how I am describing things today, how I am testifying to today").

Moreover, Dr. Schenk's supposed reliance on undocumented oral questions and answers is at odds with her other testimony. Her written testimony states that the telephone interviews were conducted "with the questions previously faxed to the site as a guideline for the discussion." 36 Tr. 19617:16-19. On cross-examination, she finally conceded—after several promptings by ANM counsel and Chairman Gleiman—that she never specifically asked her fellow survey takers to "include volumes of mail that were voluntarily entered at commercial rates." 37 Tr. 19956:8-19958:2. She acknowledged that her employees "said nothing" to her about whether the volume estimates reported to her included "mailings that were voluntarily entered at commercial rates." *Id.* at 19959:18-24, 19993. "That is how they were trained. They . . . ask the questions that they were told to ask." *Id.* And she admitted that:

> *All the information I used in my estimates is written on these forms.* As I have said before, there is not that link where they were telling me things that are not on these forms.

37 Tr. 19992.

In any event, the survey response forms indicate that voluntary entry is *encouraged* by USPS personnel at several sites where the survey reports little or no mismatched volume. The obvious inference is that the respondents were operating under the impression that voluntary volumes should *not* be included in the totals.

Dr. Schenk also argues that her results are confirmed by the absence of any references in the disqualification logs to mail bearing nonprofit markings but entered at commercial rates. 37 Tr. 19935-36, 20001, 20003-04. But there is no basis for assuming that the absence of such entries proves that no such mailings

were accepted. An inference far more plausible is that such mailings occur, but are simply not recorded in the logs.

Dr. Schenk conceded that nothing in the disqualification logs—or any other document underlying her testimony—supported her assumption that "[w]henever there is a discrepancy between the rate that is being paid in the indicia it's automatically recorded as something that needs to be checked." 37 Tr. 20001-02. She also admitted that acceptance or disqualification logs "are not used as some kind of official record of volumes for the Postal Service in general," and "headquarters" does not require local offices to record the volumes of mail accepted at commercial rates with commercial markings. 37 Tr. 20005-06. Rather, the logs "are used by the sites to help them figure out what is going on in their day, what mailings need to be addressed, what problems need to be addressed, what mailers need to be called up to verify situations." *Id.* at lines 16-29. Pressed for an explanation of why a local mail acceptance employees who made an "accommodation" allowing a mailer to enter mail with nonprofit markings at commercial rates would find any use in recording the transaction in an acceptance log, Dr. Schenk could only speculate that "they would want to inform the mailer that this is something they are not supposed to be doing and that they shouldn't do it in the future." 37 Tr. 200007:7-11.

Perhaps the most telling evidence against Dr. Schenk's interpretation of the disqualification logs is their failure to indicate the voluntary entry of mail with nonprofit markings at commercial rates *even at sites where survey forms indicate that this practice is widespread.* As noted above, however, Dr. Schenk's own post office survey forms—like Dr. Haldi's mailer survey responses—confirm that

Postal Service "accommodation" of these mailing practices is both pervasive and ongoing.

3. Dr. Haldi's proposed adjustments should be accepted as the best evidence of record.

The infirmities of Dr. Schenk's study leave Dr. Haldi's analysis as the best evidence of record. Unlike the Postal Service survey data, the mail volume data obtained by Dr. Haldi were based on mailing statements or other contemporaneous business records, rather than the frailty of unaided human memory.

The Postal Service's criticism of Dr. Haldi's study for not being "statistically valid" or drawn on a "random" sample is an attack on a straw man. ANM has never claimed that the study satisfies either of these conditions. ANM *could not* have been drawn such a sample, for the Postal Service is the only participant in this case that possesses data on the entire universe of mailers that entered mail with nonprofiot markings in FY 1996—or any other year—and the Postal Service has consistently declined to share such information with other participants in rate cases. *See* 39 U.S.C. § 412(a) (restricting disclosure of such information).

Moreover, Dr. Haldi's study is no different in this respect than Dr. Schenk's study. "No standard errors or confidence intervals are provided for the estimates presented here," Dr. Schenk conceded. 36 Tr. 19618:5-6. The Postal Service has conceded that her survey was"limited" and "qualitative."[17] Signifi-

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[17] Opposition of the USPS to Motion of ANM to Compel Production of Mail Acceptance Logs Underlying USPS-RT-2 Or, In the Alternative, To Strike Portions of That Testimony (March 19, 1998) at 3.

cantly, Dr. Schenk admitted that she had seen no information in the course of preparing her testimony to indicate that the nonprofit organizations allegedly overrepresented in Dr. Haldi's study (e.g., art museums) has mail rejection rates that differed from the universe of nonprofit mailers. *Compare* 36 Tr. 19598:15-19 and *id.* at 19652-54.

Other Postal Service criticisms of Dr. Haldi's study betray a similar double standard. Dr. Schenk criticizes Dr. Haldi's study for non-response or self-selection bias. 36 Tr. 19596:24-24 (Schenk). As explained above, Dr. Schenk's study suffers from non-response bias of its own.

Dr. Schenk criticizes Dr. Haldi's study respondents for failing to "indicate how the volumes for these mailings were recorded in Postal Service databases." 36 Tr. 19595:10-11, 19600 n. 2 (Schenk) Dr. Schenk has never explained how ANM (let alone individual mailers) could have furnished this information when the Postal Service, the sole possessor of it, continued to insist that it did not exist until after the deadline for filing intervenors' testimony had expired. *See* Presiding Officer's Ruling No. R97/1-99. What should Dr. Haldi have done in in the wake of the Postal Service's stonewalling? Why, he should have refrained from filing any study at all! "I believe he does not have the information available to make his conclusions." 36 Tr. 19651 (Schenk).[18]

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[18] Dr. Schenk's criticism that that some of the workpapers for Dr. Haldi's study include two document numbers "on a single response form," a double numbering that "does not appear to correspond to mailers who mailed at both commercial and nonprofit rates" (36 Tr. 19600:11-14, 19613) betrays a misunderstanding of the data. The double marking corresponds to mailers who entered mail at commercial rates bearing both commercial and nonprofit *markings*. ANM counsel informed Postal Service of this fact before the filing of Dr. Schenk's testimony. Moreover, the Postal Service was free to ask for

Needless to say, the courts have not shared the Postal Service's notion of the burden of proof. When a party with peculiar knowledge or control of information chooses not to produce it, it is appropriate to draw the inference that the information is adverse to the withholding party. *See* 2 Wigmore on Evidence §§ 285-91 (Chadbourne Rev. 1979) (citing authorities); *Old Ben Coal Corp. v. Interior Board of Mine Op. App.*, 523 F.2d 25 (7th Cir. 1975).

4. The only lawful alternative to an adjustment along the lines proposed by Dr. Haldi is rejection of any rate increase for Standard (A) nonprofit mail.

If the Commission determines that neither of Dr. Haldi's proposed adjustments is sufficiently documented to warrant adoption, then the only lawful option open to the Commission is to reject *any* rate changes for Standard (A) nonprofit mail. Simply accepting the cost levels attributed by the Postal Service is not a lawful option. As the proponent of increases in nonprofit postal rates, the Service bears the burden of proving that the proposed increases are justified. 39 U.S.C. § 3624(a) (incorporating 5 U.S.C. § 556(d)). For nonprofit mail, the key element to be proven is the level of costs attributable to each subclass. 39 U.S.C. §§ 3622(b)(3), 3626(a)(3). The Service can hardly meet this burden with attributable cost data that are corrupted with tallies from other subclasses, particularly without offering any data setting an upward bound on the magnitude of the overstatement.

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clarification of items of this kind when Dr. Haldi was on the stand for cross-examination. Instead of doing so, the Postal Service waited to criticize his methodology as unclear or unexplained until he was off the witness stand and no longer able to respond.

The Interstate Commerce Commission faced a similar issue two decades ago. Rail Form A, the cost system used in railroad rate cases at the time, attributed the variable costs of system-wide investment in railroad track, ties, and related items to individual freight movements in proportion to various measures of volume. *See San Antonio, Texas v. United States*, 631 F.2d 831, 841-42 (D.C. Cir. 1980). In the late 1970s, the ICC determined that this methodology understated the costs of new high-volume unit train coal movements for electric utilities—traffic that required massive new investments to rehabilitate the track over the route of the movement. Accordingly, the ICC allowed the railroads to attribute to individual coal movements a "fixed plant investment additive" based on the carrying costs of the capital improvements needed to handle the movements. *Id.*

The shippers argued that this additive would overstate costs unless the corresponding investment accounts were backed out of Rail Form A. *Id.* at 842. The ICC declined to back out any of the Rail Form A accounts. It conceded that including them would result in a slight, though unquantifiable overstatement of investment costs. *San Antonio, Texas v. Burlington Northern Inc.* ("*San Antonio II*"), 359 I.C.C. 1, 11-12 (1978), *aff'd*, 361 I.C.C. 482, 486-88 (1979) ("*San Antonio III*"). The ICC reasoned, however, that this consideration was insufficient to order an adjustment that would clearly understate the costs attributable to the movement by a significant amount. *Id.*

On appeal, the D.C. Circuit overturned the ICC's action, reasoning that failure to eliminate the double-count resulted in impermissible cross-subsidization. *San Antonio*, 631 F.2d at 844. The Court's reasoning applies with equal force here:

> Variable costs by definition are only the costs caused by the relevant service and should not include costs caused by other services. We recognize that costing is not a particularly exact science, but by occasioning cross-subsidization in variable cost calculation, the Commission's decision is not merely imprecise, but arbitrary and unreasonable.

Id.; *accord*, *Celanese Chemical Co. v. United States*, 632 F.2d 568, 575-76 (5th Cir. 1980). *See also Cleveland-Cliffs Iron Co. v. ICC*, 664 F.2d 568, 580-82 (6th Cir. 1981) (upholding ICC's subsequent policy of backing out Rail Form A accounts).[19]

III. THE TRACS METHODOLOGY OVER-ATTRIBUTES TRANSPORTATION COSTS TO STANDARD (A) NONPROFIT MAIL.

Between FY95 and FY96, the *increase* in purchased transportation costs attributed to Nonprofit Standard Mail (A) Regular amounted to $11,451,000, an increase of *29 percent* over FY95. ANM-T-1 (Haldi) at 45; 22 Tr. 11816. Total volume of Nonprofit Standard Mail (A) Regular was up only 0.8 percent, the percentage drop shipped increased by 2 percent, and the volume variability of total transportation costs did not change between FY95 and FY96. *Id.*

This disproportionate increase in transportation costs attributed to Nonprofit Standard Mail (A) Regular stems from a fundamental design flaw of

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[19] For the same reason, it would be inappropriate to shift any mailing processing costs *to* Standard (A) *commercial* if the Commission finds that the extent of the IOCS/RPW mismatch is indeterminate. The consequences of the Postal Service's failure to meet its burden of proof must be borne by the Service itself.

TRACS, the Postal Service's system for distributing transportation costs to individual classes and subclasses of mail. *Id.* at 45-55; 22 Tr. 11816-11826.

The TRACS distribution key represents the proportion of cubic foot miles that TRACS allocates to each subclass of mail. The cubic foot miles from TRACS are thus the basis for developing transportation costs attributable to each subclass. *Id.* at 45; 22 Tr. 11816.

TRACS is a sampling system. Postage evidencing on mail pieces may be used to determine the subclass of mail. Consequently, TRACS suffers the same drawback as IOCS when nonprofit evidencing is used on mail entered at commercial rates. That is, whenever such mail is sampled, the nonprofit subclass will be tagged with the transportation costs, while the regular rate subclass is credited with the volume and revenues. *Id.* at 46; 22 Tr. 11817.

The purpose of TRACS is to develop a key for distributing volume variable transportation costs to the individual classes and subclasses of mail. TRACS is a sampling system, and it samples mail from postal transportation by air, highway and rail. For highway transportation, the predominant mode of transportation for nonprofit Standard (A) mail, TRACS samples mail as it is off-loaded from randomly selected trucks. *Id.* at 46; 22 Tr. 11817.

At first blush, one might think that TRACS would distribute highway transportation costs according to:

- the *actual amount of mail* off-loaded; and
- the transportation service provided to whatever mail is found to have been off-loaded from the truck.

Id. at 46-47; 22 Tr. 11817-11818. Unfortunately, TRACS achieve neither of these results. TRACS treatment of highway transportation costs is fatally flawed in at least two important respects.

First, TRACS artificially breaks each truck's route into separate "independent" segments. Most highway routes involve round-trips, whereby trucks return to the facility from which they initially start the route.[20] On any given day, all segments of the route are necessarily served by the same truck. Capacity of the truck must obviously be sized for whatever segment or segments have the highest average volume. In other words, the route is an integral, indivisible unit from both an operational and economic perspective. *Id.* at 47-48; 22 Tr. 11818-11819. As stated by Postal Service witness Bradley,

> For the Postal transportation network, I view *the cost of a contract being jointly determined by the cost of serving all of the legs on all of the route/trips* on the contract. The cubic foot-mile capacity set on a contract reflects the *joint requirements* of moving mail over the Postal network and that *the total contract cost should not be allocated to any individual leg on the contract.* In other words, the cost of transportation on a contract varies with changes in the *total* cubic foot-miles specified in the contract and *is not directly allocable to any specific leg.* Moreover, contract specifications are set by the Postal Service in its attempt to minimize highway transportation costs subject to reliably meeting service standards.

7 Tr. 3337 (Bradley) (emphasis added); *accord,* ANM-T-1 (Haldi) at 47-48; 22 Tr. 11818-11819. In other words, the route should not be broken up artificially into

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[20] The truck may shuttle and back, more or less traversing the same route in each direction, or it may make a "circular" trip that does not entail retracing any segment in opposite directions. *Id.* at 47 n. 22; 22 Tr. 11818.

"independent" segments. Yet this is precisely what TRACS does. ANM-T-1 (Haldi) at 48; 22 Tr. 11819.

Second, TRACS is built upon an indefensible "expansion" process that distorts and biases the final distribution key by an unknown magnitude. TRACS neither measures nor records the actual volume of mail (in pieces, pounds or cube) that is off-loaded. Instead, a series of data manipulations allocates the total space available to whatever mail happens to be off-loaded from the truck at the time when the truck is sampled. In so doing, TRACS *expands* the sampled mail *to fill the entire space available*, regardless of the amount of mail actually on the truck. ANM-T-1 (Haldi) at 48-53; 22 Tr. 11819-11824.

To illustrate, assume that an over-the-road ("OTR") container is sampled upon off-loading. It may have in it only one or two sacks of nonprofit mail. Alternatively, it might be loaded full to the brim with nonprofit mail. So long as the OTR container has only nonprofit mail, it would be recorded as having 100 percent nonprofit mail. 7 Tr. 3493, 3495 (USPS witness Bradley). This is the case even if the container is practically empty and the remainder could just as easily have been filled with something else, such as regular rate bulk mail, or parcels, or whatever. In other words, the nonprofit mail in the OTR container is treated by TRACS as somehow having been responsible for whatever empty space happens to be found in the OTR at the time the sample is taken. On this basis, TRACS treats the empty space in the container as "reasonably assignable" to the nonprofit mail in the container. ANM-T-1 (Haldi) at 48-49; 22 Tr. 11819-11820.

Finally, because the actual volume of mail is not recorded, that most essential datum is simply unavailable in the TRACS database.[21]

To continue the preceding example, the TRACS expansion process does not end with the OTR container. The expansion process continues its "blame the victim" procedure until all available cube on the truck is assigned to whatever mail happens to be off-loaded from the truck, no matter how small or large the actual volume of mail. At the point where the sample is taken, the truck may be almost empty, but the expansion process nevertheless attributes all the empty space for that particular segment (as well as prior segments) to whatever mail is actually sampled.[22]

TRACS expansion process can produce bizarre results. The ratio of (1) the cubic volume attributed to a subclass and (2) the actual volume of mail on the truck can vary enormously. If the truck is practically full, the ratio will be low, perhaps less than 2 to 1. If the truck is nearly empty, however, the ratio could be quite large, perhaps exceeding 100 to 1, by virtue of the empty volume assigned to mail on the truck.[23] In other words, the emptier the vehicle, the greater the cube

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[21] *Id.* at 49; 22 Tr. 11820. The lack of this datum makes it impossible to use the TRACS data base to develop an alternate distribution key based on actual volumes of sampled mail, and transportation services provided to sampled mail. *Id.* at 49 n. 26; 22 Tr. 11820.

[22] *Id.* at 49-50; 22 Tr. 11820-11821. Assume a truck is 20 percent full and three-fourths of the mail on the truck is off-loaded. Then three-fourths of the 80 percent empty capacity is "reasonably assigned" to the off-loaded mail. In this example, mail occupying 15 percent of the truck is assigned 75 percent of the total capacity of the truck for that segment. *Id.* at 50 n. 27; 22 Tr. 11821.

[23] ANM-T-1 (Haldi) at 50; 22 Tr. 11821; 7 Tr. 3504 (USPS witness Bradley). TRACS evidence ratios of expanded cubic feet to actual feet that are well in

apportioned to the actual volume of mail that happens to be off-loaded from the truck. ANM-T-1 (Haldi).

On those segments that have low capacity utilization on a regular recurring basis, the cubic volume assigned to the distribution key will be inversely proportional to the actual volume of mail off-loaded from the truck. In other words, the ultimate cost that is attributed (via the distribution key) for each unit of actual mail volume will be high. Should a particular class of mail travel regularly over a segment where the truck is largely empty, that class will be the victim of this weird procedure for always attributing the entire cubic volume of the truck. Moreover, rates will be designed to reflect these unit costs, even though they may be inversely related to actual usage. *Id.* at 50-51; 22 Tr. 11821-11822.

In short, TRACS is an economist's nightmare come true. The emptier the vehicle, the greater the amount of cube (and, ultimately, the cost) charged to whatever subclasses of mail that happen to be on the truck. Because TRACS breaks the route into independent segments, TRACS thus operates like a game of "Old Maid" on segments where trucks are largely empty. Should volume diminish on a particular segment, until the only remaining mail on the truck is one sack or container, it gets "stuck" with the entire cube (and cost) of that particular segment (which is expanded up to the full year). It seems ironic that such an allocation procedure would be implemented by an organization which favors cost-based rates coupled with demand pricing.[24]

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excess of 100 to 1. 7 Tr. 3323, 3325 (Bradley).

[24] ANM-T-1 (Haldi) at 51-52; 22 Tr. 11821-11822. An analogy may help demonstrate the way TRACS assigns cubic-foot-miles that, ultimately, are reflected in "cost-based" rates. Suppose a ski resort spent $10 million on a lift

Under TRACS, the assignment of empty space distorts the reality of what is actually being transported, and how much transportation services are actually being provided to, or consumed by, each subclass of mail. And on those occasions when trucks are largely empty, the distortion of reality can border on the grotesque. The assignment of empty space is fundamentally wrong, because no causal nexus exists between (1) the subclasses of mail on the truck and transportation services provided to that mail, and (2) empty space on the truck that is sampled.[25]

The foregoing errors systematically over attribute the costs of cubic volume to the nonprofit subclass. First, truck capacity utilization varies systematically with the direction of haul. For example, trucks bound *from* a BMC average significantly higher capacity utilization (and correspondingly less empty space) than trucks bound *to* the BMC. This variation in utilization results from the large volume of mail that is drop shipped to destination BMCs: a substantial volume of

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that is being depreciated over 10 years; *i.e.*, $1 million per year. The average ski season at this resort lasts for 100 days, and on this basis the operator determines that depreciation of the lift costs $10,000 per day. A random sample is taken to ascertain usage of the lift. The first sample, on Tuesday, counts 100 skiers; the second sample, on Saturday, counts 1,000 skiers. Applying TRACS reasoning, people skiing on Tuesday are assigned a depreciation cost of $100 per skier, and for Saturday it works out to $10 per skier. Cost-based rates for each day of the week are set accordingly. If this result seems bizarre, we rationalize it by "reasonably assigning" all the empty chairs on Tuesday to those skiers who were counted and found to be utilizing the lift that day. *Id.* at 52 n. 29; 22 Tr. 11823.

[25] *Id.* at 52-53; 22 Tr. 11823-11824. The preceding criticism of the expansion process should not in any way be interpreted to mean that some alternative way of assigning empty space on specific legs of a specific trip to individual classes of mail would be better. *Id.*

mail is transported from BMCs to destination SCFs, while originating volume traveling from SCFs to BMCs is comparatively light. ANM-T-1 (Haldi) at 53; 22 Tr. 11824.

Second, nonprofit mailers systematically drop ship less than commercial mailers, and thus account for more of the volume on trucks bound *to* BMCs. As between the two Standard Mail (A) Regular subclasses, only 25 percent of Nonprofit Standard Mail (A) Regular was drop shipped in FY96, versus 41 percent for Standard Mail (A) Regular.[26]

In sum, TRACS is fatally flawed because it fails to measure the *actual volume of mail using Postal Service transportation,* and to develop distribution keys that incorporate only actual mail volumes. TRACS also fails to treat the cost of serving an entire route as an individual unit. ANM-T-1 (Haldi) at 54; 22 Tr. 11825. Regrettably, the circumstances of this case have not permitted development of an alternative distribution key based on the volume of mail actually transported, and the transportation services that were used by each subclass of mail. *Id.*

Given the data that are available from the TRACS sample data, the Commission could develop a distribution key that does not expand the sample beyond what the data collector initially records. That is, the expansion step or steps that unjustifiably assign absolutely empty floor space on the truck should be eliminated. This would be a step in the right direction, although it would not cure

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[26] ANM-T-1 (Haldi) at 19 (Table 6) and 54; 22 Tr. 11790, 11825. Standard Mail (A) presorted to the 3/5-Digit category is over eight times more likely to be drop shipped than Basic Mail. If TRACS were applied at the rate category level, it would contain substantial bias against Basic presort mail. *Id.* at 54 n. 30; 22 Tr. 11825.

the problems identified here, or rehabilitate the TRACS data as a lawful basis for recommending the Postal Service's proposed rate increases for nonprofit mail.

CONCLUSION

For the foregoing reasons, the proposed rate increases for nonprofit Standard (A) mail should be denied.

Respectfully submitted,

Joel T. Thomas
1800 K Street, N.W., Suite 810
Washington, D.C. 20006
(703) 476- 4646

David M. Levy
SIDLEY & AUSTIN
1722 Eye Street, N.W.
Washington, DC 20006
(202) 736-8214

Counsel for Alliance of Nonprofit Mailers

April 1, 1998

Attachment A

ERRORS, OMISSIONS AND ANOMALIES IN SURVEY FORMS AND DISQUALIFICATION LOGS

Site 1:

Exhibit USPS-RT-22-2 Shows volume disqualified that paid "reg Std. (A)" is 4,077. It is not evidence how Dr. Schenkgot this number. The attachment referred to on page 9 where volume is to be reported reflects about 32,000. The last paragraph notes a mailing of 29,555 pieces. In addition the logs appear to show more NP disqualifications than the attachment reflects. Dr. Schenk does not include the mailing on line 6 on page 0000007 even though the reasons given for rejection are 5 (Mailing Statement Irregularities) and 6 (Indicia/Meter Irregularity) reflects a disqualified nonprofit mailing. She includes the mailing on line 10 of page 0000012 but not the mailing on line 6 of that page even though the Reason Code for Disqual. Are the same, 12 (not qualified for rates claimed). Similarly someone marked line 1 of page 00000013, but it was not included. Line 5 on page 0000015 was not included even though the Reason Code for Disqual. Was 10 (Classification Identification). A mailing on line 4 of page 0000017 with a Reason for Disqual. Code of 10 was included. Ditto with a mailing line 4 of page 0000018. But, once again a mailing on line 6 of page 0000021 was not included. Suddenly in AP 11 for FY96 all disqualified mailings were 2nd class. The "2" is written backward. In any event a mailing on line 7 of page 0000023 which was disqualified for 10 (Classification Identification) was not counted but a mailing on line1 of page 0000024 was counted, even though both mailings a identified as to class with a backyard 2. The Reason for Disqual. Code for the mailing on page 0000024 was "12 - not eligible for rates for (nonprofit). Still in other cases mailing with Reason for Disqual. Code 10 were assumed to be nonprofit mailings. Unlike AP 11 when all disqualified mailing were for a class designated by a backward 2, all mailings disqualified in AP 13 were STD.

Site 2:

Exhibitusps-RT-22-2 has zero volume for "disqualified nonprofit , paid reg.Std. (A)." On page 0000020 of the Survey, Site 2 apparently said "travel adv. Biggest problem w/compliance" and states that the Site "worked w/ mailer; one-time exception." The response noted on page 0000020 also notes "a lot

more in 96 => 20/25 per A/P mellow out to 2/3 AP by AP4 of FY97. In short the survey notes reflect a serious problem in FY96, but the volume assigned to this site is "0".

Site 3:

Not included

Site 4:

The clerk providing the information supposedly on FY96 has been working only since 9/97, see Survey page 0000034. This makes the answer to question about changes since FY95 meaningless and also gives respondent to little experience to state what, if any period, might be comparable. Even though no estimate for volume included on the Survey Response and not volume is indicated on the logs, Dr. Schenk concluded that 25,010 pieces out of some 41 million of nonprofit mail were disqualified and paid reg. Std. (A). How? In additions the logs are vague at best.

The form used during the first part of the year did not have a disqualification code. The clerk was expected to write in an explanation. In a large number of case the clerk entered "$" or "$ $" as the explanation. That could apply to mail entered at nonprofit rates that did not qualify for that rate, but that is not what Dr. Shenck assumed. Just which log entries were accepted by Dr. Schenk as
disqualified nonprofit mail is not clear. The following entries were not marked with an "x" in a circle which seems to have been the way log entries for Site 1 that were counted were marked:

Fifth entry on page 0000036
First entry on page 0000039
Seventh entry on page 0000039
First entry on page 0000042
Sixth entry on page 0000042
Eighth entry on page 0000048
Eleventh line on page 0000058 ("Checking for Non-profit status could refer to the mailer or to the mail.)

Ninth entry on page 0000061 (Not eligible for 3C rates could refer to nonprofit since the mail was in fact released.)
Fifth entry on page 0000077. (Reason gvien "No Non Profit in Indicia." Wouldn't this only be a problem if the mail appeared to come from a nonprofit-i.e., was a nonprofit mailing at regular rates. It was "Sent at Profit." But wouldn' tally clerk think it nonprofit? The entry clerk did!)
Tenth entry on page 0000084 (Same as fifth on 0000077)

In AP 4 Log form changes. "Reason Code to Disqual." is now included. But Code 11 is "Other (describe on reverse). Problem: the reverse side was not provided. In many, indeed most cases some explanation was written on the log, however. But it is written where the additional postage should have been written leaving entries without volume or postage paid.

Twelfth entry on page 0000107 only information is "Incorrect Rates" why isn't this a disqualified nonprofit mailing?
Thirteenth entry on page 0000117
Fifth entry on page 0000121 (See comment on fifth entry on page 0000077)
Eleventh and Twelfth entries on page 0000124 (Couldn't "wrong rates" apply to disqualified nonprofit mail?
First, tenth and eleventh entries on page 0000127
Twelfth and fourteenth entries on page 0000128
Third entry on page 0000129 ("Indicia missing, Nonprofit Organization." What if it was entering mail at regular rates?)
Ninth entry on page 0000131
Second entry on page 0000132 (Not eligible for N.P. Rates anyway")

N.B. the fourteenth entry on page 0000138 uses Reason Code for Disqual. 11 in a case were there is "advertisement in N.P. This means 11 is used to indicate a disqualification for nonprofit rates.

Sixth entry on page 0000138 uses 11 w/o explanation. A disqal. N.P. Mailing?
Seventh entry on page 00139 ("11/3 Not Periodical Format for ads. Wouldn't this only make sense if the was a nonprofit mailing?)

Beginning on page 0000139 clerks start using "12" as a disqualification code though there is no such code and 11 is "Other".

Fourth and fifth entries on page 0000139 (disqual. For "12" w/o explanation)
Ninth entry on page 0000140 same as above

Tenth entry on page 0000141 ("Bulk Rate" in indicia N/P in paper work)

Page 0000155 begin using form were "12" means "Hopeless"

Fifth entry on page 0000161

USPS seems to concede that sixth entry where "Not N/P" is written beside Disqual. Code 8 is a disqualified nonprofit mailing, but ignores the fourteenth entry on same page were only information re reason for disqualification is "8". Why?

Fifth entry on page 0000172 (Disqualification Code 8 followed by "Used n/p form should be "BULK RATE" Isn't this a nonprofit mailing a regular rates? Third entry on page 0000174. "Didn't have non profit indicia". Isn't this the same problem?

Thirteenth entry on page 0000175 (Disqual. Code 8 with "Advertising" added is apparently accepted but "8" alone is not, see Seventh entry on page 0000176.

Fifth entry on page 0000178. Even the postal reviewer is confused as the entry is proceeded by ?? in a circle. The explanation is "'Bulk Rate' and 'N/P' in indicia." The Disposition Code indicates the Problem was correct and the mail reentered. How? Couldn't this be a nonprofit attempting to enter mail at regular rates?

Fourth entry on page 0000202 ("Illegal 'Ad Info'" must be disqualification of nonprofit mail. Ad info in regular 3C is okay.)

Third entry on page 0000213 ("indicia say Bulk Rates paper work n.p." This looks like a nonprofit mailing a regular rates. Disposition Code reflects a rate adjustment.)

Thirteenth entry on page 0000236. Notes "AD INFO" this only relevant to a third class mailing if it a nonprofit mailing

Fifteenth entry on page 0000236. See fifth entry on page 0000178 above.

Third entry on page 0000262 ("indicia say Bulk Rates and NP." This looks like a nonprofit mailing at regular rates.)

Thirteenth entry page 0000265. "Indicia sez "Bulk Rate." If a regular 3C mailing not a problem, it looks like a nonprofit mailing at regular rates.

(It is odd that every month or so someone with a good identifiable hand writing does one page of entries, exactly one page, no more, no less, then the other person or persons return.)

Site 5:

Virtually no information in Survey Form. Notes claim only that "This is not really a problem." But on page 0000060 notes reflect that there "were some problems in 96" but couldn't tell w/o looking a logs. Logs were not produced for Site 5 which has five detached mail units. Dr. Schenk resolved uncertainty by claiming no nonprofit mail was disqualified and sent a reg Std (A). This conclusion is clearly unwarranted. The person proving information at Site 5 apparently thinks a nonprofit cannot mail at regular std (A) rates while an application for a nonprofit permit is pending. This is clearly wrong and discredits rest of information.

Site 6:

Survey forms reflects at page 0000078 practice of allowing nonprofit mailers to enter mail at regular rates with nonprofit endorsement. The only volume info is a guess that most of mailing were in the 5,000 - 10,000 range proves nothing what if one was a million? At top of page 0000075 person responding to survey admits she doesn't know how many nonprofit mailing were rejected in AP% 98 but data of 10 rejected for poor preparation and 2 or 3 for content were entered. This is rediculous. Even worse she admits on page 0000072 (first page of Site 6 Survey Form) she isn't sure if AP5 98 is representative. Dr. Schenk is pounding square pegs through round holes. When respondent was asked for FY 96 volumes she said she didn't know, page 0000084 and logs do not provide this information. Site 6 should be dropped.

Site 7:

Note that respondent sees nothing inconsistent with stating that most recent AP is representative (page 0000088) and stating that there were " a large number [of nonprofit mailings] being rejected in the beginning of FY 96. This demonstrates that current or even FY97 data is not useable. What is Dr. Schenk's mid-point of the range >100,000? Seven doesn't have any logs.

Site 8:

Answer to question 3 is curious. This seems to suggest that 99% of this site's business is NP. But no logs were produced and eligibility isn't a problem? There is too little information and logs are a joke, 12 pages, one per AP. (AP11 is missing) Every log page is blank except that the word negative has been written in except for one. This page, page 0000395, is the only one where the AP was entered in the FY field and the year, 96, was entered in the A/P field.

Site 10:

Respondent for site has only "just moved into this job." Does not provide any basis for guestimates. Not all logs accounted for. Most common log entry is "Documentation does not match statement." Fails to indicate how the mismatch occurs. Since the solution is usually to revise the statement this could be non-qualifying nonprofit mail being changed to regular rates mail. Thirteenth entry on page 0000411 reflects bulk rate mailer on non profit statement. This could be a nonprofit mailer entering regular rate mail. Starting in AP3 for FY96 log for changes. Most common entries are 11 (Supporting Documentation not submitted/incorrect) and 5 (Mailing Statement Irregularities) either or both could be disqualified nonprofit mail. No basis for assuming it is not. The statement that it would take a lot of work to get nonprofit status information is disproved by logs. This information was not recorded. Respondent is aware the Pub 417 caused problems. This impeaches statement that current AP is representative. Page 0000146 reflects respondent doesn't know information on content based rejects but that "We are going to proceed from here as if there were 3 in APs." There is simply no basis for this assumption , especially when respondent just moved into the job. Cannot tell what volume range the guess of 2 entered in response to question 3 . iv. This

is also consistent with page 0000146 decision to assume 3 per AP. While 65% of mailers re-endorse mail only 20% of mail is re-endorsed. This undermines significance of assertion under question 3. iv. About "usually smaller mailers." That may be, but most of the mail must be coming from larger mailers if only 20 is re-endorsed.

Site 11: No logs

Survey Form out of order begins page 0000100 comes before Survey Form for Site
8. Answer to question A.1 fails to establish anything and A.2. says respondent doesn't know current volumes. Numbers in B1 and B.2. are not supported by logs. If respondent doesn't know current period volumes and doesn't have logs where did FY96 numbers come from. They are purse swags

Site 12:

No logs. Acknowledges at page 0000158 Pub 417 cracked down and that there were problems at the beginning of 96. Answer to B.6.c.v. on page 0000163 acknowledges that some non profit mail accepted under regular rates is not endorsed Nonprofit. The answer almost all small does not justify assuming all were under 500 pieces. If 10 were small but one was 1 million the numbers would change radically.

Site 13: Not included

Site 14: Not included

Site 15: Not included

Site 16:

Respondent estimates that of 5-10 mailings ruled ineligible in most recent AP 0-4 were for content. This variance is to great to permit use of data. The volume estimates on page 0000220 account for only 8 of 10 disqualified mailings. The missing 20% could have been large to huge. Logs are useless. Reason for Disqualification Code for 539 out of 628 entries is given as 12. But there is no 12. There are only eleven codes. If 12 means other, then we

simply don't know.

Site 17; No logs.

Dr. Schenk enter "0" for Volume of disqualified, paid at reg. Std (A) but answer on page 00000233 is "2-3 rare occurrence" and explicitly stated volume in FY96 were unknown. There is no basis for Dr. Schenk's guess. The respondent is shown as having stated that Nonprofit mail accepted for regular rates were endorsed "Blkrt" but answered "NO" to question did customer ever correct endorsement before reentering the mail.

Site 18: No logs

Acknowledges increase scrutiny of mail after Pub. 417 and content related rejections are increasing 96-98. Page 0000242. Survey form reveals practice of contacting customer to discuss problems. This should produce at least some regular rate std (A) mail by nonprofits. This is especially true since "seldom is customer required to change endorsement." If volume is unknown then guess as to ranges is totally without foundation especially with no logs.

Site 19: No logs

Only statement in Survey form is a statement, on page 0000255, that "No Problems In the 6 years he has been accepting mail." This was a response to question A.5 which asked "Was mailer compliance behavior different in FY96 compared with FY95 and with FY 97...." The answer is clearly not responsive to question and clearly insufficient of support conclusion that "0" nonprofit mail was disqualified and sent at reg. Std. (A) rates, especially without any logs. All of section B is marked N/A.

Site 20: No logs

Only statement in Survey form is a statement, on page 0000271, that "In the 10 years he has been on the job it has never happened. This was a response to question A.5 which asked "Was mailer compliance behavior different in FY96 compared with FY95 and with FY 97...." The answer is clearly not responsive to question and clearly insufficient of support conclusion that "0" nonprofit

mail was disqualified and sent at reg. Std. (A) rates, especially without any logs. All of section B is marked N/A.

Site 21: No logs

Statement that current period is representative contradicted by answer to Q. A4 on page 0000284 that may have been problems right at the beginning after publication of Pub 417. "...probably more content rejections at the beginning of 1996, then leveled off." No Volume range estimates on page 0000290 reflect FY97 which is not representative according to respondent. No usable data. This Site should be dropped.

Site 22:

Survey reflect no volume data and admits its not in logs. An entry on page 0000303 makes reference to Advertising in FY 96. Since advertising is okay at regular rates, this must refer to nonprofit mail, but Dr. Schenk says there was no disqualified nonprofit mail. Third entry on page 0000564 of logs could be disqualified nonprofit mailing. First and second entries on page 0000566 of logs not explained. Fourth entry on page 0000567 unexplained as is fourth entry on page 0000569 and first entry on page 0000570. First entry on page 0000572 not explained. None of entries on page 0000573 are explained. First and third entries on page 0000574 not explained.

Site 23: No logs

Notes on Survey form, page 0000312, indicate no log because person responsible helps mailers prepare their mail. This suggests some could have come in a reg. rate Std (A). There is no volume data, but that doesn't support conclusion there was none in absence of logs. Answer to B.5. on page 0000318 reflects working with customers. States that "...2 customers have NP status but mail reg. Rate because too much advertising..."

Site 24: Not included

Site 25: No logs

Survey form reflects 15 rejections in some period, page 0000346. These went

out with NP endorsements, page 0000348. Statement that volu,me of mail was usually less than 1000 pieces is insufficient especially with no logs to find that 3000 pieces were disqualifed and paid reg Std. (A) rates as Schenk did.

Site 26: Not included

Site 27:

Dr. Schenk's conclusion that 3000 pieces were disqualified, paid reg. Std, (A) rates is based, apparently on statement on page 0000375 that of "319,566 nonprofit pieces rejected for any reason less than 1% rejected because of volume". (emphasis added) Rejection for volume is a nonsense response cannot support conclusion that this represents all of disqualified nonprofit mail that paid regular rate. Many log forms illegible. Insufficient postage could be an explanation for a mailing that did not qualify for nonprofit rates, see Thirteenth entry on page 0000580, second entry on page 0000581, fifteenth entry on page 0000583, fifteenth entry on page 0000584, seventeenth, nineteenth and twentieth entries on page 0000585, entires six, seven and eight on page 0000586. Note "Insufficient Postage" must be different from "insufficient funds," the most common explanation for a disqualification. "Bulk Fee Due" as explanation for eight and nine on page 0000582 could be disqualified nonprofit mail. If that isn't what it is, what does it mean? After log form changes in AP2 to a form using disqualification codes, there are unexplained entries with Disqualification Codes for 5, 6 and 10. Any of these could represent the disqualification of nonprofit mail. See first and sixth entries on page 0000589, first entry on page 0000591. Several pages of logs for AP 2 or included twice see pages 000587, 0000588, 0000590 and compare with pages 0000596, 0000597, 0000595. See seventh entry on page 0000598 for an unexplained disqualification code 10 with is a classification problem clearly makes as a nonprofit problem. This demonstrates that 10 is used for disqualified nonprofit mail. Assumption that unexplained 10s are not nonprofit is unwarranted. See unexplained disqualification Code 10s in the eighth and ninth entries on page 0000608. Disqualification codes 5 and 6 could also be nonprofit mail. So unexplained entries such as the third on page 0000599 and 4 or page 0000600 could be nonprofit disqualifications. See also the fifth disqualification on page 0000601, the third and tenth entries on page 0000604, fourth entry on page 0000607, second entry on page 0000608, and sixth entry on page 0000609. Note also the completely unexplained

disqualification at the bottom of page 0000609. The second, third and fifth (and unexplained 10) entries on page 0000670 could be nonprofit disqualifications. Ditto the fourth and tenth entries on page 0000672. The fifth entry on page 0000673 is an unexplained 5 as is the last , tenth, entry on page 0000674. The sixth entry on page 0000676 appears to be an unexplained 10.

Page 0000678 entry 2 unexplained 6, entry 10 unexplained 5
Page 0000620 entry 9 is unexplained 8 (Improper Endorsement)

The next sixty pages of logs have 38 unexplained disqualification Code 5s. This is important because the second entry on page 0000675 explains that the uses Disqualification Code 5 to reflect a non-qualifying nonprofit mailing. This establishes that Disqualification Code 5 is used to reflect the disqualification of a nonprofit mailing. If this is so, then all or some portion of the thirty-eight entries on the next sixty pages that are explained solely by Disqualification Code 5 could reflect disqualification of nonprofit mail. The point this makes is that the data are insufficient to support Dr. Schenk's conclusion that only 3,000 pieces of nonprofit mail were disqualified at this site and paid regular, Std. (A) rates.

Site 28:

Only six or maybe seven AP periods out of thirteen covered by logs. Substanital number of entries in AP 6 and 7, 59 out of 319 have no explanation at all or 18.5% are not explained at all. Entries two, eleven and 12 on page 0000704, reflect nonprofit issue. Ditto sixteenth entry on page 0000705. The wrong rate entry, fifteen on page 0000707 could be a nonprofit disqualification as could "wrong postage" for entry nineteen on page 0000710. The entry "cooperative? No!" in the tenth entry on page 0000711 and Coop Mail, third entry on page 0000713 are nonprofit problems. "No-eligibility" the fifth entry on page 0000713 is clearly a nonprofit eligibility problem. All ten entries on pages 0000715, 716, and most of 717 have not explanation at all. Once the forms start using explanations they do not consistently use Disqualification Codes per the form. Nevertheless there are three entries on page 0000718 which use the Disqualification Code "10" without explanation. This is a classification problem and could be nonprofit. Only one of ten

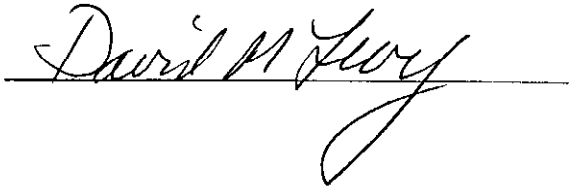
entries on page 0000719 is explained. Only half of ten entries are explained on page 0000720 but three of the explained entries are10s which means classification problems. There is one 10 on page 0000721, two more, entries one and four on page 0000722. Eventually the entries start to use 12 written in as other but never explained show up. On pages 0000723, 0000724 and 000725 fourteen of thirty entries are unexplained. On page 0000726 eight of fourteen entries are unexplained 10s. Two of ten, the third and fourth entries on page 0000727 are 5/10 or classification/mailing statement irregularities. Could be nonprofit disqualification. Four of the ten entries, the first, second, third and eighth entries on page 0000728 are 10s. Two of ten entries on page 0000731 or unexplained 10s. There are five more unexplained 10s. Most of rest of forms use form numbers, especially 3749 and 8040 rather than disqualification codes to explain reason for disqualification. In addition there are many unexplained Disqualification Code 5s. In short, it is impossible to see see how any conclusion can be drawn from such incomplete data.

Site 29: No logs or Survey Forms

Site 30: No logs or Survey Forms

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document on all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.



April 1, 1998