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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

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

SPECIAL SERVICES REFORM, 1996

Docket No. MC96-3

REBUTTAL TESTIMONY
OF
SUSAN W. NEEDHAM
ON BEHALF OF
UNITED STATES POSTAL SERVICE

DEC 6 1996
OFFICE OF THE SECRETARY
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AUTOBIOGRAPHICAL SKETCH

- 1 My name is Susan W. Needham. My autobiographical sketch is
- 2 presented in my direct testimonies, USPS-T-7 and USPS-T-8.

1 I. PURPOSE

2

3 The purpose of my testimony is two-fold. First, I rebut claims made by
4 OCA witnesses Collins and Sherman that the record concerning certified mail is
5 unclear. Second, my testimony provides examples of services that favor
6 resident or locally-based customers.

7

8

9 II. THE CERTIFIED MAIL COST COVERAGE METHODOLOGY HAS BEEN
10 EXPLAINED.

11

12

13 Witnesses Collins and Sherman claim that the record concerning certified
14 mail costs and revenues is "murky" and "not perfectly clear."¹ This is one reason
15 OCA witness Collins recommends that the certified mail fee not be changed, but
16 rather that this matter be "revisited during the next omnibus rate case."² I am
17 puzzled by these remarks, because in my view, the record has been clarified
18 and provides ample support for the proposed fee increase for certified mail.

19

20 The costs and revenues and resulting cost coverages³ for certified mail in
21 this docket have been very closely scrutinized by the Postal Service, the
22 Commission, and the OCA. For purposes of calculating the certified mail cost
23 coverage, I explained that the Postal Service had determined to remove ancillary

¹ Tr. 5/1699; Tr. 7/2289.

² Tr. 5/1700.

³ The fraction for calculating the cost coverage is: (revenues)/(costs).

1 service revenues from the numerator of the fraction used to calculate the
2 certified mail cost coverage.⁴

3
4 Historically, the CRA has included ancillary service revenues, which
5 include revenues for return receipts and restricted delivery associated with
6 certified mail, in certified mail revenues.⁵ In order to evaluate prices for certified
7 mail with precision, it is incumbent upon the pricing witness to first subtract all
8 ancillary service revenues from the revenue figure shown in the CRA. If
9 ancillary service revenues are not removed, the certified mail cost coverage is
10 inflated. Recommended fees that are based on such inflated cost coverages will
11 likely be too low.

12
13 As explained in my response to OCA/USPS-T8-8,⁶ in Docket No. R94-1,
14 the Postal Service presented a cost coverage for certified mail of 172.1 percent,
15 based on revenues of \$526,248,000 and costs of \$305,826,000.⁷ The
16 numerator of the figure used to calculate the cost coverage presented by the
17 Postal Service, however, erroneously included ancillary service revenues of
18 \$233,028,000, for restricted delivery and return receipts associated with certified

⁴ USPS-T-8 at 71.

⁵ See Tr. 4/1072-73. The CRA does *not* include ancillary service costs in certified mail costs.

⁶ Tr. 4/1073.

⁷ Docket No. R94-1, Exhibit USPS-11F, page 3.

1 mail.⁸ The Commission recommended a fee of \$1.10 based on costs of
2 \$309,213,000 and revenues of \$526,248,000.⁹ The Commission recommended
3 fee in Docket No. R94-1 followed the Postal Service cost coverage methodology
4 and was based upon the mistaken assumption that certified mail revenues were
5 free of any ancillary service revenues. If, however, the Commission
6 recommended cost coverage had been calculated without ancillary service
7 revenues in the numerator, it would have been 94.8 percent.¹⁰

8
9 The Postal Service pricing witness in Docket No. R90-1 presented a
10 certified mail cost coverage of 127 percent, based on costs of \$147,859,000 and
11 revenues of \$188,404,000.¹¹ Upon review of the pricing witness' work in that
12 docket, it appears that certified mail revenues were properly adjusted in the
13 Postal Service's pricing proposal, so that they excluded ancillary service
14 revenues.¹² Unfortunately, however, the pricing witness in that docket

⁸ Docket No. R94-1, Foster WP VIII at 5 (\$224,681,000 + \$8,347,000).

⁹ PRC Op. & Rec. Dec., Appendix G, Schedule 1.

¹⁰ This figure is calculated using revenues for the certified mail basic fee of \$293,220,000, reported at PRC Op. & Rec. Dec., Docket No. R94-1, App. G, Schedule 2 at 20, divided by certified mail costs of \$309,213,000, reported at PRC Op. & Rec. Dec., Docket No. R94-1, App. G, Schedule 1.

¹¹ Docket No. R90-1, USPS-T-22 at p. 40.

¹² Compare Docket No. R90-1, USPS-T-22 WP-6 page 1 (revenue of \$188.404 million for certified mail, free of ancillary service revenues) and USPS-T-22 page 40 (revenue of \$188.404 million for certified mail, free of ancillary service revenues) with Exhibit USPS-17E at p.23 (CRA certified mail revenue of \$379 million, including ancillary service revenues).

1 erroneously subtracted an amount representing ancillary service costs from the
2 CRA certified mail costs (which did not include ancillary service costs), resulting
3 in an inflated proposed cost coverage.¹³ The proposed cost coverage was
4 inflated because, in this instance, the *denominator* of the cost coverage fraction
5 was erroneously *understated*. The Commission, on the other hand,
6 recommended a certified mail fee of \$1.00 in Docket No. R90-1, based on
7 revenues of \$391,770,000 and costs of \$315,392,000 to arrive at a cost
8 coverage of 124 percent.¹⁴ As in Docket No. R94-1, the Commission's
9 recommended fee of \$1.00 in Docket No. R90-1 was based upon a cost
10 coverage calculation with ancillary service revenues erroneously included in the
11 numerator. (The Commission correctly did not adjust the denominator by
12 removing ancillary service costs.) If the Commission had removed certified mail
13 revenues from the numerator of the fraction used to calculate the certified mail
14 cost coverage, the cost coverage would have been 65 percent.¹⁵

15

16 As explained in my testimony, the historic practice has been to calculate
17 the cost coverage for certified mail with ancillary service revenues included in
18 the numerator.¹⁶ In this proceeding, we have attempted to remove these

¹³ Tr. 4/1200, lines 7-19.

¹⁴ Docket No. R90-1, PRC Op. & Rec. Dec., App. G, Schedule 1.

¹⁵ This figure is calculated by dividing certified mail revenue of \$205,068,000, Docket No. R90-1, PRC Op. & Rec. Dec., App. G, Schedule 2, at 19, by certified mail costs of \$315,392,000, Docket No. R90-1, PRC Op. & Rec. Dec., App. G, Schedule 1.

¹⁶ USPS-T-8 at 71.

1 revenues from the numerator of the fraction used to calculate the certified mail
2 cost coverage so that we can evaluate the certified mail fee accurately. Despite
3 our attempts to present the certified mail cost coverage without ancillary service
4 revenues in pricing testimony, the certified mail before- and after- rates cost
5 coverages of 107 percent and 146 percent, respectively, in my testimony, USPS-
6 T-8 at 71, and in my interrogatory responses, and witness Lyons' Exhibit USPS-
7 T-1C, were inflated due to the fact that return receipt for merchandise volumes
8 were included in the calculation of certified mail revenues.¹⁷ After we became
9 aware of this problem with the numerator of the fraction used to calculate the
10 cost coverage for certified mail in this docket, we undertook to correct the
11 record. Witness Lyons' response to Presiding Officer's Information Request No.
12 5 presents before- and after- rates cost coverages of 102.1 percent and 139.2
13 percent, respectively.¹⁸ These cost coverages are appropriate for the
14 Commission's evaluation of the certified mail fee proposal because the certified
15 mail revenues in these figures are free of ancillary service and return receipt for
16 merchandise revenues, and the certified mail costs have not been subject to any
17 unnecessary adjustments for ancillary service costs.

18

19 Thus, past Postal Service proposals and Commission recommended fees
20 for certified mail have been based on inflated cost coverages. I believe this

¹⁷ The volume that was originally used in the calculation of certified mail revenue included return receipt for merchandise volume. See Tr. 8/3019-20.

¹⁸ Tr. 8/3020-23; see also Tr. 8/3076.

1 serves as further justification for the Commission to recommend the proposed
2 \$1.50 fee for certified mail. Since certified mail users have been paying a fee
3 below (now slightly above) cost, it is fair and reasonable that they begin to pay a
4 fee that aligns better with the high value service they receive. Now is the time
5 for the Commission to remedy past errors, for certified mail users have been
6 paying exceptionally low fees for an extended period of time.

7
8
9 **III. MARKETPLACE EXAMPLES OF NON-RESIDENT TYPE FEES**
10 **OR RESIDENT TYPE DISCOUNTS AND DEMAND PRICING.**
11

12 OCA Witness Callow attacks the absence of a quantified cost basis for
13 the Postal Service's proposed non-resident fee for post office box service,
14 implying that such a price structure is inappropriate unless it is founded on a
15 measured cost differential.¹⁹ While I have not conducted a comprehensive
16 survey, I identified, in my testimony and on cross-examination, examples of fees
17 charged by other public and private entities which are similar to the proposed
18 non-resident fee but are not based on quantified costs. I elaborate on this
19 testimony below.

20
21 During oral cross-examination, I briefly alluded to county government non-
22 resident fees. I mentioned the holiday camps (during winter and spring breaks)

¹⁹ Tr. 5/1523-26.

1 and summer camps operated by the Arlington County Parks and Recreation
2 Department in Arlington, Virginia.²⁰ These camps, as well as two-day
3 parent/teacher conference camps set up during the school year, were
4 established for children whose parents work and need daycare for their children
5 when the public schools are closed. There are two sets of fees charged for each
6 camp: one for residents and a 50 percent higher fee for non-residents of
7 Arlington County. The operating expenses for these camps are paid for by the
8 fees charged, not by taxes. The services are the same for each child enrolled in
9 these camps (*i.e.*, supervision, materials for arts and crafts projects, two daily
10 snacks, transportation for field trips, etc.). There is thus no cost difference per
11 child, regardless of resident status. However, non-residents of Arlington who
12 work in or around Arlington are obviously willing to pay the non-resident fee. In
13 many instances, other Northern Virginia county governments do not offer
14 comparable camps when the schools are closed, and alternatives to these
15 camps can be more costly and difficult to locate. The county non-resident fee is
16 comparable to the proposed non-resident post office box fee. A demand exists
17 for a service by both local and non-local customers, and the non-local customers
18 are willing to pay more than local customers.

19

20 I also testified orally about resident golf discounts for residents of Fairfax
21 County, Virginia. The Fairfax County Park Authority operates public golf courses

²⁰ Tr. 3/909-10.

1 in Fairfax County. At some of the courses, residents of Fairfax County are able
2 to purchase golf play passes at a discount. The golf play fees, like the Arlington
3 County camp fees, are used to cover all operating expenses and are not
4 subsidized by tax revenues. This is another example of charging a higher fee
5 for non-residents when the operating costs per person are the same, regardless
6 of residency status. I believe that non-residents of Fairfax County are willing to
7 pay higher fees than the Fairfax County residents because of the value of
8 service for these non-resident customers.

9
10 There are also other examples. Afternoon or twilight moviegoers take
11 advantage of lower ticket prices. The higher, prime-time ticket prices evidently
12 are not based on costs, but rather are based on demand. Since more people
13 attend evening movie performances than afternoon and/or twilight shows, movie
14 theater operators offer discounted ticket prices for earlier shows to encourage
15 larger attendance. Finally, the former movie video chain, Erol's, would allow
16 customers who rented a movie at one location to return the movie to another
17 location, for an additional fee. This service reflects the same type of
18 convenience for customers that is reflected in the non-resident box service.

19
20 While these examples were suggested to me by my personal knowledge
21 of local practices, I believe that others would be revealed by a broader inquiry
22 into the matter. I do not believe such a study is necessary, however, because
23 these limited examples demonstrate that establishing a price differential based

1 on residency is neither irrational nor unprecedented. It can have a sound basis
2 in policy and operations, as demonstrated by the Postal Service's case here.
3 Furthermore, particularly where price levels are influenced by market
4 considerations, as in the Postal Service's proposals, the price structure and
5 levels need not be dictated by a measured cost differential.