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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Postal Rate and Fee Changes, 1997

Docket No. R97-1

DIRECT TESTIMONY OF
DONALD J. O'HARA
ON BEHALF OF
UNITED STATES POSTAL SERVICE

CONTENTS

AUTOBIOGRAPHICAL SKETCH

My name is Donald J. O'Hara. I have been employed by the Postal Service since 1981. For most of this period I was a Principal Economist in the Planning Department, where I produced information and analyses used in the strategic planning process. During this time, I also played a major role in the development and implementation of the Postal Service's Total Factor Productivity (TFP) measurement system. In the 1992 reorganization, I moved to the reclassification project. I have made two previous appearances in proceedings before the Postal Rate Commission. In Classification Reform I (Docket No. MC95-1), I provided testimony on rates and classifications for First-Class Mail, and in Classification Reform II (Docket No. MC96-2), I provided testimony on rates and classifications for Nonprofit Periodicals. Earlier this year, I became Manager of Classification and Product Development in the Marketing Systems Department.

I received a PhD in Economics from the University of California at Los Angeles in 1971, and from 1970 until 1980 I taught at the University of Rochester, first as an Assistant Professor of Economics (through 1976), and then as an Associate Professor. In 1980-81, I served on the staff of the President's Commission for a National Agenda for the Eighties.

PURPOSE OF TESTIMONY

This testimony presents the Postal Service's proposed rate levels. As has become standard practice, the proposed rate levels are described in terms of cost coverages, and the proposed rate and fee increases are presented in the form of percentage changes. For each subclass, the testimony describes how the Postal Service's proposed rate levels conform to the rate-making criteria of the Postal Reorganization Act.

My testimony concludes with seven Exhibits. Exhibits USPS-30A and USPS-30B show the test-year finances of the Postal Service on a subclass-by-subclass basis before and after the proposed rate changes. Exhibit USPS-30C shows the proposed cost coverages for the various Special Services. Exhibits USPS-30D and USPS-30E show the proposed rate changes and fee changes on a percentage increase or decrease basis. Exhibits USPS-30F and USPS-30G show the test-year after-rates cost and volume adjustments.

I. GENERAL DISCUSSION

A. Criteria of 39 U.S.C. s.3622(b)

The Postal Reorganization Act sets forth, in section 3622(b), the following nine criteria that are to be considered in determining postal rate and fee levels:

1. the establishment and maintenance of a fair and equitable schedule;

2. the value of the mail service actually provided each class or type of mail service to both the sender and the recipient including, but not limited to the collection, mode of transportation, and priority of delivery;

3. the requirement that each class of mail bear the direct and indirect postal costs attributed to that class plus that portion of all other costs of the Postal Service reasonably assignable to such class or type;

4. the effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters;

5. the available alternative means of sending and receiving letters and other mail matter at reasonable costs.

6. the degree of preparation of mail for delivery into the postal system and its effect upon reducing costs to the Postal Service.

7. simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees charged the various classes of mail for the postal services;

8. the educational, cultural, scientific and informational value to the recipient of mail matter; and

9. such other factors as the Commission may deem appropriate.

To facilitate reference to these criteria in subsequent discussion, the conventional abbreviated forms of the criteria are often utilized, as shown in the following table:

PRICING CRITERIA

CRITERION NUMBER	ABBREVIATED FORM
1	FAIRNESS AND EQUITY
2	VALUE OF SERVICE
3	COST
4	EFFECT OF RATE INCREASES
5	AVAILABLE ALTERNATIVES
6	DEGREE OF PREPARATION
7	SIMPLICITY
8	ECSI
9	OTHER FACTORS

B. Discussion of Criteria

1. Fairness and Equity

Fairness and equity are fundamental objectives of the Postal Service's proposals in this case, and they have been considered throughout its preparation. They form the foundation on which the more-specific factors addressed in the other criteria are considered and they provide a basis for arriving at a judgment as to the proper balance among the sometimes conflicting directions indicated by these other criteria.

Fairness and equity also play a key role in my discussion, in Sections D and E of this Chapter, of which cost measure should be used in setting rate and fee levels, and of how cost coverages should be adjusted in response to the new costing information provided in this case.

2. Value of Service

Subsection 3622(b)(2) refers to the value of the mail service actually provided to both the sender and the recipient, specifically mentioning collection, mode of transportation, and priority of delivery. These and other specifically identifiable aspects of the service provided to different classes of mail are often referred to as contributing to the intrinsic value of the service provided to a class of mail.

Another aspect of value of service is the degree to which usage of the service declines in response to price increases, often referred to as the economic value of service. This is conventionally measured by the own-price elasticity of demand, that is, the percentage decline in usage that results from a one percent increase in price. The lower (in absolute value) the own-price elasticity, the higher the value of service. The price elasticities mentioned in my discussion of individual subclasses are the long-run elasticities provided by Dr. Tolley (USPS-T-6) and Dr. Musgrave (USPS-T-8). For convenience they are collected in Table B-1.

Table B-1. Long-run Own-Price Demand Elasticities

First-Class Letters	-0.232	
Single-piece		-0.189
Work-shared		-0.289
First-Class Cards	-0.863	
Postal		-0.168
Private		-0.944
Priority	-0.771	
Express Mail	-1.534	
Regular Periodicals	-0.143	
Standard A Regular	-0.382	
Standard A ECR	-0.598	
Parcel Post	-0.965	
Bound Printed Matter	-0.335	
Special	-0.362	

Source: Priority and Express Mail, USPS-T-8; all others, USPS-T-6.

3. Cost

This criterion requires that the revenues from each class of mail at least equal the costs attributable to that class. In Section D of this Chapter, I summarize how the provision of additional cost information in this case makes possible an improved application of this "cost-floor" requirement for the revenues from each class of mail.

The improved cost information introduced in this case also affects the measured volume-variable costs of different mail classes to differing degrees. As discussed in Section E of this Chapter, the rate levels proposed by the Postal

Service recognize these changes in relative cost levels, in that somewhat higher percentage rate increases are proposed when the improved cost information indicates that a subclass's share of volume-variable cost is higher under the new cost methods than under the previous method. At the same time, however, the Postal Service has stopped far short of mechanically applying coverage or mark-up indices based on previous cost information. This is appropriate both in view of the effect of rate increases on mailers (criterion 4) and also in view of the fact that this case will provide the first opportunity for other parties and the Commission to review the methods underlying the new cost information and consider any longer-term implications.

4. Effect of Rate Increases

This criterion provides for consideration of the effect of rate increases on both mailers and private-sector competitors of the Postal Service.

For mailers, the percentage rate increase relative to the overall rate of inflation in the economy and relative to the rate increases for other classes of mail are useful indicators.

In developing its proposals in this case, the Postal Service has also considered the effect of its proposed rate increases on competitors, examining them to avoid unfair price competition.

5. Available Alternatives

This criterion considers the availability, at reasonable cost, of alternate means of sending and receiving letters and other mail matter. This includes the availability of similar services from other providers, such as private-sector competition in the expedited and package delivery markets and alternate delivery firms for periodicals and advertising matter. It may also include the availability of other media, such as newspapers, radio, and television, for the delivery of advertising messages, and the various electronic alternatives for First-Class Mail.

6. Degree of Preparation

This criterion addresses the degree to which the mailer has prepared the mail before presenting it to the Postal Service and the effect of this preparation in reducing postal costs. Over the past several rate cases the Postal Service has introduced a significant number of additional worksharing discounts, so that the degree of preparation by the mailer and its effects on costs is now much more directly reflected in the rates paid by mail with differing degrees of preparation. As a consequence, this criterion now plays an important role at the level of rate design within each subclass. Moreover, in Classification Reform (Dockets No. MC95-1, MC96-2, and Special Services Reform, Docket No. MC96-3), the Postal Service proposed and the Commission recommended rate designs that generally reflected greater "passthroughs" of the worksharing cost differences than had been the practice previously. This was also true of the Postal Service's proposals in Parcel Classification Reform (Docket No. MC97-2); that Request was subsequently withdrawn, but many of its basic proposals are re-introduced in the current case.

It is also worth noting that as the degree of preparation increases over time, all else equal, the coverage required to obtain the same contribution also increases. This is true for the system as a whole as well as for an individual subclass.

For example, if total system volume is 100 billion pieces, each with a cost of 10 cents for a total attributable cost of $10 billion, and institutional costs are $5 billion, a coverage of 150 percent will be required to breakeven. If half of these pieces convert to worksharing, with a cost of six cents per piece, attributable cost will drop by $2 billion (50 billion pieces x $0.04 per piece worksharing savings) to $8 billion, or a 20 percent decline. To obtain the $5 billion contribution needed to breakeven will then require a coverage of 163 percent (= (8+5) / 8). Worksharing takes attributable costs out of the system but leaves institutional costs unchanged. Thus, as the overall level of worksharing increases, the percentage of total cost that is attributable can be expected to shrink[1] and the required system-average cost coverage will increase, all else equal.

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[1]It has been suggested that, over time, improved cost analysis should permit an increasing percentage of total costs to be attributed. Working in the opposite direction, however, has been the trend toward increased worksharing, which decreases the percentage of costs that are in fact attributable. It may well be that this latter effect has outweighed the former.

Similarly, to maintain its contribution, the coverage of a subclass with a greater-than-average increase in worksharing will need to increase relative to the system-average coverage. For example, suppose that one subclass in the above example is initially making a contribution of $500 million above its attributable cost of $1 billion, or a 150 percent cost coverage (the initial system average). Further suppose that worksharing reduces its attributable costs by a greater-than-average 30 percent, to $700 million. To maintain its previous $500 million contribution, cost coverage for the subclass must rise to 171 percent (= (700 + 500) / 700), which is above the new system average of 163 percent. If instead the subclass coverage was, as before, set equal to the system average, its contribution would fall to $438 million and other subclasses would be unfairly burdened with additional contribution requirements.

7. Simplicity

This criterion points to the desirability both of simplicity in the rate schedule as a whole and of simple, identifiable relationships between different rates and fees. Over time, with the increased use of computers and software in the preparation of bulk-entered mail, the acceptable degree of complexity in the rate schedules for such mail has increased, and it has been possible to give more detailed recognition to the degree of preparation by the mailer (criterion 6). For these mailers, simplicity may be furthered by moving toward parallel rate structures and preparation requirements across subclasses. For the individual mailer, however, simple rate schedules and understandable relationships between rates remain as important as ever.

8. ECSI

This criterion directs that the educational, cultural, scientific, and informational value to the recipient be considered in setting rates for each type of mail. In the past, the Commission has applied this factor in setting rate levels for First-Class Mail letters, Regular Periodicals, Standard B Special and, to some degree, Standard B Bound Printed Matter. The Postal Service's rate-level proposals conform to this practice.

9. Other Factors

Finally, in addition to the eight specific criteria discussed above, the Act provides for the consideration of any other factors deemed appropriate by the Commission in setting rate levels.

C. Preferred Rates

Rate levels for the preferred rate subclasses are now governed by the 1993 Revenue Forgone Reform Act (RFRA). The RFRA provides that the mark-up for each preferred rate subclass is to be determined from the mark-up for the most closely corresponding commercial subclass. Over a six-year phasing process, the final year of which will be FY 1999, each preferred rate mark-up is to rise from one-twelfth the corresponding commercial mark-up to one-half the commercial mark-up.

The rates that the Postal Service proposes for Commission recommendation are the "full" or Step 6 rates, with mark-ups equal to one-half the commercial mark-ups. However, because the test-year corresponds to Step 5 of the phasing process, the test-year financial analysis utilizes the Step 5 rates that correspond to the Postal Service's proposed Step 6 rates.

D. Attributable Cost, Incremental Cost, and Volume-Variable Cost

In the past, the Commission has assessed rate levels by comparing revenue to attributable cost, defined as the sum of volume-variable cost and specific-fixed cost. For each subclass, the resulting "cost coverage" ratio has been evaluated against the nine criteria of Section 3622(b). These criteria embody two somewhat distinct considerations. First, criterion three imposes a definite requirement that revenues equal or exceed attributable costs, thus preventing any cross-subsidy between subclasses. Second, the nine criteria jointly provide guidance in determining how the burden of meeting the total revenue requirement should be distributed among the subclasses. In the past, the ratio of revenue to attributable cost has been used for both of these purposes.

As Dr. Panzar testifies, these two purposes are actually better served if two distinct cost measures are used. For purposes of avoiding cross-subsidy, the appropriate test is whether revenue is at least equal to incremental cost.[2] For assessing the burden of meeting the revenue requirement, the appropriate comparison is the ratio of revenue to volume-variable cost. See USPS-T-11, especially Sections I.A and I.B.

In evaluating rate levels for individual subclasses, I employ both these cost measures. I believe this is an improvement over previous practice, but it is clearly not a major departure. This is because, in the past, volume variable cost and attributable cost have as a practical matter been quite similar; specific-fixed costs for most subclasses have been very small (often zero).[3] Thus, the qualitative judgements required in setting rate levels are likely to have been largely unaffected by the inclusion or exclusion of specific-fixed costs.

1. The Cost-Floor Requirement

For the cost-floor requirement of criterion three, incremental cost is similar to attributable cost in that it incorporates information on both specific-fixed cost and volume-variable cost.[4] However, for each subclass, instead of simply adding

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[2]Recognizing this, the Commission has specifically recommended that the Postal Service develop incremental cost estimates to allow it to perform the cross-subsidy test. See Opinion and Recommended Decision, Docket No. R94-1, Appendix F at paragraph 170.

[3]In FY 1996, Express Mail was the only subclass for which specific-fixed cost constituted more than a few percentage points of attributable cost; in that case, specific-fixed cost made up 19% of attributable costs.

[4]Due to the introduction of new costing methods, the Postal Service is for the first time able to provide incremental cost data for all subclasses. In R87-1, the Postal Service provided incremental cost for certain subclasses, but the

to its specific-fixed cost the amount of its volume-variable cost at current volume, incremental cost incorporates information as to how unit volume-variable cost would change as volume decreased from its current level to zero. Thus, the incremental cost of a subclass is the cost that would be eliminated if the subclass were discontinued (holding the volume of mail in other subclasses constant). See USPS-T-41 (witness Takis).

If revenue from a subclass equals or exceeds its incremental cost, then there is no cross-subsidy; any excess of revenue over incremental cost means that the Postal Service's provision of that subclass does not burden other subclasses but in fact benefits them.

2. Rate Levels

I noted above that with the previous costing methods, there was only one subclass, Express Mail, for which attributable cost differed by more than a few percentage points from volume-variable cost. With the new costing methods, differences between volume-variable cost and incremental cost arise for more and larger subclasses. For example, for First-Class Mail letters, the difference is about 9 percent. Thus, the choice of the cost concept to be used in evaluating rate levels with respect to the criteria of the Act becomes more important.

For the reasons explained in Dr. Panzar's testimony, I believe that the ratio

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Commission indicated its belief that, to be useful, such information needed to be available for all subclasses. Opinion and Recommended Decision, Docket No. R87-1, at 102-103.

of revenue to volume-variable cost is the more appropriate cost concept for this purpose. This is perhaps more clearly seen by considering an equivalent form of this ratio, namely the ratio of price to marginal cost.[5] This form of the ratio highlights the determinants and consequences of an individual mailer's decision about how much to mail. A mailer will deposit an additional piece of mail only if its value to him or her is at least equal to its price (or unit revenue); once deposited, this piece imposes unit volume-variable costs on the system and thus makes a contribution to other costs equal to the difference between price and unit volume-variable cost.

Therefore, any rate-setting process based on something other than volume-variable costs, whether it be attributable cost (calculated as the sum of volume-variable and specific-fixed costs in accordance with previous practice) or incremental cost, will be constructing its rates on a cost concept that does not accurately reflect the cost consequences of the decisions that mailers will make in response to those rates.[6] This will tend to result in both unfairness and economic inefficiency, as illustrated by the following example.

Consider a situation in which there are two postal products, both having the same evaluation on all the non-cost criteria, and hence deserving the same cost coverage, assumed for simplicity to be 150 percent. Assume that for one

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[5]This is simply the per-piece form of the ratio; price equals unit revenue and marginal cost equals unit volume-variable cost.

[6]Of course, if specific-fixed costs are zero, as has previously been the case for many subclasses, then attributable costs and volume-variable costs are identical.

product the attributable (or incremental) cost is 10 percent above its volume-variable cost and that for the other this cost is 10 percent below its volume-variable cost.[7]

If both products have a unit volume-variable cost of $0.20, and rates are set by applying the 150 percent coverage factor to volume-variable cost, each will be priced at $0.30. The users of both products will be equally treated. For an additional unit of either product, its users will pay $0.20 to offset the additional cost they impose on the system and will make a $0.10 contribution to other costs.

In contrast, if rates are set by applying the coverage factor to attributable (or incremental) cost, the first product will be priced 10 percent higher, or $0.33, and the second product 10 percent lower, or $0.27. An additional unit of either product will still impose $0.20 in additional cost on the system, but users of the first product will be making a $0.13 contribution to other costs for each additional unit while users of the second product contribute only $0.07, a contribution ratio of almost 2-to-1. This seems to me unfair, given that the two products received equal evaluations on the non-cost criteria.

Rate-setting based on attributable (or incremental) cost instead of volume-

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[7]The discussion that follows would be more complicated, but its conclusions unchanged, if both products had incremental cost above volume-variable cost but by different percentages. In fact, for most postal products, incremental cost does exceed volume-variable cost; for example, for First-Class Mail letters incremental cost is 9% above volume-variable cost. However, there are several Special Services for which the reverse is true; for example, the incremental cost for Certified Mail is 9% below its volume-variable cost.

variable cost also has unfortunate implications for economic efficiency; although both products have the same marginal cost, use of one product will be limited to applications where it is worth at least 33 cents while use of the other product will be expanded until the last unit is worth only 27 cents.[8] Thus, rate-setting on the basis of attributable (or incremental) cost has the effect, perhaps unintentional, of sacrificing applications of the first product that would have been worth 32 or 31 cents in order to allow applications of the second product that are worth only 29 or 28 cents.

Thus, except for the cost-floor requirement of criterion three, it is the ratio of revenue to volume-variable costs that I use in my discussion of rate-levels for individual subclasses in the remainder of my testimony.

E. Mark-ups and Coverages After A Reduction in Measured Costs

In this proceeding, the Postal Service has introduced significant improvements in its costing methods. These improvements are especially important for cost segment three, as described in the testimonies of witnesses Bradley (USPS-T-14) and Brehm (USPS-T-21), where the previous assumption of 100 percent volume variability has been replaced by an analysis of actual volume variability.

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[8]This inefficiency will be larger, the larger is the two products' price-elasticity (the same for both in this example, by the assumed equal evaluation for all non-cost criteria) and the larger the differences between incremental and volume-variable cost.

As a consequence of replacing 100 percent-variability assumptions with variability analysis, the percentage of Postal Service costs found to be volume variable declines. Stated differently, the total amount of "other" cost that for revenue generation purposes must be assigned to subclasses through the use of cost-coverage ratios is now larger. This means that the required system-average coverage rises significantly.

A natural question is whether there is some way to utilize previously developed mark-ups and cost coverages to arrive at a starting point, at least, for determining rate levels under the new costing method. Table E-1 uses a simple example to investigate two possible approaches: (1) a mark-up index, and (2) a coverage index. Panel I of the table describes the situation before the introduction of the new costing method. The revenue requirement is 100, Products A and B each have a cost of 33.3, but coverages of 167 percent and 133 percent respectively, and the system-average coverage is 150 percent or a mark-up of 50 percent.

In Panels II and III, a new costing method is introduced which reduces the measured cost for each product to 25 (leaving total system cost unchanged; costs formerly thought to be volume-variable are shifted to "other costs"). With an unchanged revenue requirement of 100, the required system-average coverage is now 200 percent, or a 100 percent mark-up.

Table E-1. Effect of Holding Mark-up Index or Coverage Index Constant, With Changes in Measured Volume-Variable Costs

I. Initial Situation, Before Changes in Cost Measurement

Product	Volume-Variable Cost	Contri-bution	Revenue	Coverage	Mark-up	Coverage Index	Mark-up Index
A	33.3	22.2	55.6	167%	67%	1.11	1.33
B	33.3	11.1	44.4	133%	33%	0.89	0.67
Total	66.7	33.3	100.0	150%	50%	1.00	1.00
Revenue Requirement			100.0				

II. Equal Reduction in Measured Costs, Previous Mark-up Index Applied

Product	Volume-Variable Cost	Contri-bution	Revenue	Coverage	Mark-up	Coverage Index	**Mark-up Index = Initial**
A	25.0	33.3	58.3	233%	133%	1.17	**1.33**
B	25.0	16.7	41.7	167%	67%	0.83	**0.67**
Total	50.0	50.0	100.0	200%	100%	1.00	**1.00**

III. Equal Reduction in Measured Costs, Previous Coverage Index Applied

Product	Volume-Variable Cost	Contri-bution	Revenue	Coverage	Mark-up	**Coverage Index = Initial**	Mark-up Index
A	25.0	30.6	55.6	222%	122%	**1.11**	1.22
B	25.0	19.4	44.4	178%	78%	**0.89**	0.78
Total	50.0	50.0	100.0	200%	100%	**1.00**	1.00

In Panel II, the mark-up index from Panel I is used to calculate new mark-ups for each product. For example, Product A's mark-up index of 1.33 is applied to the new system-average mark-up (100 percent) to get its mark-up of 133 percent. Similarly, Product B's new mark-up is calculated to be 67 percent. With these mark-ups, the revenue generated from Product A is 58.3, compared to 55.6

in Panel I, or a rate increase of 4.9 percent. For Product B, on the other hand, the new mark-up generates less revenue than in Panel I; Product B thus gets a rate decrease of 6.1 percent (= (41.7/44.4) - 1). Thus, even though the measured costs of Products A and B are <u>equally</u> affected by the change in costing method, a straightforward application of the Panel I mark-up index produces distinctly <u>unequal</u> effects on their rates. This hardly seems consistent with fairness and equity.

Panel III presents a parallel calculation using the coverage index from Panel I. For example, Product A's coverage index of 1.11 is applied to the new system-average coverage (200 percent) to get its coverage of 222 percent. Similarly, Product B's new coverage is determined to be 178 percent. With these coverages, the revenue from each product turns out to be the same as in Panel I; in effect, both products get an equal rate increase (zero, since the revenue requirement is unchanged).

This suggests to me that, for setting rate levels based on the new cost information, the cost coverage index provides a better starting point than the mark-up index. Since applying the cost coverage index results in the same revenue for each subclass as before, this is equivalent to unchanged rates (volume does not change). Therefore, there is no need for mechanical adjustments in response to the higher system-average cost coverage resulting from the change in costing methods; one can simply use existing rates as the starting point for developing new rates and rate-levels under an increased revenue requirement.[9]

Naturally, the new costing methods did not in fact reduce measured costs for each subclass by an equal percentage. The differential reductions for different subclasses have been reflected in the Postal Service's proposals by a tendency, other things equal, to propose coverages that result in lower-than-average rate increases for those subclasses that experienced greater-than-average reductions in their measured volume-variable cost.

F. Ramsey Prices

One issue that generally arises in postal rate proceedings is that of Ramsey pricing. Although the Postal Service does not advocate a mechanistic application of this approach to pricing, it does provide a useful framework for demonstrating the effects of different pricing decisions and provides a sense of direction toward prices that reduce the excess burden of raising the revenue needed to operate the Postal Service on a breakeven basis. At the same time, the Postal Service recognizes that the Act directs that postal ratemaking consider a variety of factors, not all of which are directed toward economic efficiency.

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[9]Of course, existing rates are only the starting point. In the light of the new costing information, rate levels may need to be considered afresh against the criteria in the Act. It should be noted, however, that the existing rates, when evaluated relative to the new costs, do preserve whatever trade-offs between economic efficiency and other objectives were reflected in their original selection. For example, if Product A's price was below the Ramsey price derived from the original costs, it will also be below the Ramsey price derived from the new costs. This is because the coverage index preserves the <u>relative</u> positions of various products in terms of their ratios of price to marginal cost.

I make no formal use of the Ramsey prices developed by witness Bernstein in USPS-T-31. In general, however, all else being equal, I view movement of rates in the direction of Ramsey prices to be beneficial. Therefore, whether a particular rate level would move rates closer to, or farther away from, Ramsey prices was one of the many factors I considered in evaluating potential rate levels. In this case, given the modest overall increase, the Postal Service's desire to keep the increase for all subclasses close to the overall average where possible, and its desire to exercise restraint in reflecting the new costing information in rate levels, the consideration of movement toward or away from Ramsey prices did not have a major effect on my conclusions.

II. RATE LEVELS - MAIL CLASSES AND SPECIAL SERVICES

In the following subsections, I discuss how I have applied the nine criteria to develop rate level proposals for the subclasses not subject to the Revenue Forgone Reform Act (RFRA). Coverages for the preferred-rate subclasses are determined from the corresponding commercial subclasses in accordance with the RFRA, and are simply mentioned in the appropriate subsection.

The overall percentage rate increase requested in this proceeding is historically low, and the rate increases for individual subclasses also fall within a relatively narrow range.

A. First-Class Mail

1. Letters

The Postal Service is proposing a cost coverage of 200 percent for First-Class Mail letters. This corresponds to an average rate increase of 3.3 percent for the subclass as a whole. For single-piece letters the increase is 2.5 percent, including a one-cent increase in the first-ounce rate, to 33 cents, no change in the additional ounce rate, and a new first-ounce rate of 30 cents for Prepaid Reply Mail and Qualified Business Reply Mail. For work-shared letters, the average increase is 4.5 percent.

Value of service (criterion 2) for First-Class Mail letters is high in terms of both intrinsic and economic measures. It benefits from the extensive collection system, which is designed primarily for First-Class Mail, it travels by air when travelling longer distances, and it receives a high priority of delivery. It is sealed against inspection and receives forwarding without additional charge.

First-Class Mail letters also have a relatively low price elasticity of demand (-0.23), indicating a high economic value of service, but it must be acknowledged that this elasticity may be due in part to the Private Express Statutes.

The effect of the proposed rate increase (criterion 4) is certainly modest. The proposed rate increase is 3.2 percent and will only go into effect after more than three years of rate stability. This is well below overall inflation in the economy and is also below the average requested increase.

For many mailers, the available alternatives (criterion 5) to First-Class Mail letters are quite limited. In addition to the restrictions imposed by the Private Express Statutes, considerations of cost and accessibility mean that many mailers have few practical alternatives to the use of First-Class Mail letters for transmitting correspondence, bills, and bill payments. Nevertheless, the availability of alternatives to First-Class Mail letters is clearly expanding, with growth in the number of facsimile machines, in the number of businesses and households with access to the internet, and with increased availability of electronic payment options. Somewhat counterbalancing this, the proposed new Prepaid Reply Mail rate category will have the effect of making First-Class Mail letters more convenient and affordable for certain uses.

The degree of preparation by the mailer and its effect on reducing Postal

Service costs (criterion 6) is reflected in the rate structure, which provides an array of discounts for mail that is prebarcoded and presorted. The Prepaid Reply Mail and Qualified Business Reply Mail rates reflect preparation by the recipient, who is the party making payment to the Postal Service.

In a broader sense, of course, one can argue that the sender pays Prepaid Reply Mail postage, either explicitly through a separate line item on the bill if the participating business chooses to do so, or implicitly through having the postage cost built into the price of the product or service. Thus, the Postal Service's exclusion from this rate of courtesy reply mail, for which postage is applied directly by the sender, does not hinge on who makes the payment to the Postal Service, but on the difficulties of administering a two-stamp system that are most recently summarized on page 4 of the Governors' Decision on the Courtesy Envelope Mail portion of Docket No. MC95-1. Indeed, the Postal Service hopes and expects that over time much of what is now courtesy reply mail will convert to Prepaid Reply Mail.

The Prepaid Reply Mail and Qualified Business Reply Mail rates do add a degree of complexity to the rate schedule (criterion 7), but do so in a way that minimizes the administrative impact of this complexity and actually provides additional convenience to the individual mailer.

In recent proceedings, the Commission has also recognized the informational value of the business and personal correspondence that constitutes the great majority of First-Class Mail letters (criterion 8), and the Postal Service proposal reflects this as well.

At projected test-year after-rates volumes, revenue is \$33,615 million and estimated incremental cost is \$18,329 million, so that revenue clearly exceeds incremental cost (criterion 3).[10]

The proposed rate level is fair and equitable (criterion 1); it reflects a careful consideration of the Section 3622(b) criteria.

2. Cards

The Postal Service is proposing a cost coverage of 184 percent for First-Class Mail cards, lower than that for First-Class Mail letters. This corresponds to an average rate increase of 5.9 percent for the subclass as a whole. For single-piece cards the increase is one cent to 21 cents, with a new rate of 18 cents for Prepaid Reply Mail and Qualified Business Reply Mail. For work-shared cards, the average increase is 7.9 percent.

The intrinsic value of service (criterion 2) for First-Class Mail cards in many ways mirrors that of First-Class Mail letters, although it is somewhat reduced by their limited message capacity and lesser degree of privacy. At -0.86, the price elasticity for cards is much higher than for letters, implying a lower economic value of service as well.

At 5.9 percent, the percentage rate increase for cards is above average.

[10]For each subclass, revenue is taken from my Exhibit USPS-30B, and estimated incremental cost is taken from Exhibit USPS-41B (witness Takis).

This is partly due to the whole-cent rounding constraint for the single-piece rate; a one-cent increase represents a larger percentage increase on card rates than it does First-Class Mail letter rates. However, in view of the fact that this will be the first overall increase in card rates since Docket No. R90-1, the effect of this increase on mailers is clearly acceptable (criterion 4).

The availability of alternatives for First-Class Mail cards is somewhat broader than for First-Class Mail letters (criterion 5). In addition to the electronic alternatives mentioned in the discussion of letters, First-Class letters can be used for personal messages and Standard (A) Mail can be used for many of the sale announcements and other advertising, which are a more significant portion of volume in cards than in letters.

The rate structure for First-Class Mail cards parallels that for First-Class Mail letters, so that considerations of mailer preparation (criterion 6) and simplicity (criterion 7) are also parallel.

At projected test-year after-rates volumes, the First-Class Mail cards revenue of $1,089 million exceeds their estimated incremental cost of $609 million (criterion 3).

The proposed rate level reflects a balanced consideration of all the relevant criteria; it is fair and equitable (criterion 1).

B. Priority Mail

The Postal Service is proposing a cost coverage of 198 percent for Priority

Mail, which corresponds to an average rate increase of 7.4 percent. Both the coverage and the rate increase are above the system average.

Priority Mail clearly has a high intrinsic value of service (criterion 2). It enjoys the same priority of delivery as First-Class letters, receives even greater use of air transportation in view of the two-day service standard between most metropolitan areas, and enjoys the convenience of the collection system for the unzoned two-pound rate packages that constitute a large share of its volume. The availability of the proposed Delivery Confirmation Service will also contribute to its intrinsic value of service. On the other hand, the Priority Mail price elasticity (-0.77) is considerably higher than that of First-Class Mail, indicating a lower economic value of service.

The 7.4 percent rate increase, though above-average, is still below inflation in the economy as a whole, and thus should not have an unacceptable effect on mailers (criterion 4). At the same, the relatively significant rate increase, together with the significant margin between revenue and incremental cost, means that the rate increase is not unfair to competitors.

The Priority Mail rate structure is relatively simple (criterion 7), with unzoned rates up to five pounds, where much of the volume is concentrated, and an understandable weight- and distance-based structure for heavier pieces. The rate structure will be further simplified by the proposed elimination of the presort discount, which has seen relatively little use.

At projected test-year after-rates volumes, revenue is $4,353 million and estimated incremental cost is $2,598 million, so that revenues are comfortably above incremental cost (criterion 3).

The proposed rate level is appropriate in the light of all relevant criteria; it is fair and equitable (criterion 1) to both mailers and competitors.

C. Express Mail

The Postal Service is proposing an Express Mail cost coverage of 204 percent, which corresponds to an average rate increase of 3.7 percent.

Express Mail's value of service (criterion 2) is very high when intrinsic factors are considered. It receives the highest delivery priority, extensive air transportation, and a significant collection system, though not as extensive as the general collection system used by First-Class Mail. It also benefits from a tracking capability. On the other hand, Express Mail's price-elasticity, at -1.53, is well above 1.0 in absolute value, and is uniquely so among the subclasses and special services for which the Postal Service proposes rate levels.[11] This indicates an extremely low economic value of service.

The 3.7 percent increase will have a modest and clearly acceptable effect on mailers (criterion 4). Given Express Mail's small market share and its quite modest growth (less than 2 percent in FY 1996) even in the absence of a rate increase, the proposed rate increase should not have an unfair effect on

[11]At -1.18, the Classroom Periodicals own-price elasticity also exceeds 1.0 in absolute value.

competitors.

There are a number of private-sector alternatives available to Express Mail users (criterion 5). However, for the individuals and small-volume business users who now appear to account for the bulk of Express Mail, these alternatives may only be available at a higher price, though also with additional service features.

For Express Mail, the deposit and/or pick-up of mail at the post office or airport, as provided for in separate rate schedules, reduces postal costs and constitutes a form of preparation by.the mailer (criterion 6).

At projected test-year after-rates volumes, revenue is $841 million and estimated incremental cost is $710 million, so that revenues exceed incremental cost by $131 million (criterion 3).

The proposed rate level is fair and equitable (criterion 1), reflecting a consideration of all the relevant criteria, including the effects on both competitors and Express Mail users.

D. Periodicals

1. Regular

The Postal Service is proposing a cost coverage of 107 percent for Regular Periodicals, or an average rate increase of 3.5 percent for the subclass.

The value of service (criterion 2) received by Periodicals is moderately high in terms of intrinsic service characteristics, although not as high as First-Class Mail, since they receive much less air transportation and no collection system, and receive forwarding at no additional charge for a shorter period. Periodicals have a higher priority of delivery than Standard Mail. The own-price elasticity for Periodicals is very low (-0.14), even lower than that of First-Class Mail, for which the Private Express Statutes presumably act to make the elasticity less than it otherwise would be. This indicates a correspondingly quite high economic value of service.

The educational, cultural, scientific, and informational value (criterion 8) of Periodicals has historically led to relatively low cost coverages for this mail, and this factor has been fully considered in setting the proposed Regular Periodicals coverage.

In this case, however, the proposed coverage has been further reduced due to consideration of the effect of rate increases (criterion 4). Without this consideration, the large increase in unit cost for Periodicals would have led to much higher percentage rate increases. For example, the coverage approved by the Commission in Docket No. R94-1 was 116 percent (when the system-average was 157 percent). Applied to test-year costs, this coverage would have resulted in a rate increase approximately nine percentage points higher than actually proposed, and any upward adjustment to reflect the increased system-average coverage would only intensify the problem.

The Postal Service is undertaking an analysis to understand what factors may have contributed to increases in flats mail processing costs, especially for Periodicals. Rather than mechanically reflecting the full cost increase in rates, I believe it is appropriate to first see whether these cost trends can be reversed as a result of the additional equipment deployment and operational changes that are expected over the next several years. See USPS-T-4 (witness Moden) at Section II.B. This approach also provides more time for mailers to prepare for future increases if necessary.

The fact that smaller publications with geographically dispersed circulation had recently experienced significant rate increases as a result of Classification Reform was also taken into account under criterion four.

Non-postal alternatives (criterion 5) include alternate delivery firms and newsstand sales, but the degree to which different publications can utilize these alternatives varies considerably.

The Periodicals rate structure is far from simple. However, in this proceeding revised definitions of presort categories are proposed that will better conform to the way Periodicals mail is actually processed. Under the revised definitions, the rate paid by a 3-digit presorted piece will no longer depend on whether that particular 3-digit area is a "unique 3-digit city" or some other 3-digit area. This change will somewhat improve the degree to which there are simple, understandable relationships between rates (criterion 7).

Revenue at projected test-year after-rates volumes is $1,689 million, which exceeds the estimated incremental cost of $1,601 million by a margin of $88 million (criterion 3).

The proposed rate level is fair and equitable (criterion 1); it has been developed after a careful consideration of all the criteria, taking into account the effect on users that would result from the immediate application of previous cost coverages to current Periodicals costs, pending an improved understanding of why they have grown so rapidly in the past several years.

2. Preferred-Rate

The RFRA requires that Within County, Nonprofit, and Classroom Periodicals each have a mark-up equal to one-half that of Regular Periodicals for full rates, or a cost coverage of 103.5 percent. For the test-year, Step 5 rates will apply, with a mark-up equal to five-twelfths that of Regular Periodicals; this results in rate increases averaging 3.4 percent, 3.9 percent, and 4.8 percent respectively.[12]

E. Standard A Mail

1. Regular

The Postal Service is proposing a cost coverage of 154 percent for the Regular subclass, which results in an average rate increase of 4.1 percent.

In common with other Standard subclasses, Regular has a relatively low

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[12]Witness Kaneer (USPS-T-35) describes why, given the difficulties in accurately measuring cost for very small subclasses, applying Nonprofit Periodicals rates to Classroom mail is appropriate pending further analysis to develop an improved cost framework to apply the RFRA mark-ups to Classroom. The financial summary in my workpapers, which relies strictly on the test-year cost developed from reported FY 1996 cost data, reflects the fact that this cost is greater than after-rates revenues.

intrinsic value of service (criterion 2) due to its deferability for delivery, ground transportation, and lack of access to the collection system. While the Postal Service often attempts to satisfy mailer requests for delivery within a specific time frame, these typically involve advance planning and coordination by the mailer in order to facilitate the achievement of these delivery requests. The price elasticity for Regular is higher than that of First-Class letters but lower than that of Enhanced Carrier Route, suggesting an intermediate economic value of service.

The 4.1 percent average rate increase is well below inflation and will have an acceptably small impact on the users of Regular mail (criterion 4). The fact that it is only slightly below the 4.5 percent system-average increase, together with the 154 percent cost coverage, indicates that competitors are not unfairly targeted by this increase.

The Regular subclass is somewhat more suited to demographic targeting of commercial messages and the Enhanced Carrier Route subclass is somewhat more suited to geographic targeting. For this reason, the availability of alternatives (criterion 5) is somewhat less for Regular, but a number of alternatives for demographically targeted advertising exist, including special-interest magazines, cable television channels, and internet web sites.

The mail within the Regular subclass all has a substantial degree of mailer preparation (criterion 6), with some of it being both prebarcoded and sorted to 5-digit areas. Overall, however, it does not have the same degree of preparation as Enhanced Carrier Route.

At projected test-year after-rates volumes, the $8,022 million revenue from the subclass easily exceeds its estimated incremental cost of $5,305 million (criterion 3).

The proposed rate level is fair and equitable (criterion 1); it appropriately balances all the relevant criteria, including the effects on both users and competitors.

2. Nonprofit

Under the RFRA, the Standard A Nonprofit subclass is required to have a mark-up equal to one-half that of Standard A Regular for full rates, or a coverage of 127 percent. For the test-year, Step 5 rates will apply, with a mark-up equal to five-twelfths that of Standard A Regular; when this mark-up is applied to Nonprofit costs, it results in a rate increase of 15.1 percent. Although this increase is well above the system average, the RFRA provides no mechanism for mitigation.

3. Enhanced Carrier Route

The Postal Service is proposing a cost coverage of 228 percent for the Enhanced Carrier Route (ECR) subclass, which results in a 3.2 percent average rate increase. This is somewhat below the system-wide average increase, reflecting a desire to lower the very high cost coverage of this subclass.

In common with Regular, the intrinsic value of service (criterion 2) for ECR is relatively low (criterion 2), since it lacks access to the collection system, receives ground transportation, and its delivery may be deferred. Where the Postal Service is able to accommodate mailer requests for delivery within a specific time frame, this again often requires mailer preparation, coordination, and planning. For the high-density and saturation rate categories, this is also facilitated by the regularity with which many of these mailings are deposited. The price-elasticity of ECR is higher than that of Standard A Regular, First-Class letters, or Periodicals, indicating a relatively low economic value of service as well.

Like the increase for First-Class letters, the average rate increase for ECR is well below the rate of inflation, limiting its effect on mailers (criterion 4). Given the very high cost coverage of the ECR subclass, this rate increase does not result in unfair competition for its competitors.

The availability of alternatives (criterion 5) for users of ECR mail is relatively high; due to its geographic concentration, both alternate delivery firms and newspaper inserts may provide alternative ways of delivering the same advertising message. Also, this mail has a very high degree of preparation by the mailer (criterion 6); even the basic rate category must be line-of-travel sequenced, and the high-density and saturation categories are walk-sequenced.

At projected test-year after-rates volumes, revenue is $4,304 million and estimated incremental cost is $1,969 million, so that revenue exceeds incremental cost by a wide margin (criterion 3).

While most of the factors considered above would indicate a cost coverage lower than that actually proposed, this could only be achieved by imposing greater rate increases on other subclasses, thereby widening the range of increases around the modest overall average. Also, a lower coverage for ECR would have made it more difficult to design rates so that the Automation 5-digit rate in Standard Regular was below the ECR basic rate, encouraging the movement of ECR basic letters into the automation mailstream. As has been the case since at least Docket No. MC95-1, this is an important operational goal of Postal Service management. See USPS-T-4 (witness Moden) at Section II.A.3.

In view of this overall fairness and equity objective and the modest average ECR rate increase of 3.2 percent, with even smaller increases for the more highly work-shared rate categories within the subclass, I believe the rate level proposed for ECR satisfies the fairness and equity criterion.

4. Nonprofit Enhanced Carrier Route

Under the RFRA, the Nonprofit Enhanced Carrier Route subclass is required to have a mark-up equal to one-half that of commercial ECR for full rates, or a coverage 164 percent. For the test-year, Step 5 rates will apply, with a mark-up equal to five-twelfths that of commercial ECR. When this mark-up is applied to Nonprofit ECR costs and full Step 6 rates are imposed for those rate cells where Step 5 rates are below the RFRA phasing-period rate-floor for nonletters,[13] the

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[13]See USPS-T-36 (witness Moeller) at Section VII.B and Section VIII.

result is a 4.8 percent decrease in average rates.

F. Standard B Mail

1. Parcel Post

The Postal Service is proposing a Parcel Post cost coverage of 103 percent, which corresponds to an average rate increase of 10.2 percent for the subclass.

In general, Parcel Post exhibits a low intrinsic value of service (criterion 2); it has a low delivery priority and uses primarily ground transportation. Due to increased security concerns, it no longer enjoys its former access to the collection system. Moveover, its own-price elasticity is just below 1.0 (in absolute value), indicating a low economic value of service.

The proposed 10.2 percent average rate increase is one of the highest in this proceeding, and will undoubtedly have some effect on mailers who use Parcel Post (criterion 4). Unfortunately, due to cost increases and the need to ensure that revenue covered incremental cost, there was very little room to mitigate this increase. Parcel Post competitors have been able to compete successfully at current Parcel Post rates, and a 10.2 percent rate increase will not adversely affect their competitive position.

In one sense, alternatives to Parcel Post are plentiful, especially for large-volume business shippers. For individuals, however, these alternatives are not uniformly accessible. Direct access to competitor's services may be limited to a few locations, while retail mail sending and receiving services, whose numbers have increased substantially in recent years, may charge a premium over the competitors' standard rates. And for mailers in more remote locations, there may be no practical alternative to Parcel Post.

At projected test-year after-rates volumes, revenue is $783 million and estimated incremental cost is $769 million, so that revenue is just above incremental cost (criterion 3).

The proposed rate level is fair and equitable (criterion 1); it reflects a balanced consideration of the relevant criteria and takes into consideration the interests of the diverse users of Parcel Post and its competitors.

2. Bound Printed Matter

The Postal Service is proposing a cost coverage of 152 percent for Bound Printed Matter (BPM); this results in an average rate increase of 5 percent.

In common with Parcel Post, the intrinsic value of service for Bound Printed Matter is relatively low (criterion 2). On the other hand, its own-price elasticity is -0.34, or little less (in absolute value) than that of Standard A Regular, suggesting a moderately high economic value of service.

Although slightly above the 4.5 percent system-average increase, the 5 percent increase proposed for BPM is well below overall inflation and thus should have an acceptable effect on the users of BPM (criterion 4). At the same time, this increase, together with the 152 percent cost coverage, indicates that actual and potential competitors are not unfairly targeted.

The alternatives available to BPM users vary somewhat (criterion 5). For mailers of books, the Special subclass provides an alternative. For mailers of catalogs and telephone directories, alternate delivery firms provide at least a potential alternative, although there do not appear to be widespread efforts by such firms to develop service offerings targeted at this portion of BPM.

Over a period of years, an increasing number of books have been mailed as BPM. The Commission accordingly has given the subclass some ECSI consideration in setting rate levels, and the Postal Service proposal in this proceeding does so as well (criterion 8).

At projected test-year after-rates volumes, revenue is $525 million and estimated incremental cost is $348 million; revenue is well above incremental cost (criterion 3).

The proposed rate level is fair and equitable (criterion 1); it reflects an appropriate balance among all the criteria of Section 3622(b).

3. Special

The Postal Service is proposing a cost coverage of 137 percent for the Special subclass; this translates into a zero percent average rate increase for the subclass.

In common with other Standard B subclasses, the intrinsic value of service for the Special subclass is relatively low (criterion 2). Its price elasticity is -0.36, near that of Bound Printed Matter, suggesting a moderately high economic value of service.

The zero percent increase will not have an unacceptable effect on current users of the Special subclass (criterion 4), and it will also help to mitigate the effective rate increase for current Library subclass users, as explained in the following paragraph. For many business users of the Special subclass, the BPM subclass provides an alternative (criterion 5), but for many individual users alternatives are more limited.

The books, films, sound recordings, and similar matter mailed in the Special subclass have a significant ECSI value (criterion 8), and this has been taken into account in setting its cost coverage with the accompanying zero percent rate increase. Because the Special subclass cost coverage directly determines the Library subclass coverage through the RFRA, the zero percent increase for the Special subclass helps to mitigate the rate increase for Library. Moreover, even with this effect, the new RFRA-driven rates for Library will be above Special rates, and the overwhelming majority of Library mail is expected to migrate to Special. Therefore, holding the rate increase for Special to zero also mitigates the effective rate increase that Library mail will experience in moving from current Library rates to Special rates.

At projected test-year after-rates volumes, estimated incremental cost is $258 million and revenue is $352 million, so that revenue exceeds incremental cost by $94 million (criterion 3).

The proposed rate level reflects a careful consideration of all the criteria; it is fair and equitable (criterion 1).

4. Library

Under the RFRA, the Standard B Library subclass is required to have a mark-up equal to one-half that of Standard B Special for full rates, or a coverage 119 percent. For the test-year, Step 5 rates will apply, with a mark-up equal to five-twelfths that of Standard A Regular. Rates corresponding the required mark-up on Library costs are developed in the testimony of Witness Adra (USPS-T-38). However, this results in rates that are generally higher than those for the Special subclass. Therefore, the financial summary in my workpapers recognizes that the vast majority of Library mail that is eligible to mail at Special rates will do so. When this shift is taken into account, the actual coverage on what is now Library Mail will be 107 percent, which corresponds to an average rate increase of 14 percent.

G. Special Services

Exhibit USPS-30C summarizes the Postal Service's proposed fee levels for the various Special Services. The detailed development of these fee levels is described in USPS-T-39 (witness Needham) and USPS-T-40 (witness Plunkett). I have reviewed these testimonies and the proposed fee levels, and I conclude that they are consistent with the Section 3622(b) criteria.

SUMMARY OF ESTIMATED FISCAL YEAR 1998 BEFORE RATES FINANCES
(Dollars in Thousands)

Line No.	Description	Volume Variable Costs (1)	Revenues (2)	Percent of Costs (Col 2/Col 1) (3)	Contribution To Other Costs (Col 2 - Col 1) (4)
1	First-Class Mail				
2	Single Letters	12,638,882	21,564,407	170.62%	8,925,525
3	Worksharing Letters	4,114,765	11,103,853	269.85%	6,989,088
4	Total Letters	16,753,648	32,668,260	194.99%	15,914,612
6	Private Postcards	444,640	648,970	145.95%	204,329
7	Worksharing Postcards	166,266	410,873	247.12%	244,606
8	Total Cards	610,907	1,059,843	173.49%	448,936
9	Total	17,364,554	33,728,103	194.24%	16,363,548
10	Priority Mail	2,152,263	3,983,422	185.08%	1,831,159
11	Express Mail	423,481	823,885	194 55%	400,404
12	Mailgrams	508	4,676	920.45%	4,168
13	Periodicals				
14	In County	82,273	82,586	100.38%	314
15	Outside County				
16	Nonprofit	335,896	311,453	92.72%	(24,443)
17	Classroom	13,806	10,577	76.61%	(3,229)
18	Regular-Rate	1,586,274	1,630,774	102.81%	44,500
19	Total	2,018,248	2,035,389	100.85%	17,141
20	Standard Mail A				
21	Single Piece	230,228	157,506	68 41%	(72,722)
22	Commercial Regular	4,954,646	7,192,729	145.17%	2,238,083
23	Commercial Enhanced Carrier Route	2,165,716	4,722,276	218.05%	2,556,561
24	Total Commercial	7,120,362	11,915,005	167.34%	4,794,644
25	Nonprofit	1,088,999	1,165,260	107 00%	76,260
26	Nonprofit Enhanced Carrier Route	157,659	261,791	166.05%	104,132
27	Total Nonprofit	1,246,658	1,427,051	114.47%	180,393
28	Total Standard Mail A	8,597,248	13,499,562	157.02%	4,902,314
29	Standard Mail B				
30	Parcel Post	794,829	737,970	92 85%	(56,859)
31	Bound Printed Matter	336,114	493,286	146.76%	157,172
32	Special Rate	258,023	353,938	137.17%	95,915
33	Library Rate	51,770	48,267	93.23%	(3,502)
34	Total	1,440,735	1,633,461	113.38%	192,726
35	Free-for-the-Blind, etc.	31,839	0	0.00%	(31,839)
36	International Mail	1,228,423	1,625,558	132.33%	397,135
37	Special Services				
38	Registry	83,553	91,928	110 02%	8,375
39	Certified	342,121	410,607	120.02%	68,486
40	Insurance	42,778	64,816	151.52%	22,038
41	COD	17,204	16,287	94.67%	(917)
42	Money Orders	147,432	237,331	160.98%	89,899
43	Stamped Envelopes	12,284	13,843	112 70%	1,560
44	Special Handling	1,285			(1,285)
45	Post Office Boxes	613,811	616,536	100.44%	2,724
46	Other		301,695		
47	Total	1,260,468	1,753,043	139.08%	492,575
48	Other Costs *	161,607			(161,607)
49	Other Income		215,531		215,531
50	Attributable Costs and Revenues	34,679,376	59,302,629	171.00%	24,623,253
51	Total Other Costs	26,719,265			(26,719,265)
52	Prior Years Loss Recovery	446,933			(446,933)
53	Continuing Appropriations		67,274		67,274
54	Investment Income		33,580		33,580
55	GRAND TOTAL	61,845,574	59,403,483	96.05%	(2,442,091)

* Includes costs for stamped cards

SUMMARY OF ESTIMATED FISCAL YEAR 1998 AFTER RATES FINANCES
(Dollars in Thousands)

Line No	Description	Volume Variable Costs (1)	Revenues (2)	Percent of Costs (Col 2/Col 1) (3)	Contribution To Other Costs (Col 2 - Col 1) (4)
1	First-Class Mail				
2	Single Letters	12,784,417	22,148,759	173.25%	9,364,342
3	Worksharing Letters	4,061,736	11,466,010	282 29%	7,404,273
4	Total Letters	16,846,154	33,614,769	199.54%	16,768,615
5	Single Postcards	432,714	661,012	152.76%	228,298
6	Worksharing Postcards	160,219	427,967	267.11%	267,747
7	Total Cards	592,934	1,088,979	183.66%	496,045
8	Total	17,439,087	34,703,748	199 00%	17,264,660
9	Priority Mail	2,194,585	4,352,693	198.34%	2,158,108
10	Express Mail	413,255	841,217	203.56%	427,962
11	Mailgrams	508	4,676	920.49%	4,168
12	Periodicals				
13	In County	81,360	83,665	102.83%	2,305
14	Outside County				
15	Nonprofit	331,724	342,631	103 29%	10,907
16	Classroom	12,763	10,286	80.59%	(2,477)
17	Regular-Rate	1,578,996	1,688,946	106.96%	109,950
18	Total	2,004,843	2,125,528	106.02%	120,685
19	Standard Mail A				
20	Single Piece	0	0	0.00%	0
21	Commercial Regular	5,192,942	8,022,045	154 48%	2,829,103
22	Commercial Enhanced Carrier Route	1,885,382	4,304,004	228.28%	2,418,622
23	Total Commercial	7,078,324	12,326,049	174.14%	5,247,725
24	Nonprofit	1,107,575	1,351,433	122.02%	243,858
25	Nonprofit Enhanced Carrier Route	125,122	201,408	160.97%	76,286
26	Total Nonprofit	1,232,697	1,552,841	125.97%	320,144
27	Total Standard Mail A	8,311,021	13,878,890	166 99%	5,567,869
28	Standard Mail B				
29	Parcel Post	761,146	782,916	102.86%	21,769
30	Bound Printed Matter	346,168	524,608	151.55%	178,440
31	Special Rate	256,914	352,330	137.14%	95,416
32	Library Rate	49,111	52,427	106 75%	3,316
33	Total	1,413,339	1,712,281	121 15%	298,941
34	Free-for-the-Blind, etc.	31,780	0	0.00%	(31,780)
35	International Mail	1,207,118	1,643,844	136.18%	436,726
36	Special Services				
37	Registry	76,778	122,606	159.69%	45,828
38	Certified	326,039	438,879	134.61%	112,840
39	Insurance	48,287	74,453	154.19%	26,166
40	COD	16,988	18,024	106.10%	1,036
41	Money Orders	147,365	239,797	162.72%	92,432
42	Stamped Envelopes	12,308	14,945	121.43%	2,637
43	Special Handling	1,283			(1,283)
44	Post Office Boxes	595,854	688,001	115.46%	92,148
45	Other		448,909		
46	Total	1,224,901	2,045,614	167.00%	820,713
47	Other Costs *	218,009			(218,009)
48	Other Income		215,531		215,531
49	Attributable Costs and Revenues	34,458,447	61,524,021	178.55%	27,065,575
50	Total Other Costs	26,698,560			(26,698,560)
51	Prior Years Loss Recovery	446,933			(446,933)
52	Continuing Appropriations		67,498		67,498
53	Investment Income		54,371		54,371
54	GRAND TOTAL	61,603,939	61,645,890	100.07%	41,951

* Includes BPRS, stamped cards, delivery confirmation, and packaging service costs

Proposed Cost Coverages for Special Services

SPECIAL SERVICES	
Post Office Boxes and Caller Service	115%
Certified Mail	133%
C.O.D.	106%
Insurance	154%
Money Orders	205%
Registered Mail	160%
Stamped Cards	251%
Stamped Envelopes	130%
SERVICES ASSIGNED TO CLASSES	
Address Correction	127%
Business Reply	114%
Certificates of Mailing	132%
First Class Presort Fees	113%
Standard (B) Special Presort	113%
Parcel Airlift	N/A
Periodicals Applications	129%
Special Handling	102%
Standard (A) Presort	113%
OTHER SERVICES	
Correction of Mailing Lists	124%
Furnishing Address Changes to Election Boards	124%
Merchandise Return	128%
On-Site Meter Setting	130%
Permit Imprint	113%
Zip-Coding of Mailing Lists	118%
Return Receipts	147%
Restricted Delivery	159%

Proposed Percentage Changes in Rates

CLASSIFICATION	PERCENT CHANGE
First Class Mail	
Letters	3.2%
Cards	5.9%
Priority Mail	7.4%
Express Mail	3.7%
Periodicals	
In County	3.4%
Nonprofit	3.9%
Classroom	4.8%
Regular Rate	3.5%
Standard Mail A	
Commercial Regular	4.1%
Commercial Enhanced	3.2%
Nonprofit	15.1%
Nonprofit Enhanced	-4.8%
Standard Mail B	
Parcel Post	10.2%
Bound Printed Matter	5.0%
Special	0.0%
Library	13.1%

Proposed Percent Changes in Special Service Fees

SPECIAL SERVICES	PERCENT CHANGE
Post Office Boxes and Caller Service	18%
Certified Mail	15%
C.O.D.	12%
Insurance	17%
Money Orders	0%
Registered Mail	51%
Stamped Cards	new fee
Stamped Envelopes	16%
SERVICES ASSIGNED TO CLASSES	
Address Correction	0%
Business Reply	51%
Certificates of Mailing	15%
First Class Presort Fees	18%
Standard (B) Special Presort	18%
Parcel Airlift	13%
Periodicals Applications	-1%
Special Handling	221%
Standard (A) Presort	18%
OTHER SERVICES	
Correction of Mailing Lists	18%
Furnishing Address Changes to Election Boards	18%
Merchandise Return	0%
On-Site Meter Setting	1.5%
Permit Imprint	18%
Zip-Coding of Mailing Lists	17%
Return Receipts	32%
Restricted Delivery	0%

Test 'Year After-Rates Cost Adjustments
($000's)

Classification	CRA Roll Forward	Total Adjustments	Total Cost
First Class Mail			
Single Letters & Parcels	12,500,050	157,789	12,657,839
Worksharing Letters	4,021,521	0	4,021,521
Total Letters	16,521,571	157,789	16,679,360
Single Cards	432,970	-4,540	428,430
Worksharing Cards	158,633	0	158,633
Total Cards	591,603	-4,540	587,063
Total First Class Mail	17,113,174	153,249	17,266,423
Priority Mail	2,068,016	104,840	2,172,856
Express Mail	413,661	-4,498	409,163
Mailgrams	503	0	503
Periodicals			
In County	80,554	0	80,554
Nonprofit	328,440	0	328,440
Classroom	12,637	0	12,637
Regular Rate	1,563,362	0	1,563,362
Total Periodicals	1,984,993	0	1,984,993
Standard Mail A			
Single Piece	222,080	-222,080	0
Commercial Regular	5,365,333	-223,806	5,141,527
Commercial Enhanced	1,898,382	-31,667	1,866,715
Commercial Total	7,263,715	-255,473	7,008,242
Nonprofit	1,122,147	-25,538	1,096,609
Nonprofit Enhanced	128,227	-4,344	123,883
Nonprofit Total	1,250,374	-29,882	1,220,492
Total Standard Mail A	8,736,169	-507,435	8,228,734
Standard Mail B			
Parcel Post	739,062	14,548	753,610
Bound Printed Matter	329,298	13,443	342,741

Classification	CRA Roll Forward	Total Adjustments	Total Cost
Special	255,068	-698	254,370
Library	48,615	10	48,625
Total Standard Mail B	1,372,043	27,302	1,399,345
Free Mail-Blind, Hndc&Serv	31,465	0	31,465
International Mail	1,195,166	0	1,195,166
Special Services			
Registry	76,018	0	76,018
Certified	326,677	-3,865	322,812
Insurance	41,224	6,585	47,809
COD	16,820	0	16,820
Money Orders	145,906	0	145,906
Stamped Envelopes	12,186	0	12,186
Special Handling	1,270	0	1,270
Post Office Box	589,954	0	589,954
Stamped Cards	0	4540	4,540
Other	155,167	56,144	211,311
Total Special Services	1,365,222	63,404	1,428,626
TOTAL	33,053,278	-163,137	32,890,141

Test-Year After-Rates Volume Adjustments
($000's)

Classification	Volume Forecast	Total Adjustments	Total Volume
First Class Mail			
Single Letters & Parcels	54,413,387	104,415	54,517,802
Worksharing Letters	40,993,006	40,176	41,033,182
Total Letters	95,406,393	144,591	95,550,984
Single Cards	2,476,656	0	2,476,656
Worksharing Cards	2,463,385	0	2,463,385
Total Cards	4,940,041	0	4,940,041
Total First Class Mail	100,346,434	144,591	100,491,025
Priority Mail	1,087,829	64,584	1,152,413
Express Mail	63,410	-689	62,721
Mailgrams	4,757	0	4,757
Periodicals			
In County	901,870	0	901,870
Nonprofit	2,161,077	0	2,161,077
Classroom	47,452	0	47,452
Regular Rate	7,147,574	0	7,147,574
Total Periodicals	10,257,973	0	10,257,973
Standard Mail A			
Single Piece	161,574	-161,574	0
Commercial Regular	37,627,554	1	37,627,555
Commercial Enhanced	28,686,181	0	28,686,181
Commercial Total	66,313,735	1	66,313,736
Nonprofit	10,550,968	0	10,550,968
Nonprofit Enhanced	2,571,283	0	2,571,283
Nonprofit Total	13,122,251	0	13,122,251
Total Standard Mail A	79,597,560	-161,573	79,435,987
Standard Mail B			
Parcel Post	231,879	2,781	234,660
Bound Printed Matter	561,718	13,024	574,742

Classification	CRA Roll Forward	Total Adjustments	Total Cost
Special	200,511	0	200,511
Library	28,709	19	28,728
Total Standard Mail B		15,805	1,038,641
Free Mail-Blind, Hndc&Serv	56,390	0	56,390
International Mail	1,006,682	0	1,006,682
Special Services			
Registry	14,288	0	14,288
Certified	293,118	-398	292,720
Insurance	30,600	0	30,600
COD	3,886	0	3,886
Money Orders	236,570	0	236,570
Stamped Envelopes		460,000	460,000
Special Handling		0	
Post Office Box		0	
Stamped Cards		0	
Other		0	
Total Special Services	578,462	459,602	1,038,064
TOTAL		0	