BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C.

POSTAL RATE AND FEE CHANGES, 2000 : DOCKET NO. R2000-1

SECOND INTERROGATORIES AND REQUEST FOR PRODUCTION
OF DOCUMENTS FROM GREETING CARD ASSOCIATION TO
UNITED STATES POSTAL SERVICE WITNESS PETER BERNSTEIN
(GCA/USPS-T41-34 THROUGH 48)
(MARCH 7, 2000)

Pursuant to Section 20 of the Commission's Rules of Practice, Greeting Card

Association ("GCA") hereby serves the following further interrogatories and request for

production of documents directed to United States Postal Service witness Peter

Bernstein: GCA/USPS-T41-34 through 48. GCA incorporates by reference the

instructions in OCA interrogatories OCA/USPS-1-14 (January 24, 2000).

Respectfully submitted,

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GCA/USPS-T41-34

a.   Please confirm that the "Ramsey pricing" principle derives from Frank Ramsey's pioneering article, "A Contribution to the Theory of Taxation", Economic Journal, 37: 47-61.

b.   Please confirm that Ramsey's principle concerned how a national tax authority, a monopolistic entity, could maximize tax revenues across various taxpayers when imposing small changes in tax by, in essence, using what has come to be called the inverse elasticity rule. If you do not so confirm, please provide your understanding of the principle set forth in the Ramsey article.

c.   As applied to the Postal Service, please confirm that Ramsey pricing is a revenue maximization scheme.

GCA/USPS-T41-35

a.   Please confirm that wide, unpredictable swings in postal pricing are generally undesireable in the view of the Postal Service.

b.   Please confirm the following percentage changes in USPS own price elasticity estimates for various mail categories between R97-1 and R2000-1:

Percentage Change in Own Price Elasticities

Category	R97-1	R2000-1	% Change
First Class S. P.	-0.189	-0.262	38.6%
Standard A Regular	-0.382	-0.570	49.2
Standard A ECR	-0.598	-0.808	35.1

b.   Please confirm that wide swings in elasticity estimates would lead to wide swings in postal prices if Ramsey pricing were adopted.

GCA/USPS-T41-36

a.   Please confirm that economic welfare is measured by continuous utility
       functions such as that found at page 50 in <u>Microeconomic Theory</u>, (1995),
       a textbook authored by Andreu Mas-Colell, Michael Whinston and Jerry
       Green.

b.   Please confirm that your Summary Table 3 on page 13, "Changes in
       Consumer Surplus", does <u>not</u> show that economic welfare will increase (or
       even stay the same) as a result of moving from R97-1 Index prices to
       Ramsey prices.

c.   Please confirm that your estimated increase in consumer surplus in Table
       3 from reliance on Ramsey pricing is:
          i.   less than 2.2% of postal revenues for FY1997.
          ii.   less than the Postal Service's 2.5% contingency proposed in
                 R2000-1.

d.   Please confirm that <u>even if</u> your estimated positive change in consumer
       surplus from reliance on Ramsey pricing is correct, economic welfare as
       defined in a. above could be substantially lower under the Ramsey prices
       than under the R97-1 Index prices.

GCA/USPS-T41-37

a.   Does the Postal Service subscribe to the principle that as many of its total
       costs as possible should be attributed by class, subclass and rate
       category?

b.   As a percentage of total costs for the Postal Service as a whole, and by
       major class, have attributable costs gone up or down in R2000-1 and in
       R97-1, by comparison with R94-1 and R90-1?

c.   Please confirm that under Ramsey pricing, reducing attributable costs and
       increasing the common cost pool, e.g. by using less than 100% volume
       variabilities for mail processing labor costs, results in more total costs
       being absorbed by the most price inelastic classes of mail, and fewer total
       costs being absorbed by the most price elastic mail classes.

GCA/USPS-T41-38

a. Please confirm that the Ramsey pricing exercise you perform in your testimony is statical pricing, as that term is commonly understood in microeconomic theory.

b. In arriving at your conclusion about the superiority of Ramsey pricing for postal services, did you consider any of the dynamic factors that might render Ramsey pricing inappropriate, such as the GAO report on electronic diversion?

c. Have you examined what the impact of your Ramsey prices are for the investment planning decisions of the Postal Service, or other dynamic considerations? If so, please explain fully what your examination consisted of. If not, please explain why not.

GCA/USPS-T41-39

a. Please confirm that in a market environment of rapid technological change generally, Ramsey pricing can have seriously adverse consequences for investment planning, for example premature or excessive investment, or misallocated investment.

b. Please confirm that the Postal Service faces rapid technological change in at least two of its major market segments: (1) on the positive side, the emergence of e-mail commerce which creates an opportunity for increased package business; (2) on the negative side, the emergence of electronic diversion of letter mail including bills, bill payments, advertising and the like, which creates conditions for disinvestment in personnel and equipment.

GCA/USPS-T41-40

a. Please confirm that Ramsey pricing would enable the Postal Service to shift the costs of R&D and investment, for example in delivery systems, needed to capture the emerging dynamic e-mail commerce package business onto price inelastic customers in First Class mail and elsewhere.

b. Please confirm that such cost shifting could constitute cross-subsidization where costs that could have much higher attribution, such as delivery costs, instead are largely assigned as institutional costs.

GCA/USPS-T41-41   A point made about Ramsey pricing by Dennis Carlton in
Modern Industrial Organization (1990), page 798 is as follows: "This solution is similar
to optimal monopoly price discrimination.".

    a. Do you agree or disagree with this statement with respect to your
        calculation of Ramsey prices?

    b. If you agree, please explain why the regulatory process in postal rate
        making should support any form of monopoly pricing, as opposed to
        replicating the price structure of a competitive market.

    c. If you disagree, please explain fully why your Ramsey prices are not a
        form of monopolistic price discrimination.

GCA/USPS-T41-42

    a.   Please confirm that Ramsey pricing would never be advocated for a
          multiproduct competitive firm in competitive product markets.

    b.   Please confirm that it is a goal of postal pricing sine qua non to reproduce
          in a regulatory setting a set of prices for postal services that would exist
          as if each price were set in a fully competitive market.

GCA/USPS-T41-43   The mail processing business now has a number of
competitors, indicating the absence of any remaining economies for the Postal Service
in this area. Assume mail processing was a separately priced postal service for each
category of mail. Please confirm that Ramsey pricing would not make sense.

GCA/USPS-T41-44

    a.   Due to the amount of purchased transportation used by the Postal
          Service, is it not reasonable to conclude that there are no local economies
          for the USPS in this postal service as such?

    b.   Assume mail transportation was a separately priced postal service for each
          category of mail. Please confirm in the circumstances indicated in a. above
          (whether or not you agree with a.), Ramsey pricing would not make
          sense.

GCA/USPS-T41-45

    a.   In contrast to Ramsey pricing, have you or the Postal Service considered any form of non-linear pricing? If so, please provide all such studies or citations to same if publicly available.

    b.   Please confirm that non-linear pricing can dominate Ramsey pricing efficiency in general, and by way of example, if bulk purchases of postage stamps for Christmas cards were priced in a non-linear way.

GCA/USPS-T41-46   Do the Postal Service's rate proposals in R2000-1 represent a movement even further toward pure Ramsey prices:

    a.   relative to your R97-1 index prices?

    b.   relative to the rates adopted in R97-1 and implemented in 1999?

GCA/USPS-T41-47   Please confirm that a welfare goal which simply aggregates an unweighted sum of producer and consumer surplus is:

    a.   essentially an arbitrary goal.

    b.   <u>not</u> a goal required or encouraged by the Postal Reorganization Act.

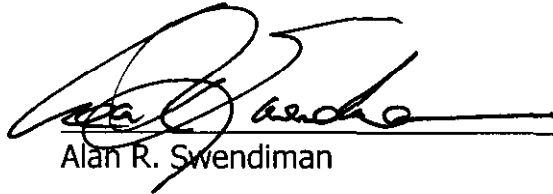If you do not confirm a. or b., please explain why.

GCA/USPS-T41-48

    a.   Please confirm that second best solutions, including Ramsey pricing, are quite sensitive to the assumptions being made.

    b.   Please confirm that the following assumptions are among those necessary for the Ramsey inverse elasticity rule of demand pricing to hold true:

        1.   economies of scale or scope such that marginal cost pricing would not cover all costs

        2.   all cross price elasticities of demand are zero <u>or</u>

        2.a.   demand interdependencies that require direct and cross price elasticities to act in a multiplicative fashion

        3.   the rest of the economy is perfectly competitive

4. no production or consumption externalities

5. equal welfare weights between producer surplus (profit)
    and consumer surplus (utility)

6. no nonmarket clearing, no taxation or government
    regulation and no public sector

7. no income effects

8. monopoly under no threat of entry

9. constant factor prices

10. constant marginal costs

11. no intermediate good production by the firm

12. *no two part tariffs, or other form of taxation to raise revenue*

13. costs can be measured without institutional contraint

14. information is accurate and reasonably priced

15. income distribution is optimal

16. dynamic efficiency is optimal

c. If you believe <u>any</u> of the above assumptions <u>can</u> be assumed to be true
    for Ramsey pricing in the institutional context of the Postal Service,
    please list by number and defend your answer fully.

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.

Alan R. Swendiman