

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

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POSTAL RATE COMMISSION  
OFFICE OF THE SECRETARY

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POSTAL RATE AND FEE CHANGES, 2000

Docket No. R2000-1

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RESPONSES OF UNITED STATES POSTAL SERVICE WITNESS MAYES  
TO INTERROGATORIES OF VAL-PAK DIRECT MARKETING SYSTEMS, INC.,  
VAL-PAK DEALERS' ASSOCIATION, INC., AND CAROL WRIGHT  
PROMOTIONS, INC.  
(VP-CW/USPS-T32-12-15)

The United States Postal Service hereby provides the responses of witness Mayes to the following interrogatories of Val-Pak Direct Marketing Systems, Inc., Val-Pak Dealers' Association, Inc., and Carol Wright Promotions, Inc.: VP-CW/USPS-T32-12-15 (filed on March 15, 2000).

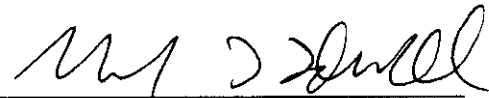
The interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.  
Chief Counsel, Ratemaking



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March 29, 2000

RESPONSE OF POSTAL SERVICE WITNESS MAYES TO VP-CW INTERROGATORIES

VP-CW/USPS-T32-12. The price elasticity of Standard A ECR Mail has risen from  $-0.60$  in Docket No. R97-1 (*Op. & Rec. Dec.*, Docket No. R97-1, para. 5534) to  $-0.808$  in this docket (Table 2 of your testimony, p. 6).

- a. Did you consider this increase in price elasticity (of more than 25 percent) in setting your cost coverage for Standard A ECR?
- b. The Commission stated that it "relies on the precedential value of its past evaluations of the evidence as a starting point and then evaluates new evidence presented to determine whether changes from its past allocation decisions are appropriate." (*Op. & Rec. Dec.*, Docket No. R97-1, para. 4005). Is Standard A ECR's increase in price elasticity (since the most recent omnibus rate docket) evidence that a change from the allocation decision in that docket would be appropriate? Please explain your answer.
- c. Does the increase in elasticity reflect an increase or a decrease in the Value of Service? Please explain your answer.

**Response:**

- a. Yes, although the price elasticity as measured in this docket was more relevant to my determinations than was the change from the most recent case.
- b. Consideration of the measured price elasticity in determination of the cost coverage is appropriate. If witnesses Thress and Tolley indicated that the increase in the price elasticity measured in this case relative to the elasticity measured in the most recent case were statistically significant, *and if nothing else had changed since the last case*, then it would be appropriate to consider a change in allocation of institutional burden. However, the price elasticity for ECR is not the only thing that has changed since the last docket. Nor is it the only thing considered when setting cost coverages. As the goal of setting rate levels is to achieve financial breakeven, ECR and changes in its price elasticity cannot be considered in isolation.

RESPONSE OF POSTAL SERVICE WITNESS MAYES TO VP-CW INTERROGATORIES

Response to VP-CW/USPS-T32-12, cont'd

- c. Under criterion 2, an increase in the own-price elasticity would indicate a decrease in the value of service.

RESPONSE OF POSTAL SERVICE WITNESS MAYES TO VP-CW INTERROGATORIES

VP-CW/USPS-T32-13.

- a. Please refer to page 4 of your testimony. In your discussion of 39 U.S.C. sec. 3622(b)(2), you mention the level of privacy afforded by the mail class, the reliability and image associated with the mail class, and the availability of ancillary services. Do these considerations support a higher or lower cost coverage for Standard A ECR Mail? Please explain your answer.
- b. Please refer to page 6 of your testimony. In your discussion of 39 U.S.C. sec. 3622(b)(2), you mention the availability of alternative services which have features valued by customers, but which are not available in the comparable postal services. (i) Is this consideration applicable to Standard A ECR Mail? (ii) If so, does this consideration support a higher or lower cost coverage for Standard A ECR Mail?

**Response:**

- a. As I stated on page 38 of my testimony, isolated consideration of criterion 2 would suggest that Standard Mail (A) ECR receive a relatively lower cost coverage on the basis of the level of privacy afforded the mail, the reliability of the mail and the availability of ancillary services.
- b. (i) Yes. Alternative delivery firms may be able to better meet a specific delivery day or even delivery time of day. Also, some alternative means of delivery would not require the piece to bear an address.  
(ii) The presence of viable alternatives providing services not available to postal customers could translate into a higher own-price elasticity which, under criterion 2, would argue for a lower cost coverage. As I noted in my response to DFC/USPS-40, redirected from the United States Postal Service, criterion 5 has often been interpreted as providing a basis for mitigating a cost coverage when a low own-price elasticity is the result of few available alternatives. While criterion 5 has not generally been

RESPONSE OF POSTAL SERVICE WITNESS MAYES TO VP-CW INTERROGATORIES

Response to VP-CW/USPS-T32-13, cont'd

used to suggest a higher cost coverage was necessary when alternatives are abundant and the price elasticity is high, the Commission has cited some conflicting views of the implications of criterion 5.

RESPONSE OF POSTAL SERVICE WITNESS MAYES TO VP-CW INTERROGATORIES

VP-CW/USPS-T32-14.

Which index provides the superior method for analyzing and comparing institutional contribution by subclass between dockets – a markup index or a coverage index? Please explain why you prefer one index over another.

**Response:**

I do not advocate the use of any mechanistic approach to setting rate levels. However, in his testimony in Docket No. R97-1, witness O'Hara (USPS-T-30) provided an explanation, including numerical examples, of why the use of a cost coverage index might be more useful in analyzing changes from case to case, especially when measured costs and the systemwide average change. As witness O'Hara demonstrated, when measured costs of two products were equally affected by a change in costing methodology, application of a markup index resulted in very unequal effects on their rates, whereas application of a cost coverage index resulted in the same rates as before. In addition, the cost coverage index preserves the relative positions of various products in terms of their ratios of price to marginal cost.

RESPONSE OF POSTAL SERVICE WITNESS MAYES TO VP-CW INTERROGATORIES

VP-CW/USPS-T32-15.

Please refer to page 39 (ll. 14-17) of your testimony, where you state that although the percentage rate increase for the Standard A ECR subclass "is below the system average in this case, many of the factors considered above would indicate a cost coverage even lower than that actually proposed. However, this would mean shifting the additional burden of covering institutional costs to other subclasses."

- a. Is it your testimony that the avoidance of shifting institutional costs to other subclasses takes priority over the application of the statutory noncost criteria in the setting of coverage factors? Please explain your answer fully.
- b. If the cost coverage for Standard A ECR Mail were to be reduced, to what other subclasses would the additional burden most likely be shifted?

**Response:**

- a. No. In addition to satisfying criterion 3, as you have noted in your question, the cost coverage satisfies criterion 4, the impact on mailers, by resulting in a relatively low rate increase. Furthermore, in my testimony I have addressed the other statutory criteria. The pricing criteria are to be used to apportion the institutional burden to achieve financial breakeven, and are applied to all subclasses. The proposed rate level may appear to be the result of the application of only one criterion, but is the result of balancing all of the criteria in the effort to achieve financial breakeven. As noted in your question VP-CW/USPS-T32-12, the Commission has, in the past, used the cost coverage recommended in previous rate proceedings as the starting point, given that the cost coverage from the previous rate case is presumed to have embodied an appropriate consideration and balancing of the pricing criteria.
- b. Please refer to my response to AAPS/USPS-T32-6b. As I noted there, any shifted revenue burden would be apportioned to other subclasses in accordance

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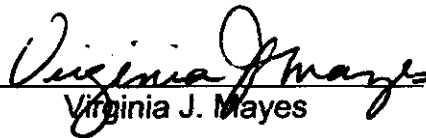
Response to VP-CW/USPS-T32-15, cont'd

with the pricing criteria. However, there were several subclasses for which consideration of criterion 4 would not permit larger increases in rates.



**DECLARATION**

I, Virginia J. Mayes, declare under penalty of perjury that the foregoing answers are true and correct, to the best of my knowledge, information, and belief.

  
Virginia J. Mayes

Dated: 3-29-00

**CERTIFICATE OF SERVICE**

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



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