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

POSTAL RATE AND FEE CHANGES, 2000

Docket No. R2000–1

RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS BERNSTEIN TO INTERROGATORIES OF THE GREETING CARD ASSOCIATION (GCA/USPS–T41–85 - 88)

The United States Postal Service hereby provides the responses of witness Bernstein to the following interrogatories of the Greeting Card Association: GCA/USPS–T41-85 - 88, filed on March 29, 2000.

Each 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

Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260–1137
(202) 268–2992 Fax –5402
April 12, 2000

RESPONSES OF POSTAL SERVICE WITNESS BERNSTEIN
TO INTERROGATORIES OF GCA

GCA/USPS-T41-85 Please refer to your response to GCA/USPS-T41-50. a. Would you agree that the continuity you assume in your utility functions is a cardinal, and not an ordinal, property of those functions? If your answer is "no", please explain why not. If your answer is "yes", can you state that the $1,272.0 increase in total consumer surplus in your Summary Table 3 is a clear cut Pareto improvement in welfare?

RESPONSE:

Continuity is both a cardinal and an ordinal property of utility functions because any function that is cardinal is also ordinal. The 1,272.0 million increase in consumer surplus is a clear cut improvement in welfare. With respect to issues of Pareto optimality, please see my response to GCA/USPS-T-78.

RESPONSES OF POSTAL SERVICE WITNESS BERNSTEIN
TO INTERROGATORIES OF GCA

GCA/USPS-T41-86 Please refer to your response to GCA/USPS-T41-52. You state that the total demand for a mail product that you measure is "the sum of the individual mailer demands".

a. Would you agree that what underlies individual mailer demands are individual utility functions as you seem to imply in your response to GCA/USPS-T41-50?

b. If your response to a. is in the affirmative and if these individual utility functions are cardinal utility functions, can you state that the $1,272.0 increase in total consumer surplus in your Summary Table 3 is a clear cut Pareto improvement in social welfare?

RESPONSE:

a. Yes.

b. The overall gain in consumer surplus is clear cut to me. With respect to issues of Pareto optimality, please see my response to GCA/USPS-T-78.

RESPONSES OF POSTAL SERVICE WITNESS BERNSTEIN
TO INTERROGATORIES OF GCA

GCA/USPS-T41-87 Please refer to your response to GCA/USPS-T41-53. Would you agree that some of the individual mailers in your analysis are not individual consumers in households but very large mailer organizations, e.g. publishing houses or public utilities, whose cost to mail monthly bill may be as much as 50% of the total cost of generating the bill? If you agree, is it not true that your use of uncompensated rather than compensated demand curves could have more than a "trivial" adverse impact on such organizations?

RESPONSE:

The relevant issue is not postage expenditures as a share of total cost of generating a bill, but *the change* in postage expenditures as a share of *total income* (or operating revenue in the case of a business). For most consumers, including most businesses, the change in postal expenditures is a small portion of total income. Certainly, there may be some businesses where this change is more than trivial, but overall, across all consumers whose demands make up the market demand curve, I think the impact is extremely small.

For example, within First-Class letters, there is a $2.6 billion reduction in consumer surplus at the Ramsey prices as opposed to the R97-1 Index prices. The compensated demand curve would essentially be the demand for letter mail that would result if First-Class letter mailers, as a group, were given $2.6 billion to compensate them for the loss of consumer surplus due to the price rise. The difference between the compensated and uncompensated demand curves for letters reflects the change in letter volume that results from the $2.6 billion of income compensation. Thus, the relevant question is: what fraction of this $2.6 billion of income compensation would be spent on additional First-Class letters? Very little, since expenditures on First-Class letter mail represent a small portion of the income of First-Class letter mailers. Even if mailers spent one percent of this $2.6 billion of income compensation on additional

letters, that would only represent $26 million of additional letter demand, or about 70 million pieces. Therefore, under this hypothetical, the consumer surplus calculation would take account of the consumer surplus impacts of an additional 70 million pieces of First-Class letter mail. Given that the total volume of letters is about 100 *billion* pieces, I think it is fairly obvious that the difference between the compensated and uncompensated demand curve for First-Class letters is quite small.

RESPONSES OF POSTAL SERVICE WITNESS BERNSTEIN
TO INTERROGATORIES OF GCA

GCA/USPS-T41-88 Please refer to your response to GCA/USPS-T41-61. b. Is there a marginal cost approach to cost accounting, for example as found in a standard textbook: Cost Accounting, a Managerial Emphasis, by Charles T. Horngren and George Foster?

RESPONSE:

The use of accounting costs to derive marginal costs was a topic of the testimony of Dr. John Panzar in the R97-1 case (USPS-T-11). Please also see "On Setting Prices and Testing Cross-Subsidy with Accounting Data," by Michael Bradley, Jeff Colvin, and John Panzar, *Journal of Regulatory Economics, 16:83-100 (1999).*

DECLARATION

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

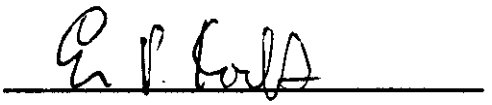
(Signed)

4-10-00

(Date)

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.



Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260–1137
(202) 268–2992 Fax –5402
April 12, 2000