

BEFORE THE
POSTAL RATE COMMISSION

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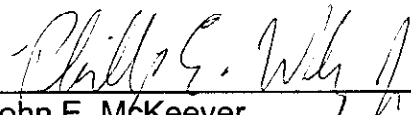
POSTAL RATE AND FEE CHANGES, 2000

DOCKET NO. R2000-1

ANSWERS OF UNITED PARCEL SERVICE WITNESS
DAVID E. M. SAPPINGTON TO UNITED STATES
POSTAL SERVICE INTERROGATORIES
(USPS/UPS-T6-1 through 5)
(June 22, 2000)

Pursuant to the Commission's Rules of Practice, United Parcel Service hereby files and serves the answers of UPS witness David E. M. Sappington to the following interrogatories of the United States Postal Service: USPS/UPS-T6-1 through 5.

Respectfully submitted,



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ANSWER OF UNITED PARCEL SERVICE WITNESS SAPPINGTON
TO INTERROGATORY OF THE UNITED STATES POSTAL SERVICE

USPS/UPS-T6-1 Refer to your testimony on pages 4 - 5 where you state: "High rates and large rates increases can be onerous for individual and business mailers alike, and so should be avoided whenever possible."

- a. At what level does a rate increase become "onerous"? In your answer, please explain fully what you meant by "onerous" in the quoted passage of your testimony, and what you mean by "onerous" in the general context of the postal rate proposals currently being reviewed by the Commission.
- b. Please describe fully the conditions under which you believe it is possible to avoid high postal rates and large postal rate increases.
- c. Please describe fully the conditions under which you believe it is not possible to avoid high postal rates and large postal rate increases.

RESPONSE TO USPS/UPS-T6-1:

(a) The definition of onerous is "burdensome, oppressive, or troublesome; causing hardship." *Webster's Encyclopedic Unabridged Dictionary of the English Language*, Portland House, 1989. This is the meaning of the term "onerous" as it is employed on page 5 of my testimony and as it pertains to the rate proposals currently being reviewed by the Commission.

Virtually all rate increases are "onerous" to some degree from the standpoint of mailers. That is why it is generally important to insist on credible demonstrations of harm by mailers, rather than unsubstantiated assertions, before reducing an otherwise appropriate rate increase. The extent of the hardship that a rate increase causes

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should be weighed, and that typically varies with the circumstances of individual mailers, including their income, the value they derive from the Postal Service product in question, and the terms on which they can secure alternative delivery services. In taking into account whether to moderate an assertedly onerous increase, it should be remembered that when one rate increase is moderated, another rate increase must be augmented.

(b)-(c) High rates and large rate increases for Postal Service products can be avoided when the Postal Service's costs and cost increases are low. High rates and large rate increases are difficult to avoid when the Postal Service's costs and cost increases are high.

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USPS/UPS-T6-2. Refer to your testimony on page 5 where you state: "Rates that disadvantage competitors unfairly should be avoided." Do you believe that rates giving an advantage to the Postal Service's competitors ever should be encouraged? If so, under what conditions?

RESPONSE TO USPS/UPS-T-6-2:

Rates should be set in accordance with the nine criteria specified in § 3622(b) of the Postal Reorganization Act. While these criteria do not include "giving an advantage to the Postal Service's competitors," they do guard against imposing an unfair disadvantage on competitors in a number of ways.

First, § 3622(b)(3) requires that each Postal Service mail subclass generate sufficient revenue to cover its attributable costs plus a reasonable share of institutional costs. If the revenues derived from a service fall below its incremental (attributable) cost, the service will be cross-subsidized by other services. Such cross-subsidization is unfair to customers of other services who must make up the shortfall in net revenue. It is also unfair to firms who supply a service in competition with the cross-subsidized Postal Service product.

Second, § 3622(b)(4) states that the effect of rate increases on "enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters" should be considered. Such consideration is appropriate in light of the many advantages that the Postal Service enjoys because of its status as a public enterprise. Some of these advantages are listed in footnote 14 on page 14 of my testimony. As

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explained there, these artificial advantages may allow the Postal Service “to drive more efficient producers from the market.” To guard against this undesirable outcome, “it is wise to ensure that each service for which the Postal Service faces competition bears a meaningful portion of institutional costs.”

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USPS/UPS-T6-3. Refer to your testimony on page 5 where you state: "When mailers can obtain comparable services at reasonable cost from suppliers other than the Postal Service, high postal rates impose few hardships on those mailers."

a. Please provide all rate tables (including published and discounted rate tables for UPS services) that demonstrate that "mailers can obtain comparable services" to Priority Mail "at a reasonable cost from suppliers other than the Postal Service."

b. Are the services provided by the United Parcel Service (UPS) comparable in all respects to the services provided by the Postal Service, including Priority Mail? If not, please explain fully.

c. Are Postal Service price levels considered in setting UPS's published rates? If so, please explain how and to what extent.

d. Does UPS compete for some customers with the Postal Service?

e. Does UPS consider the Postal Service's prices in determining what price to offer any of its customers?

f. Please confirm that if UPS considers the Postal Service's prices in determining what price to offer some customers, a 40.3% average rate increase for Priority Mail could allow UPS greater latitude to increase the prices it charges these customers. If you do not confirm, please explain fully.

g. Please confirm that a 40.3% average rate increase for Priority Mail would, all other things equal, improve the competitive position of UPS with respect to the Postal Service. If you do not confirm, please explain fully.

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RESPONSE TO USPS/UPS T6-3:

(a) UPS-LR-4 contains UPS's published rates for all of its services, including a number of services that compete with Priority Mail. I do not have any other rate schedules.

(b) The two-day and three-day delivery services offered by United Parcel Service are not identical to Priority Mail. For example, Priority Mail includes Saturday delivery in its base price, while the UPS services do not. Priority Mail may also be delivered at no extra charge on Sunday during peak delivery seasons; UPS's services do not provide Sunday delivery. The UPS products include automatic coverage for loss up to \$100, an on-time guarantee, and track and trace in their base prices, while Priority Mail does not.

(c) I do not know what factors UPS considers when it establishes its published rates.

(d) Yes.

(e) Please see my answer to part (c), above.

(f) Confirmed that a Priority Mail average rate increase of 40.3% would increase Priority Mail rates relative to UPS's current rates.

(g) Confirmed.

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USPS/UPS-T6-4. Refer to your testimony on pages 18 - 19 where you state that a higher cost coverage for Priority Mail (as compared to the systemwide cost coverage or the First-Class Mail cost coverage) is appropriate, in part, given “. . .the Commission’s long-standing emphasis on protecting users of monopoly mail services” (footnote omitted).

a. Is it your understanding that a portion of Priority Mail volume is subject to the Postal Service’s statutory monopoly? Please explain fully.

b. If so, how are these Priority Mail customers “protected” by a higher cost coverage? Please explain fully.

RESPONSE TO USPS/UPS-T6-4:

(a) Yes. Postal Service witness Mayes cites an estimate (by an unidentified source) that in 1998, “approximately one-fourth of Priority Mail volume was protected by the Private Express Statutes.” Response to APMU/USPS-T32-4(b), Tr. 11/4220. In contrast, virtually all of First Class Mail is protected by the Private Express Statutes. ODIS reports that in FY1998, less than 1% of First Class Mail consisted of packages. See USPS-LR-I-170.

(b) As noted in your question, I cite on pages 18-19 of my testimony “the Commission’s long-standing emphasis on protecting users of monopoly services.” As the accompanying footnote 15 indicates, this emphasis is on protecting users of First Class Mail, where letter mail users are much more numerous and represent a greater proportion of users compared to Priority Mail. In the passage cited in the footnote, the

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Commission states that "care must be taken to avoid unfairly penalizing First-Class Mail, which is the basic means of written personal and business communication in this country, yet is subject to a statutory monopoly."

The Senate Report on the Postal Reorganization Act reflects a similar concern with protecting the users of First Class Mail. As indicated in footnote 3 of my testimony on page 5, the Senate Report states: "The temptation to resolve the financial problems of the Post Office by charging the lion's share of all operational costs to first class is strong; that's where the big money is. The necessity for preventing that imposition upon the only class of mail which the general public uses is one of the reasons why the Postal Rate Commission should be independent of operating management." S. Rep. No. 912, 91st Cong., 2d Sess. (1970) at 13.

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USPS/UPS-T6-5. Regarding the proposals explicit or implicit in your testimony:


- a. Confirm that you are proposing a 40.3% average rate increase for Priority Mail. If not confirmed, please explain fully.
- b. Confirm that $\$3.20 * (1 + 40.3\%) = \4.49 . If not confirmed, please explain fully.
- c. Are you proposing that the Postal Rate Commission recommend that the 2-pound Priority Mail rate (currently \$3.20) increase to \$4.49? If not, what rate are you proposing for 2-pound Priority Mail pieces?
- d. Please provide a rate table showing your proposed Priority Mail rates.
- e. Please explain fully all of the rate implications of your testimony. In your response, describe each of the specific rates that you believe the Commission should recommend.

RESPONSE TO USPS/UPS-T6-5:

- (a) Confirmed.
- (b) Confirmed.
- (c) No. My testimony does not address rate design issues.
- (d) Please see my answer to part (c), above.
- (e) Please see my answer to part (c), above.

DECLARATION

I, David E. M. Sappington, hereby declare under penalty of perjury that the foregoing answers are true and correct to the best of my knowledge, information, and belief.

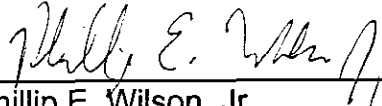


David E. M. Sappington

Dated: 6/21/00

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document by first class mail, postage prepaid, in accordance with Section 12 of the Commission's Rules of Practice.



Phillip E. Wilson, Jr.
Attorney for United Parcel Service

Dated: June 22, 2000
Philadelphia, Pa.

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