

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

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OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES

Docket No. R2000-1

**Pretrial Brief Of
KeySpan Energy**

Michael W. Hall
34693 Bloomfield Road
Round Hill, Virginia 20141
540-554-8880

Counsel For
KeySpan Energy

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Pursuant to the Presiding Officer's Ruling No. 4, KeySpan Energy ("KeySpan") hereby submits its pretrial brief. In this case, KeySpan is presenting its case-in-chief on QBRM reply mail issues through the testimony (KE-T-1) and exhibits (Exhibits KE-1A through G) of its witness, Richard E. Bentley. Mr. Bentley also sponsors two library references, KE-LR-1 and 2. Mr. Bentley is an expert witness who has testified before this Commission in numerous rate and mail classification proceedings for over twenty years.

Statement Regarding KeySpan's Interests In This Proceeding

KeySpan is engaged primarily in the distribution of natural gas and the generation of electricity. KeySpan is a large user of mail services. KeySpan Energy incurs over \$12,000,000 annually in total postal charges, primarily for customers' billing and business reply mail ("BRM").

BACKGROUND

For several years prior to the Docket No. R97-1 proceeding, all BRM service recipients who maintained advance deposit accounts and whose reply mail pieces met certain automation standards were charged a per piece fee of 2 cents. These recipients were generally referred to as BRMAS BRM recipients.

In Docket No. R97-1, the Postal Service proposed to "deaverage" the BRMAS BRM fees by (1) instituting a new type of business reply mail service, called Prepaid Reply Mail ("PRM"), for qualifying high volume business reply mail recipients with advance deposit accounts and (2) establishing Qualified Business Reply Mail ("QBRM") as the service for the remaining, lower volume BRMAS BRM recipients.

One of KeySpan's subsidiaries, The Brooklyn Union Gas Company ("Brooklyn Union") participated in the R97-1 proceeding and actively supported the Postal Service's proposal to implement the new PRM service and rate category.

In its R97-1 Opinion and Recommended Decision, the Commission

recommended approval of the new PRM service *exactly* as the Postal Service's proposed it. Docket No. R97-1, Opinion and Recommended Decision at 320-22 ("Op. R97-1"). The Commission also approved QBRM but found that the per piece fee should be set at 5 cents, not 6 cents as proposed by the Service. *Id.* at 319-320.

In June 1998, the Board of Governors took the unprecedented step of rejecting the Postal Service's own Commission-approved proposal for PRM service.¹ For high volume BRMAS BRM recipients such as Brooklyn Union, the immediate effect of the Governors' rejection of PRM was that the per piece fee they paid went from 2 cents to 5 cents (the QBRM per piece fee intended for lower volume BRMAS BRM recipients), a 150 percent increase and a patently unfair result.²

When the Board of Governors rejected PRM, the Governors directed the Postal Service to "explore further such matters as the extent to which reply mail volume should influence fees charged to different recipients."³

Introduction And Overview Of The Postal Service's QBRM Proposals

In this proceeding, the Postal Service has made a new proposal to deaverage the fees for QBRM service by instituting a new service for high volume QBRM recipients. Recipients electing High Volume QBRM service will pay a fixed fee of \$3,400 per year (payable quarterly) to recover the cost of rating and billing QBRM plus a per piece fee of 3 cents to cover the cost of counting QBRM. The Postal Service estimates that 1,358 High Volume QBRM recipients will receive 154 million pieces.

The remaining lower volume QBRM recipients would pay a higher per piece fee of 6 cents, but no separate fixed fee for the rating and billing functions.

Finally, the Postal Service recommends that the QBRM First-Class rate be raised by 1 cent, to 31 cents.

Summary Of KeySpan's Position On QBRM Issues

KeySpan generally supports the Postal Service's proposal to deaverage the fees for QBRM service by establishing separate service and fee structures for high volume

1 Decision of the Governors Of The United States Postal Service On The Recommended Decisions Of The Postal Rate Commission On Prepaid Reply Mail And Courtesy Envelope Mail, Docket No. R97-1, issued June 29, 1998 ("*Governors' PRM Decision*") at 1-4.

2 Upon rejecting the 2-cent PRM fee, the Governor's did not modify the cost analysis underlying the 5-cent fee for other QBRM. Consequently, the impact of 333.7 million low-cost qualifying PRM pieces were omitted completely from the QBRM unit cost derivation. See KE witness Bentley's response to KE/USPS-T1-1.

and low volume QBRM recipients. The overall rate structure proposed here for QBRM is very similar to the rate structure for nonletter-sized BRM that the Postal Service recently proposed, the Commission recommended, and the Governors approved.

Further, KeySpan supports the concept of establishing a separate, fixed fee for the rating and billing ("accounting") functions. The current method of recovering the costs of these functions in a single per piece assumes that all QBRM processing costs are variable in nature. Accounting function costs are not variable. Once a final count is obtained, the costs to complete the QBRM accounting function, largely clerical in nature, are essentially the same whether an account receives 1 piece, 1,000 pieces, or 10,000 pieces at a time. KE-T-1 at 5; USPS-T-29 at 14.

KeySpan also supports establishment of separate per piece fees for high volume and low volume QBRM recipients. When QBRM is received in high volumes, the Postal Service has the opportunity to employ highly efficient counting methods, such as the BRMAS system, End Of Run ("EOR") Reports, Weight Averaging Techniques, and Special Counting Machines. Conversely, when QBRM is received in low volumes, the Postal Service has fewer opportunities to employ such highly efficient counting techniques and in some cases may have to resort to inefficient manual counting. In principle, therefore, separate per piece fees allow the Postal Service to track more closely the costs that are incurred for these different types of QBRM recipients, reducing inequitable cross subsidization of low volume recipients by high volume recipients.

While KeySpan supports many features of the Postal Service's fee structure for high and low volume QBRM recipients, it strongly disagrees with the way in which the Postal Service derives the two separate per piece fees. First, instead of heeding the Governors' directive to "explore . . . the extent to which reply mail volume should influence fees charged to different recipients," the Service effectively assumes that volume has no effect on the counting methods used or the cost of counting. Second, instead of using current data that was ready-to-hand, the Postal Service witness relied upon the results of a special study called the 1997 BRM Practices Study and productivity factors developed over a decade ago for the BRMAS fee structure that combined the costs of all three functions (counting, rating, and billing) into a one-fee-fits-all per piece fee.

3. *Governors' PRM Decision* at 3.

Mr. Bentley also suggests that the QBRM First-Class rate be raised by .5 cents, to 30.5 cents.

Reproduced below is Table 1 from the testimony of KeySpan witness Richard E. Bentley. This table compares the QBRM fees proposed by KeySpan with those proposed by the Postal Service.

Table 1
Comparison Of USPS And KeySpan Proposed QBRM Fees
(Cents)

Fee Category	USPS	KeySpan
QBRM First-Class Rate	31.0	30.5
QBRM High Volume Per Piece Fee	3.0	0.5
Annual Fixed Fee	\$3,400	\$12,000
QBRM Low Volume Per Piece Fee	6.0	4.5

As Table 1 shows, the principal areas of disagreement between KeySpan and the Postal Service lie in the levels of the per piece fees for high and low volume QBRM recipients.⁴

KeySpan estimates that approximately 300 recipients will elect its High Volume QBRM service and that they will receive approximately 345 million pieces. KE-T-1 at 20; Library Reference KE-LR-1.⁵

ARGUMENT

At this juncture, there is no dispute about *whether* the existing one-fee-fits-all QBRM rate structure is inequitable and in need of change. All parties agree that it must be changed. The only remaining question is *how* to change the QBRM rate structure so

⁴ KeySpan is proposing a higher fixed accounting fee for high volume QBRM recipients. However, the level of KeySpan's proposed accounting fee does not reflect any dispute over the underlying accounting costs. KE-T-1 at 8. As explained below, KeySpan's higher accounting fee is necessary to make the breakeven volume large enough to insure that the Postal Service can count high volume QBRM efficiently.

⁵ Library Reference KE-LR-1 provides current QBRM data by account for almost all of the large accounts. As shown, there are 288 recipients who have either received more than 300,000 pieces in the past 12 months, or in FY 99.

that it is fair to all recipients. That is the central issue addressed in Mr. Bentley's testimony.

I. Derivation Of KeySpan's Proposed Fees For High Volume QBRM

A. The High Volume Per Piece Fee

KeySpan Energy proposes a .5-cent per piece fee for High Volume QBRM.

Table 2, reproduced below, shows the derivation of KeySpan's proposed per piece fee cost for High Volume QBRM.

Table 2

Derivation Of Unit Counting Cost
For High Volume QBRM
(Cents)

Counting Method	Percent	Unit Cost
BRMAS	51.6%	0.00
EOR	28.1%	0.00
Manual	11.2%	1.50
Weighing/SCM	9.2%	0.06
Total	100%	0.17

In deriving the unit cost of .17 cents per piece, Mr. Bentley uses the same unit cost that USPS witness Campbell uses for the BRMAS and EOR counting methods. For pieces counted manually and by weight conversion techniques or special counting machines ("SCM"), Mr. Bentley had to develop his own productivity factors because Mr. Campbell, improperly, had used a combined counting and sorting productivity (951 PPH) for manual counting and, further, assumed that the 951 PPH productivity applies to counting by Weighing/SCM. Mr. Bentley performed studies to determine appropriate productivity factors for counting QBRM manually and by weight conversion. See Exhibit KE-1C.

Mr. Bentley next determined the percentages that would be counted by each counting technique. During discovery, the Postal Service produced actual current data on the methods used to count QBRM received by the highest volume accounts. ***This is information that the Postal Service had at its disposal but never used in the derivation of its proposed High Volume QBRM per piece fee.*** Using this data, which

accounted for 241 million QBRM pieces or more than 50% of the QBRM universe, Mr. Bentley was able to project the volumes and percentages that would be counted by each of the counting methods for all High Volume QBRM recipients, as shown on Exhibit KE-1B.

B. KeySpan's Fixed Fee For High Volume QBRM Recipients

For the separate fixed fee designed to recover accounting costs, Mr. Bentley accepts USPS witness Campbell's monthly cost of \$232 (\$2,784 per year). However, for other reasons, he recommends that the fixed fee collect \$12,000 per year rather than \$3,400, the amount proposed by the Postal Service.⁶

KeySpan's fixed annual fee amount is higher than the Postal Service's amount because KeySpan wants to be certain that High Volume QBRM recipients will receive sufficiently high volumes each year (at least 300,000 pieces) to warrant use of the highly efficient QBRM counting methods. In addition to providing a conservative annual breakeven volume, the fee provides additional revenue that will be credited to QBRM recipients. KE-T-1 at 10.

C. KeySpan's Per Piece Fee For Low Volume QBRM Recipients

For Low Volume QBRM service, KeySpan uses the combined per piece fee approach used by the Postal Service but proposes that the fee be set at 4.5 cents per piece, rather than 6 cents as the Service proposes. Table 3, below, shows how KeySpan witness Bentley derived his 3.43 cent per piece fee cost for Low Volume QBRM.

⁶ Under KeySpan's proposal, High Volume QBRM recipients will pay \$1,000 per month. Under the Postal Service's proposal, there would be a quarterly fee of \$850. KE-T-1 at 10.

Table 3

Derivation Of Unit Cost
For Low Volume QBRM
(Cents)

QBRM Processing	Percent	Unit Cost
PERMITS Rating & Billing	46.0%	0.55
Manual Rating & Billing	44.4%	5.52
Manual Counting	48.0%	1.50
Weight/SCM Counting	7.6%	0.06
Total		3.43

Mr. Bentley accepted USPS witness Campbell's productivities and costs for the accounting (rating and billing) functions. As for the cost of counting QBRM received in low volumes, Mr. Bentley uses the same productivities for hand counting and weight conversion techniques that he developed for High Volume QBRM. See Exhibit KE-1B.

II. The Postal Service's QBRM Per Piece Fee Cost Analysis Is Flawed And Must Be Rejected

The Postal Service's QBRM per piece costs and resulting fees are based on a flawed cost analysis that overstates the cost of counting both High Volume and Low Volume QBRM. Accordingly, this analysis must be rejected by the Commission.

A very significant defect in the Postal Service's case lies in the study design utilized by the Service. That defect is most apparent in the case of High Volume QBRM but it also affects Low Volume QBRM as well. For High Volume QBRM, USPS witness Campbell correctly isolated and measured the costs associated with the rating and billing functions. Therefore, the only costs to be recovered in the High Volume per piece fee is the cost of counting QBRM. That was precisely what the Postal Service did when it developed the 1.0-cent per piece fee for counting nonletter-size BRM. However, in this instance, the Service's convoluted study design first uses a 951 PPH productivity factor for manual counting that combines counting and sorting functions and then deducts some *but not all* of the sortation costs.

A second flaw in the Postal Service's QBRM cost analysis is that the Service never studied the very question that the Governors directed them to study: whether and how QBRM processing costs are affected by the volumes recipients receive. Instead,

USPS witness Campbell made what were then counter intuitive, and now are demonstrably incorrect, assumptions that the cost of counting QBRM received in high volumes would be the same as the cost of counting QBRM received in low volumes. KE-T-1 at 13-14.

Perhaps the most significant flaw in the Postal Service's QBRM presentation is that the Service disregarded recent actual information from its own computer data systems, called the CBCIS system, that *directly* refute the BRM Practices Study its witness relied upon to determine the percentages of QBRM counted by the various counting methods. Table 4, below, compares the percentages of QBRM counted by various counting methods as reported by the CBCIS system with Mr. Campbell's survey with similar percentages taken from the 1997 BRM Practices Study.⁷

Table 4
Comparison of Percentages of QBRM Letters Counted By
Various Methods From Two Data Sources

		% Of QBRM COUNTED BY:					Total
QBRM Category	Data Source	BRMAS	EOR	SCM	Weight	Manual	
High Volume QBRM	BRM Practices Study	14%	19%	10%	9%	47%	100%
	CBCIS Data System	52%	28%	1%	8%	11%	100%
Low Volume QBRM	BRM Practices Study	14%	19%	10%	9%	47%	100%
	CBCIS Data System	21%	23%	1%	7%	48%	100%
All QBRM	BRM Practices Study	14%	19%	10%	9%	47%	100%
	CBCIS Data System	44%	27%	1%	8%	20%	100%

Among other things, this up-to-date QBRM customer specific information shows that for high volume QBRM recipients, (1) the very efficient BRMAS counting, rating, and billing

⁷ As Mr. Bentley explains (KE-T-1 at 16), USPS witness Campbell obtained volume data for 74 of the top 77 QBRM recipients and then conducted a telephone survey to determine the counting method used for each recipient. See **Exhibit KE-1D**, p. 2. Utilizing that data, Mr. Bentley estimated the percentage by counting method for all High Volume QBRM pieces; he also estimated comparable

system is much more widely used (52%) than assumed by Mr. Campbell (14%); and (2) hand counting is used much less frequently (only 11%) than the 1997 BRM Practices Study showed (47%).⁸

For all of these reasons, the Postal Service's per piece fee costs for both High Volume and Low Volume QBRM must be rejected.

III. **KeySpan's Proposed First Class Fee For QBRM**

As Table 1 shows, the Postal Service proposes a First-Class rate of 31 cents for all QBRM reply pieces while KeySpan proposes 30.5 cents. Mr. Bentley generally employed the same cost savings derivation methodology as USPS witness Campbell did with the following exceptions:

- Mr. Bentley uses the Commission's cost methodology for attributing costs whereas Mr. Campbell uses the Postal Service's proposed method which assumes that labor costs do not vary 100 percent with volume;
- Mr. Bentley uses a more stable Cost and Revenue Analysis ("CRA") proportional adjustment factor than the CRA adjustment factor witness Campbell uses; and
- Mr. Bentley credits QBRM recipients with a portion of avoided window service costs, a cost savings that Mr. Campbell did not include in his analysis.

percentages for Low Volume QBRM using the method described in **Exhibit KE-1G**.

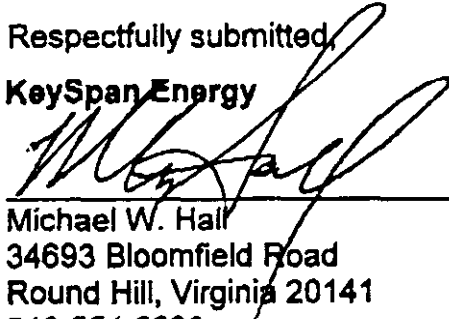
⁸ USPS witness Campbell's derived unit cost for high volume QBRM is based on a 67% manual counting percentage since he combined the percentages for Weighing/SCM with manual counting.

CONCLUSION

For the foregoing reasons, the Commission should recommend that QBRM High Volume recipients pay a monthly fixed fee of \$1,000 and a per piece fee of .5 cents. Low Volume QBRM recipients should pay a per piece fee of 4.5 cents. Finally, the First-Class rate for all QBRM recipients should be 30.5 cents.

Respectfully submitted,

KeySpan Energy

By: 

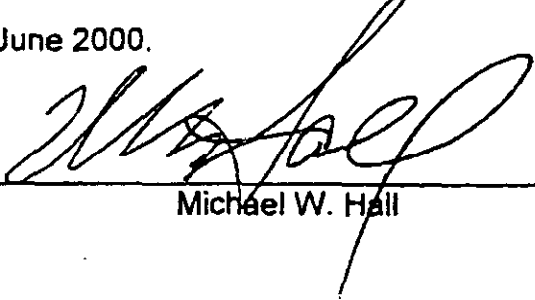
Michael W. Hall
34693 Bloomfield Road
Round Hill, Virginia 20141
540-554-8880
Counsel for
KeySpan Energy

Dated: Round Hill, VA
June 29, 2000

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all parties to this proceeding, in compliance with Rule 12 of the Commission's Rules of Practice.

Dated this 29th day of June 2000.



Michael W. Hall