

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

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Postal Rate and Fee Changes, 2000

POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY
Docket No. R2000-1

**TRIAL BRIEF OF THE
NEWSPAPER ASSOCIATION OF AMERICA**

June 29, 2000

Robert J. Brinkmann

NEWSPAPER ASSOCIATION OF AMERICA
529 14th Street, N.W.
Suite 440
Washington, D.C.
(202) 638-4792

William B. Baker
E. Joseph Knoll, Jr.
Isaac R. Campbell

WILEY, REIN & FIELDING
1776 K Street, N.W.
Washington, DC 20006-2304
(202) 719-7000

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The Newspaper Association of America ("NAA"), by its attorneys, hereby respectfully submits its trial brief in this proceeding. As in Docket No. R97-1, NAA understands the Commission's purpose in soliciting trial briefs to be "an opportunity for the parties to summarize their 'theory of the case.'"¹

For the reasons stated herein and in the testimony of its witness Dr. William B. Tye (NAA-T-1), NAA believes that the Postal Service is improperly targeting selected advertising mail for rate reductions while increasing the institutional cost burden on First Class mailers. Accordingly, the Commission should:

1. Reject the Postal Service's proposed reduction of the pound rate for ECR Standard (A) Mail, and instead raise ECR piece-rated and pound-rated rates by a common amount;
2. Reduce the grossly disproportionate institutional cost burden on First Class Mail by decreasing the gap between the institutional cost contributions of First Class and Standard A mail.

Dr. Tye's testimony expounds upon these recommendations by addressing (1) the Postal Service's failure to offer any credible justification for its proposed reduction in the pound rate for Standard A Enhanced Carrier Route ("ECR"); and (2) the excessive

¹ In addition to this trial brief, NAA expects to address these and other issues (including legal issues and rate design matters raised by intervenors) in its subsequent filings in this case.

institutional cost burden placed on First Class mail and the corresponding reduction in the relative burden borne by Standard A ECR mail. He points out that these problems in part arise from an artificial “compartmentalization” of responsibilities between the Postal Service’s pricing and rate design witnesses, which resulted in cost coverages being set without regard for the rate implications and without acknowledging effects on private firms set out elsewhere in the Postal Service’s direct case.² As a result, the Postal Service’s proposal ignores the statutory requirements that rates consider the effect on private competitors and that rational relationships exist between rates.

In addition, NAA wishes to note its concern with the large rate increases proposed for Periodicals Mail, although NAA recognizes that Periodicals Mail must bear its proper share of attributable costs. NAA does not, at this point, have a specific recommendation for the Commission, but will continue to evaluate the evidence in hopes of being able to offer an appropriate suggestion.³

I. INTRODUCTION AND SUMMARY

A. The Newspaper Association of America

The Newspaper Association of America is a non-profit organization representing more than 2,000 newspapers in the United States and Canada. Most NAA members are daily newspapers, accounting for 87 percent of the daily circulation in the United

² Nor did the Postal Service offer a witness to integrate the various components of its direct case, or even submit a trial brief to tie the pieces together.

³ It is interesting that substantial rate increases are now proposed for Periodicals mail only a few years after reclassification (with the enthusiastic support of large periodicals mailers) effectively destroyed private delivery competition for periodicals. In other contexts, cutting rates with the effect of driving out competitors, then raising rates substantially, might raise certain concerns.

States. More than 75 percent of NAA's members have circulations of 20,000 or less. As such, NAA members have a strong interest that the Postal Service, which now as ever remains a part of the federal government, and should be focusing on its public service mission of providing universal service at equitable, non-discriminatory rates.

While NAA members use all classes of mail, they most heavily use Standard Mail and , Periodical mail. However, the newspaper industry has a very strong First Class interest, for it is wholly dependent upon the Postal Service's First Class mail for the delivery of more than 90% of its income.

B. Statement of Interest

NAA's primary interest in this proceeding is in the rates to be recommended for Standard (A) Enhanced Carrier Route ("ECR") mail -- in particular, the rates for saturation mail. While newspapers make extensive use of ECR mail themselves, saturation mail advertising—as a medium— competes most directly with newspapers' run-of-press ("ROP") advertising and preprint advertising. The revenues from newspapers' advertising literally pays for the newspapers' editorial content, which enables the American public to receive news and other editorial information at a very modest price. From the largest national daily to the many suburban newspapers around our nation, ROP and preprint advertising allow newspapers to operate as the Fourth Estate, and serve as a watchdog over all levels of government. An ongoing concern of ours is that that the persistent attempts by the Postal Service to shift advertising out of newspapers and into direct mail will eventually impair the ability of newspapers to finance the editorial content on which newspaper readers across the nation depend. When newspapers lose advertising, they have no choice but to cut

editorial information. When Postal Service advertising rate reductions cause newspapers to cut editorial information, it is the American public that suffers, much more than newspapers.

Over the years, NAA member newspapers have seen the Postal Service repeatedly propose to tilt the playing field in favor of saturation mailers by either reducing, or offering smaller than average rate increases, to saturation advertising mail. The Postal Service has often accompanied such proposals with excessive allocations of institutional costs to the individual and business First Class mailers held captive to the Private Express monopoly, rather than striving to hold down these rates as much as possible.

Unfortunately, the Postal Service's proposals in this case are more of the same. Despite requesting an overall 6.4 percent rate increase, the Postal Service again proposes a below-systemwide average increase for ECR mail. Moreover, in an effort to increase the volume of heavier (more ad-filled) mail,⁴ the Postal Service proposes substantial *decreases* for much pound-rated saturation mail.⁵ At the same time, the Postal Service again is unable to resist the temptation to saddle First Class mailers with an overwhelming share of the institutional costs of the system, as is attested by the proposed increase in the relative institutional cost burden borne by First Class mail.

⁴ A recent Consumer Federation of America poll reports that the great majority of consumers are irritated by the amount of unsolicited advertising mail that they receive. See Consumer Federation of America Press Release, "Public Continues To Rate U.S. Postal Service Positively, But Opposes Deregulatory The Institution" (June 6, 2000).

⁵ One need only review the testimony of saturation mailers themselves to confirm that pound-rated saturation mail is the most competitively significant today. See Testimony of Harry Buckel (SMC-T-1) and Testimony of Roger Merriman (SMC-T-2).

See, e.g., NAA-T-1 at 26-27. This builds upon a trend in recent cases of continually placing an excessive burden on First Class mailers in order to draw advertising dollars out of newspapers.

What is particularly perverse about this situation is that, since its inception in Colonial times, one of the fundamental charges of the Postal Service has been to *help*—not hinder—the growth and development of newspapers and the expansion of the editorial content which support the American political, economic, and social institutions. That charge has remained constant throughout the Postal Service's history. The Postal Service's internal repositioning into an entity devoted to helping direct mail grow at the expense of newspapers flies in the face of this legislative charge, and is simply wrong. This Commission should not tolerate it, and should make every effort to reverse the situation.

The Postal Reorganization Act does not allow imposing a disproportionate share of the institutional cost burden on monopoly First Class mailers while targeting selected mailers with reductions in heavy-weight advertising rates. On the contrary, Section 101(a) of the Act establishes that the Postal Service is a government-provided public service. The ratemaking criteria of Section 3622(b) reinforce this public service role by directing the Commission to consider many factors which private enterprises would not take into consideration in pricing services. Accordingly, the Postal Service's proposals must be rejected as contrary to the Act's purposes as well as unsupported by record evidence.

II. THE COMMISSION SHOULD ONCE AGAIN REJECT THE POSTAL SERVICE'S PROPOSED REDUCTIONS FOR POUND-RATED STANDARD A ENHANCED CARRIER ROUTE MAIL

This proceeding marks the second consecutive omnibus rate case in which the Postal Service, despite proposing billions of dollars in rate increases, has targeted selective decreases in Standard A ECR pound-rated mail. In this case, the Postal Service's proposed reductions would begin with mail weighing 5 ounces, and the decreases get progressively steeper as weight increases. The Commission correctly rejected a similar – even larger – proposed reduction in Docket No. R97-1 as wholly unjustified. Now with the Service's revenue requirement growing steadily, there is even less reason to recommend the Postal Service's proposal. As mentioned above, this major reduction in pound rates is to NAA members the most important proposal in this case, and NAA urges the Commission to reject it as unjustified and unwarranted.

Dr. Tye identifies the numerous flaws in the Postal Service's attempted justification for the pound-rate reductions. In particular, Dr. Tye demonstrates that the "distribution key analysis" presented by USPS witness Daniel – the *only* cost evidence offered in support of the pound rate reductions -- is (1) little changed from a similar analysis that the Commission rejected in Docket No. R97-1, (2) based on unreliable data, most notably an extreme thinness of tallies, and (3) that it has been misused by rate design witnesses. The overall impression is that Postal Service witnesses use that analysis when convenient to support particular objectives, but not in a principled,

systematic basis. NAA notes that Val-Pak/Carol Wright witness Haldi also identifies a number of serious methodological flaws in the Daniel's distribution analysis.⁶

Dr. Tye further note the Postal Service's curious reluctance to admit any competitive motivations for reducing the pound rate. A comparison between the Postal Service's testimony in this case with that in Docket No. R97-1 makes this evident. Although most of the Postal Service's rationales in this case for reducing the pound rate track those offered in Docket No. R97-1, and the proposed reduction is similar, there is one striking omission. In this case, the Postal Service disavows any competitive justification – although it indisputably had attempted to justify the quite similar decrease in Docket No. R97-1 on “competitive” reasons.⁷

This is easily explained by the fact that in Docket No. R97-1 the Commission found the Postal Service's competitive motivations problematic. In Docket No. R97-1, this Commission held that “rate reductions not firmly supported by reliable cost evidence” that could adversely affect private competitors must be rejected.⁸ Here, the Postal Service apparently believes it can deflect competitive concerns by professing not to have a competitive purpose in targeting heavy-weight advertising mail alone for a rate reduction. This ruse must fail.

⁶ See VP/CW-T-1 at Appendix B.

⁷ At the same time, the Postal Service seems to have shielded its witnesses from material information that could shed light on its competitive motivations, such as the SAI analysis. NAA also has moved to compel the Postal Service to produce its current marketing plans, which could shed significant light on the Postal Service's true motivations for reducing the pound rate.

⁸ *Opinion and Recommended Decision*, Docket No. R97-1 at 403, ¶5425.

Here, not only has the Postal Service failed to offer any reliable cost evidence, but the record contains substantial evidence that the proposed pound rate reductions could cause devastating harm to the private delivery industry. NAA respectfully refers the Commission to the testimony of AAPS witness John White (AAPS-T-1), which discusses at length the threat posed by the pound rate reductions to alternate delivery firms. It is important to note that AAPS represents the interests of the private delivery industry, and not that of newspapers. While some of AAPS' members are owned by newspapers, that is not unusual among participants in postal rate cases.⁹

In addition, the Postal Service's own testimony indicates that reducing the pound rate would shift advertising from newspapers to direct mailers with which they compete. Dr. Tolley's volume forecasting formulas expressly use a cross-elasticity between postal volumes and newspaper advertising rates. Dr. Tye notes that a substantial amount of the volume increase in ECR mail in the recent few years is due to the relative decline in the real pound rate over the prices of private firms. NAA-T-1 at 45.

Although the Postal Service purports to disclaim any competitive purpose behind its proposed pound rate reductions, the chorus of support for reducing the pound rate filed by self-interested saturation mailers and their constituencies amply attests to the competitive nature of the proposal. The testimony of Mr. Buckel (SMC-T-1) and Mr.

⁹ NAA members also own members of the Agricultural Publishers Association, the American Business Media, the Association for Postal Commerce, the Association of American Publishers, the Direct Marketing Association, the Magazine Publishers of America, MASA, and the National Newspaper Association. Of the individual companies that have intervened, NAA members own Carol Wright, Conde Nast, Hearst Magazines, Cox Consumer Sampling, and Val Pak. As is obvious from this list, each company subdivision generally pursues its own interest. Dow Jones, Knight-Ridder, and McClatchy are also NAA members.

Merriman (SMC-T-2), as well as the testimony of AISOP witnesses Smith (AISOP-T-1) and Baro (AISOP-T-2), provide descriptive testimony that argue in support of the Postal Service's reduced ECR pound rate for saturation mail, the category of mail that they principally use. However, they provide no independent cost or economic analysis for the rate reduction.

As noted above, the Commission rejected a Postal Service proposal to reduce the pound rate in Docket No. R97-1, retaining the ECR pound rate at the 66.3 cents level it remains today. Consequently, the carrier route pound rate has not changed since the current rate, set in Docket No. MC95-1, was implemented in July 1996. As Dr. Tye points out, the pound rate therefore has steadily declined in real terms since that time. NAA-T-1 at 47-50. Accordingly, NAA submits that it is appropriate for the pound rate to increase. Dr. Tye's testimony recommends, given the absence of any reliable evidence for a different result, that the Commission raise the undiscounted piece and pound rates in Standard A ECR mail by a common amount.

III. TO REDUCE THE BURDEN ON FIRST CLASS MAILERS, THE REAL CONTRIBUTION PER PIECE OF STANDARD A ECR MAIL SHOULD EQUAL OR EXCEED THE UNIT CONTRIBUTION OF ECR MAIL SET IN DOCKET NO. R97-1

For many years, the Postal Service has assigned a disproportionate share of institutional costs to First Class Mail, which is captive to the postal statutory monopoly. These assignments have been disproportionate whether stated in terms of (1) absolute dollars, (2) relative percentage of revenues compared to percentages of volume or weight, or (3) unit (per-piece) contributions in cents per piece. This trend has worsened in recent cases. The net result is that advertising mail generally, and ECR mail in

particular, accounts for a substantially smaller share of both revenue and institutional cost contributions than its proportion of volume or weight. This misallocation of institutional costs harms the very mailers the postal monopoly and the Commission are to protect, has competitive consequences, and results in less editorial information being delivered to the American public.

Several witnesses have submitted testimony demonstrating that First Class mailers pay an excessive share of institutional costs, regardless of how it is measured. For example, Dr. James Clifton (ABA/NAPM-T-1) demonstrates that the gap between the cost coverages of First Class mail and both Standard A Regular and ECR mail have widened in recent years when measured by either the cost coverage index or by comparison to the systemwide average (ABA/NAPM-T-1 at 59). Dr. Clifton also shows that the contributions from First Class mail has soared since 1994, increasing by some \$5 billion while Standard A ECR's total contribution has inched up by a comparatively trivial \$375 million. ABA/NAPM-T-1 at 61.

Mr. Bentley, testifying on behalf of the Major Mailers Association, notes that the institutional cost burden on First Class mailers has risen steadily over the past few years. He also provides, as Table 3 of his testimony, a chart which presents the following comparisons using the USPS's proposed rates:

	<u>First Class</u>	<u>Standard (A)</u>
Percent of volume variable costs	45	23
Percent of total inst. costs	66	17
Unit inst. cost contribution	.1608	.0568

Furthermore, the testimony of Mr. Callow, for the Office of the Consumer Advocate, shows that the problem in reality has turned out worse than forecasted, for the *actual*

institutional cost contributions of First Class mail have turned out to greatly exceed the Commission's recommended contributions. See OCA-T-6 at 10-14.

The Postal Service in this case largely attempts to justify the relative reduction in Standard A ECR contribution on the basis of that subclass's allegedly high cost coverage.¹⁰ Cost coverages, however, are not mentioned in the Section 3622(b) criteria. Moreover, as the Commission recognized in Docket No. R97-1 and as Dr. Tye explains, high cost coverages for highly workshared subclasses are not anomalous or even troubling, but are simply the mathematical consequence of worksharing. For precisely this reason, the Commission in Docket No. R97-1 stated that it would de-emphasize the role of cost coverages for heavily workshared mail, stating that it "will continue to review the adequacy of contributions from subclasses [notably ECR] that heavily rely on functions which account for a large share of the institutional costs of the Postal Service." *Opinion and Recommended Decision* at 259, ¶ 4086.

Consequently, NAA urges the Commission to place greater reliance on the unit contributions of heavily workshared mail, including First Class and Standard A ECR. Based on the testimony of Dr. Tye, NAA recommends that the Commission set ECR rates so that the real contribution per piece, measured on the basis of a costing methodology consistent with Docket No. R97-1, equals or exceeds that recommended by the Commission in Docket No. R97-1, and that the cost coverage or markup indices do not decline in absolute or relative terms.

¹⁰ As Dr. Tye notes, the testimony of the Postal Service's pricing witness in this case (Ms. Mayes) often tracks word for word that of the corresponding witness in Docket No. R97-1 (Dr. O'Hara), but is offered to support much different cost coverages. See NAA-T-1 at 33-34.

These proposals are fully consistent with the Commission's repeated statements that it wants to bring the contributions of First Class Mail and advertising mail closer together. For example, in Docket No. R90-1, the Commission found that "we do not consider it to be consistent with the Act to shift an excessive proportion of the institutional cost burden onto First-Class (or any other) mailers."¹¹

In addition to Dr. Tye's proposal to adjust upwards the institutional cost contribution of Standard A ECR mail, the Commission has received several other reasonable proposals for reducing the institutional cost disparity between Standard (A) mail and First Class mail. Mr. Callow, on behalf of the OCA, testifies that the Commission should recommend retention of the current 33 cent single piece First Class letter rate. MMA witness Bentley is strongly sympathetic to the same proposal, although his specific recommendations concern other First Class rates. On behalf of the ABA/NAPM, Dr. Clifton proposes to reduce the institutional cost burden on First Class extra ounce mail.

The testimony of Dr. Tye, Dr. Clifton, Mr. Callow, Mr. Bentley and Mr. White take issue with the assignment of institutional costs proposed by USPS witness Mayes. Taking the opposing view – that competitive classes should pay less institutional costs, thereby forcing monopoly mailers to pay higher rates by virtue of the nature of the ratemaking system—are testimony of witnesses sponsored by direct mailers seeking no end other than lower prices for themselves, such as Dr. John Haldi (VP/CW-T-1), Mr.

¹¹ *Opinion and Recommended Decision*, Docket No. R90-1 at IV-34, ¶¶ 4107; see also *Opinion and Recommended Decision*, Docket No. R97-1 at 275-76, ¶ 5047; *Opinion and Recommended Decision*, Docket No. R94-1 at IV-15, ¶¶ 4040-41; *Opinion and Recommended Decision*, Docket No. R87-1 at 367.

Buckel (SMC-T-1), Mr. Merriman (SMC-T-2), Mr. Smith (AISOP-T-1), and Mr. Baro (AISOP-T-2), who generally support the Postal Service's institutional cost allocations.

IV. CONCLUSION

The Newspaper Association of America respectfully urges the Commission (1) to reject the unjustified and competitively motivated reduction in the pound rate, and (2) to improve the institutional cost assignments by using a measure of costs appropriate for today's worksharing environment and by relieving the burden on First Class mail.

Respectfully submitted,

NEWSPAPER ASSOCIATION OF AMERICA

By: 

William B. Baker
E. Joseph Knoll
Isaac R. Campbell


Robert J. Brinkmann
NEWSPAPER ASSOCIATION OF AMERICA
529 14th Street, N.W.
Suite 440
Washington, D.C.
(202) 638-4792

WILEY, REIN & FIELDING
1776 K Street, N.W.
Washington, DC 20006-2304
(202) 719-7000

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the instant document on all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

June 29, 2000



William B. Baker