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POSTAL RATE AND FEE CHANGES, 2000

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TRIAL BRIEF

OF

PARCEL SHIPPERS ASSOCIATION

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TABLE OF CONTENTS

I. THE POSTAL SERVICE HAS OVERSTATED ITS REVENUE REQUIREMENT IN THE TEST YEAR.

While the Postal Service has asked for a 6.4% increase to cover an anticipated $3.68 billion deficit, in fact, the actual estimated deficit is only $1.7 billion. The other $2 billion is intended to cover adverse contingencies that cannot be anticipated and to amortize the recovery of prior losses. (Zimmermann, p. 7) The Service has failed to offer an explanation of why, after successfully operating in the black over the last two rate cycles with rate increases less than the rate of inflation, it is now necessary to request rate increases that are twice the rate of inflation. The Postal Service's estimated costs for FY 2000 and 2001 are cumulatively 2.7% greater than the estimated CPI-W for those two years. (Zimmermann, p. 8) The fact that the Postal Service was able to operate in the black in the previous two rate cycles with rate increases 5% less than inflation is, itself, proof that the Postal Service does not need increases that greatly exceed the rate of inflation. (Zimmermann p. 8) The contingency request should be reduced by $1 billion, which would produce rate increases much more in line with the expected rate of inflation in the economy. (Zimmermann, p. 8)

II. COMPETITION IN THE PARCEL SHIPMENT MARKET.

A viable Postal Service is an indispensable ingredient in the maintenance of competition in the Parcel Shipment Market. (Zimmermann, p. 9) The over 1 pound parcel market, excluding Bound Printed Matter and Books, shows that UPS's share was over 78%, and the Parcel Post share was only 10.4%. (Zimmermann, p. 10)

Because of the regulatory constraints, Parcel Post is singularly handicapped in attempting to compete with the negotiated incentive rates offered by UPS, the principal Parcel Post competitor. (Zimmermann, p. 11)

In the application of Criterion 4 of The Act, the important consideration is competition, not the impact on individual competitors. That Criterion argues for Parcel Post rates that will further competition and not shield the dominant competitor. (Zimmermann, p. 12) United Parcel Service is predicting substantial growth in market share and earnings for 2000, attributing these strong results to carving out new markets in the e-business and business-to-business services. It is the competitive process and not UPS that needs protection. (Zimmermann, p. 12)

III. PRIORITY MAIL AND BOUND PRINTED MATTER MAIL.

Priority Mail is becoming an increasingly important service for mail order companies. (Zimmermann, p. 13) A 15% increase for a sub-class of mail which has such high cost coverage cannot be justified except on a rationale of charging what the traffic will bear. The effect of increases of this size will be two-fold:

1. The Postal Service will lose market share to the aggressive tactics of its competition; and

2. Such high rates create an umbrella under which the competition will also be able to significantly increase rates, with consequent damage to competition and consumers. (Zimmermann, p. 13)

Bound Printed Matter is also an important rate category for a number of PSA's members. It is clear that the Postal Service has not taken into account the ESCI value of Bound Printed Matter when it proposes an 18.15% increase. (Zimmermann, p. 14)

IV. THE INCREASED SURCHARGE ON STANDARD (A) PARCELS IS UNWARRANTED.

The Postal Service has not justified the fact that they have carved out a portion of a rate category for special surcharge treatment. Standard (A) parcels are simply a component of the non-letter Standard (A) rate category. (Zimmermann, pp. 15-16) The presumed justification for such a surcharge, i.e., that it will help the remainder of the rate category avoid higher rates than would otherwise have to be paid without the surcharge, is a justification that lacks any support from the intended beneficiaries, the Standard (A) flat mailers. (Zimmermann, p. 16) This is not surprising because the mailers of those flats are the very same people who are also mailing Standard (A) parcels. (Zimmermann, p. 16)

The Postal Service has avoided the statutory rigors that must be met in order to create a new sub-class, the course of action which the Postal Reorganization Act contemplated for treating a category of mail in a separate and discrete manner. The Postal Service has avoided the various evidentiary demands and policy considerations that are required in order to establish a new sub-class by using the artifice of a surcharge. (Zimmermann, p. 16) The difficulties of creating a new sub-class should not be underestimated; in fact, depending upon how one defines sub-classification, there has arguably only been one actual reclassification in the last twenty years, that is, the adoption of a carrier route sub-class in Standard (A), after years and years of attempts to create such a sub-class.

Comparing the costs of flats and parcels is like comparing the costs of apples and oranges. While a parcel may cost 65¢ more to process than a flat in the Test Year, a parcel will also produce 45.2¢ more revenue than a flat. (Zimmermann, p. 18)

Even utilizing the Postal Service's data, the cost revenue gap for a parcel, after effectuating the proposed rate increases and the surcharge, would only be the difference between costs of 79.17¢, and revenues of 70.8¢, around a 9¢ per piece cost difference. (Zimmermann, pp. 17-18) The Postal Service's proposal of an 8¢ increase in the current 10¢ surcharge, an 80% increase, is simply disproportionate to the size of the problem. Without any increase in the surcharge whatsoever, Standard (A) parcels, according to Postal Service data would contribute 62.8¢ revenue in order to cover costs of 79.17¢, a cost coverage of about 80%. This is a coverage that compares favorably to the coverage of vast quantities of mail, for example, particular types of First-Class single piece letter mail, the volume of which is far greater than the volume of Standard (A) parcels. Given the small relative size of the Standard (A) parcel market, and the relatively small contribution this surcharge will make to mitigate the burden of coverage of Standard (A) as a sub-class, or Standard (A) non-letters as a rate category, there is no justification, under Criterion 4, for imposing an 80% increase on the users of Standard (A) parcel service. This is particularly true when the Postal Service's cost estimates are, on their face, ridiculous for certain portions of the Standard (A) parcel group, and inexplicably increased from the 1996 Base Year for all Standard (A) parcels. (Zimmermann, p. 18)

V. DELIVERY CONFIRMATION.

The Postal Service should provide free delivery confirmation for parcel delivery service, just as it does for Priority Mail. As the Postal Service itself acknowledges, the delivery confirmation service for Priority Mail generated $170 million in new revenue in its first year of use, $140 million because the Service attracted that much new Priority Mail business by offering the free service. (Zimmermann, p. 20)

The Postal Service is simply handicapping itself by not arming itself with the kind of internal information it needs to manage properly, and discouraging potential business because it is charging for a service that its competitor provides for free. (Zimmermann, p. 20) There is relatively little, if any, use of this service at the 25¢ fee; this should tell the Postal Service something. (Zimmerman, p. 19)

VI. PROPOSED INCREASES FOR OVERSIZE PARCELS.

For oversize parcels whose length and girth combined are between 108 inches and 130 inches the Postal Service has proposed extremely high rates which range up to $30.24 a piece for parcel select (drop-shipped). For all practical purposes no one is using this service because the rates are so high. These rates are based on assumed costs, which costs, in turn, are based on what the Postal Service assumes to be the average cube per oversize parcel. (Karls, pp. 2-3)

The Postal Service's assumed average cube for an oversize parcel, as corrected, is 8.04 cubic feet. However, this estimate is based on data derived from a sample that totals 64 pieces, including an intra-BMC cube estimate derived from a sample of only five pieces. (Karls, p. 3)

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The theoretical minimums and maximums for cube are 11.77 cubic feet on the extreme high side and less than 1 on the low side. It is obvious that the Postal Service's assumed average is considerably on the high side, whereas the mean of the extremes would be around 6 cubic feet. (Karls, p. 4) Given the confidence intervals of the Postal Service's own estimates, they concede that they would have to consider all possible values in the range between 6.5 and 9.5 cubic feet. (Karls, p. 4) In the real world, the average cube is quite different than the Postal Service's estimates, based on their skimpy sample. The Postal Service estimated the total volume of oversize parcels in the Test Year would be 169,000, testifying to the scant usage of this service. (Karls, p. 4) PSA member Fingerhut itself shipped a total of 522,399 oversize parcels, more than three times the Postal Service's entire estimated volume. (Karls, p. 4) Fingerhut's oversize parcel cube averaged 6.03 cubic feet in 1999, and PSA member CTC, a consolidator of parcels, and probably the largest parcel shipper, estimated an average cube of its oversize parcels to be 5.6 cubic feet. (Karls, p. 5) This is much better evidence of what the probable oversize parcel cubic foot average is. Because the oversize rates are based upon the presumed costs, which in turn, are based upon the presumed average cube, this real world lower cube of oversize parcels dictates a substantially reduced oversize parcel rate.

VII. PARCEL POST COST COVERAGE.

The Postal Service's proposed 115.1% coverage for Parcel Post is a result of current excessively high rates due to the fact that the Postal Service seriously erred in its prior estimation of the revenues and pieces of Parcel Post.

In Docket R97-1, the Postal Service, while correctly reporting estimated costs in the Test Year, underestimated the volume of Standard (B) parcels by almost 50 million, and underestimated the revenues by $124.3 million. (Zimmerman, p. 24) Using the corrected data, it means that the Before Rates cost coverage in the Test Year for Parcel Post is 122%, using Postal Service methodology, or 112.4% utilizing Postal Rate Commission costing methodology. Consequently, with no increases whatsoever, Parcel Post would have a 3.4% higher cost coverage than the Postal Rate Commission, using its own methodology, recommended in R97-1. (Zimmermann, p. 24) A zero increase in Parcel Post would still have exceeded the recommended coverage by 3.4%. (Zimmermann, p. 25) It seems clear that, had it known the true volumes and revenues, the Commission would never have recommended a 12.3% rate increase for the second most price elastic category of mail in a proceeding where the average recommended rate increase was 2.5%. (Zimmermann, p. 25)

In fact, the kind of coverage that would be expected for the second most price elastic class of mail dictates a Parcel Post rate reduction in this proceeding. It is for that reason that the Postal Service recommends overall only a 1% to 2% increase in Parcel Post. In fact, Parcel Post rates should be no more in the Test Year After Rates than they would be if Parcel Post were to have been given the average rate increase in R97-1 and the average increase in the current case, for a total combined increase of 8.9%. That would require a 4% reduction in current Parcel Post rates. (Zimmermann, p. 25)

As the Postal Service itself has stated, Parcel Post has a lower intrinsic value of service, lower delivery priority, not good security and delivery, lack of free services such as insurance tracking and confirmation, and an own price elasticity above 1.0, indicating a low economic value of service. (Zimmermann, p. 26) It is difficult to believe that had the true revenues and pieces been known that Parcel Post would have received increases larger than the systemwide average in R-97-1 or in the current rate case.

It is demonstrably the case that the history of Parcel Post declines and rises in volume have coincided with higher or lower Parcel Post rates over the last three decades. (Zimmermann, p. 26)

VIII. DROP SHIP RATES.

As a group, the DBMC, DSCF, and DDU overall rates are not proposed to increase. That is not surprising, given the fact that Parcel Post rates are higher than they should have been, because of the revenue and piece underestimates in the past.

In fact, however, there are DBMC rate cell increases that, in some cells range up to 8%. Because of the past errors there is no case to be made whatsoever for any increases in Parcel Post rates, including all drop ship rates. (page 21) Since Postal Service wage increases have exhibited more inflation than that in the general economy, the importance of avoiding labor intensive postal operations is ever more emphasized and is all the more reason for making the drop ship discounts sufficiently attractive to customers. (Zimmermann, p. 22)

The Postal Service has understated the amount of cost avoidance in DSCF and DDU because they failed to apply the normal CRA Parcel Post Adjustment Factor, even though it was elsewhere applied. (Zimmermann, p. 22) The justification for failing to make the adjustment, that, was not a well-established service and that therefore this was a conservative approach, simply does not hold water. The fact of the matter is that the Postal Service, in designing DSCF and DDU rates constrained the rates so that the effective passthrough of the modeled cost avoidance was only 80%. Because the Postal Service, out of conservatism, had not applied the CRA Adjustment Factor, and further passed through only 80% of the modeled cost avoidance, there is a doubling of the impact so that the proposed rates fail to reflect the amount of avoided costs by as much as 25%. (Zimmermann, p. 23)

IX. CONCLUSION.

The Postal Service has advanced no justification for the current or the proposed cost coverage of Parcel Post. Overall a rate reduction is dictated by historical coverage factors and the low economic value of service of Parcel Post. The current rates and the current coverage, as well as the proposed rates and coverage, are an accident of the gross errors that the Postal Service committed in estimating parcel revenues and pieces, and the Postal Service is simply declining to correct the mistakes of the past; rather USPS seems happy to have profited from them by receiving much more revenue for parcels than would have been the case had the true facts been known. At the very minimum there is no case for any increases in any of the Parcel Post rates across-the-board. Delivery confirmation should be extended free of charge to all parcels, both for competitive reasons and for the Postal Service's own information needs.

Respectfully submitted,

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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.

Timothy J. May

Dated: June 29, 2000