

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

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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES, 2000

Docket No. R2000-1

TRIAL BRIEF OF THE
RECORDING INDUSTRY ASSOCIATION OF AMERICA

Members of the Recording Industry Association of America ("RIAA") make extensive use of Standard (A) Regular rates to send their club members and other purchasers the sound recordings and videos that these consumers have bought. Many of these shipments are subject to the "residual shape surcharge" established in January, 1999. In this proceeding, the Postal Service has proposed to increase the surcharge by 180% from 10 to 18 cents per piece. RIAA contends that there is not only a "theoretical basis" for the inclusion of revenues in computing the putative cost differential between residual shaped pieces and flats in the Standard (A) subclass but that the revenue difference must, as a matter of law and equity, be taken into account in setting the residual shape surcharge in this case. Witness Glick's testimony provides the evidentiary foundation for this claim.

A. The Commission's Decision in Docket R97-1 Expressly Invited the Analysis Supplied by RIAA Witness Glick.

Although the Commission ultimately recommended the residual shape surcharge at the level proposed by the Postal Service in Docket R97-1, it

recognized that this was "only a beginning step" and that a number of issues including the proper treatment of revenue differences between flats and "residual shape" pieces in the determination of the surcharge warranted further examination. The Commission concluded that it should not "permanently rule out the use of revenues" but that "in the instant case there is not sufficient theoretical basis justifying its use." *Opinion and Recommended Decision*, Docket R97-1 at V-426 ("R-97-1 Decision"). It also held that there was need to focus on both the similarities and differences between worksharing and shaped-based differentials." R97-1 Decision at V-427. The Postal Service has made no attempt to address the issues left open by the Commission. Witness Glick's testimony explicates the questions raised by the Commission and compellingly explains why, in application to Standard (A) Regular parcels, the revenue difference between parcels and flats must be taken into account.

Witness Glick explains that the worksharing model for establishing discounts is inappropriate for determining a parcel surcharge. Rather, in determining the appropriate amount of a shape-based surcharge, the inquiry should be intended to isolate "differences resulting from shape, among other cost causing characteristics, of different recognizable types of mail pieces." His conclusion is that:

to perform the equivalent of a single 'exact piece' comparison, one must control for cost differences caused by all characteristics other than shape.

RIAA-T-1 at 2 (emphasis supplied).

In developing the estimate of cost differences, Postal Service witness Crum has controlled for some, but not all, of the relevant characteristics other than shape. He did adjust his cost estimates for the difference between parcels and flats resulting from depth of presort and depth of drop ship. The fatal flaw in his analysis as applied to Standard (A) Regular is that he "did not correct [the cost differential] for differences in weight." RIAA-T-1 at 3.

When the two shapes of mail being compared are approximately of the same weight, this omission may be reasonable or certainly not fatal. That is the case in the letter/flat differential. The same may be true for the comparison of parcels and flats if -- within a particular subclass -- the average weight of the two pieces is closely similar. However, as witness Glick points out, the average weight of a Standard (A) Regular parcel is 2.5 times greater than the average weight of a Standard (A) Regular flat. In that context, ignoring weight-related revenue effects amounts to "double charging parcels for weight-related costs." RIAA-T-1 at 3.

In short, there is not only a sound economic "theoretical basis" for taking into account the weight-related revenue differences between flats and parcels but, in the case of Standard (A) Regular mail, the failure to do so is legally indefensible. 39 USC §403(c).

B. The Revenue Contribution Issue Needs to be Considered in the Context of Other Infirmities in the Postal Service's Residual Shape Surcharge Showing.

At this stage of the proceeding there are at least three fundamental issues that reinforce the conclusions reached by witness Glick:

First, the Postal Service has not performed any fresh studies to demonstrate that shape is the dominant factor explaining the apparent difference in cost between parcels and flats. In R97-1, the Commission recognized that the Postal Service's analysis of cost causation left a great deal to be desired. Indeed, in application to Standard (A) Regular, the Commission did not rely upon that analysis at all. Rather, it pointed out that the average weight of "ECR flats and ECR parcels is essentially equal" and therefore, in the ECR subclass, the cost differential "cannot be due to differences in weight." *Decision in R97-1* at V-425. The Commission then extrapolated "to the conclusion" that the difference between flats and parcels in the Standard (A) Regular commercial subclass "must be somewhat attributable to the difference in shape." *Id.* The Postal Service has treated the cost difference between flats and parcels as entirely attributable to shape; and that is not what the Commission held. Given the absence of clear evidence that shape is the dominant cost-causing characteristic of Standard (A) Regular parcels, the Postal Service's failure to take into account the weight-related revenue differences in that subclass is fatal.

Second, In R97-1 the Commission's explicitly recognized that a single surcharge covering all Standard (A) subclasses "does not reflect the variation in

average cost or the cost differential between flats and parcels by subclass." The Postal Service in this case continues to propose a uniform surcharge for all four of the Standard (A) subclasses. Given the known differences in weight (and possibly shape) and in revenue differences between flats and parcels among the four subclasses, this is indefensible.

Third, the Commission's initiation of the 10-cent surcharge proceeded on the premise that the Postal Service could and would track the cost of residual shape pieces separately from flats and that there would be no "confusion" on this matter. R97-1 Decision at V-424. It turns out that is not the case: the Postal Service uses one definition of a residual shape piece for purposes of costing and yet another for volume and revenues. Tr. 8/3433-34; 3515-17. This issue is particularly critical in application to Standard (A) Regular residual shape pieces because some (unquantified) percentage of Standard (A) Regular parcels in fact meet the dimensional definition of a flat. This mismatch of definitions casts further doubt on the reliability of the extrapolated conclusion that shape is the predominant causative factor of cost differences between flats and parcels.

CONCLUSION

The entirety of the revenue effect analysis performed by Postal Service witness Moeller is based on FY1998 data. Since the surcharge did not take effect until after the conclusion of that fiscal year, these data are of little probative value. This is a matter that will be taken up at the appropriate time in this proceeding. There is, however, nothing in the FY1999 data that either calls into question witness Glick's explanation of why revenue differentials must be

taken into account in setting the Standard (A) Regular surcharge or cures the infirmities we have demonstrated in the Postal Service's showing.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Ian D. Volner". The signature is stylized with a large, sweeping initial "I" and a cursive "Volner".

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CERTIFICATION

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding having requested service of discovery documents in accordance with Section 12 of the rules of practice.


Ian D. Volner