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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON DC 20268-0001

POSTAL RATE AND FEE CHANGES, 2000

)
) Docket No. R2000-1
)
)

SUPPLEMENTAL TESTIMONY
OF
RITA D. COHEN
ON BEHALF OF
MAGAZINE PUBLISHERS OF AMERICA, INC.
ALLIANCE OF NONPROFIT MAILERS
AMERICAN BUSINESS MEDIA
COALITION OF RELIGIOUS PRESS ASSOCIATIONS
DOW JONES & COMPANY, INC.
THE MCGRAW-HILL COMPANIES, INC.
NATIONAL NEWSPAPER ASSOCIATION
TIME WARNER INC.

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1 **Autobiographical Sketch**

2 My name is Rita Dershowitz Cohen. My autobiographical sketch can be
3 found in my direct testimony on behalf of Magazine Publishers of America,
4 Alliance of Nonprofit Mailers, American Business Media (formerly American
5 Business Press), Coalition of Religious Press Associations, Dow Jones &
6 Company, The McGraw Hill Companies, Inc., National Newspaper Association,
7 and Time Warner Inc., whom I will refer to collectively as “Periodicals mailers.”
8 Tr. 24/11262-63 (MPA-T-1 at 1-2).

9 **I. Purpose and Scope of Testimony**

10 This testimony also is sponsored by the Periodicals mailers. It updates
11 my direct testimony, MPA-T-1, by providing Test Year After Rates (TYAR) costs
12 for Periodicals using Government Fiscal Year (GFY) 1999 as the Base Year.
13 Section II provides updated estimates of the TYAR cost savings that will result
14 from joint Postal Service/Periodicals industry efforts to reduce costs. Section III
15 discusses the updates made to Periodicals mailers-proposed costing methods to
16 incorporate GFY 1999 data. Section IV provides an update on annual
17 Periodicals Ride-Along revenues based upon the availability of actual data.
18 Section V discusses the need for a final adjustment to TYAR Periodicals costs to
19 account for differences in mail mix between the GFY 1999 Base Year for costs
20 and the Hybrid Year FY 1999 Q3 - FY 2000 Q2 Base Year for revenues. Section
21 VI discusses the appropriate contingency for the Periodicals class and estimates
22 TYAR costs by subclass. Section VII explains why a system-wide average rate
23 increase for Periodicals mail is reasonable.

24 I find that TYAR costs for Periodicals are \$1.9 billion, more than \$500
25 million less than the costs projected by Postal Service witness Patelunas (USPS-
26 ST-44). As a result, the record in this case supports a rate increase for
27 Periodicals that does not exceed the system average and certainly is in the
28 “single digits” – a goal espoused by William J. Henderson, Postmaster General
29 and CEO, United States Postal Service. See, e.g., Tr. 24/11279, fn. 1 (excerpt

1 from testimony of Postmaster General Henderson before the Subcommittee on
2 Treasury, Postal Service and General Government, U.S. House of
3 Representatives (April 4, 2000); Tr. 35/16816 (Statement of Postal Rate
4 Commission Chairman Edward J. Gleiman, characterizing testimony of
5 Postmaster General Henderson before the Subcommittee on International
6 Security, Proliferation and Federal Service, Governmental Affairs Committee,
7 United States Senate (July 13, 2000)).

8 **II. Joint Postal Service/Industry Efforts to Reduce Cost**

9 In the TYAR cost estimates that it provided in response to PRC Order No.
10 1294 (May 26, 2000), the Postal Service incorporated \$77 million in cost savings
11 for Periodicals that that will result from the joint initiatives that I discussed in my
12 direct testimony.¹ The Postal Service also incorporated additional savings for
13 Periodicals from breakthrough highway transportation productivity and from
14 increased investment in and improved performance from the flats automation
15 program. There are, however, three additional cost savings that I identified in my
16 direct testimony that the Postal Service did not incorporate into the TYAR cost
17 estimates contained in its response to Order No. 1294. The simplified roll
18 forward I present in this testimony incorporates these three additional cost
19 reduction programs that were not included by the Postal Service:

20

- 21 • **Bundle Breakage** – As described on pages 14-15 of MPA-T-1, I and
22 witnesses Stralberg (TW-T-1) and Glick (MPA-T-2) developed data that
23 demonstrate that efforts to reduce the breakage of periodicals bundles will
24 result in \$21 million in cost savings in the test year, rather than the \$15
25 million the Postal Service is now projecting for the test year – an increase
26 of \$6 million. Tr. 24/11275-11276.

27

¹ Table 1 in my direct testimony provides the savings from each initiative. Tr. 24/11264. I provided additional detail regarding these initiatives on pages 11-19 of my testimony. Tr. 24/11272-11280.

1 • AFSM 100 Correction – On page 17 of MPA-T-1, I described DMA
2 Witness Buc's (DMA-T-1) re-estimation of TYAR cost savings from
3 implementation of the flats automation program. Tr. 24/11278. The
4 Postal Service has now updated its cost savings estimates in its response
5 to Order No. 1294. Witness Buc has reviewed the Postal Service's
6 updated estimates and still finds that the Postal Service has
7 underestimated the test year cost savings from improvements in
8 automation. See DMA-ST-1. Utilizing the same methodology as in MPA-
9 T-1, I use witness Buc's updated estimates to calculate the true TYAR
10 cost savings for Periodicals. This adds \$24 million to the savings now
11 projected by the Postal Service.

12
13 • Rail Transportation – Based on analysis performed by witness Nelson,
14 MPA-T-3, my direct testimony identified \$22 million in test year cost
15 savings related to the rail and highway transportation of Periodicals. Tr.
16 24/11279-11280 (MPA-T-1 at 18-19). While the Postal Service has now
17 acknowledged highway transportation cost savings, it has not yet
18 incorporated savings from easily achievable efficiencies in rail
19 transportation. This yields \$16 million more in cost savings for Periodicals
20 than estimated by the Postal Service.

21
22 These costs savings are reflected in Exhibits 5.1 and 5.3 in library
23 reference MPA-LR-13.

24 **III. Update Costing Methods With FY 1999 Data**

25 The TYAR costs that I presented in my direct testimony reflected changes
26 in costing methods in addition to the cost savings that will result from joint Postal
27 Service/Industry initiatives. In this testimony, I update the effect of adopting
28 these costing methods on GFY 1999 and Test Year costs by subclass. The GFY
29 1999 and Test Year cost impacts by segment that result from these methods are
30 shown in library reference MPA-LR-13, Exhibits 3.1-3.4, and are summarized in

1 Table 1 below. I have also included the SAS programs used to calculate GFY
 2 1999 mail processing costs by subclass in library reference MPA-LR-12. The
 3 estimates for the impact of Periodicals mailers' proposed changes in the
 4 variability of driving time for park and loop routes and highway transportation
 5 have not been updated due to time constraints. Tr. 24/11291-93 (MPA-T-1)

6
 7
 8
 9

Table 1. Impact of Proposed Cost Attribution and Distribution Improvements on Periodicals Costs (Millions of Dollars)

Cost Segment	Base Year 1999 Cost Reductions (Without Piggybacks)
Mail Processing	\$126
City Carriers	\$59
Rural Carriers	\$9
Transportation	\$96
Total	\$290

10 Source: MPA-LR-13, Exhibits 3.1-3.4

11 **IV. Periodicals Ride-Along Revenue**

12 In my direct testimony, I noted that in Docket No. MC00-1, Postal Service
 13 witness Taufique estimated that Periodicals Ride-Along pieces would generate
 14 approximately \$10 million in annual revenue. Tr. 24/11296 (MPA-T-1 at 35).
 15 Data collected by the Postal Service indicate that, even without taking
 16 seasonality and ramp up time into account, actual Periodicals Ride-Along
 17 revenues are in line with Taufique's \$10 million estimate. Response to
 18 MPA/USPS-69. Therefore, I believe that the Commission should include at least
 19 \$10 million in Ride-Along revenue in its TYAR revenue estimate for Periodicals.

20 **V. Final Adjustments to TYAR Periodicals Costs**

21 In response to Order No. 1294, the Postal Service estimated TYAR costs
 22 by subclass using GFY 1999 as the Base Year. In response to P.O. Information
 23 Request No. 16 (July 14, 2000), the Postal Service estimated TYAR revenues by
 24 subclass using the Hybrid Year FY 1999 Q3 – FY 2000 Q2 as the Base Year. As
 25 the Postal Service indicated in its Motion of the United States Postal Service for
 26 Clarification or Reconsideration of Presiding Officer's Information Request No. 18

1 filed August 1, 2000 (Motion), using different base years is not necessarily
2 incorrect, as long as "these estimates intersect appropriately in the test year."
3 Motion at 7.

4 As the Postal Service further notes in that Motion, to ensure that the
5 estimates do intersect appropriately in the test year, "the roll forward model
6 incorporates 'final adjustments' for many subclasses permitting additional means
7 by which to more closely align costs with mail mix." Id. at 7, fn. 1. Performing
8 final adjustments to TYAR cost estimates is clearly an appropriate way to take
9 into account the cost consequences of differences in mail mix. For this reason,
10 the Postal Service correctly performed final adjustments for First-Class Mail,
11 Priority Mail, Standard (A) Mail, and Standard (B) Mail. USPS-LR-I-419.

12 The Postal Service, however, did not perform a final adjustment to its
13 TYAR cost estimates for Periodicals despite the fact that the mail mix underlying
14 the TYAR revenue estimates (the Hybrid Year mail mix) is different from the mail
15 mix underlying the TYAR cost estimates (the GFY 1999 mail mix). To correct for
16 this omission, I used the Postal Service's method to calculate a final adjustment
17 for the Periodicals Regular and Nonprofit subclasses. Using the Periodicals
18 mailers' mail processing cost avoidance model, MPA-LR-2, witness Stralberg's
19 DDU cost avoidance estimate, Tr. 24/11405, and the Postal Service's unit
20 delivery and transportation costs for Periodicals, the final adjustment for the
21 Periodicals Regular subclass reduces costs by \$31 million, and the Periodicals
22 Nonprofit final adjustment reduces costs by \$8 million. MPA-LR-13, Exhibits 7.1
23 and 8.1. For the reasons discussed above, these final adjustment reductions
24 should be made to TYAR Periodicals costs.

25 **VI. Contingency and TYAR Costs by Subclass**

26 Witness Buc describes in his supplemental testimony four reasons why
27 the contingency to accompany witness Patelunas' revised cost estimates for
28 TYAR should be less than the one percent he recommended in his direct
29 testimony. Tr. 22/9528 et seq. (DMA-T-1). He concludes that the proper
30 contingency to accompany witness Patelunas' TYAR cost estimate is one quarter

1 of one percent. I agree with witness Buc insofar as an overall level of
2 contingency is concerned.

3 Nevertheless, for reasons expressed in my initial testimony and in the
4 testimony of William Morrow, Tr. 29/543-60 (ABM-T-1), there should be no
5 contingency added to estimated Periodicals costs. Nothing that has happened
6 since the filing of that testimony, including the updating of costs and revenues,
7 detracts from witness Morrow's reasoning and conclusions. In fact, as late as
8 August 3rd, the Postmaster General wrote to the coalition of publishers and
9 stated that "we continue to look for new cost reduction opportunities" beyond
10 those reductions to Periodicals costs included in the latest updates. Letter dated
11 August 3, 2000, from Postmaster General and CEO, William J. Henderson,
12 United States Postal Service to Periodicals Rate Case Coalition (Attachment A).
13 Because I believe that this effort will succeed, I have used zero contingency in
14 my Periodicals cost estimates. Table 2 below provides TYAR costs by subclass
15 based upon this contingency, the cost reduction programs described in Section
16 II, the costing methods described in Section III, and the final adjustments
17 discussed in Section V.

18

1 **Table 2. TYAR Costs by Subclass (Dollars in Thousands)**

2

Class	Subclass	USPS	MPA
		Attributable Cost	Attributable Cost
		[1]	[2]
First-Class	Letters & Parcels	\$13,565,268	\$12,530,949
First-Class	Presort Letters & Parcels	\$5,081,634	\$4,561,869
First-Class	Private Postcards	\$543,567	\$518,665
First-Class	Presort Private Postcards	\$173,866	\$154,835
Priority Mail	All	\$3,194,542	\$2,781,406
Express Mail	All	\$467,914	\$416,881
Mailgrams	All	\$854	\$720
Periodicals	Within County	\$86,222	\$72,277
Periodicals	Regular Rate	\$1,947,554	\$1,514,239
Periodicals	Nonprofit	\$383,833	\$301,610
Periodicals	Classroom	\$14,311	\$11,027
Standard (A)	Enhanced Carrier Route	\$2,629,439	\$2,199,516
Standard (A)	Regular	\$6,512,735	\$5,618,753
Standard (A)	Nonprofit ECR	\$199,829	\$167,809
Standard (A)	Nonprofit Regular	\$1,363,390	\$1,194,867
Standard (B)	Parcels Zone Rate	\$1,077,003	\$771,074
Standard (B)	Bound Printed Matter	\$498,658	\$392,303
Standard (B)	Special Standard	\$357,987	\$288,285
Standard (B)	Library Rate	\$54,015	\$41,117
Free Mail	All	\$31,833	\$26,709
International Mail	All	\$1,570,744	\$1,488,264
Special Services	All	\$1,546,107	\$1,454,149

3 [1] Exhibit USPS-ST-44W at 1-2.

4 [2] MPA-LR-13, Exhibit 1

5 **VII. Rate Proposal**

6 The cost data required by PRC Order No. 1294 (May 26, 2000) has
 7 permitted the Postal Service to provide for the record additional cost savings that
 8 will be achieved for Periodicals. Based upon these savings, the additional cost
 9 savings described in Section II of this testimony, and the methodological changes
 10 reflected in the record, I continue to believe that the record in this case supports
 11 a rate increase for Periodicals that is no more than the system average.



August 3, 2000

Periodicals Rate Case Coalition
1211 Connecticut Avenue, Suite 610
Washington, DC 20036-2705

Dear Coalition Members:

This is in response to your June 19 letter regarding the proposed Periodicals postage rate increase. We remain committed to identifying cost savings and refining our costing methodologies in a manner that enables the Postal Rate Commission to recommend a single-digit Periodicals increase. So far, we have identified over \$170 million of changes in that effort.

I recognize the desire to obtain more cost savings. However, I cannot let this desire result in changes that would undermine the service improvements the industry and the Postal Service have worked so hard to achieve. In addition, these savings must be documented and be able to be implemented in the upcoming year as required by the rate case process.

Our efforts are by no means complete. We will continue to look for new cost reduction opportunities and work with the industry throughout the rate proceeding to ensure that our mutual objective of a single-digit increase is achieved.

Sincerely,

A handwritten signature in black ink, appearing to read "William J. Henderson".

William J. Henderson

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document upon all participants of record in this proceeding in accordance with the Commission's Rules of Practice.


James Pierce Myers

Washington DC
August 14, 2000