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

POSTAL RATE AND FEE CHANGES, 2000	:	Docket No. R2000-1

INITIAL JOINT BRIEF OF

GREETING CARD ASSOCIATION

AND

HALLMARK CARDS, INC.

Alan R. Swendiman
JACKSON & CAMPBELL, P.C.
1120 – 20TH Street, N.W.
Suite 300 South
Washington, DC 20036
(202) 457-1646 (Tel.)
(202) 457-1617 (Fax)

Counsel for Greeting Card Association

David F. Stover
2970 S. Columbus Street
Suite 1-B
Arlington, VA 22206-1450
(703) 998-2568 (Tel.)
(703) 998-2987 (Fax)

Sheldon L. Bierman
P.O. Box 338
417 Fourth Avenue
Washington Grove, MD 20880-0338
(301) 926-4786 (Tel.)
(301) 926-2680 (Fax)

Counsel for Hallmark Cards, Inc.

Dated: September 13, 2000

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES:

RULES:

STATUTES:

LEGISLATIVE HISTORY:

ADMINISTRATIVE DECISIONS:

MISCELLANEOUS:

INTRODUCTION AND STATEMENT OF POSITION

The Greeting Card Association ("GCA") and Hallmark Cards, Inc. ("Hallmark"), jointly submit this brief in support of the propositions that:

(a) The Postal Rate Commission ("Commission") should give greater recognition to the educational, cultural, scientific and informational ("ECSI") value criterion of § 3622(b)(8) for single-piece First-Class letters and greeting cards. The Commission should give equal weight to all of the non-cost factors, including § 3622(b)(8), in setting rates. The testimony of Dr. Ken C. Erickson provides evidentiary support, therefore, in setting rates and fees. Dr. Erickson's testimony also relates to Section 101(a) which directs the Commission to consider the importance of the mail in binding the Nation together, and to Section 403 which directs the Postal Service to provide adequate and efficient postal services at fair and reasonable rates, to provide types of mail service to meet the needs of different categories of mail and mail users, and to avoid undue rate discrimination among mail users;

(b) The Commission should reject the Postal Service's effort to increase the portion of institutional costs imposed upon First-Class letter mail. This effort to raise First -Class letter share of the institutional cost burden to an unprecedented level is particularly inappropriate in light of the decade-long trend of recovering shares of institutional costs from First-Class letter mail that exceed those approved by the Commission. The effort is inconsistent with considerations of fairness, of ECSI value and of the legislative purpose of postal regulation as a protection for the captive citizen mailer.

(c) The Commission, therefore, should continue to reject Ramsey pricing as a standard for postal ratemaking.

(d) The Commission should credit First-Class letter mail with the excess revenues from overpaid postage, and should rely on properly projected extra-ounce revenues in determining the adequacy of the First-Class letter rate it recommends. Most postage overpayments originate in First-Class letter mail and should be credited accordingly. The extra-ounce revenues should be estimated according to the Postal Service's initial rate filing, which reflects the past decade's experience; the Service's proposal, at a late stage in this proceeding, of a contrived reduced estimate of such revenues should be rejected. It is both untimely filed and not consistent with the historical evidence; and

(e) The Commission should reject the effort of the Postal Service to pump up its contingency provision. The Service has not provided the evidence that might reasonably justify its proposal to hike its contingency provision by 150 percent, and there is substantial evidence to the contrary. Allowing the unsubstantiated effort to hike the contingency amount would contravene the basic notion of regulatory restraint on postal rate increases: the Postal Service is not to raise rates on the basis of unexplained and unjustified subjective estimates of future costs.

Removal of the unjustified hike in the contingency allowance, proper crediting of postage overpayments, and proper estimation of extra-ounce revenues should be coupled with recognition of ECSI values for First-Class single piece letter mail and restraint on the institutional burden placed upon such mail. This matter is discussed in the final argument Section (D) of this brief.

The Greeting Card Association is a Washington, D.C.-based trade association, the members of which market approximately ninety (90%) percent of the greeting cards in the United States. In 1999, more than 6 billion greeting cards were purchased by American consumers with over $7.0 billion in retail sales. Approximately two-thirds of these cards were sent by First-Class single-piece mail and generated an estimated $1.3 to $1.6 billion in annual revenue for the Postal Service.

The Greeting Card Association represents the interests of its members and also the interests of more than ninety-five (95%) percent of American households which mail greeting cards. Greeting cards comprise approximately fifty (50%) percent of the household-to-household First-Class Mail.

Hallmark, a limited participator in the proceeding, is the Nation's largest publisher of greeting cards, most of which are sent as single-piece First-Class Mail, as well as a substantial user of First-Class Mail in its own business.

The Greeting Card Association and Hallmark each have a vested interest in the efficiency and effectiveness of the Postal Service generally, and in this rate case particularly.

ARGUMENT

A. The Excessive, and Growing, Institutional Cost Burden on First-Class Letter Mail Violates Fundamental Statutory Policies

Factual background. The institutional cost burden on First-Class letter mail has been growing. As shown by OCA witness Callow, during the past twelve years, First-Class letter mail has been carrying an increasing burden of the Postal Service's institutional costs. Also, as shown by Mr. Callow, that burden has become more prominent in recent years. (Tr. 22/10094-10167)

This growth in institutional cost burden has occurred at a time when the attributable cost of First-Class letter mail has declined. In this period, the institutional cost burden on First-Class letter mail has increased relative to the institutional cost burden on Standard (A) Regular Mail. Moreover, the actually incurred burden of institutional costs on First-Class letter mail has far exceeded the institutional cost burden intended by the Commission for such mail. By any relevant measure[1], the cost burden thrust on First-Class letter mailers violates the Act's requirement of fairness and equity in the rate schedule. 39 U.S.C. § 3622(b)(1).

In the twelve-year period FY 1988 through FY 1999, the cost coverage of First-Class letter mail rose from 162% to 197%, exceeding 200% in FY 1997 and FY 1998. After rising from 162% to 175% between FY 1988 and FY 1996, the rate of increase jumped in the late 1990's. The mark-up index for First-Class letter mail rose from 1.256 to 1.439 during the twelve year period FY 1988 through FY 1999. During the five-year period beginning with FY 1995, the mark-up index increased from 1.169 to a high of 1.439 and a still higher index is expected in FY 2000.

The cost coverage index for First-Class letter mail grew from 1.084 in FY 1988 to 1.177 in FY 1999 and is expected to be still higher in FY 2000. This index rose steadily from 1.065 in FY 1995 to 1.177 in FY 1999.

A comparison of the mark-ups actually experienced with those recommended by

---

[1] Institutional costs are those postal costs that are not attributed. The burden of those costs to a class or subclass of mail is commonly considered, in Commission proceedings, to be measured in terms of "cost coverage" - the ratio of revenues to attributable costs, or by a "mark-up" index. Such an index is calculated by dividing the percentage by which revenues exceed costs, (i.e., the mark-up), for a class or subclass of mail by the total mark-up for all mail and special services. The cost coverage index is another method of considering this burden. That index is calculated by dividing the cost coverage of a class or subclass of mail by the aggregated cost coverage of all mail. A comparison of these measures of the institutional cost burden on First-Class letter mail indicates that severely unfair burdens have been imposed upon First-Class letter mail and that these burdens will be continued if the Postal Service's proposed rate hike for First-Class letter mail is allowed. An alternative measure, unit contribution (cents/piece) also shows First-Class letter mail bearing an excessive, and increasingly disparate, burden. NAA witness Tye shows that First-Class contributes, per piece, more than twice the amount contributed by Standard A ECR (Tr. 30/14730-32) – a trend exacerbated by the Service's proposed rates.

the Commission shows that the experienced mark-ups have substantially exceeded the recommended mark-ups. This occurred in all but three of the twelve years from FY 1988 to FY 1999. (Tr. 22/10111) In that twelve-year period, the cost coverage index for First-Class letter mail exceeded the recommended index in all but two years. (Tr. 22/10112)

As the burden on First-Class letter mail has grown, so too has the gap between the mark-up indices for First-Class letter mail and Standard (A) Regular mail been growing. In the five-year period FY 1995-FY 1999, the mark-up index for First-Class letter mail rose steadily from 1.169 to 1.439 while the index for Standard (A) Regular mail declined from 1.080 to 0.828. (Tr. 22/10114). A similar comparison regarding cost coverage indices shows the same widening gap. This widening gap is evident when cost coverages and mark-up indices for First-Class letter mail and Standard (A) Regular Mail are compared to Commission recommendations. (Tr. 22/10117-18) The burden on First-Class letter mail is greater, and that on Standard (A) Regular Mail is less, than the burdens the Commission has recommended.

As reflected in the coverage and mark-up indices, First-Class letter mail has provided revenues to the Postal Service that have been greatly in excess of Commission recommendations. (Tr. 22/10121).

The systematic and unjustified imposition of institutional cost burdens upon First-Class letter mail has occurred while attributable costs of First-Class letter mail have declined and are expected to further decline. They have gone from 53% of all attributed costs in FY 1995 to 44.99% in the test year. (Tr. 11/4540-4542) The actual imposition of institutional costs on First-Class letter mail may exceed the reported numbers because of the Postal Service's efforts in this proceeding:

- to inflate costs or reduce expected revenues in response to the disclosure of errors whose correction would reduce such costs, i.e., as regards extra-ounce and oversize letter mail (discussed below);
- to neglect any serious consideration of ECSI for First-Class letter mail, and
- to promote Ramsey-type pricing.

Postal Service data may be expected to contain a distinct bias against First-Class letter mail and in favor of Standard (A) Regular Mail.

The statutory requirement of fairness and equity. To mitigate the increased and unauthorized institutional cost burden on First-Class letter mail, the Commission should invoke the first ratemaking criterion laid down in the Act: "the establishment and maintenance of a fair and equitable [rate] schedule" [§ 3622(b)(1)].

The quoted language has been part of the Act since 1970. That it is not a mere pious generality is shown by the blunt language of the Senate Committee on Post Office and Civil Service:

> The recent proposal for a 10-cent first-class stamp in order to raise sufficient revenue to balance the books of the Post Office in one single step is fair proof of that quest for catching up with costs. Most of the money in the postal system comes from first-class mail. . . . *The temptation to resolve the financial problems of the Postal Office by charging the lion's share of all operational costs to first-class is strong; that's where the big money is. The necessity for preventing that imposition upon the only class of mail which the general public uses is one of the reasons why the Postal Rate Commission should be independent of operating management.*

Postal Reorganization, S. Rep. No. 91-912 (June 3, 1970), at 13 (italics added).

Protection of the citizen mailer from gouging was thus not just a reason for reorganizing the Post Office Department; it was also a reason for instituting independent rate regulation by this Commission. Correspondingly, the Commission should halt, and reverse, the demonstrated trend toward charging the "lion's share" of institutional costs to First-Class Mail.

The Commission should take into account the institutional cost burdens actually imposed on First-Class letter mailers. As OCA witness Callow has shown, what First-Class letter mailers in fact pay toward the institutional costs of the Postal Service has often exceeded what the Commission expected them to pay. The Commission can and should bear this in mind when choosing an appropriate markup for First-Class Mail in this proceeding.

The demonstrated cultural value to recipients of greeting cards arriving through the mail also requires reduction of the First-Class markup. Fairness is, of course, a ratemaking standard that applies to all classes; in this case, it requires reduction in the markup applied to First-Class Mail. A second, independent criterion — the requirement that the Commission heed the educational, cultural, scientific, and informational ("ECSI") value of mail to the recipient[2] — applies to a limited range of classes. The Commission has traditionally applied it to classes used by books and periodicals and, in less fully articulated fashion, to First-Class Mail.

The circumstances of this case call for a fuller and more effective application of the "ECSI" criterion to First-Class Mail, as discussed below, so that its markup above attributable costs is reduced to a more appropriate level.

---

[2] 39 U.S.C. § 3622(b)(8), added to the Act by Pub. L. 94-421 (1976) after it had become apparent that the original statutory language had failed to guarantee that the intrinsic value of mail to the recipient would be recognized. See *Association of American Publishers* v. *Governors*, 485 F.2d 768, 774-775

B. The Postal Reorganization Act Requires That The Commission Consider Economic and Non-Economic Factors in Setting Postal Rates.

In developing and recommending a rate proposal, the Postal Service has as its statutory mission "to bind the Nation together through the personal, educational, literary, and business correspondence of the people" by providing "prompt, reliable, and efficient service to patrons in all areas." 39 U.S.C. § 101(a). Under this overarching policy consideration, the development of postal rates involves the application of the statutory criteria set forth in § 3622(b) of the Postal Reorganization Act ("Act"). The Commission must recommend rates and fees that will generate sufficient revenues so that total income will recover all costs, both attributable and non-attributable. The Commission allocates responsibility for recovering non-attributable costs among mail users through the application of nine specific statutory criteria and the above-referenced public policy guidelines set out in the Act. While the subsection (b)(3) criterion[3] is largely accounted for by the attribution process, the other non-cost criteria must be applied through a process of balancing *all* of these competing factors. The Commission has done this in past rate cases. The Act does not give primacy to any single factor but requires that each be given equal weight. Direct Marketing Association v. U.S. Postal Service, 778 F.2d 96, 104 (2nd Cir. 1985). Among the relevant factors is the educational, cultural, scientific and informational value ("ECSI") to the recipient of the mail in each subclass. 39 U.S.C. § 3622(b)(8).[4]

(D.C. Cir. 1973).

[3] That all classes of mail and types of mail service recover their attributable costs and make some contribution to all other costs.

[4] The most relevant of those factors are the relative value of service of these subclasses to both sender and recipient [(b)(2)], the impact of rate increases on users and others [(b)(4)], the alternatives available to the

In Docket No. R94-1, the Commission stated that "it considers the lack of alternatives available to users of the monopoly First-Class letter subclass, and the higher ECSI value of First-Class letters as important reasons for seeking to minimize the difference" in institutional-cost responsibility between First-Class and third-class mail. Opinion and Recommended Decision, Docket No. R94-1, ¶ 4037. The Commission further said that "[t]his factor [ECSI] has been interpreted to benefit second class and special rate fourth class mail. . . . [W]e recognize [ ] that this factor could have broader application . . .." Opinion and Recommended Decision, Docket No. R87-1, ¶ 4100. USPS witness O'Hara testified in the past that the Postal Service does not mean to depart from what the Commission stated in Docket R87-1 with regard to the ECSI value of First-Class Mail. In this case, USPS witness Mayes said much the same. (Tr. 11/4256-57)

The rate proposal submitted by the Postal Service gives little, if any, weight to § 3622(b)(8) and the non-economic criteria. No effort has been made to determine the value of First-Class Mail, and in particular greeting cards, to recipients.[5] The Postal Service has turned a blind eye to the special status accorded to personal correspondence from individuals that 39 U.S.C. § 101 guarantees.

Instead, the Postal Service and many intervenors focus on the mailer's view of economics and on pure market factors. In particular, the Postal Service makes an elaborate presentation on Ramsey pricing and submits a rate schedule obtained from

---

users of each subclass [(b)(5)], fairness particularly to the users of the monopoly classes [(b))(1)], and the educational, cultural, scientific and informational value to the recipient of the mail in each subclass [(b)(8)].

[5] The Postal Service did not submit any rebuttal to Dr. Erickson's testimony in this case, nor to his testimony and the survey introduced in Docket No. R97-1.

the application of its version of Ramsey pricing principles. Despite formally acknowledging the need for careful consideration of all the statutory ratemaking factors, the Postal Service has ignored or minimized the non-cost factors and has focused on a demand-rationing approach which reflects economic concepts that form only a part of the complex set of criteria Congress established for postal rates, and which fails to reflect the Postal Service's statutory mandate to foster and not ration the people's correspondence and to recognize the value of mail to recipients as well as senders.

USPS witness Mayes claims to recognize Section 3622(b)(8) and to present a balanced application of all the factors (USPS-T-32, p.12); however, she endorses the movement of rates in the direction of Ramsey prices as beneficial. (USPS-T-32, pp. 19-20; Tr. 11/4345) No studies were undertaken to measure or assess the value of mail to recipients. (Tr. 11/4255) Postal Service witness Bernstein sets forth an alternative rate schedule in which *only* his version of Ramsey principles is applied, (USPS-T-41, pp. 70-74), and which does not reflect ECSI value for First -Class Mail. (Tr. 6/2195) "Cultural value" to the recipient is subsumed by "economic value", even though Ramsey pricing as presented by the Postal Service does not consider recipients and is ill-equipped to deal with value that cannot be expressed in dollars and cents. Ramsey pricing does not recognize the non-economic value of First-Class personal letters and greeting cards to recipients.

GCA and Hallmark believe that the Commission should give equal weight to all the non-cost factors, including subsection (b)(8), and should be mindful of value to recipients. In applying § 3622(b)(8), the Commission also should give the terms of that provision, particularly the word "culture," their proper scope.

Value to American culture of greeting cards received through the mail. Dr. Erickson addresses the particular cultural significance of greeting cards that are sent through the mail. [6] Dr. Erickson concludes that these greeting cards have a high degree of cultural value to recipients. His testimony shows the cultural importance of greeting cards to American individuals and groups and how such greeting cards are part of American public cultural life. This value, which includes and transcends social and symbolic values, can be only partially known to senders. (Tr. 34/16467, 16479; Tr. 16491-94) Greeting cards sent through the mail are displayed by recipients and evidence family social connections. (Tr. 34/16490-94; 16514-15). The value of these cards to recipients is different from the cultural value of other materials such as advertising catalogues received in the mail. (Tr. 34/16469; 16472-73)

Dr. Erickson first provides an anthropological perspective on economics to shed light on the cultural value of greeting cards that are received in the mail. He notes that in this context arguments about price elasticity of goods are meaningless. Cultural values are not defined by dollar amounts. For most people, reciprocal exchange whose value cannot be measured by price has been the mainstay of social systems. For the greater period of human history, people have not used price to assess value. (Tr. 34/16435-36)

While the Postal Service simplistically suggests that the one way to measure the value of greeting cards to recipients is price, Dr. Erickson demonstrates that the value to mailers is not coterminous with the value to recipients or to our American culture. Price

---

[6] Dr. Erickson's R97-1 presentation has been filed as a Category II Library Reference, GCA-LR-1, and received into evidence. (Tr. 34/16481-82)

does not offer a complete account of a good's social or cultural value. Many goods are not bought or sold; some are given and others are exchanged. And some material goods — like greeting cards and letters — arrive in the mail without the recipient having to pay the sender or the letter carrier. The value of such things to recipients cannot be directly established with reference to the price paid for them in a market setting. However, cultural anthropologists such as Dr. Erickson have developed objective methods to account for and establish the value of these kinds of goods. (Tr. 34/16439-40) He cites a large body of recent anthropological research to demonstrate the cultural value of a greeting card sent through the mail.

Dr. Erickson shows that one way of documenting cultural value is through what is called the itinerary method. (Tr. 34/16441) Dr. Erickson traces the itinerary of a greeting card from production through use to assess the cultural value of greeting cards that are sent and received in the mail. Cultural value is transformed as a greeting card moves through its itinerary. This value or values is beyond the value measured by price. By sketching the itinerary of a greeting card, starting with its manufacture, Dr. Erickson shows how cultural meanings grow through the people who interact with it and through it up to the point at which the Commission's determination begins.
(Tr. 34/16441-44)

From design to disposal, Dr. Erickson finds that the greeting card includes, inter alia, two kinds of cultural value: social value and symbolic value. Socially, greeting cards: (1) create new relationships; (2) extend or expand those new relationships; and (3) limit or terminate relationships. (Tr. 34/16444) In addition to these three social values, greeting cards carry symbolic value, that is, they communicate ideas about those relationships in a public way. Greeting cards offer a market-based consensus of what Americans think about themselves, their families, friends, and acquaintances. (Tr. 34/16446)

Dr. Erickson addresses the cultural non-cost factors and places the term "cultural" in its proper context. He then reviews his research and survey conducted two years ago about the cultural salience of greeting cards and links them to the continued American tradition of sending greeting cards through the mail. (Tr. 34/16447) The research shows that greeting cards have a cultural life of their own, that they play roles in the celebration of American family rituals, and that greeting cards facilitate much more than me-to-you communication. In addition, the survey demonstrated that, for Americans, greeting cards are especially salient at moments of family transition or difficulty. (Tr. 34/16447-48) The survey conducted supported the conclusion that greeting cards are highly salient elements in the celebration of family rituals and that they are used to maintain and enhance social ties. He concludes that greeting cards sent through the mail have a high degree of cultural value to recipients.

Dr. Erickson points out important differences among age, gender, ethnic and income groups. The survey showed significant variation in the salience of greeting cards according to ethnicity and income. (Tr. 34/16447) For example, African-Americans attach more importance to most greeting cards at all levels than do other groups. (Tr. 34/16447) Greeting cards sent through the mail are especially important to low and middle-income groups. Decreases in greeting card receipt will have a differential impact on these groups. (Tr. 34/16448)

Since Docket No. R97-1, Dr. Erickson has continued his research on the consumption of greeting cards. His research demonstrates two new and critical features about greeting cards: their importance in display, and their importance in the social life of women. (Tr. 34/16448) The cultural value of greeting cards includes their display. This finding was set out in Dr. Erickson's testimony in Docket No. R97-1. (GCA-LR-1) Dr. Erickson's recent research as well as that of Mary Herbaugh simply reinforces this fact. This suggests an important social value. Greeting cards have more than the one-to-one exchange value measured by price paid by an individual for a greeting card. (Tr. 34/16449) Thus, the consumption stage in the itinerary of a greeting card is a time during which the non-economic value of a greeting card becomes especially evident. (Tr. 34/16450)

Research both in the United States and China shows that women are the primary senders and recipients of greeting cards. Women use greeting cards to extend and manage social relationships to thank relatives, to engage neighbors and friends, and to enculturate children in annual family rituals. (Tr. 34/16450)

Dr. Erickson concludes that decreases in the receipt of greeting cards would have a different effect according to ethnicity, income and gender. Changes in postal rates for First-Class Mail, therefore, may have a greater impact on certain segments of the American population for lower and middle-income persons, African-Americans, and women - than other segments. (Tr. 34/16451-52) (GCA-LR-1)[7] Reduction in the volume of greeting cards sent through the mails would reduce their general American cultural value and would be particularly adverse to the groups in our society who place great

[7] In contrast, the Postal Service has not conducted any studies on the effect of its rate recommendation on fixed and lower income households. (Tr. 11/4254)

value on cards. These groups' use of cards would be reduced, and they would thereby become less connected to American cultural norms. As suggested by Postal Service counsel in cross-examination, they might find themselves, in order to continue sending and receiving greeting cards for social functions that others have other means of performing, paying the increased rates that others avoid. [8]

In summary, Dr. Erickson presents anthropological testimony in support of the cultural value and nation-binding[9] role of greeting cards. He provides a context to the meaning of "cultural" and demonstrates that the term applies to much more than institutional or intellectual manifestations of "culture." His testimony, and the survey which he conducted more than two years ago, demonstrate that "culture" includes "popular" material manifestations such as greeting cards, and that greeting cards received by mail are an important part of American culture. Greeting cards have a social and symbolic value that is not entered into a traditional economic calculus. (Tr. 34/16452) Culture encompasses and transcends economics. Greeting cards have a high decree of ECSI value to recipients, and help bind the Nation together. The cultural value of greeting cards to recipients may be assessed anthropologically through objective means other than by the price paid by the sender. Section 3622(b)(8) requires that the Commission take cultural value into account in setting rates for First-Class Mail. Dr. Erickson's testimony and prior research should be applied by the Commission in setting First-Class rates.

---

[8] The possibility of this tax-like burden on women, minorities and the poor - whether coupled with their reduced receipt of greeting cards or in the alternative - raises questions regarding both fairness and the cultural effect of increased social differentiation.

[9] 39 U.S.C. § 101(a)

C. Ramsey Pricing Should Continue to be Rejected as an Approach to Postal Pricing Inconsistent with the Act and Because the Version of Ramsey Pricing Presented and Relied Upon by the Postal Service Has Serious Methodological Errors

1. Ramsey pricing is not an appropriate guide for postal ratemaking

Introduction. Much as it did in Docket R97-1, the Postal Service presents a set of Ramsey prices — fairly strict theoretically, though technically flawed — alongside the prices it is actually proposing.[10] The Service's pricing witness, Ms. Virginia J. Mayes, disclaims reliance on USPS witness Peter Bernstein's Ramsey prices, but her recommendations are not very different from his. (Mr. Bernstein calculates that his Ramsey prices produce about $14 million more "consumer surplus" than her prices. (Tr. 6/2289.)[11] She states that her testimony fully reflects relative demand (USPS T-32 at 19; Tr. 11/4252), and she considers the allocative-efficiency benefits ascribed to Ramsey pricing both important and consistent with other statutory goals. (Tr. 11/4251) She claims to have taken account of pricing criteria other than relative demand, but does not document any *independent* consideration of them. (Tr. 11/4239-42, 4254-4255, 4295) In particular, her treatment of the educational, cultural, scientific, and informational ("ECSI") value to recipients of First-Class Mail amounts merely to quoting snippets from Commission decisions[12] and declining to carry the inquiry further. (Tr. 11/4239-40, 4256-57)

Because little has changed since the Postal Service's pricing presentation in

---

[10] USPS-T41 (Bernstein; Ramsey prices); USPS-T32 (Mayes; requested prices).

[11] While claiming this small increase in "consumer surplus," Mr. Bernstein indicates a decline in consumer surplus for First-Class letters of over 1.7 billion dollars.

[12] Those in Dockets R87-1 and R94-1. She mentions GCA witness Erickson's R97-1 testimony on the cultural value of greeting cards, but does not claim to have utilized it. (Tr. 11/4243)

Docket R97-1, much that was said in the briefs submitted by Hallmark in Docket R97-1[13] bears repeating. The Service again puts forward Ramsey pricing as an ideal — despite its inappropriateness as a canon for pricing under the Postal Reorganization Act, despite its acknowledged inability to reflect statutorily pertinent non-monetary or non-quantifiable values, despite its inefficacy where externalities are present, and despite the technical deficiencies in the way it has been applied in this record. GCA and Hallmark again urge the Commission to reject it.

Not all the values the Commission must recognize are, or can be reflected in price — and thus in the mailer's demand curve. Witness Bernstein again assumes that the value of mail to the recipient is somehow "implicitly" reflected in the sender's demand curve.[14] Value (including cultural value) of mail to the recipient is, of course, a mandatory subject of consideration under § 3622(b)(8). Hence, to be responsive to the Act, Mr. Bernstein's assumption would have to include an "implicit" perception by the sender of the mailpiece's cultural value to the recipient. But Mr. Bernstein has stated that such value is not objectively quantifiable.[15] (Tr. 6/2193) GCA witness Erickson has shown that senders often do not know, or do not fully know, what value the greeting cards they mail will have to the recipients. (Tr. 22/16491, 16494.) If, therefore, this value is both objectively unquantifiable and often unknown to the sender, it makes no

[13] Initial Brief of Hallmark Cards, Incorporated, April 1, 1998; Reply Brief of Hallmark Cards, Incorporated, April 10, 1998

[14] Tr. 6/2179-80. Compare Docket R97-1, Tr. 10/5043-45, a very similar discussion by Mr. Bernstein in answer to an OCA interrogatory. The basic idea is that the mailer will weigh costs to himself against benefits to himself and to the recipient in deciding whether to mail the item. The process is assumed to be quantitative; see especially Tr. 6/2179.

[15] GCA and Hallmark agree, as has the Commission. See PRC Op. R87-1, ¶ 4007; PRC Op. R94-1, Appendix F, ¶ 154 (warning against the tendency to "give greater weight to empirically quantifiable benchmarks than to purely qualitative ones").

practical sense to treat it as subsumed in the sender's demand curve; doing so amounts to ignoring it.[16]

Ramsey pricing will not work if significant externalities exist. An externality is a cost or benefit incurred or received by a non-buyer or non-seller as a result of the transaction being priced (here, the purchase of a stamp). The cultural value of a greeting card to the recipient is an example. As the Commission has recognized, non-economic factors such as ECSI value to recipients represent externalities.[17] Ratemaking under the Act must take them into account. But a pricing scheme that focuses on the producer's (internal) marginal cost and the buyer's demand curve excludes effects of the transaction on non-parties. Ramsey pricing is such a scheme.[18] Hence, in the context established by § 3622(b) — which mandates consideration of certain externalities — it will not succeed in minimizing loss to society.

The demand-regulating function of demand pricing was critically reviewed more than 20 years ago, in *National Association of Greeting Card Publishers* v. *U. S. Postal Service,* 607 F.2d 392 (D.C. Cir. 1979). The Court said:

---

[16] This is why Mr. Bernstein's magazine subscription example (Tr. 6/2179) is irrelevant. Recipients of greeting cards, unlike magazine readers, neither pay to receive them nor have subscriptions that they may cancel in order not to receive them. Mr. Bernstein, indeed, lets the cat out of the bag when he states that the sender's decision to send a birthday card "reflects the sender's view of the value of the birthday card to the recipient." *Ibid*, italics added. See also PRC Op. R87-1, ¶ 4081, fn. 11 (value of service to recipients not necessarily determinable from prices senders are prepared to pay).

[17] PRC Op. R87-1, ¶¶ 3021 *et seq*. The Commission put the same general thought differently at id., ¶ 3018, when it recognized that the Act sets out

> . . . to produce certain effects, judged to be desirable for noneconomic reasons, by means of postal rates. Moderation of the institutional cost burden to be borne by educationally valuable material [subsection (b)(8)] is a policy whose effects are expected outside the "market" for postal services.

[18] Indeed, pure competitive pricing (prices equal to marginal cost) — a state to which Ramsey pricing represents a "second-best" — suffers from the same disability. It would "efficiently" allocate resources from the standpoint of the producer (Postal Service) and buyer (mailers) while still producing loss to society insofar as it reduced the receipt of culturally valuable mail.

> In the context of postal ratemaking . . . the dominant objective of Congress . . . was not so much the regulation of demand for postal services, as the prevention of discrimination among the mail classes.

607 F.2d at 403. Ramsey pricing, by loading institutional costs onto the least elastic mail classes - including, especially, First-Class letters[19] - frustrates this Congressional objective.

2. Witness Bernstein's version of Ramsey prices is faulty and relies upon artificial, unrealistic assumptions

Witness Bernstein testifies to prices derived using his understanding of Ramsey pricing, modified so as to provide for ECSI values for periodical mail — but not for First-Class Mail. (USPS-T41, at 85-86, 104; Tr. 6/2196-97) In addition to this selective deviation from Ramsey pricing, the prices he presents cannot be relied upon as Ramsey prices because of problems with data and with assumptions regarding price elasticities.

Inadequate marginal cost data. The postal cost data used by witness Bernstein is not adequate to the task for which it is used. Ramsey prices seek to distribute costs in excess of marginal costs among customer classes. To accomplish this task, marginal costs must be known.[20] Since such marginal costs are not available for the Postal Service, witness Bernstein relies on the Postal Service's accounting variable costs.[21] (USPS –T-41, pages 23-24; Tr. 6/2345-46) Moreover, he does this without reference to

---

[19] See Section A above, where the inequitable, and growing, disproportion in the institutional cost burden borne by First-Class was discussed.

[20] The theory requires such distribution, because an enterprise with economies of scale cannot price at marginal cost and remain solvent. Ramsey pricing is thus a "second-best" substitute for pure competitive prices — which would equal marginal cost.

[21] As long ago as Docket R84-1, the Commission expressed doubt that such costs were an adequate stand-in for marginal costs. PRC Op. R84-1, ¶ 4121.

any particular time span during which the proposed rates would be in effect. (Tr. 6/2202) Although he testifies that the marginal costs obtaining when the rate is being charged should be used, USPS-T-41 at 57, clearly the correlation between the costs he used and the marginal costs being experienced when the rates would be charged is improbable and speculative.

Elasticity data problems. Ramsey pricing seeks to charge customer groups with the costs in excess of marginal costs on the basis of the relative demand elasticity of the respective mailer groups. To do this accurately, the own-price and cross-price elasticities must be known. (USPS-T-41 at 6, 23, 24, 47 and 49) Correct prediction of elasticities is key.

If elasticities are to be correctly predicted, factors that would cause them to change in the future must be accounted for. Here, however, witness Bernstein would use constant elasticities[22] even though the price changes that would be occasioned by Ramsey pricing would cause the demand curve of each customer to shift and elasticities to change. (Tr. 6/2361-62) The use of constant elasticities has major flaws, stemming from the difficulty or impossibility of accurately predicting demand elasticity after substantial price shifts of and among postal products, and from the mathematical necessity that the elasticity will change when the demand curve relocates in response to a price change.

For the non-linear demand curve that corresponds to the discussion during witness Bernstein's cross-examination, (Tr. 6/2362-63), a shift in the location of the demand curve (e.g., a lessening of demand) will affect the slope of that curve for any

---

[22] Tr. 6/2203-2204; Tr. 6/2350-2359.

given demand volume or price. Elasticity is the percentage change in demand volume for a percentage change in price.[23] In the standard rendition of the demand curve, as illustrated in exhibit GCA/USPS-T41-XE-1, (Tr. 6/2390), where the vertical axis, "y," represents price and the horizontal axis, "x," represents volume, elasticity is the percentage change in x percentage change in y. This relative change is determined by taking the first differential of the equation of the demand curve.[24] For the curve relevant to the discussion on cross-examination, the equation is in the form $x = y^n$ and the first differential is $dx/dy = ny^{n-1}$. Accordingly, a change in the value of y will change the value of dx/dy.[25]

Because of this mathematical fact, witness Bernstein could not explain how the slope of the curve could not change as the demand curve was relocated. (Tr. 6/2363-65) Because the slope, which determines the elasticity, must change when the demand curve moves — signaling, *e.g.*, a decline in volume — the use of constant elasticities is wrong in principle.

Witness Bernstein attempted to defend his use of constant elasticities by referring to their use by Postal Service witness Thress to predict test year after rates volumes. (Tr. 6/2203-2204). The historically-based equations fashioned by the volumes witnesses rest on the normally, fairly limited changes recommended and

---

[23] At pages 24 and 25 of his testimony, USPS-T41, witness Bernstein gives the formulae for own-price and cross-price elasticity. His formula is elasticity = (% change in volume/volume)/(% changes in price)/price.)

[24] If the demand curve is a straight line, its slope is constant but will still be changed if the post-hike demand curve is not parallel with the initial such curve.

[25] See, *e.g.*, LaTorre *et al.*, *Calculus Concepts*, (Lexington, Mass: D.C. Heath and Company, 1995), page 4-229. In the case of a straight line, Volume = a +bP where b, the slope is equal to the change in Volume divided by the change in price at a point. Elasticity then is equal to -b(Price/Volume). With each change in price, elasticity changes. Maria Moschandreas, Business Economics, 122 2nd ed. 2000

adopted in § 3622 rate-change cases. Mr. Bernstein's defense thus fails in light of the fact that the rate changes associated with witness Thress's projections are of far lesser magnitude than those that Ramsey pricing would call for, and relationships among rate categories are maintained. Such smaller rate changes may be expected to be associated with more limited changes in demand. Witness Bernstein lacks a reasonable basis for his use of constant elasticities even as a practical approximation.

Witness Bernstein's myopia regarding how demand might change as prices increase in the magnitudes his Ramsey prices would call for is reflected in his apparent inability to consider what the actual effects of cross-elasticity would be for rate differentials of the magnitude shown in his Table 11.[26]

Reaction to Perceived Unfairness. The relationship between letter mail volume and the growth of electronic communication has been projected in this proceeding to be limited, and is somewhat of a black box. Witness Bernstein fails to consider both the unfairness, and what consumer reactions might be to the unfairness, of large rate hikes developed on the basis of relative demand for postal services — if the Service were allowed to price its services on the basis of such demand while retaining its statutory monopoly over letter mail. (Tr. 6/2208) In a similar vein, he fails to recognize how the

---

[26] Table 11 is a comparison of R97-1 index and Ramsey prices:

Mail Category	Prices using R97-1 Mark-up Index	Ramsey prices
First-Class Letters	0.3442	0.3704
First-Class Cards	0.2111	0.1794
Priority Mail	4.4382	3.0037
Periodicals Non-profit	0.1881	0.2650
Periodicals Regular	0.2927	0.5482
Standard A ECR	0.1594	0.0864

value of a sum of money might vary among differently situated people (Tr. 6/2206)[27], or how businesses might react to postal price revisions. (Tr. 6/2319-21) And while urging the use of Ramsey prices to maximize "consumer surplus"[28], he neglects mail recipient values despite the requirements of § 3622(b)(8). "Consumer surplus," in other words, measures only projected benefit to purchasers of postage; hence, it cannot be the canonical measure for designing a postal rate schedule.

Allocation of Inefficiently Incurred Costs to Captive Trade. Ramsey pricing allocates non-marginal costs so that those costs are preferentially loaded onto captive customers such as those covered by the letter mail statutory monopoly. Since the *market for postal services is conditioned by the long existence of the governmental* letter mail monopoly, any own-price elasticity for letter mail derived from historic data will reflect that monopoly. Thus: (i) any inefficiency-driven losses associated with that monopoly would be reflected in Ramsey prices, and (ii) even assuming efficiency on the monopolist's part, the perceived demand for letter mail service would be distorted by the statutory monopoly.[29] Since Ramsey prices fully accept and treat as unproblematic the

---

27 In that response, witness Bernstein says that "My testimony addresses equity in that it treats all users of the mail equally. I view a dollar gained (or lost) by a user of one mail product to be equal to a dollar gained (or lost) by a user of another mail product. This consideration allows me to use the sum of the changes in consumer surpluses across different mail products as a measure of the overall impact of price changes on users of the mail."

28 Consumer surplus is defined by witness Bernstein as the increased revenue to the Postal Service less the product of the volume lost through a price hike multiplied by the differential between the price and cost per unit. USPS-T41 at page 4-5; Tr. 6/2189, 2195.

29 Once again, the Commission pointed out this problem over 15 years ago:

> . . . A fundamental question arises over the fact that some of the elasticities may not be determined independently and, in fact, may be endogenously determined by the same body that created the Postal Service. This question would not arise if the Postal Service were a complete natural monopoly. However, its monopoly position and the magnitude of the demand elasticity it faces in the supply of some of its services actually derives from the Private Express Statutes. . . .

costs, including inefficiently incurred costs, used as the basis for pricing, costs of *inefficiency will be directed by Ramsey pricing onto captive customers. This raises* grave questions regarding fairness, and regarding the proper relationship between pricing and encouraging efficiency and sound cost allocation.

Ramsey pricing — which the Postal Service advocates in this case in essentially the same terms as in Docket R97-1 — is not responsive to the requirements of the Postal Reorganization Act. Even if it were, the Service's presentation of it, through witness Bernstein, is so technically deficient that it would be an unsound guide to pricing. The Commission should continue its established policy of effectuating *all* the pricing criteria of § 3622(b) and, in particular, should not underweight the ECSI value of mail to recipients.

D. The Postal Service's Effort to Inflate Its Revenue Requirement Should Be Rejected.

The Postal Service has sought to inflate its needed contingency allowance and to underestimate its collection of extra-ounce and over-payment revenues. This effort to increase its revenue requirement is the faulty basis of the Service's request for an increase in the letter stamp rate.

1. The Postal Service has submitted an inflated request for a contingency provision

Introduction. The Postal Service has asked the Commission for a 2½ percent ($1.68 billion) contingency provision. In the last case, the requested, and recommended, contingency provision was 1% ($599.0 million).[30] Three witnesses have

---

PRC Op. R84-1, ¶ 4140.

[30] PRC Op. R97-1, Appendix C. The $599 million figure reflects Commission adjustments to the filed numbers.

provided convincing evidence that this request for 2½ percent is unreasonable and should be rejected. DMA and other parties, including GCA, sponsored the testimony of Lawrence G. Buc[31]; Office of Consumer Advocate sponsored Robert E. Burns (Tr. 22/9706-19) and Edwin A. Rosenberg (Tr. 22/9802-33). Among them, they demonstrate plainly that the Service has failed to justify its 2½-percent contingency request. The Commission should recommend a contingency provision of not more than 1%.[32]

Witness Buc and the OCA witnesses have fully justified reducing the contingency request. The three witnesses have demonstrated that the Service's requested contingency is ultimately supported only by unexplained, subjective judgments; that the concrete factors advanced by Postal Service witness Tayman[33] to justify it are largely irrelevant or are already reflected elsewhere; and that the currently foreseeable situation of the Postal Service (and the economy as a whole) fails to justify more than doubling the existing contingency provision.

GCA and Hallmark would underscore, in particular, one conclusion which is clear from Mr. Buc's testimony: that in seeking to justify the 2½-percent contingency, Mr. Tayman has engaged in extensive double counting. That is, factors already reflected in the Postal Service's data cost, volume, and revenue submissions for the test year are relied on a second time to argue for a higher contingency.

At pages 43-44 of USPS-T-9, Mr. Tayman lists seven factors that he believes

---

[31] Tr. 22/9528-58; Tr. 38/17183-17203.

[32] As Mr. Buc's Supplemental Testimony shows, if the Commission accepts the revised test year costs offered by Postal Service witness Patelunas (Tr. 38/17139-47), the contingency should be one quarter of one percent. (Tr. 38/17185-90)

could affect costs or revenues in the future:

1. Volume growth "below historical norms";
2. A requirement that FY 2000 workyears not exceed those for FY1999, while volume and delivery points continue to grow;
3. Higher health benefit and contract-driven labor costs;
4. Diversion of transaction, correspondence, and advertising mail volume onto the Internet;
5. Aggressive pursuit of legislative limitations on the Postal Service by its private sector competitors;
6. Expanded U.S. operations by foreign postal administrations;
7. Implementation of rates no earlier than January of the test year.

As Mr. Buc points out, the first three factors, on Mr. Tayman's acknowledgment, are already reflected in the rollforward (Tr. 22/9542; see Tr. 2/280). Internet diversion is reflected in the Service's volume testimony. (*Ibid.*; see Tr. 2/570 for Mr. Tayman's acknowledgment of this fact.) One may start from the well-established rule[34] that the *contingency provision is meant to cover the unknown and unforeseeable* (misforecasts and unexpected adversities not preventable by sound management), or from the common sense view that one cannot both point to a phenomenon as known (for the test year) and also claim it as unknown and indeed unknowable (for the same time period). In the first case, the factors, being known, fail to meet the established test for a proper contingency provision; in the second, they are simply double counted. In either case, it

[33] USPS-T-9.

[34] PRC Op. R76-1, at 52; PRC Op. R84-1, ¶ 1017.

is plain that these factors do not pass muster as reasons for a 2½-percent (or any other) contingency.

Similarly, the circumstance that the test year[35] will be partly over when rates are implemented was foreseeable and, presumably, foreseen. It cannot be a basis for the contingency provision.[36] This leaves standing very little of Mr. Tayman's proposed justification for a 150% increase in the contingency provision.[37]

Postal Service rebuttal (witness Strasser). On rebuttal, Postal Service witness Richard J. Strasser, Jr. (USPS-RT-1) defends the 2½-percent contingency request.[38] On the key question of whether the 2½ percent is justified, Mr. Strasser adds hardly anything to Mr. Tayman's direct testimony. (USPS-T-9) Like Mr. Tayman, he acknowledges that the 2½ percent figure was chosen judgmentally. (Tr. 46-A/2082) He observes that witnesses Buc, Burns, and Rosenberg have proceeded in the same way, and indeed objects to their arguments for this reason.[39] The use of "judgment" is a non-

---

[35] Chosen by the Postal Service; See § 54(f)(2) of the Rules of Practice, 39 CFR § 3001.54(f)(2).

[36] PRC Op. R94-1, ¶ 2043.

[37] With regard to Mr. Tayman's legislative worries, proposed or threatened legislation is not a reason for increasing the contingency provision (PRC Op. R84-1, ¶ 1055; PRC Op. R80-1, p. 36). Moreover, Mr. Tayman has not elaborated on how competitor-sponsored legislation would put "limitations on the Postal Service's ability to operate in a business-like manner." If, as is possible, he means that the Service could be restricted from entering new lines of business, then he is asking the Commission to assume that such new business ventures would improve the Service's financial position. This is not a guaranteed result. See, generally, PRC Op. R83-1. Nor should current users of traditional postal services be taxed today to compensate for the loss of future net revenues — which are entirely hypothetical — from new services. PRC Op. R80-1, ¶ 0130, fn. 2.

[38] The Service also sponsored the testimony of Dr. Zarnowitz. (Tr. 41/18135-18226) Dr. Zarnowitz presents extensive economic statistics and concludes — in highly generalized fashion — that economic instability and uncertainty are on the increase. He makes no effort to relate his interpretation to the Postal Service's situation in the test year, which is the Commission's basic concern.

[39] Mr. Strasser states:

> . . .it seems ironic that each intervenor witness who insists that judgment should not be the basis for determining the contingency has in fact used the very approach he has argued against. Each of them has considered historical data, examined forecasts and trends related to the future, and

issue: none of the three witnesses advocating a smaller contingency condemns "judgment" as such. Their objection is to Mr. Tayman's use of *unexplained, subjective* judgment, and to his use of irrelevant or double-counted "risk" factors to buttress the 2½-percent contingency request. His testimony does not refute Mr. Buc's showing that much of Mr. Tayman's claimed support for the 2½-percent contingency comes from factors already reflected in the cost and revenue estimates underpinning the filing — and hence double counted when used a second time to more than double the contingency. (Tr. 22/9540-43; Tr. 38/17186-89)

Thus, Mr. Strasser does not strengthen the Service's case. Focusing on whether circumstances are more like those in Dockets R94-1 (2% contingency) and R97-1 (1% contingency) than in earlier cases (a range of 3% to 5%), he argues that FY 2000 has been "one of the most challenging years for Postal Service managers in recent memory", (Tr. 46-A/20184-85), and that FY 2001 will likely be worse. He doubts that FY 2000 will show a positive net income, (Tr. 46-A/20185), and that inflation is higher than in Docket R97-1. *(ibid.)* [40] If this means what it appears to mean, Mr. Strasser would have the Commission recommend a drastically increased contingency in part because postal-related inflation, as demonstrated by the cost levels reflected in the requested new rates, is greater than in the previous case. Mr. Strasser, apparently, has even fewer qualms about double counting than did Mr. Tayman. He further seeks to

---

> the judgmentally determined that a lower contingency is warranted based on the facts that they have considered. . . . [Tr. 46-A/20183]

[40] Mr. Strasser contends that

> . . . the fact that overall inflationary pressures specific to the Postal Service are quite different comparing Docket Nos. R97-1 and R2000-1 is suggested by the relative magnitude of the rate increases — 2.9 percent in Docket No. R97-1, versus a proposed 6.5 percent in the current rate case. [Tr. 46A/20185]

differentiate Docket R97-1 by arguing that the present test year will see the expiration of all but one of the Service's major labor contracts. (Tr. 46-A/20186)

Mr. Strasser is thus arguing that because certain facts about costs and revenues are known today, the Service's situation in the test year is less predictable than it would otherwise be. But these facts were either known or could have been predicted when the present case was filed. As noted above, the change in cost levels between R97-1 and this case is, according to Mr. Strasser, reflected in the cost figures filed to support the request.[41] When the labor contracts would expire was, or should have been, known at all relevant times. Indeed, Postal Service witness Patelunas apparently tries to provide against possible increased labor costs in his revised rollforward.[42] The fact is that Mr. Strasser has confused a perception of coming hard times with an actual increase in uncertainty.[43] That such uncertainty will increase has not been shown, and has scarcely even been argued. This confusion leads Mr. Strasser to defend the 2½-percent contingency as though it were a remedy for uncertainty although he, like Mr. Tayman, has failed to show that it is anything more than an increment in gross revenue — based, in large part, on anticipated events already reflected in the Service's test year figures.

The Commission has the legal authority to reduce the contingency provision. Mr.

---

[41] The same will be true if the Commission uses the Service's updated base year figures.

[42] Mr. Patelunas discards the Service's customary labor cost escalation assumption of "ECI minus one" in favor of an assumed escalation equal to the ECI. (Tr. 38/17142-47) As Mr. Buc has pointed out this change — if the Commission accepts it — negates most of the justification for even a 1% contingency. (Tr. 38/17186-88) That is, of course, a quite separate issue from the question whether the change Mr. Patelunas sponsors will turn out to be a self-fulfilling prophecy.

[43] The contingency is meant to insure against (I) misestimates of test year cost and revenue and (ii) unforeseeable events that proper management cannot forestall (PRC Op. R82-1, ¶ 1017); that is, the existence of uncertainty in some degree justifies a non-zero contingency, and the amount recommended

Strasser hints that a reduction in the requested contingency might be reversible error. (Tr. 46-A/20184, 20210-11, 20214-16, 20237-38) The Court of Appeals decision he quotes but fails to cite is *Newsweek, Inc.* v. *U.S. Postal Service,* 663 F.2d 1186 (2d Cir. 1981). Since this argument is likely to emerge in the Service's brief, a short discussion of the case is in order.

Newsweek, properly read, does not bar the Commission from recommending a smaller contingency in this case. As Judge Meskill's opinion makes clear, the Commission in Docket R80-1 had cut the revenue requirement largely to force more frequent rate filings, and in that way to make Postal Service deficits more manageable. The *Newsweek* court stated:

> We . . . conclude that the PRC's recommended decision in this case, which drastically reduced the Postal Service's revenue requirements [sic], had the effect of *undermining the Board's exclusive authority in timing changes in postal rates and fees.* Thus . . . the PRC has improperly encroached upon the managerial authority of the Board.

663 F.2d at 1204 (italics added). Reducing the revenue requirement in order to compel the Board of Governors to change its rate cycle policy is, obviously, a quite different matter from finding a request unsupported by the record and modifying it for that reason.[44] The Board of Governors' "managerial authority" does not trump the statutory requirement that the recommended rates be supported by the record, nor does it permit the anticipated cost and revenue changes to be double counted so as to inflate the

---

should be related to the reasonably judged level of uncertainty.

[44] The court also remarked that "in view of the four percent contingency provision approved by the Board in the last rate case . . . we agree with the Board that the reduction of the [contingency] fund to less than half the percentage of the previous rate filing was arbitrary." 663 F.2d at 1205. Here, of course, it is the Postal Service that has proposed a drastic change from the contingency requested and approved in the last case.

contingency provision. See the analytical discussion to this effect at PRC Op. R84-1, ¶ 1028 *et seq.*, especially ¶¶ 1046-1047.

Postal Service equity. Mr. Strasser objects (Tr. 46-A/20188-89) to Mr. Buc's argument that Postal Service equity, judged by real-world standards is both more substantial than the Postal Service's books of account suggest and capable of improvement by more enterprising management of, *e.g.*, postal real estate (see Tr. 22/9567; Tr. 22/9600-9601). Insofar as the contingency provision is meant to insure the long-run financial solidity of the Postal Service, the true nature, and value, of its equity is clearly relevant to the question of the appropriate level of contingency.

The Postal Service, however, is required to measure its equity by the standard set forth in 39 U.S.C. § 2002(a):

> . . . The value of assets . . . transferred to the Postal Service upon the commencement of operations of the Postal Service shall be determined by the Postal Service subject to the approval of the Comptroller General, in accordance with the following guidelines:
>
> > (1) Assets shall be valued on the basis of original cost less depreciation, to the extent that such value can be determined. The value recorded on the former Post Office Department's books of account shall be prima facie evidence of asset value.

That is, the Service's equity — the original $1.7 billion referred to by Mr. Strasser (Tr. 46-A/20188) — is valued at depreciated original cost. (Tr. 46-A/20227, 20241-43) This is a highly conservative valuation method, as Mr. Buc's example of the L'Enfant Plaza property shows. (Tr. 22/9567) The Commission — without interfering with the Board's policy determination that original book equity be restored[45] — can, in evaluating

[45] The contingency provision, of course, is not meant as an equity-restoration mechanism.

the Service's overall financial health, take account of this fact, which shows that the real-world value of Postal Service equity is substantially higher than it appears by the depreciated original cost standard.

2. Net revenues have been underestimated by the Postal Service

Most postage overpayments occur in First-Class; they should be credited to it, and not misapplied through a last-minute postal accounting gimmick. The Postal Service has offered what is at least a partial correction of the failure in its filed case to properly account for overpayments of postage. Some $192.3 million of the total overpayments of $219.4 million are made by mailers of single-piece First-Class letter mail.

In responding to an institutional discovery request regarding the net overpayment, the Postal Service put forth, in a matter unrelated to the overpayments, a "revised" methodology for forecasting the number of additional ounces per piece for single-piece First-Class Mail. (Tr. 21/9178) While the "as-filed" Postal Service rate case shows an increase in the number of additional ounces per piece between the base year and the test year — consistent with a decade-long trend — the "revised" methodology produces a forecast that the number of additional ounces remains the same.[46] This late-appearing new method was rebutted by OCA witness Callow. (Tr. 36/16879-16900)

The "revised" methodology does not reflect the decade-long historical trend, and tries to offset most of the overpayment-related net postal revenue correction. It attempts this by proposing to reduce the net revenue for First-Class letter mail by

---

[46] The as-filed methodology has not been withdrawn by the Postal Service.

$172.2 million.

In the "as-filed" methodology, the base year ratio of additional ounces per piece for both presort letters and the First-Class letters subclass as a whole is calculated and then applied to the test year volumes of presort letters and total First-Class letter mail to derive the forecast number of additional ounces. (USPS T-7, Workpaper 4 and LR-1-122). In every year of the FY 1990-FY 1999 period, the number of additional ounces per piece of single-piece mail has increased. (Tr. 36/16887). The trend for all First-Class letters is quite similar.

The Postal Service concedes that additional ounces per piece, rather than weight per piece, more directly relates to revenue. However, increases in average weight may be expected to be reflected in additional ounces. The "revised" methodology ignores the long-term trend in additional ounces. It attempts to do this on the basis of 1998 through the third quarter of 2000 data, even though the number of additional ounces grew both in 1999 and in the hybrid year 1999-2000. (Tr. 36/16895) In spite of this fact, Postal Service witness Fronk attempts to project negative growth for 2000, and zero growth for 2001.

The revised methodology should be rejected, not only because of its neglect of 1999 and 2000 data, but also because it is a new methodology introduced only late in the course of the proceedings — without any relation to the overpayment matter being simultaneously corrected.

The benefit of the net revenue from overpayments comes from single-piece First-Class letter mail (Tr. 34/16536) and should be credited to such mail without any offset based upon the Postal Service's late filed and contrived "revised" methodology. The creation of that methodology appears to reflect the Postal Service's desire to extract additional revenues from mailers of single-piece First-Class letters, no matter what regardless of history or methodological consistency.

CONCLUSION

In this proceeding, the Commission has the opportunity, and obligation, to reject the Postal Service's effort to inflate its revenues from First-Class letter mail and to continue seeking to tax such mail with ever increasing, unfairly large portions of its non-attributed costs. The Service's unjustifiable effort to inflate its contingency allowance from the last-allowed 1% to 2.5% lacks any record support remotely commensurate with the huge sums involved, and has been shown on the evidence presented on behalf of OCA and intervenors to be uncalled for and largely an exercise in double-counting. In a similar vein of attempting to heap cost burdens on First-Class Mail, the Service, in its filed case, overlooks the revenues derived from First-Class Mail through overpayments. These revenues should be credited to First-Class. Subsequently, the Service's late filed and erroneous effort to cancel out this revenue increment by underestimating the properly anticipable level of extra-ounce revenues from First-Class Mail should, as explained by OCA witness Callow, be rejected.

After so properly establishing attributable costs and revenues, the Commission must allocate institutional costs in a manner consistent with all of the requirements of the Act. In so doing, the Commission should continue to reject the Postal Service's efforts to have reliance placed on demand-rationing Ramsey pricing, and particularly on the Service's flawed presentation of such prices. Rather, the Commission should halt and reverse the demonstrated trend towards charging the lion's share of institutional costs to First-Class Mail. This trend, with its history of actual burdens on First-Class Mail not only growing but exceeding those allowed, is totally inconsistent with the Act's requirements for fairness and equity, avoidance of rate discrimination, and respect for the value of mail to recipients.

The allocation of the costs of the Postal Service determines what is effectively taxation to support a governmental statutory monopoly. In making that allocation, the Commission should be mindful of the unfair ramifications of the Postal Service's preference to maximize the allocation of that tax to the most captive customers for its utility service. The Commission should also carefully consider the cultural value of First-Class letter mail to the American people, including especially women, minorities and those on limited and fixed incomes.

Dr. Erickson's testimony demonstrates the cultural value of First-Class Mail of which greeting cards are an important component to the American public. The testimony and previous survey results provide additional evidence that greeting cards sent through mail have a high degree of ECSI value to recipients, and help bind the Nation together under Section 101(a) by linking Americans in a shared culture through an artistic and textual medium. Section 3622(b)(8) requires that the Commission take ECSI into account in setting rates for First-Class Mail. Although the Commission has viewed ECSI largely in connection with periodicals and books, the statutory language is not limited to that category of mail or to a narrow definition of cultural. In this light, Section 403 directs the Postal Service to provide adequate and efficient postal services at fair and reasonable rates, and to meet the needs of different mail users.

The Postal Service's proposal places a disproportionate emphasis on a faulty consideration of an exercise in demand rationing. The Act requires the Commission to give full recognition and equal weight to all pricing factors not just those of a purely economic nature. The Commission should continue its traditional practice of doing so. The Greeting Card Association on behalf of its member organizations as well as the general public, and Hallmark, urge the Commission both to reject Ramsey pricing principles and to correct and reverse the trend to ever higher and disproportionate mark-ups for First-Class, and to give more weight to the "cultural value" of First-Class Mail to recipients and to § 3622(b)(8) in setting First-Class postal rates in this case.

Respectfully submitted,

Alan R. Swendiman

JACKSON & CAMPBELL, P.C.
1120-20th STREET, N.W.
Suite 300 SOUTH
Washington, DC 20036-3437
(202) 457-1646 (Tel)
(202) 457-1617 (Fax)
aswendiman@jackscamps.com

Counsel for Greeting Card Association

David F. Stover

2970 S. Columbus Street
No. 1-B
Arlington, VA 22206-1450
(703) 998-2568 (Tel)
(703) 998-2987 (Fax)
postamp@crosslink.net

Sheldon L. Bierman

P.O. Box 338
417 Fourth Avenue
Washington Grove, MD 20880-0338
(301) 926-4786 (Tel)
(301) 926-2680 (Fax)
utilpost@crosslink.net

Counsel for Hallmark Cards, Inc.

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 § 12 of the Rules of Practice.

Alan R. Swendiman
JACKSON & CAMPBELL, P.C.
1120 - 20th Street, N.W.
Suite 300 South
Washington, D.C. 20036
(202) 457-1646 (Tel)
(202) 457-1617 (Fax)
aswendiman@jackscamp.com

September 13, 2000