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POSTAL RATE COMMISSION
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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

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Docket No. R2000-1

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Postal Rate and Fee Changes, 2000

REPLY BRIEF OF
ALLIANCE OF NONPROFIT MAILERS

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The Alliance of Nonprofit Mailers (“ANM”) respectfully submits this reply post-trial brief. This brief replies to Section II.C of the Postal Service’s initial brief, which concerns the adequacy and efficiency of the Service’s recent investments in automated flat processing capacity. ANM is also cosponsoring the joint reply brief of Direct Marketing Association *et al.* on the revenue requirement and the joint reply brief of American Business Media *et al.* on issues of concern to periodical publishers generally.

SUMMARY

In its initial brief, ANM explained why the “honest, efficient, and economical management” constraint of 39 U.S.C. § 3621 requires disallowance of the extra test year costs that result from the Postal Service’s chronic underinvestment in automated flat sorting technology. ANM also showed that the appropriate adjustment to the test year costs attributed to nonprofit periodicals, and from the overall test year revenue requirement, is \$94 million, reduced by any test year cost savings from the AFSM 100 reflected in the Commission’s test year figures.

The Postal Service's initial brief offers only a cursory defense of the Service's paltry investment in automated flats processing. USPS Br. at II-10-13. Instead, the Postal Service rewrites the statute. The standard of "honest, efficient, and economical management," the Service contends, establishes a floor under allowable revenues, not an "upper limit." *Id.* at II-14-20. There are "no grounds on which to believe that Congress ever contemplated that the provision would . . . be used as a basis to argue that *less* funds (and hence lower rates) are required . . ." *Id.* at I-20 (emphasis added). In any event, the power to enforce Section 3621 (so the Postal Service argues) rests solely with the Governors: whether the Postal Service's management is honest or efficient or economical is none of the Commission's business. *Id.* at II-20-26.

ANM responds first to the Postal Service's fanciful legal arguments, and then to its factual claims.

ARGUMENT

THE COMMISSION SHOULD DISALLOW THE TEST YEAR ATTRIBUTABLE COSTS AND REVENUE REQUIREMENT THAT RESULT FROM THE POSTAL SERVICE'S CHRONIC UNDERINVESTMENT IN FLAT SORTING EQUIPMENT AND FACILITIES.

A. 39 U.S.C. § 3621 Requires Disallowance Of Test Year Costs That Result From Inefficient Or Uneconomical Management.

1. The Postal Service's reading of 39 U.S.C. § 3621 ignores nearly 30 years of Commission precedent.

The Postal Service's construction of 39 U.S.C. § 3621 has an air of unreality. The Commission has rejected essentially the same arguments from the

Postal Service in case after case since the enactment of the Postal Reorganization Act of 1970. Rather than confront these decisions, the Postal Service simply ignores them.

In Docket No. R71-1, responding to the Postal Service's claim that the Commission has "no statutory power at all to consider the honesty, efficiency, and economy of Postal Service management," the Commission held that "[t]hese considerations, like the requirement that costs match revenues, are plainly among the "policies of this title," and thus, pursuant to § 3622, *must properly be taken into account in recommending rates and fees.*" *Postal Rate and Fee Increases, 1971*, R71-1 Op. & Rec. Decis. (June 5, 1972) at I-330 (emphasis added); *accord, id.* at I-332 (finding 12).

In Docket No. R76-1, the Commission reemphasized that "the 'honest, efficient, and economical management' standard is a part of § 3621 of the Act. It governs the proper level of rates, and therefore—because of the break-even basis of postal finance, also mandated by that section—governs the propriety of cost recovery through rates as well." *Postal Rate and Fee Increases, 1975*, R76-1 Op. & Rec. Decis. (June 30, 1976) at 52.

In Docket No. R90-1, the Commission reiterated that the "Commission and the Governors have a *joint* obligation to develop rates generating revenue as nearly as practicable equal to total costs, incurred under honest, efficient, and economical management. 39 U.S.C. § 3621." *Postal Rate and Fee Changes, 1990*, R90-1 Op. & Rec. Decis. (Jan. 4, 1991) at ¶¶ 2004, 2065.

The Commission has likewise rejected the Postal Service's claim that enforcement of Section 3621 would "interfer[e] with the Postal Service's managerial prerogatives":

No participant suggests that the Commission should function as an "inspector general," attempting constantly to oversee or vouch for the Postal Service's performance or efficiency. The Commission firmly rejects any such role. Rather, we hold here only that the Commission, in rendering rate recommendations, must advise the Governors whether the cost estimates on which the rates are based reflect the § 3621 criteria.

R71-1 Op. & Rec. Decis. (June 5, 1972) at I-330; *accord*, *Postal Rate and Fee Increases, 1973*, R74-1 Op. & Rec. Decis. (Aug. 28, 1975) at 23-24. While the Board of Governors and senior postal management are responsible for governing the Postal Service, the Commission nonetheless "may not recommend rates based on costs that have been shown to result from management actions failing the 'honest, efficient, and economical test' of § 3621." *Postal Rates and Fee Changes, 1990*, R90-1 Op. & Rec. Decis. (Jan. 4, 1991) at III-115 n. 30; *accord*, *id.* at ¶ II-51-52 n. 54 (rejecting USPS contention that disallowing portion of proposed rate increase under Section 3621, and thereby forcing the Postal Service "to reduce its costs," would "intrude upon the managerial authority of the Postal Service").

The Postal Service has offered no plausible ground for reconsidering the Commission's long-settled construction of Section 3621. We respond in the following subsection to the Service's claim that the standard of "honest, efficient and economical management" operates as a rate floor, not a rate ceiling. We respond in Subsection A.3 to the Service's alternative argument that the Governors have exclusive authority to enforce Section 3621.

In the decades that followed, the balance struck in Section 15a(2)—codifying the right of regulated monopolies to earn a fair return on invested capital, but conditioning that right on “honest, efficient, and economical management”—became a fixture of rate regulation under federal and state law.³ By 1970, when Congress enacted 39 U.S.C. § 3621, the reference to “honest, efficient, and economical management” was well recognized as a term of art requiring disallowance of needlessly high costs, even if actually incurred by the regulated firm. *See, e.g., D.C. Transit System, Inc. v. Washington Metropolitan Area Transit Commission*, 466 F.2d 394, 407-10 & n. 101 (D.C. Cir.) (citing precedent), *cert. denied*, 409 U.S. 1086 (1972); *Democratic Central Committee Of D.C. v. Washington Metropolitan Area Transit Commission*, 485 F.2d 886, 903-08 (D.C. Cir. 1973) (standard of “honest, efficient and economical management” does not entitle a regulated firm to the revenue of a “high-cost plus company”).

Absent a contrary indication, when a statute uses a term of art, it is presumed that Congress intended the term to have its established meaning at the time the statute was enacted.⁴ Thus, a term of art used in a Congressional statute should be interpreted by reference to the art or science involved.⁵ Nothing in the

³ Other current federal statutes that include a similar provision include 49 U.S.C. § 10704(a)(2) (railroad rates); *id.*, § 15503(b)(2) (petroleum pipeline rates); *id.*, § 41509(a)(3)(E) (rates for foreign air transportation).

⁴ *See, e.g., McDermott International, Inc. v. Wilander*, 498 U.S. 337, 342 (1991); *Republic of Argentina v. Weltover, Inc.*, 504 U.S. 607, 612-13 (1992).

⁵ *See, e.g., Corning Glass Works v. Brennan*, 417 U.S. 188, 202 (1974); *Greenleaf v. Goodrich*, 101 U.S. 278, 284 (1880).

language or legislative history of the Postal Reorganization Act suggests that Congress, when it incorporated the management efficiency constraint in 39 U.S.C. § 3621, meant to depart from the established meaning of this term of art.

The Postal Service asserts that the management efficiency constraint of 39 U.S.C. § 3621 should not be read as modifying the “breakeven provision” of the same section because the latter provision is located in an “entirely separate portion” of Section 3621. USPS Br. at II-14-15. But Section 3621 is not divided into “portions,” separate or otherwise: the entire section is a single four-sentence block of text. The “honest, efficient, and economical management” standard appears in the second sentence; the breakeven requirement appears in the third. It is a fundamental rule of statutory construction that provisions of this kind should be read together, not in isolation.⁶

The notion that the reference to “under honest, efficient and economical management” cannot limit the Postal Service’s revenues because the statute omits the word “only” (USPS Br. at II-15) is equally wrongheaded. The word “only” is also missing from 49 U.S.C. § 15a(2) and other embodiments of the management efficiency constraint, yet courts and agencies have held repeatedly that language of this kind establishes a binding *upper* limit on allowable earnings. See p. 6, *supra*.

⁶ See, e.g., *Lexecon Inc. v. Milberg Weiss Bershad Hynes & Lerach*, 523 U.S. 26, 36 (1998); *United States Central Bank of Oregon v. Independent Insurance Agents of America*, 508 U.S. 439, 454-55 (1993); *Crandon v. United States*, 494 U.S. 152, 158 (1990).

This outcome is the only sensible one. With or without the word “only,” the phrase “sufficient . . . under honest, efficient and economical management” necessarily implies a proportionality of financial means to regulatory ends. As the D.C. Circuit held in construing a similar ratemaking statute, a provision directing an administrative body to consider a carrier’s need for “revenues sufficient to enable [it], under honest, economical, and efficient management,” to provide “adequate and efficient transportation service”

could hardly have more plainly mandated the well settled principle that ratemaking appropriately encompasses an examination and evaluation of the economy and efficiency of a public utility’s operations and the adequacy of its service.

D.C. Transit System, supra, 466 F.2d at 408. Moreover, eliminating the qualification of “honest, efficient and economical management” from the statutory ceiling on revenues would reduce the former to empty surplusage, thereby violating the fundamental rule of statutory construction that a statute should be interpreted, if possible, to give meaning to all of its parts.⁷

The Postal Service tries to escape this problem by recasting the statutory language as an entitlement to sufficient funds “to allow the development of efficient and economical operations”—i.e., a *floor* on revenues. *Cf.* USPS Br. at II-18-19. The paraphrase, however, rewrites the statute. The stated goal of the second sentence of Section 3621 is to provide funds sufficient for “the development of postal services of the kind and quality adapted to the needs of the United

⁷ See, e.g., *Kawaauhau v. Geiger*, 523 U.S. 57, 62 (1998); *Walters v. Metropolitan Educational Enterprises, Inc.*, 519 U.S. 202, 209 (1997); *Mackey v. Lanier Collection Agency & Service, Inc.*, 486 U.S. 825, 837 (1988).

States”—*not* to provide funds sufficient for “the development of efficient and economical operations.” The reference to “honest, efficient and economical management” is a constraint on the funding goal, not the goal itself. *Id.*⁸

Equally without merit is the Postal Service’s claim that Congress could not have intended the management efficiency constraint to be binding, because enforcing it in the early 1970s, when Postal Service operations were at their nadir, would have made the breakeven constraint “dead on arrival.” USPS Br. II-16-18. The Commission considered and rejected this argument in the very first omnibus rate case. Rather than nullify the management efficiency constraint, the Commission gave effect to both provisions by holding that, for an interim “transitional stage,” the benchmark for judging the management efficiency of the Postal Service would be its progress in eliminating the massive inefficiencies inherited

⁸ The Postal Service asserts that the silence of the “Sectional Analysis” of the House committee report on the 1970 Act concerning the management efficiency constraint warrants an inference that the “primary thrust” of Section 3621 was to establish a revenue floor, not a revenue ceiling. USPS Br. II-17 at n. 14. The issue here, however, is not whether the revenue adequacy was the “primary thrust” of Section 3621 (a proposition that ANM does not dispute), but whether that goal was unconditioned on any obligation of the Postal Service to spend its revenue prudently. The notion that the silence of the “Sectional Analysis” on this point betrayed a legislative intent to allow management waste to go unchecked is absurd. The “sectional analysis” was a 28-page *summary* of a long and complex bill, and necessarily omitted many of its details and implications. See H.R. Rep. No. 1104, 91st Cong., 2nd Sess. 23-50 (1970).

from the Post Office Department. R71-1 Op. & Rec. Decis., *supra*, at I-329-330. Today, nearly 30 years later, this “transitional stage” has long since expired.⁹

Finally, the Postal Service’s speculation that taking the management efficiency constraint of Section 3621 seriously “could” render the Service insolvent, unable to “meet its actual payroll” or “pay the actual bills its receives” for the inputs it “needs to deliver the mail” (USPS Br. at II-25), is completely unsupported by the record. ANM is asking the Commission to disallow \$94 million or less in annual costs—i.e., less than *one-sixth of one percent* of the Service’s total revenue requirement. 22 Tr. 9656 (Haldi). No one can seriously contend that an adjustment of this size will force the Postal Service into insolvency.

3. The Postal Service has offered no valid reason for the Commission to abdicate its long-established authority to enforce 39 U.S.C. § 3621 in recommending rates.

The Postal Service’s renewed effort to persuade the Commission to abdicate its authority under Section 3621 is equally unsupported. Before responding to the Service’s individual arguments, however, it is useful to place them in context.

The Postal Service is a “regulated monopolist.” *Postal Rate and Fee Changes, 1997*, R97-1 Op. & Rec. Decis. ¶ 4048 (May 11, 1998). Competition for delivery of letter mail is, with limited exceptions, a crime. 18 U.S.C. §§ 1693-1699; 39 U.S.C. §§ 601-606; 39 C.F.R. Part 310. The monopoly covers not only

⁹ The legislative history cited by the Postal Service indicates that Congress intended that the transitional stage would end in 1978. *See* USPS Br. at II-16 (quoting H.R. Rep. No. 1104, 91st Cong., 2nd Sess. 16-17 (1970)).

First Class letter mail, primarily personal correspondence, but also Standard (A) letter mail. *Associated Third Class Mail Users v. USPS*, 600 F.2d 824 (D.C. Cir.), cert. denied, 444 U.S. 837 (1979). Moreover, the Postal Service also has considerable market power over many subclasses of mail for which competition is legal. *See* R97-1 Op. & Rec. Decis. at V-1 *et seq.*

Until 1970, the primary constraint on this market power was political: Congress and the Executive branch controlled the operations of the Post Office Department and set its rates. The Postal Reorganization Act, however, transformed the Post Office into an independent establishment of the executive branch, 39 U.S.C. § 201, and removed postal ratemaking from the direct control of either the executive or legislative branches. The Act also permitted only limited judicial oversight of the Service's economic power: the Postal Service is immune from suit under the antitrust laws (*see* 39 U.S.C. §§ 409-410), and appellate review of postal rate changes is deferential in scope. *See, e.g., Ass'n of American Publishers v. Governors*, 485 F.2d 768 (D.C. Cir. 1973); *Mail Order Ass'n of America v. USPS*, 2 F.3d 408 (D.C. Cir. 1993). As the law now stands, the Commission is the *only* expert body that provides an independent check on the Postal Service's ability to exploit its market power in setting overall revenue levels.

The Postal Service's construction of 39 U.S.C. § 3621 would remove even this constraint, leaving the Postal Service unique among monopolies in the United States. Its overall earnings would be unchecked by the political branch, unconstrained by effective competition, immune from the antitrust laws, and exempt from oversight by any independent expert body. If Congress intended in 1970 to

create such a leviathan, the Postal Service has failed to disclose any evidence in the text or history of the Act.

First, the Service asserts that 39 U.S.C. § 3622(b), which directs the Commission to recommend rates that are “fair and equitable” and “in accordance with the policies of this title” does not incorporate Section 3621. USPS Br. II-20-22. The Commission has squarely held, however, that Section 3622(b) incorporates Section 3621. *See pp. 3-4, supra.* Moreover, if the law were otherwise, the Commission would be obliged to disregard not only the standard of “honest, efficient and economic management” of Section 3621, but also the breakeven constraint and the contingency provision of the same section. Yet the Postal Service contends that the Commission must comply with both:

A reasonable provision for contingencies is *required by the statute* to be included with total estimated costs in evaluating whether rates and fees are sufficient to allow the Postal Service to break even. 39 U.S.C. § 3621 . . .

See, e.g., USPS Br. at II-2 n. 4 (emphasis added). The Service cannot have it both ways.

Second, the Postal Service claims that the Commission’s exercise of jurisdiction under 39 U.S.C. § 3621 usurps the “exact same functions” reserved to the Governors of the Postal Service by 39 U.S.C. §§ 401(3) and 404(a)(3). USPS Br. II-21-22. The Commission, however, has considered and rejected the same argument from the Postal Service in virtually every omnibus rate case since 1971. As the Commission has emphasized repeatedly, the managerial role of the Governors (deciding what equipment to buy, when to buy it, how much to pay for it, and how to finance it) is clearly distinct from the regulatory role of the Commission (deciding what costs should be recovered in the *rates* that the Commission

recommends to the Governors under 39 U.S.C. § 3622(b)). See pp. 3-4, *supra* (citing Commission decisions).

The Postal Service's claim that *Newsweek v. USPS*, 663 F.2d 1186, 1204 (2d Cir. 1981), "bars the Commission from attempting to . . . disallow recovery of" any "estimated future costs" that are likely to be incurred in the test year (USPS Br. II-22-24) is another chestnut that the Commission has repeatedly interred. The actual holding of *Newsweek* is considerably narrower: the Commission may not make arbitrary and unsupported reductions in key components of the revenue requirement (e.g., the contingency), make adjustments to the revenue requirement based on extra-record information, or manipulate the revenue requirement to "stimulate more frequent rate filings" or "discipline" the Postal Service for a "delinquent" rate filing. 663 F.2d at 1203-05; *accord*, R84-1 Op. & Rec. Decis. at ¶¶ 1028-47 (discussing *Newsweek*). The court clearly recognized that the Commission could adjust the revenue requirement under 39 U.S.C. § 3621 if the Commission's action rested on reasoned findings and relevant statutory criteria. See 663 F.2d at 1205 (directing the Commission, if it modified the revenue requirement on remand, to "subject its productivity adjustment rationale to the same hearing process as all other materials upon which it bases its recommend decisions," and "articulate its reasons for any modification of the schedule proposed by the Board").

Nor is there any basis for characterizing the relief sought by ANM as "disciplinary." Cf. USPS Br. at II-24 & n. 19 (citing *Newsweek*, 663 F.2d at 1204). The Commission's power to disallow expenses resulting from inefficient or uneconomical Postal Service management arises not from any "discipli-

nary” authority over the Service, but from the Commission’s duty under Section 3622 to protect mailers and consumers by recommending rates that satisfy Section 3621. See R71-1 Op. & Rec. Decis., *supra*, at I-330; R74-1 Op. & Rec. Decis., *supra*, at 23-24; R90-1 Op. & Rec. Decis., *supra*, at II-51-52 and III-115 n. 30.¹⁰

B. The Postal Service Has Failed To Refute The Substantial Evidence That Chronic Underinvestment In Automated Processing of Flat-Shaped Mail Has Inflated The Test Year Costs Of Periodicals Mail.

The Postal Service’s defense of its modest investment in automated flat processing during the 1990s leaves unchallenged much of the most damning evidence collected by ANM witness Haldi. See USPS Br. II-10-13. In particular, the Postal Service does not dispute that:

- Net investment in automated processing equipment for flat-shaped mail declined precipitously in 1993, remained at extraordinarily low levels for

¹⁰ The Postal Service’s reliance on *Governors of the USPS v. Commission*, 654 F.2d 108, 113-15 (D. C. Cir. 1981), and *Mail Order Ass’n of America v. USPS*, 2 F.3d 408, 422-25 (D.C. Cir. 1993), is also misplaced. In *Governors*, the Court held only that the Commission could not interfere with Postal Service management discretion by recommending that the Service’s experimental e-mail service be designated as “experimental” with a fixed terminal date (thereby usurping the Service’s control over the timing of its rate and classification changes). The relief sought by ANM here imposes no constraints on the timing of any future rate cases. In *MOAA*, the Court held only that that the Commission erred in failing to give affected parties adequate notice and opportunity to challenge the Public Automation Rate that the Commission recommended. 2 F.3d at 422-25. The extent of the Commission’s authority under Section 3621 was not at issue.

several years thereafter, and was no higher at the end of the decade than at the beginning. ANM Br. 3 (citing record).

- Postal Service investment in automated processing of flats has lagged hundreds of millions of dollars behind even the Service's own modest capital spending goals. *Id.* at 3 (citing 22 Tr. 9628-29 (Haldi)); 46-A Tr. 20487 (Dowling) (admitting that the Postal Service purchases of flat sorting equipment in the 1990s were approximately \$500 million under plan).
- This chronic investment lead to a severe shortage of mechanized and automated processing capacity for non-letter mail. *Id.* at 3-4 (citing USPS witnesses Kingsley and O'Tormey).¹¹
- Today (as well as in Base Year 1998), the Postal Service still has a capacity shortage equivalent to as many as 175 AFMS 100s or 450 FSM 881s. *Id.* at 5-6 (citing record).
- The Postal Service's failure to achieve over 25 percent of its planned commitments for acquisition of land and construction of buildings

¹¹ The Postal Service insists that these shortages are merely "investment opportunities" that "exist today." USPS Br. II-11. The record makes clear, however, that the unmet "investment opportunities" identified by Dr. Haldi, and the resulting in chronic congestion and inflated operating costs, have persisted for years. ANM Br. at 3-5, 9-10, 17-19. In these circumstances, "investment opportunity" is merely a euphemism for mismanagement.

between 1988 and 1999 has led to a similar shortage of floor space for processing flat-shaped mail. *Id.* at 8-9 (citing record).

- Knowledgeable outside observers, including the Postal Service's hand-picked Blue Ribbon Committee, have agreed that the Postal Service's investment in automated processing is inadequate. *Id.* at 9-10 (citing record).
- In response to these criticisms, future-Postmaster General Henderson agreed in 1997 that keeping pace with "current USPS programmed labor cost increases" would "require a yearly investment of \$4 billion at a minimum return-on-investment." *Id.* In Fiscal Year 2000, however, the Postal Service projects that its net investment as a percentage of operating revenue will be *lower* than in 1997—2.6 percent vs. 2.7 percent. *Id.* at 10.
- Between 1993 and 1998, when the average wage-adjusted unit cost of processing single-piece First Class mail decreased by 0.2 to 0.5 cents per piece, the corresponding unit cost for processing periodical mail *increased* by approximately 1.2 cents per piece. *Id.* at 18-19.

The handful of rejoinders offered by the Postal Service are irrelevant or unsupported by the record.

(1) The Postal Service's self-congratulatory rhetoric about its "continuously increased capacity" and "expanded . . . capabilities" for handling flats in the 1990s, USPS Br. at II-10, and the "full support" of "postal management and the Board of Governors" for purchasing new equipment, upgrading existing equipment, and "encouragement of industry" to perform the R&D needed by the

Postal Service, *id.* at II-13, is completely nonresponsive. No one disputes that the Postal Service installed *some* new capacity, has made *some* investments, and provided *some* support for these purposes since 1990: the issue is whether the Postal Service has used its available resources to do *enough*. The mailers who face higher unit costs in this rate case because of past underinvestment gain small consolation from learning that the underinvestment was even more severe in the past. 22 Tr. 9678 (Haldi).

(2) The Service's main excuse for not investing more after the early 1990s—that appropriate technology was unavailable—amounts to a sort of Goldilocks logic in reverse: the FSM 775/881 was too old and “outdated”; the AFSM 100 was too new, untried and unreliable; and nothing in between was just right. *See* USPS Br. at II-11-13; 5 Tr. 1590 (Kingsley). This excuse does not withstand scrutiny.

The notion that the FSM 881 was obsolete by the early 1990s is belied by the Postal Service's own investment decisions. The Postal Service invested hundreds of millions of dollars to retrofit and update the FSM 881 in the 1990s—most recently in 1997. 46A Tr. 20476-77 (Dowling). The Postal Service has conceded that it regarded these additional investments as “worthwhile,” that that the investments had a quick payoff, and that foregoing them would not have made the Service “better off.” *Id.* at 20498, 20500.

The notion that the AFSM 100 was too new and untried to implement in 1994 is also a self-serving rationalization. *Every* advance in technology is likely to experience shakedown bugs. When the Postal Service refuses to spend the money needed to solve them, and fobs off most of the needed R&D on the

Service's vendors,¹² the problems will remain unsolved. Canada Post, unlike the Postal Service, stepped up to the plate. In 1995, when the Postal Service was just beginning its testing of an Alcatel prototype, Canada Post was already deploying the machine in the field.¹³ As the Postal Service concedes, the bugs have been solved, and the machines are generating economies that the Postal Service is only beginning to match.¹⁴ In this context, the Postal Service's bluster that "ours worked" while the Canadian version required "several years" of refinement after 1994¹⁵ ignores the obvious rejoinder: if the Service had seriously invested in deploying the Alcatel machine in 1994, the machine would have "worked" that much earlier, and periodicals mailers in the United States would have savings today instead of empty excuses.¹⁶

¹² The Postal Service concedes that "it is only by conducting [research and development] that firm conclusions can be drawn about how many of which type of machine to buy." USPS Br. II-12. Yet the Service has chosen to spend barely \$10 million on R&D on flat sorting machinery in the past 10 years, relying instead to pressure its vendors to make the necessary investments in new technology. 46A Tr. 20507-08 (Dowling).

¹³ See 46A Tr. 20506 (Dowling); "Technology Update: New FSMs Set to Arrive in 1995," *Performance* (Dec. 1994/Jan. 1995) at 34-35.

¹⁴ See 46A Tr. 20507, lines 2-3 (Dowling) (conceding that shakedown problems have been resolved in Canada); *Performance, supra*, at 34 (noting that Canadian equivalent of AFSM 100 can process 21,000 pieces per hour).

¹⁵ USPS Br. II-12; 46A Tr. 20506-07 (Dowling).

¹⁶ See 46A Tr. 20484 (Dowling) ("the distribution costs would have gone down even further if the [AFSM 100] had been deployed prior to the beginning of the test year"); *id.* at 20499 ("it's still not outmoded").

Moreover, the proposition that the AFSM 100 was effectively unready for widespread deployment until early 2000, if taken at face value, demolishes the Service's argument for halting further deployment of the FSM 881 or 1000. *Cf.* 5 Tr. 1590 (Kingsley) ("the thought was why invest capital in old technology when there was much better equipment technologies available"). If the Postal Service regarded the Alcatel/AFSM 100 technology in 1994 as too immature to begin deploying until six or more years later, the Service had no excuse for freezing further deployment of less advanced equipment on the theory that deployment of the AFSM 100 was imminent.

The internal contradictions in the Postal Service's reasoning are most glaring with the FSM 1000, a technology intermediate to the FSM 881 and AFSM 100. In 1992, when the Postal Service bought a "prototype" from Siemens, its manufacturer, the machine was already operational in Germany. *See* 46A Tr. 20499 (Dowling). Moreover, the FSM 1000 was not outdated in 1994-95, and is not outdated today. *Id.*; 5 Tr. 1554 (Kingsley). Indeed, the Postal Service plans to deploy further enhancements to the FSM 1000 next year. 46A Tr. 20478 (Dowling). The record demonstrates that the FSM 1000, compared with the FSM 881, can handle pieces that are bigger, heavier, thicker, flimsier, not enveloped and polybagged.¹⁷ By 1998, the Postal Service had a capacity shortfall equivalent to about 455 FSM 1000s.¹⁸ The obvious question is why did the Postal Service

¹⁷ 22 Tr. 9633 (Haldi); USPS-T-10 (Kingsley) at 11 ("This machine is intended to process a vast majority of the 25-33 percent of the non-carrier route flats that are non-machineable on the FSM 881."); 46A Tr. 20497-99 (Dowling).

¹⁸ *See* 46A Tr. 20500 (Dowling). 455 FSM 1000s or FSM 881s have the capacity of about 175 AFSMs. *See* 46A Tr. 20501, 20502 (Dowling).

not buy another 300-400 of these machines in 1994? The Postal Service concluded that it needed additional flat sorting capacity (46A Tr. 20501, lines 19-10 (Dowling)), yet bought an insufficient number of FSM 1000s to fill the void.

During the third and final round of hearings, the Postal Service belatedly asserted that no additional sites existed where the FSM 1000 could have been profitably installed. 46A Tr. 20502 (Dowling). The Commission should give no credence to this claim. It is inconsistent with the testimony of previous Postal Service witnesses that shortages of mail processing equipment were widespread (*see* ANM Br. 3 (citing record)), and the Service's projections that the automated flat sorting equipment actually deployed would generate enormous returns on investment.¹⁹ How can the Postal Service have a shortage of 455 FSM 1000s, yet lack any additional sites where the FSM 1000 could be profitably deployed?

Further, Mr. Dowling conceded that the decision analysis reports ("DARs") supporting the purchase of automated flat sorting equipment contained no analyses of the potential returns from deploying additional pieces of equipment beyond those sought by management. 46A Tr. 20494-96 (Dowling). In response to a follow-up document request prompted by this exchange, the Postal Service stated that it had been unable to identify or locate any other documents containing such an analysis.²⁰ William Tayman, an earlier Postal Service witness on the

¹⁹ *See* 22 Tr. 9639-40 (Haldi) (citing testimony and discovery responses of USPS witnesses Tayman and O'Tormey). The high projected returns have been borne out by experience. 21 Tr. 8342 (O'Tormey).

²⁰ Notice of USPS Regarding Hearing Question Posed to Witness Dowling, USPS-RT-3 (Sept. 11, 2000).

same subject, professed complete unawareness that such an analysis had ever been performed. 2 Tr. 442-44 (Tayman). And the Postal Service made a point of pride out of its failure to “analyze whether” its “operating plan is actually cost minimizing.” 21 Tr. 8611 (USPS institutional interrogatory response).²¹

(3) The Postal Service’s suggestion that a “projected . . . dip” in the volume of flat mail suitable for automated processing in the “early 1990s” justified the Postal Service in shifting the “focus” of its “investment strategy” to “newer technology” (USPS Br. at II-11) is flagrant revisionism. What the Postal Service calls a change in “focus” was in fact a precipitous decline in investment that brought the Postal Service’s automation program to a near standstill. 22 Tr. 9625, 9627 (Haldi). Moreover, the decline in capital spending continued through 1995, although the decline in mail volume was just a one-year blip. *See* 46A Tr. 20487 (Dowling); 22 Tr. 9627 (Haldi). And the precipitating cause of the decline in capital spending was not a reasoned review of the Service’s investment opportunities, but the chaos that followed Postmaster General Runyon’s purge of top headquarters management in 1992-93.²²

²¹ That “each of more than a dozen proposed purchases presented by Mr. Dowling has been approved by senior management,” USPS Br. II-12-13, reveals nothing about the adequacy of the Postal Service’s capital spending. A manager with as much experience as Mr. Dowling is not going to invest the time and resources needed to prepare the written documentation for a major purchase request without first reaching an informal understanding with senior management about how much it approve. *See id.* (alluding to the “solid foundation” developed by the Postal Service for “each such purchase”).

²² *See* 2 Tr. 201 (Tayman); 22 Tr. 9700 (Haldi); *cf.* 21 Tr. 8335-36 (O’Tormey).

(4) The Postal Service asserts that 1993 is an unfair benchmark for estimating the later growth in periodicals costs caused by underinvestment in automated processing equipment because 1993 unit labor costs were temporarily low in that year “due to reductions in craft employees during restructuring” at the beginning of Postmaster General Runyon’s tenure. USPS Br. at II-13; 46A Tr. 20202 (Strasser). In essence, the Postal Service contends that cost comparisons between 1993 and subsequent years are inapposite because mail service in 1993 was of lower quality than in later years, and hence not a comparable output. *Id.*

The argument has two flaws. First, as the Postal Service and ANM agree, the reductions in craft employees during restructuring “didn’t last very long.” USPS Br. II-13; 22 Tr. 9700 (Haldi). By contrast, the unit costs of processing periodicals increased year after year from 1993 through 1998.²³ Second, the Postal Service has offered no credible evidence that the average speed or reliability of periodicals mail service actually increased from 1993 to 1999. Indeed, the Postal Service has conceded that “we don’t track service [quality] for periodicals per se.” 21 Tr. 8236 (Unger). Hence, a comparison of unit costs between 1993 and 1999 is entirely appropriate.

(5) Finally, the Postal Service’s claim that the relief sought by ANM is unnecessary because mailers need not “pay higher rates in order to fund operational practices which demonstrably can be improved” (USPS Br. II-25-26) is incomprehensible. The dispute here involves expenses which the Postal Service

²³ See Order No. 1289, *Order Requesting the Submission of Evidence on Periodicals Processing Costs* (Mar. 28, 2000), Attachment A, p. 4.

claims *cannot* be avoided during the test year because the automated equipment needed to achieve the savings will not go on line soon enough. The cost savings expected to result during the test year from rollout of the AFSM 100, although welcome and long overdue, are considerably less than the Postal Service would have through timely rollout of the FSM 1000 or the AFSM in the 1990s.²⁴

In this regard, the Postal Service's assertion that the cost adjustment proposed by Dr. Haldi would double-count savings generated in the test year by "cost reduction programs" *other than* the AFSM 100 is wholly unsupported. *Cf.* 46A Tr. 20201-03 (Strasser) (cited in USPS Br. II-13). Mr. Strasser, the proponent of this argument, made no effort to quantify the savings likely to occur during or before the test year as a result of these programs, or even to identify what programs he had in mind. *Id.* at 20203.²⁵

²⁴ The Postal Service admits the deployment of the AFSM 100 did not begin until March 2000—i.e., well after the end of the base year—and will not be completed until April 2002. 46A Tr. 20483-84 (Dowling). To avoid any possible double count, ANM has proposed that all programmed test year cost savings from the AFSM 100 be offset against its proposed remedy for the same classes of mail. *See* ANM Br. 19; 22 Tr. 9689 (Haldi).

²⁵ The Postal Service's cryptic assertion that Dr. Haldi also erred in "reliance upon total factor productivity" is unsupported by Mr. Strasser's testimony. *Cf.* USPS Br. at II-13; 46A Tr. 20203 (Strasser).

CONCLUSION

ANM respectfully requests that the Commission recommend rates that reflect the adjustments proposed in this brief, ANM's initial brief, and the coalition briefs that ANM has co-sponsored.

Respectfully Submitted,



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September 22, 2000

CERTIFICATE OF SERVICE

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



September 22, 2000