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

POSTAL RATE AND FEE CHANGES, 2000 | Docket No. R2000–1

MEMORANDUM OFTHE UNITED STATES POSTAL SERVICE
ON RECONSIDERATION AND REQUEST FOR EXPEDITION

On December 4, 2000, the Governors of the United States Postal Service (Governors) acted on the Opinion and Recommended Decision of the Postal Rate Commission in Docket No. R2000-1. The Governors issued two Decisions. In the first, they exercised their authority under 39 U.S.C. § 3625(c) to allow under protest rates, fees, and classification changes recommended by the Commission.[1] In accordance with 39 U.S.C. § 3625(c)(2), they also returned the case to the Commission for reconsideration of the Postal Service's revenue requirement and several other matters. In a second decision, the Governors rejected several classification recommendations, pursuant to 39 U.S.C. § 3625(d).[2]

[1] Decision of the Governors of the United States Postal Service on the Recommended Decision of the Postal Rate Commission on Postal Rate and Fee Changes, Docket No. R2000-1 (Dec. 4, 2000) (Reconsideration Decision). By Resolution No. 00-16, the Board of Governors ordered the rates and fees allowed under protest to take effect on January 7, 2001.

[2] Decision of the Governors of the United States Postal Service on the Recommended Decisions of the Postal Rate Commission on Selected Mail Classification Matters, Docket No. R2000-1 (Dec. 4, 2000) (Rejection Decision).

On December 11, 2000, the Commission issued Order No. 1301 initiating further proceedings on reconsideration.[3] Order No. 1301 instructed the Postal Service and other parties to proceed according to one of two alternative schedules. Under the first, the Postal Service would file an initial statement on January 3, 2001, followed by intervenor responses on January 24, and a Postal Service reply on January 31, 2001. Alternatively, if the Postal Service were to file initially on December 20, 2000, intervenor responses would be due on January 12, and a Postal Service reply would be due on January 19, 2001. After outlining the issues identified by the Governors in their Reconsideration Decision, Order No. 1301 directed the Postal Service to provide "detailed statements on each of these issues, setting out evidentiary and legal support for the outcomes deemed proper by the Governors." Order No. 1301 at 3.

As indicated by the Governors, the Commission's recommended rates and fees would result in a serious revenue deficiency. The Governors therefore have requested the Commission to provide further recommendations as expeditiously as possible. Reconsideration Decision at 12. Accordingly, the Postal Service has elected to file its statement on the earlier of the two dates indicated in Order No. 1301. Furthermore, as explained below, in light of the Governors' concerns for its financial condition, the Postal Service is requesting reconsideration of the Commission's alternative schedule to accelerate deliberations and a subsequent Recommended Decision.

The following elaborates on the Governors' Decision returning Docket No. 2000-1 to the Commission for reconsideration of the Postal Service's revenue requirement

[3] Notice of Request for Reconsideration and Order Establishing Procedures, Docket No. R2000-1 (Dec. 11, 2000).

and several other discrete issues. In the interest of economy and expedition, and in accordance with past practice, the Postal Service submits that further proceedings should be limited to these issues.

While the Governors protested the Commission's recommendations based on its estimate of the Postal Service's overall revenue needs in the test year (FY 2001), they focused their request for reconsideration on three elements of the Commission's revenue requirement determinations. Reconsideration Decision at 5. The Governors concluded that the Commission had exceeded its lawful authority and acted contrary to the established record in effectively eliminating from the revenue requirement approximately $200 million designated as the "Field Reserve." They concluded that the Commission had erred in reducing the revenue requirement by approximately $97 million through expanding cost reduction estimates in accordance with a faulty analysis of supervisory cost savings. Finally, the Governors concluded that the Commission had erroneously reduced the provision for contingencies included in the revenue requirement from 2.5 percent endorsed by the Board of Governors in the Postal Service's Request to an effective contingency of 1.2 percent. In this regard, the Governors determined that the Commission had exceeded its lawful authority by going beyond assessing the reasonableness of the contingency component, as contemplated in the statute and established on the record. Rather, the Commission unlawfully substituted its own determination of this important component of the revenue requirement.

In addition, the Governors identified three other matters where reconsideration and adjustment might be warranted. First, they expressed concern that the

Commission may have erred in forecasting revenue from additional ounces of First Class Mail. Second, they indicated that the Commission may have forecasted revenues from Bound Printed Matter rates inaccurately. Finally, they asked the Commission to reconsider rates recommended for the nonprofit Standard Mail subclasses, in light of an apparent inconsistency between the Commission's methodology and recently enacted amendments to 39 U.S.C. § 3626.

The Postal Service believes that each of these errors or potential errors can be explored and reevaluated, and appropriate adjustments recommended, based on review of the existing evidentiary record, the Commission's Opinion and workpapers, the following discussions, and appropriate responses by other parties. Accordingly, the Postal Service submits that there is no need at this time to reopen the record to develop further evidence. In fact, the serious financial consequences of the Commission's recommendations, which have been allowed to take effect under protest, militate strongly in favor of expeditious consideration without unnecessary further proceedings.

REVENUE REQUIREMENT

The Governors, to whom the Postal Reorganization Act gives final ratemaking authority and the authority and responsibility to ensure that the Postal Service breaks even, have determined that "a 2.5 percent contingency provision is both reasonable and necessary in the current circumstances" and that the total revenue requirement, based on the record before the Commission, is $69.832 billion. Reconsideration Decision at 7, 12. The Governors have requested that the Commission adjust its recommended rates and fees to provide revenues sufficient to meet this revenue requirement. *Id.* at 12.

Update

The Postal Service took the position during the course of the proceeding that the Commission should recommend the rates requested by the Postal Service when it filed its Request in January of 2000, and should not attempt to incorporate the increases in costs shown in the cost update filed by the Postal Service in response to Commission Order No. 1294. The Commission nevertheless used the updated costs, but made adjustments in those costs resulting in rates that produce less revenue than the rates requested by the Postal Service,[4] leaving the Postal Service in a precarious financial position in the test year and beyond. The Governors accepted the Commission's determination to use the updated costs and determined that the difference between properly updated test-year costs and the revenues to be produced by the rates recommended by the Commission to be $1 billion.[5]

The Commission contends that it accepted most of the Postal Service's cost revisions provided in the Order 1294 Update. The benefit of recognizing these higher costs is illusory, however, since a large portion of the Postal Service's revisions were offset by the Commission's disallowance of other real costs. The disallowances included almost $100 million of supervisor costs and the $200 million "field reserve." Postal Service testimony that these costs would be incurred was either ignored or disregarded. In addition, the Commission reduced the provision for contingencies from

[4] The Commission recommended an overall increase of 4.6%, compared with what it calculated as the Postal Service's proposed increase of 6.0%..

[5] The Commission's estimated revenues of $68.836 billion compared to the updated costs, including the 1.5 percent contingency provision, of $69.832 billion. PRC Op., Vol. 2, App. C.

2.5 percent to a nominal 1.5 percent. Due to its treatment of the field reserve as a contingency amount, the effective contingency included by the Commission in its recommended rates and fees is 1.2 percent.[6] These items are discussed in more detail below. In no meaningful way did the Commission account for the fact that the Postal Service's interim financial performance was worse than assumed in the Postal Service's filing.

In its Table 2-2 on page 74 of its Opinion, the Commission depicts the amount of additional revenue resulting from its recommended rates as only $280 million less than the revenue requested by the Postal Service. For several reasons, this depiction has obscured, rather than elucidated, the effect of the recommended decision. The true effects are more accurately portrayed in the Commission's Appendix K (p. 7), which shows that the recommended rates will generate $726 million less revenue than the rates requested by the Postal Service.

The difference between these amounts is easily reconciled. First, in Table 2-2 the Commission incorporates $304 million in additional revenue that the Postal Service indicated in the Order 1294 update that it hopes to generate from co-branded advertising, retail sales, and e-commerce programs. These are not revenues that result from the Commission's rate recommendations. Rather, these are high-risk initiatives

[6]

PRC recommended contingency	1,012,425
minus field reserve	-200,000
amount remaining for true contingencies	812,425
over PRC Total Accrued Costs	÷67,495,012
equals effective contingency	1.2%

Source: PRC Op., Vol. 2, App. C.
This 1.2 percent is less than half of the Postal Service contingency provision of 2.5 percent.

much less certain to produce the targeted revenue than the additional revenue that would result from new rates. Moreover, these additional revenues are to a large extent offset in the test year by expenses related to these revenue generation programs. In other words, the net revenue from these programs is much smaller and riskier than Table 2-2 would suggest.

The Commission also recalculated test year after rates revenues for technical reasons. These re-estimates added an additional $142 million of revenue to the test year.

In summary, the effect of eliminating $726 million of revenue that would have resulted from the requested rates is concealed in Table 2-2 by inclusion of revenue resulting from technical re-estimates and high-risk and greatly offset revenue projections unrelated to rate increases. The Postal Service does not take issue with the mathematical basis for these offsetting amounts, but believes that their embodiment in Table 2-2 distorts the consequences of the Commission's recommendations. They should not be portrayed as revenue increases recommended by the Commission that will offset the updated costs that the Commission used. [7]

[7] In particular, these re-estimates and tenuous estimates of revenue from program initiatives should not be used to offset the need for higher rates when actual events show that the level of revenue reflected by the recommended rates does not account for the weakness in revenue that is actually occurring. Actual revenue growth is weaker than reflected in both the Request and the Recommended Decision. For example, actual FY 2000 revenue is $236 million less than the amount estimated by the Postal Service in its Request and by the Commission in its Recommended Decision. The Commission's reduction of the contingency provision is all the more troubling In light of this unacknowledged revenue shortfall. The fact that the Commission has reduced the contingency and increased the basic revenue forecast, when actual data show that revenues are overprojected, belies the notion that the Commission has used sound judgment in employing more recent data to fashion its version of the revenue

(continued...)

Field Reserve

The Commission excluded from the revenue requirement the $200 million "field reserve" described in connection with the update as a test year expense. Instead, the Commission subsumed this expense within the already-reduced contingency provision.

According to its Opinion, the Commission based this action on its reading of footnote 2 in Attachment I to the Postal Service's response to Presiding Officer's Information Request No. 14, Question 2. That footnote indicated that the Field Reserve "recognizes the difficulty in achieving the aggressive cost reductions in FY 2001, the first year of the Breakthrough Productivity Initiative." *See* PRC Op., Vol. 1, at 71, citing Tr. 46D/21595. Based on that footnote, the Commission concluded:

> This is a somewhat unusual, but appropriate, example of the kind of insurance against uncertainty the contingency provision provides, and the Commission believes it should be reflected in the amount of that item.

Id. While the Commission's conclusion might have been tenable if the only record evidence regarding the Field Reserve was footnote 2, its conclusion is contradicted by clear evidence on the record, which the Commission ignored, that the $200 million item represents actual test year expenses. The Commission failed even to mention, let alone analyze, the significant testimony on the subject provided by witness Strasser, the Postal Service's Chief Financial Officer. In his written testimony, alluding to testimony by participants' witnesses, witness Strasser testified:

(...continued)
requirement. In this regard, the Commission's Recommended Decision shows a misunderstanding of the Postal Service's financial condition and the financial trends affecting the postal system. In this context, the importance of an adequate provision for contingencies to provide a cushion for any unanticipated occurrences is paramount.

> *In discussions pertaining to these adjustments, there has been some confusion* regarding the character and impact of the approximately $200 million "field reserve." There has been some suggestion that this expense is merely an element of the contingency provision. This conclusion is wrong. ...
> The field reserve is *an actual budget expense item* that the Postal Service *projects it will spend during the test year.* It is as real as any other expense in the Postal Service's budget. It has not yet been assigned to a particular expense account, pending evaluation in the field of the particular needs of each location as the year progresses. Its status is similar to a series of other reserved line items in the Postal Service's budget process. For example, budgeted field expenses for projected COLAs and increased health benefit expenses are held in a headquarters reserve account at the beginning of the year. They are not allocated to field operating units until well into the budget year, when the actual CPIs (in the case of COLAs) and the actual health benefit increases are known. The reserve is then distributed to the field as needed as the year progresses. In the same way, the breakthrough productivity field reserve will be distributed as needed as the year progresses, once it is known where and for what the funds are needed.

Tr. 46D/20207-09 (emphasis added).

In cross-examination conducted by counsel for the OCA, witness Strasser elaborated on this matter in some detail:

> Q If this amount is pending evaluation, does that suggest that these needs may not materialize as the year progresses?
>
> A No. It is evaluation as to what they will be used on. *These will definitely be spent.* What we did in our budget process is that we have a list of investments that should be made, and there is too many on the list to fund and end up anywhere near where we want to end the year in terms of net income.
>
> In addition, we have, as you know, added our breakthrough productivity to the normal array of cost reductions we have given to the Postal field, and the field units are going to have to reduce work hours, compared to this year, twice as much as they have achieved in the reductions this year. In other words, it is going to be somewhere in the range of 1.5 percent to a 2 percent reduction in work hours compared to the work hours in this fiscal year.
>
> So there is increased, with our breakthrough productivity, there is increased uncertainty as to whether the opportunity for — we are discussing with the field where the opportunity is for breakthrough productivity and what the specified amounts are by field location. So we have created this $200 million field reserve by *holding back the investments* that equate to $200 million. And specifically, what we have done is we have reduced the budget *for mail*

> *transport equipment*, which is a risk due to the fall mailing season next year. We have reduced the *advertising* budget and held it steady and constant when we, in fact, are having new production introductions like Priority Mail Global Guaranteed.
>
> We have held back on infrastructure, *information platform infrastructures* that we need for this mail, the mailing community, and we are trying to create an opportunity to give the mailers a window on the process to find out where their mail is, and there is $100 million in infrastructure expenses that need to be put towards that program.
>
> We have *held those specific expenses in reserve until* we are sure that the breakthrough productivity and the allocation of the *breakthrough productivity works* in this process. *If it works* and we get indications during the beginning of the year that it is being achieved, *we will spend the $200 million on those specific investments* that I just mentioned. *It if doesn't work, we will* have to hold back on those investments for a future fiscal year and *cover the shortfall in the breakthrough productivity.*

Tr. 46A/20295-97 (emphasis added).

Counsel for the OCA, preshadowing the Commission's insistence on treating this item as part of the contingency, then asked:

> Q [A]s I understood it, it sounded like there was a chance that the $200 million might not be spent. If certain events didn't fall into place, then you might not spend that $200 million, is that right?
>
> A *No, that is not correct.* What I said was, *if we don't need it to cover the breakthrough productivity*, and if the field achieves the reduction in the work hours that we have targeted to achieve with this very massive effort, *we will spend it on the infrastructure for the information platform, the advertising for product introductions, and the mail transport equipment that we believe we need for next fall's mailing season.*

Id. at 20297 (emphasis added). If there was any misunderstanding as to the nature of this item, this unequivocal testimony from the Chief Financial Officer made clear that the $200 million will be spent, either to fund field operations, if needed, or on already approved projects that have been deferred pending evaluation of the progress of the breakthrough productivity initiatives. The record does not support, and indeed contradicts, the notion that the $200 million was being held to fund unanticipated contingencies, or that there is any possibility that it will not be spent. Based on the record, the Postal Service asks the Commission to reconsider its previous conclusion and include this $200 million as an actual test year expense. It will not be available to fund contingencies and its inclusion in the contingency provision effectively reduces the contingency further to 1.2 percent, contrary to the Commission's conclusion that a contingency of 1.5 percent is needed.

Supervisor Cost Reduction

The Commission's Opinion gives its rationale for the elimination of approximately $100 million in test year supervisor costs at pages 32-34. Although the Commission cites the supporting testimony of intervenor witness Buc, it ultimately relies directly on statements contained in a document entitled "Summary Description of USPS Development of Costs by Segments and Components, Fiscal Year 1998," which was furnished in this case as a Category 1 library reference (USPS-LR-I-1), but never formally admitted into evidence.

The Commission's Opinion misapprehends the nature of the "Summary Description" document. That document explains the process by which the Postal Service goes about taking accounting information from an historical year and converting it into economically-relevant marginal and incremental costs estimates for individual mail categories and services. See USPS-LR-I-1, Appendices H & I. That process, as Prof. Panzar very explicitly noted in his testimony in Docket No. R97-1, presumes a reasonably well-defined and stable set of operating procedures. See USPS-T-11, Docket No. R97-1, at 3-4, 13-17. It is within the context of such an operating plan that the effects of changes in mail volume on particular types of costs are examined in order to derive what, for rate case purposes, become known as the base year costs.

Technically, the "Summary Description" document relied upon by the Commission relates to the FY 1998 CRA, and does not reflect the various methodological changes proposed by the Postal Service witnesses in this docket that distinguish Base Year 1998 from the Fiscal Year 1998 CRA. That distinction is not necessarily relevant in this context because Supervisor costs were treated essentially the same in Base Year 1998 as in the Fiscal Year 1998 CRA. In any event, however, the scope of the "Summary Description" is clearly limited to discussion of the process used to derive cost estimates by product for an historical period, taking as given a stable operating plan, and estimating the effect of changes in volume on changes in costs.

Perhaps more important than what the "Summary Description " document *does* is what the document *does not* do. The "Summary Description" simply does not purport to describe the process by which the Postal Service moves from the observed historical level of accrued cost in the base year to a forecast of accrued costs in the test year. As the Commission is well aware, that process is instead the province of the revenue requirement and roll-forward witnesses. It is the testimonies of those witnesses which describe the effects of factors, in addition to changes in mail volume, that will cause accrued test year costs to differ from accrued base year costs. Factors of one type that are very explicitly accounted for in the roll-forward process, in contrast with their deliberate omission from the base year analysis, are changes in the operating plan. In the roll-forward process, changes in the operating plan show up either as cost reduction programs, or as other programs. Both theoretically and practically, cost changes resulting from cost reduction programs and other programs are quite distinct from the cost changes associated with changes in mail volume, as even the most cursory review of the roll-forward testimony shows.

On the record in this proceeding, Postal Service witness Tayman testified that the Postal Service had in this case specifically addressed the issue of reductions in supervisor costs and had included the appropriate amount of supervisor costs in its cost reduction estimates. Moreover, Postal Service witness Patelunas explained why the cost reduction programs incorporated into the rollforward model cannot be expected to have the additional effect on test year supervisor costs postulated by witness Buc. Tr. 37/17142-45. In rejecting the Postal Service's testimony in favor of a conclusion supposedly supported by statements in the "Summary Description," the Commission makes two fundamental errors. First, the Commission confounds the effects of two distinct types of changes. As suggested above, the purpose of a cost reduction program is to incorporate the effects of a change in the operating plan -- changes which have the potential to alter preexisting relationships. Mr. Patelunas, in fact, explained why operational factors in this instance will do just that, by creating situations in which craft hours can be reduced, but supervisor hours cannot be reduced proportionately. Tr. 37/17142-43.[8]

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[8] Mr. Patelunas also showed how, with respect to the test year used in the last case, the Commission's estimate of supervisor costs which was adjusted to mechanistically achieve a constant supervisor/employee ratio, materially understated actual accrued supervisor costs, while the unadjusted (i.e., non-constant ratio) estimate did not. Tr. 37/17144. That instance is therefore one potential example of cost reduction programs causing changes in the operating plan which altered the supervisor/employee ratio.

(continued...)

The "Summary Description" is not inconsistent with the testimony of Mr. Patelunas, because it does not address changes in the operating plan. Instead, its discussion is limited to changes caused by changes in mail volume. This is explicit in the portion of the document quoted on page 33 of the Commission's Opinion – "It is recognized that a change in employee workhours, caused by a change in mail volume, may not be accompanied immediately by a corresponding change in firstline supervisory workhours" (emphasis added). Mr. Patelunas is not discussing changes in craft employee workhours caused by a change in mail volume; he is discussing something entirely different.[9]

The only correct inference that could reasonably be drawn from the "Summary Description" is that *after* the changes in the operating plan implicit in the cost reduction programs have worked their way through the system and become the new status quo (albeit one in which, according to witness Patelunas, there will be a new ratio of supervisors to craft employees), any *further* changes in craft hours caused by changes in mail volumes can once again eventually be expected to cause proportional changes

(...continued)
While the Commission chooses not to consider this result to be "probative," there is no apparent reason why such an empirical result should be discounted merely on the basis of theoretical statements which demonstrably do not apply to the situation at hand.

[9] The same point can be made with respect to the next sentence from the "Summary Description," also quoted by the Commission on page 33. That sentence refers to a change in the level of craft employee effort "for a given work activity." A mere volume change, all else equal, would presumably cause employees to do more or less of the same work activities that they were performing to process the previous level of mail volume. A program change, however, often involves employees in work activities that are different from those in which they might have been engaged under the previous operating plan. The Commission seeks to interpret the document as if this explicit qualifying language had not been included.

in supervisor hours (assuming no further changes in the operating plan). Because cost changes caused by changes in the operating plan are distinct from cost changes caused by changes in mail volumes, and because program changes may affect the operating relationship between craft and supervisory workloads in any of a variety of ways, the "Summary Description" cannot support the conclusion which the Commission erroneously seeks to draw from it.[10]

The second flaw in the Commission's reliance on the "Summary Description" relates to the issue of timing. As the Commission itself acknowledged on page 34, the "Summary Description," in the context of cost changes caused by volume changes, recognizes that only "in the long run" will changes in craft hours match up with proportional changes in supervisor hours. Thus, even assuming no change in the operating plan, and therefore ultimately a return to the pre-existing employee/supervisor ratio, there may be a substantial lag time between an increase in craft employee hours, and the ability of the organization to put in place necessary supervisory resources. In the context of an analysis of cost causation, such as that which is the subject of the "Summary Description," it is entirely appropriate to allocate to products the costs of the supervisory hours that will be caused by the addition of craft hours used to handle those products, even if the additional supervisory hours may not appear until time periods

[10] As this paragraph should make clear, the Postal Service is not disputing the general proposition that craft employee hours are a primary cost driver for supervisory hours. It is a far cry to go from such a general proposition, however, to the implicit finding that changes in craft employee hours from *any* source will automatically and necessarily cause an exactly proportional change in supervisory hours, particularly in the face of explicit testimony that the specific programs at issue in this instance will not achieve any such result in this test year.

subsequent to the year of analysis. By the same token, however, when the purpose of the exercise is to estimate as accurately as possible accrued costs in a given year, it would be entirely *inappropriate* to include the costs (or in this case, exclude the costs) of any changes in supervisory hours that simply will not occur during the year in question. While the rollforward in general assumes that the lagged response of supervisor hours *to mail volume changes* will nonetheless be completed during the same year as the craft employee changes engendered by the volume changes, Mr. Patelunas has specifically testified that the test year cost reduction programs at issue will not cause the change in test year supervisory costs hypothesized by witness Buc.

In theory, a change in the operating plan could ultimately (i.e., "in the long run") cause a higher employee/supervisor ratio, a lower ratio, or the same ratio. During the period following such an operating change, however, transitory effects could cause changes in the ratio that are diametrically the opposite of those expected in the long run. The logic behind this result is precisely the same as the logic behind the lagged effects which are, within the context of the effects of mail volumes changes, discussed in the "Summary Description" and noted in the Commission's Opinion. It would be perfectly reasonable to expect that the potential lag time in supervisor cost changes associated with changes in the mail processing environment could materially exceed the potential lag time associated with mere changes in mail volumes. In that case, no matter what assumption is made about the long term ratio trend, based purportedly on the "Summary Description" or on anything else, the "long run" assumption may be entirely irrelevant to the level of accrued costs in the test year.

Mr. Patelunas explained that, in reality, there are practical limits on the portion of the mail flow for which individual supervisors can be held responsible. Tr. 37/17143. This suggests an expectation that, even in the long term, cost reduction programs of the nature at issue in this case may increase the ratio of supervisors to craft employees. Even if that possibility is put aside, however, the issue of timing cannot be blithely ignored, as the Commission appears to have done. The very portion of the "Summary Description" document upon which the Commission relies emphasizes the potentially critical fact that responses in supervisor costs to changes in the underlying costs of craft employees tend to be lagged. The cost reduction program savings in this case were estimated not on the basis of some assumed long-term mathematical proportion, but on the practical experience of program managers contemplating concrete budgets for a discrete period of time.

This highlights, once again, why the Commission cannot properly rely on the statements in the "Summary Description" to justify its rejection of witness Patelunas's explicit testimony explaining how the cost reductions programs have been developed by the program managers, to be integrated into the field budgets, with respect to the specific years for which accrued cost savings have been estimated. The totally different objectives of the analysis described in the "Summary Description" and the analysis presented by witness Patelunas make it inappropriate for the Commission to proffer alleged inconsistencies between the two as a basis to reject his testimony. The two analyses are unconnected. Even if the analyses were connected, differences in timing provide another reason why the alleged inconsistencies are illusory.

Contingency

The Commission's assertion that the record failed to show "how much and why" the contingency provision should be "increased" from the amount used in Docket No. R97-1 is simply wrong. *See* PRC Op., at 75. The discussion of the Postal Service's contingency provision presented by witness Tayman is similar in scope, subject, and length to the discussions he and other previous revenue requirement witnesses have provided, all but one of which were accepted by the Commission. There is no rational basis for concluding that this evidence failed to convey the bases for the 2.5 percent contingency provision. There is ample such testimony on the record and ample citation to the record in the Postal Service's briefs in this proceeding. There is no need to repeat that material here. There is a need, however, for the Commission to explain why such testimony, which was adequate in the past, is no longer adequate. The Commission should reconsider its opinion and recognize that the record supports the Postal Service's contingency provision as adequately as did any past record.

The Commission's insistence on "a clear identification of the nexus between specific test year management goals and revenue sufficiency, and an explanation of why achieving those goals requires the specific contingency amount requested" is unfounded. *See* PRC Op., at 67-68. The Commission apparently is basing this standard on a misreading of testimony regarding the past two omnibus cases in which the contingency provisions were low. Given the unusual nature of those contingency provisions, the Postal Service explained that they were based on extraordinary circumstances in order to meet certain defined management goals in those circumstances. Those extraordinary circumstances are now past, and the Postal

Service has returned to a traditional level of contingency protection. There are no particular goals other than those of the contingency provision itself: to provide a cushion sufficient to ensure that the Postal Service can both operate as required and break even, even in the face of unforeseen events or circumstances. There is no basis for the Commission to impose a requirement that the Postal Service justify the contingency provision on the basis of specific management goals beyond that. As the Governors stated, and the Commission knows well:

> Unlike firms in the private sector, the Postal Service cannot eliminate unprofitable services in hard times. If its volumes and revenues fall short of expectations, it does not compensate by curtailing deliveries in neighborhoods with less mail per stop, or by declining to expand its delivery service to add more stops demanded by new housing and new businesses. Current legal provisions that freeze six-day delivery and allow post office closings to be appealed to the Commission both trace back to Congressional concerns of the mid-1970s when a period of double-digit inflation threatened to overwhelm the Postal Service's finances. Congress intended the ratemaking process to maintain the Postal Service as a healthy going concern with a sufficient contingency provision to overcome unexpected financial adversity.

Governors Decision at 7.

The threat of unexpected financial adversity is as real as ever. The record contains extensive testimony from Dr. Zarnowitz on the uncertain state of the economy. Since he testified, his concerns have been validated by the current state of the economy and the direction it may take toward reduced growth, with the only question remaining whether the landing will be soft or hard. As this is written, the Federal Reserve Open Market Committee has changed its direction to lean toward a reduction in interest rates in order to stimulate the economy and prevent a recession. The President-elect strongly advocates the need to stimulate the economy by means of a massive tax cut. Both he and the Vice President-elect have been quoted as saying that a recession is looming.[11] A recession could further exacerbate the reduction in mail volume growth. In any event, there is no doubt that the economic tide which propelled the Postal Service to financial success in recent years is receding. It should not be a matter of wonder that the Postal Service needs more protection against financial adversity in 2001 than it needed in 1995 and 1998.

The fact that the Commission used updated costs does not reduce the risk. As the above discussion shows, having more and later information can often demonstrate that there is more risk, not less. As the Governors noted, "experience in relatively stable economic times may not necessarily provide a valid basis for predicting the future as business uncertainty increases. ...[T]he odds of unpredictable events' occurring in a future time period do not decrease as that time period approaches." Reconsideration Decision at 9.

The Governors also clearly expressed their disagreement with the notion that analysis of the variance of past estimates provides a basis for determining the appropriate contingency provision for the future. *Id.* They noted, furthermore, that the 2.5 percent contingency provision is reasonable even on the basis of the variance analysis presented in this case.

As the Governors explained, the point of the contingency is not to give the Postal Service an even chance of breaking even or not, but to increase the odds that it will break even or even generate a surplus. *Id.* at 9, 10. In the judgment of the Governors:

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[11] John M. Berry, *A New Bush, the Same Greenspan*, Washington Post, Dec. 19, 2000, at E1.

> The Act plainly contemplates that a reasonable contingency is a natural outgrowth of the need for flexibility in operating and managing the postal system and of the requirement that the Postal Service break even over time. Assuming unbiased cost and revenue projections, revenues are as likely to cover costs on average as not; break-even is theoretically achieved—even without a contingency provision. ...[T]he Act, by specifically including a contingency provision, embodies the expectation that net incomes can be legitimately achieved whenever total unforeseeable expenses are less than the amount of the contingency provision. The possibility of net incomes contributes to the Board's policy options regarding its determination of the timing of future rate increase and the restoration of equity. In Resolution No. 95-9, the Board made clear its belief that restoring equity is important to the financial stability of the Postal Service. This view has been maintained by the Commission as well over the years. Much progress has been made in recovering prior years' losses since the adoption of that Resolution. Continuation of that progress is threatened if the contingency provision is inadequate to fund unforeseeable expenses. Such failures could lead to increasing deficits in successive rate cases, which would seriously undermine the Board's ability to recover past losses. Furthermore, if net incomes were never achieved, because the revenue requirement including contingency exactly met the break-even point on average, then every year would have to be a rate case test year, in order for the Postal Service to break even, even in times of moderate inflation. Neither the Postal Service, its customers, nor the Commission would benefit from such endless rate litigation.

The Commission's reduction of the contingency interferes with the financial goals of the Postal Service, as contemplated by the Postal Reorganization Act and as expressed by the Governors. The Commission has substituted its judgment for that of the Board in fixing the contingency provision. Absent some extraordinary showing of unreasonableness in the Board's judgment, the Commission may not do so.

Finally, the Governors took issue with the Commission's novel reliance on the OCA's analysis of the percentage of the total increase in revenue represented by the contingency provision. *See* PRC Op., at 71-74 and Table 2-1. As the Governors noted, "[t]he measure of the protection that a reasonable contingency should provide depends on the scale of the Postal Service and its obligations to the public, not on the size of the revenue shortfall." Reconsideration Decision at 11. The Commission's reasoning is, as the Governors point out, contrary to the plain language of the statute, which provides for a contingency, even if revenues and operating costs balanced perfectly. Moreover, if the size of the contingency were limited by the size of the shortfall, there would be an incentive toward maximization of future rate increases, contrary to the interests of most mailers. The contingency must protect the entirety of postal operations, at the level of nearly $70 billion annually, and with delivery and service obligations that will grow even if mail volume declines. In light of the relatively small rate increase requested by the Postal Service, and the even smaller increase recommended by the Commission, the drastically reduced contingency provision incorporated in the recommended rates and fees puts the Postal Service at significant risk in the test year.

Appropriate Revenue Contributions

Order No. 1301 directs the Postal Service to provide guidance as to the "appropriate portions of total revenues that each subclass and service should contribute toward collecting sufficient test year revenues in light of the Governors' revenue requirement finding." Order No. 1301 at 3. It further states that the Postal Service "may also suggest specific rates that would achieve these subclass and service specific revenue goals." In this regard, the Postal Service notes that during the hearing stages of Docket No. 2000-1, it persistently cautioned against the consequences of fundamental revision of the financial foundation of its Request by substituting updated data that would in effect create a new FY 1999 base year.[12] In particular, the Postal Service repeatedly noted that replacing the base year at the stage contemplated by the

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[12] *See* Initial Brief of the United State Postal Service, Part I; Reply Brief of the United States Postal Service, Part I.

Commission would have the effect of denying basic due process opportunities to the Postal Service, as well as to other parties, since time and resources would not permit reformulation of specific rate proposals, and exposure of them to record scrutiny, in the time left available in the case. At this juncture, the Postal Service is still not in a position to undertake a comprehensive translation of the new revenue goals dictated by the Order No. 1294 updates and the Commission's recommendations into specific rates. The Postal Service considers this situation to be one of the most difficult problems presented by the Commission's failure to recommend rates that would properly reflect the Postal Service's true revenue needs, once it determined to rely only partially on the updated information.

Nevertheless, the Postal Service submits that critical guidance on the necessary allocation of the appropriate revenue objectives identified by the Governors is already in the record. In particular, the principles that would inform such apportionment should be the same as those proposed by the Postal Service during the hearing phase of the proceeding in connection with its Request. In this regard, we note that the Postal Service was the only party in Docket No. R2000-1 to provide comprehensive proposals guiding the apportionment of the institutional cost burden under the terms of 39 U.S.C. § 3622(b). Specifically, the rate policy testimony of Postal Service witness Mayes (USPS-T-32), and her responses to interrogatories and inquiries from the Commission, provide guidelines for establishing markups. While the specific cost coverages proposed by the Postal Service in USPS-T-32 do not utilize the updated cost and other information relied upon by the Commission in its Recommended Decision, the approach to the assignment of the revenue requirement burden is still applicable.

Specific guidance regarding application of the pricing criteria enumerated in §3622(b) to subclasses of mail is embodied in the record and need not be listed separately here. It would be worthwhile, however, to highlight the pricing considerations that may be of particular importance at this stage of the Commission's deliberations. In particular, subsection 3622(b)(3) dictates that the attributable costs for each subclass and service be treated as a floor for ratemaking purposes. In other words, each subclass of mail must cover its attributable costs. Once that criterion has been met, subsection (b)(4), which calls for consideration of the effect of the rate increases on business mail users, must also be considered.

In this regard, the Commission's Opinion and Recommended Decision reflects disparate treatment of mailers with regard to the effect of rate changes that could be remedied upon reconsideration. For example, despite evidence of increasing costs, the Commission recommended that some subcategories of mailers or users of postal services should benefit from rate and fee decreases. In its Opinion, at Appendix J, page 7, the Commission provides a summary of the changes in unit attributable costs from the test year used in Docket No. R97-1 to the test year used in Docket No. R2000-1. A comparison of these unit cost changes to the percentage rate increases recommended by the Commission demonstrates that, in some cases, the two movements are not consistent. For example, despite the increase in Money Order costs of 17.93 percent, as reported in Appendix J, the Commission recommended that the fees for Money Orders be decreased by more than 4 percent. Similarly, despite the increase in unit attributable costs for First-Class Cards of 12.27 percent, as reported in Appendix J, the Commission recommended a rate increase of only 0.4 percent, and even this small increase in card revenue per piece is due to the increase in the misapplication of First-Class Mail letter postage to cards rather than to increases in card rates.

Furthermore, the Commission reduced the additional ounce rate for First-Class Mail in the face of cost information that is inconclusive with respect to determining a rate with the highest degree of precision. In other words, as reflected in the testimony presented, the same cost data could be used to support a range of possible prices encompassing both the Postal Service's proposed 1-cent increase to 23 cents, as well as the Commission's recommended 1-cent reduction to 21 cents. In this regard, the Commission's Opinion points to the objective of reducing the cost coverage for First-Class Mail Letters as the primary reason to reduce the additional ounce rate. There is no evidence, however, that additional-ounce costs, whatever their level, have declined from the test year used in the previous omnibus rate case, Docket No. R97-1. Under either the Postal Service's proposed increase or the Commission's recommended decrease, there was never any question that the rate covered the cost of the additional ounce. Therefore, the Postal Service urges that § 3622(b)(4) be given more weight in the decision regarding the additional ounce rate, in the context of the need for additional revenue, and in light of the impact of any decision to transfer the revenue from additional ounces to other categories of mail.

It is also important to note that institutional costs have been rising at a greater rate than attributable costs, as a result of increased mailer worksharing, which tends to reduce attributable costs but has no effect on institutional costs. This phenomenon was noted in the testimonies of both witnesses O'Hara in Docket No. R97-1 (USPS-T-30) and Mayes in Docket No. R2000-1. Consequently, even if the Commission were to modify its recommended rate increases in accordance with the increases in attributable costs displayed in its Docket No. R2000-1 Opinion, Appendix J at page 7, the revenue raised through such means would be inadequate to cover the institutional cost burden. Therefore, the Postal Service notes that Appendix J might be useful for discussion of some pricing criteria, but is not especially useful in raising adequate revenue to cover the entire cost of operating the Postal Service. By cutting the revenue requirement, the Commission appears to have tried to avoid many of the tough decisions associated with assignment of institutional cost burden and has simply given much of the benefit of the reduced revenue requirement to First-Class Mail.

FIRST-CLASS MAIL ADDITIONAL OUNCES

In its Opinion at page 250, the Commission states that, of the two approaches for handling additional ounces of First-Class Mail advanced on the record -- the "as-filed" method and the "historical" method -- it chose to use the "as-filed" method, albeit applied to the most recent billing determinant data from the Hybrid period. The mechanics of the "as-filed" method were presented during the proceeding by Postal Service witness Thress (USPS-T-7) in his Workpaper 4, and the accompanying spreadsheets were filed as part of USPS-LR-I-122.

From examining the additional ounce results relied upon by the Commission in light of the "as-filed" methodology detailed by witness Thress, it appears that the Commission has correctly followed the first portion of that methodology to derive the total number of test year additional ounces. That is the portion of the process described in section II.A of Workpaper 4 ("Total Additional Ounces Associated with Single-Piece First-Class Letters"). In Section II.B of Workpaper 4, however, witness Thress further describes the second portion of the "as-filed" methodology which generates the "Distribution of Single-Piece First-Class Letters Additional Ounces by Weight Increment." This additional step is necessary because the "as-filed" methodology assumes shifts in the pattern of additional ounces between the base period and the test year, in contrast with the "historical" methodology, which assumes a constant, identical pattern of additional ounces in both the base period and the test year. The shifts assumed in the "as-filed" methodology affect the distribution by weight as well as the total number of additional ounces.

It appears, however, that the Commission has neglected to take the second portion of the "as-filed" methodology into account in estimating test year expenses associated with the test year additional ounces it has forecast. Witness Thress developed his weight distribution analysis to provide input into the final adjustment models sponsored by witness Daniel (USPS-T-28). The Commission, in turn, also used those final adjustment models (with modifications not relevant to this discussion). Therefore, to the extent that the Commission stated its intent to use the "as-filed" methodology, one would have expected to see the Commission take account of a changed additional-ounce weight distribution when calculating its final adjustments, just as witness Daniel initially used the new weight distribution provided by witness Thress. Instead, it appears that the Commission's final adjustment models assume the exact same weight distribution for additional ounces as observed in the Hybrid base period. This assumption would have been appropriate under the "historical" approach, which is why it was the assumption applied in USPS-LR-I-483 and I-484, but it is inappropriate for the "as-filed" approach upon which the Commission's revenue estimates are based.

Assuming that the above discussion accurately describes the situation, it would appear that the Commission's final adjustment models need to be revised to apply the "as-filed" methodology consistently, and to recognize the implicit shift in the additional ounce weight distribution assumed by that methodology. [13] What are believed to be the appropriate weight distribution changes are appended as Attachment 1, which updates witness Thress's weight distribution analysis for the hybrid year base period and the Commission's TYAR volumes. This analysis was originally performed by witness Thress in file AO_BR_wk4 of USPS-LR-I-122 and was described in part II.B of his Workpaper 4. When this new, heavier single-piece weight distribution is incorporated into the final adjustment model, the result appears to be a single-piece final adjustment of $80.053 million, or $21 million higher than the $59.387 million calculated by the Commission in its Recommended Decision.[14]

BOUND PRINTED MATTER

At page 13 of their December 4, 2000, Decision, the Governors expressed concern about the Commission's recommended rates for Bound Printed Matter. The

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[13] Alternatively, if that is not the case, the Commission is requested to identify where within its supporting documentation it has otherwise taken account of the cost effects of the shifting weight distribution of additional ounces.

[14] Although there are probably a number of ways to update the final adjustment models for the heavier weight distribution associated with the as-filed method, one way that seems computationally direct is to overlay the new distribution on the existing line for Standard A ,and disable the other lines for less than 11 oz., new 11-12 ounce Priority

(continued...)

Commission's November 13, 2000, Opinion indicates that its recommended Bound Printed Matter rates reflect an average increase of 17.6 percent. It appears,however, that, as a consequence of an error in the Commission's calculation of the revenue consequences of the new dropship discounts, the recommended rates only reflect an average increase of 9.8 percent. Thus, instead of the $560.7 million revenue projection shown in Appendix G of the Commission's Opinion, the recommended Bound Printed Matter rates, using the Commission's volume projections, will produce revenues of only $530.1 million. In addressing the Governors' concerns, the Commission is invited to review its Workpapers in PRC Library Reference 17, which pertain to Bound Printed Matter. There appear to be four errors in the Revenue Workpaper that, when combined, result in the approximately $30 million dollar overstatement of revenues generated by the Commission's recommended Bound Printed Matter rates. These apparent errors are described below:

- Destination Sectional Center Facility (DSCF) per-piece revenue leakages seem to have been incorrectly calculated by multiplying DSCF piece volume by the DSCF *per-pound* discount;
- DSCF per pound revenue leakages appear to have been erroneously calculated by multiplying DSCF pounds by a hardwired number that is not the Commission's estimated per-pound discount;
- Destination Delivery Unit (DDU) per-piece revenue leakages seem to have been calculated by multiplying DDU piece volume by the DDU *per-pound* discount; and
- DDU per pound revenue leakages appear to have been erroneously calculated by multiplying DDU pounds by a hardwired number that is not the Commission's estimated per-pound discount.

(...continued)
Mail, and new 12-13 ounce, Priority Mail, as none of those lines are needed for their original function in the context of this updated final adjustment.

In re-examining PRC-LR-17, the Commission should review the Piece Workpaper. There, it seems that Carrier Route leakages have been incorrectly calculated by multiplying the number of Carrier Route pieces by the unrounded Carrier Route discount and then inappropriately dividing the result by 100. In that same Workpaper, it also appears that the single-piece barcode revenue leakage was incorrectly calculated by multiplying the per-piece barcode discount by the number of single mail pieces and then, inappropriately multiplying the result by the share of Bound Printed Matter drop-shipped to Auxiliary Service Facilities, rather than by share of single-piece Bound Printed Matter with barcodes.

The Commission's re-examination of PRC-LR-17 also should include the Pound Workpaper, which appears to reflect a discrepancy in the calculation of the zones 1&2 per pound charge. The markup factor used to calculate the charge for these zones is hardwired into the spreadsheet and differs slightly from the markup factor used for all other zones.

The following discrepancies also seem evident in the PRC-LR-17 Revenue Workpaper calculation of presort revenues:

- Piece revenues are calculated by multiplying the number of presort pieces by the per-piece rate, rounded to three decimals, and not by the Commission's recommended piece rate, which is rounded to two places; and
- Pound revenues are calculated by multiplying the number of zoned postage pounds by the zoned per-pound charges, rounded to three decimal places, and not by the Commission's recommended pound rates, which are rounded to two places.

The PRC-LR-17 Revenue Workpaper also seems to include a discrepancy between the single piece revenues and the recommended rate table. Single piece Bound Printed Matter revenues are calculated by multiplying the number of single pieces and pounds by zone times the per-piece and per-pound elements, rather than by using the recommended rate table. The per-piece and per-pound rate elements cannot generate the rate table , since the table has many *ad hoc* adjustments made to various rate cells, without any discernable pattern.

In the PRC-LR-17 Revenue Workpaper, there also appears to be a discrepancy in the manner in which the carrier route adjustment to presort revenues is calculated. Carrier route pieces are multiplied by the carrier route discount, rounded to three decimal places (rather than two, as in the discount recommended by the Commission), and this calculated revenue leakage is used to adjust the presort revenues.

Finally, in the PRC-LR-17 Revenue Workpaper, there may be a discrepancy in the method by which the revenues are adjusted. Destination Bulk Mail Center (DBMC) revenue leakages are calculated using the DBMC per-piece and per-pound discounts, rounded to three decimal places, rather than the two decimal place figures which appear in the recommended rate schedule. This calculated revenue leakage is used to adjust the presort revenues.

If, as a result of addressing the discrepancies listed above, the Commission should deem it appropriate to change its Bound Printed Matter rate recommendations, the Postal Service requests that the Commission's new rates not reduce the worksharing differentials reflected in the rates which have been allowed into effect under protest.

NONPROFIT STANDARD MAIL

In its discussion of the impact of legislation on the rates recommended for the preferred subclasses of Standard Mail, the Commission notes that the timing of the enactment of the new legislation precluded the opportunity for discussion by the parties of how this legislation should be implemented. Opinion at 398. The Postal Service recognizes this fact, and appreciates the need for swift action by the Commission to incorporate the new legislative directions into its recommendations. Nonetheless, in one respect, it appears as if the Commission may have departed from the intent of the new legislation.

The Opinion correctly notes that the new law "provides that Standard A Nonprofit rates, overall, are to be set so that the estimated average revenue per piece from each subclass is equal, as nearly as practicable, to 60 percent of the estimated average revenue per piece from the corresponding regular rate category." Opinion at 397. This description, while accurate, omits one critical detail further provided in the new legislation. Section 1(d) of the bill (Public Law No. 106-384) includes a section, which will now appear as subsection 6(B) of 39 U.S.C. 3626(a), specifying that in calculating the average revenues per piece necessary to calibrate the recommended rates to the prescribed relationship, the volumes and mail mix employed shall be those expected "at current rates in the test year of the proceeding." In more vernacular rate case jargon, this provision establishes the TYBR billing determinants as those at which, when applied to potential TYAR rate schedules, the resulting average revenue per piece of each preferred subclass should be as nearly as practicable 60 percent of that of the corresponding commercial subclasses.[15] The benefit of this provision is that it allows the rate designer to know, even in advance of the final after-rates volume forecasts, whether the proposed rates meet the 60 percent target. The necessary TYBR billing determinants appear in USPS-LR-I-436.

It appears that instead of using the TYBR billing determinants contemplated by the statute, the Commission may have used TYAR billing determinants. Specifically, its workpapers look as if the Commission established a target Nonprofit average revenue per piece by applying the 60 percent factor to a commercial average revenue per piece calculated with TYAR billing determinants. The Commission apparently then designed its Nonprofit rates to yield, when iteratively applied to new TYAR Nonprofit billing determinants, the target revenue per piece derived by that procedure.[16]

If this is an accurate description of the process, the obvious result is a TYAR to TYAR comparison (in terms of billing determinants), rather than the required TYBR to TYBR comparision. In that case, to bring rate design into conformance with the new statute, TYBR billing determinants would need to be substituted for TYAR billing

[15] For purposes of this discussion, the term "TYBR billing determinants" is used to describe the volume distribution by rate cell that is generated by applying the base period mail mix proportions to the TYBR volume forecast.

[16] In fact, the revenue per piece information in Appendix G, page 1, which is based on TYAR volumes, suggests that indeed the target was developed, and met, using TYAR volumes. For both Nonprofit and NECR, the revenue per piece shown on that page is almost exactly 60 percent of the commercial counterpart. In contrast, as shown in the following table, applying the same new rates to TYBR billing determinants generates average revenue per piece relationships that, while certainly in the near vicinity of 60 percent, are not as close to that target as those implicit in Appendix G, based on the TYAR billing determinants. Although it is acknowledged that the calculations shown on the bottom of the attachment are merely illustrative, because of complications involving fee revenues, it is not believed that the apparent direction of the effect (of using TYAR rather than TYBR billing determinants) is altered by that complication.

determinants when developing the target, and again when determining if the proposed nonprofit rates meet that target. The effect of substituting TYBR for TYAR billing determinants *in this instance* seems to suggest that the recommended nonprofit rates are actually below the intended statutory target. It perhaps bears noting that in other instances, the effect could just as easily be the reverse (i.e., a *lower* target nonprofit revenue per piece using TYBR, rather than TYAR, billing determinants).

COMMISSION RECOMMENDED RATES AND FEES
APPLIED TO TYAR BILLING DETERMINANTS
(APPENDIX G, SCHEDULE 1)

	Regular	Nonprofit	ECR	Nonprofit ECR
Revenue	$9,075,572	$1,520,815	$5,156,258	$266,550
Volume (000)	41,000,842	11,463,830	32,905,893	2,844,821
Rev/PC (cents)	22.135	13.266	15.67	9.37

Nonprofit as Percentage
of Commercial **59.93%** **59.80%**

COMMISSION RECOMMENDED RATES
APPLIED TO TYBR BILLING DETERMINANTS*

	Regular	Nonprofit	ECR	Nonprofit ECR
Revenue**	$9,500,751	$1,505,299	$5,272,094	$268,927
Volume(000)	42,783,773	11,510,795	33,630,517	2,907,206
Rev/PC (cents)	22.206	13.077	15.677	9.250

Nonprofit as Percentage
of Commercial **59.89%** **59.00%**

*TYBR Billing Determinants

TYBR Volumes Distributed on Hybrid PeriodBilling Determinants,
from USPS-LR-I-436, Standard Mail (A) portion:
WP 1, pages 5-6 (Regular); WP 1, page 7 (ECR);
WP 2,Pages 5-6 (Nonprofit); and WP 2, page 7,(Nonprofit ECR).

** Revenues

Revenues have been calculated using recommended rates, but existing (R97-1) fees. It is anticipated that the likely effective of using recommended fees would have been to push the percentages in the direction of 60 percent, but still leave them lower than those implicit in Appendix G, shown above.

REQUEST FOR EXPEDITION

As explained above, the Postal Service has elected to initiate comments on reconsideration on the earlier of two alternative dates proposed by the Commission in Order No. 1301. The Postal Service strongly believes that expedition at this stage is critical, in light of the substantial difference between the Governors' estimate of the Postal Service's revenue needs, and the Commission's recommendations. Currently, the test year on which those recommendations are based is already one-quarter completed. Furthermore, even the accelerated schedule proposed by Order No. 1301 envisions pleadings being filed in the last part of January. Clearly, Commission deliberations and the effort needed to produce a Further Recommended Decision will consume a significant amount of time, especially if the Commission agrees with the Governors on the need to recommend rates that will generate additional revenue. Under the current schedule, the test year could be half completed before the Governors are able to consider the Commission's next recommendations.

As noted above, the Governors have strongly urged the Commission to reconsider and issue a further recommended decision as quickly as possible. Reconsideration Decision at 1, 12. The Governors' concern regarding the Postal Service's financial situation, and the prospects for the remainder of the test year, as reflected on the record, were among the factors that motivated them to elect to allow under protest and accept the partial revenue relief afforded by the Commission's inadequate rate recommendations. Those same considerations militate strongly in favor of a quick disposition of the limited issues raised on reconsideration. The Governors must be in a position to act effectively under their options in 39 U.S.C.

§ 3625, whether or not the Commission decides to recommend rates that will produce needed additional revenue.

In light of the approaching holidays, as noted in Order No. 1301, it may be unrealistic to expect that much time could be eliminated from the Commission's alternative schedule. Nevertheless, the Postal Service believes that at least an additional week could be gained, if the parties commenting on this memorandum were not given as much as three weeks to respond.[17] In this regard, we note that, except for the relatively smaller technical issues related to First-Class Mail, Bound Printed Matter, and nonprofit Standard Mail, the issues raised by the Governors regarding the revenue requirement were all thoroughly discussed and briefed by the parties during the hearings stages of the case. Furthermore, the prospects for recommendations of rates within the range indicated by the Governors' disagreement with the Commission on revenue needs are no greater or more complicated now than they were when the record closed. In other words, it is unlikely that the parties could be expected to need considerably more information or time to respond to the issues raised by the Governors than they already have had. None of the revenue requirement issues is new. In a comparable situation in Docket No. R90-1, where arguably the issues raised on reconsideration were technically much more complex, the Commission afforded parties only 15 days to respond to the Governors' request for reconsideration.[18] Accordingly,

[17] The Postal Service notes that the $1 billion at issue in the reconsideration averages to nearly $20 million per week.

[18] Order Allowing Participants to Comment on Governors' Request for Reconsideration, Order No. 877, Docket No. R90-1 (Feb. 5, 1991). The Postal Service's lengthy memorandum addressing the issues raised by the Governors was filed on the same day Order No. 877 was issued. Memorandum of the United States Postal Service in (continued...)

the Postal Service strongly requests that the responding parties be allowed no later than January 3, 2001, to comment. The Postal Service would reply as soon as possible thereafter, in no event later than January 10. This would allow the Commission three weeks to deliberate and issue a Further Recommended Decision prior to Governors' subsequent meeting in February.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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December 20, 2000

CERTIFICATE OF SERVICE

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

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(...continued)
Support of Reconsideration, Docket No. R90-1 (Feb. 5, 1991). Responding parties were able to reply to the Postal Service's memorandum in their comments filed approximately two weeks later.

	Hybrid, 1999Q3 - 2000Q2		Additional Ounces by Weight Increment (ounces):											
	Pieces	Addl. Ozs.	1.0-2.0	2.0-3.0	3.0-4.0	4.0-5.0	5.0-6.0	6.0-7.0	7.0-8.0	8.0-9.0	9.0-10.0	10.0-11.0	11.0-12.0	12.0-13.0
First-Class Letters & Flats														
-- Single-Piece	53,098.013	19,412.381	18.06%	14.14%	11.62%	10.01%	8.45%	7.63%	6.64%	6.14%	5.29%	4.70%	4.01%	3.31%
-- Workshared	43,725.202	2,638.365	46.47%	20.23%	8.53%	5.29%	2.94%	2.48%	2.85%	3.02%	2.62%	1.91%	2.03%	1.61%
Total First-Class Letters	96,823.215	22,050.746	*21.46%*	*14.87%*	*11.25%*	*9.45%*	*7.79%*	*7.02%*	*6.19%*	*5.77%*	*4.97%*	*4.36%*	*3.77%*	*3.10%*

	GFY 2001													
	Pieces	Addl. Ozs.	1.0-2.0	2.0-3.0	3.0-4.0	4.0-5.0	5.0-6.0	6.0-7.0	7.0-8.0	8.0-9.0	9.0-10.0	10.0-11.0	11.0-12.0	12.0-13.0
First-Class Letters & Flats														
-- Single-Piece	52,828.895	19,952.919	3,568.533	2,813.841	2,322.237	2,003.741	1,693.192	1,529.230	1,329.677	1,228.897	1,058.118	940.901	802.664	661.893
-- Workshared	47,320.291													
Total First-Class Letters	100,149.186													

Notes:

1. This table modifies the table originally filed in USPS-LR-I-122 (File: AO_AR.wk4) by using the hybrid year as the base period and by using the PRC's after rates volume forecast.
2. The hybrid year single-piece weight distribution is Attachment B to the USPS response to NOI 3 (originally Attachment 1b to POIR No. 11, Question3).
3. The hybrid year workshare weight distribution can be derived by adding the workshare components shown in the Attachment to POIR No. 13, Question 7.

ATTACHMENT 1