REPLY OF THE UNITED STATES POSTAL SERVICE TO COMMENTS OF PARTICIPANTS IN RESPONSE TO THE POSTAL SERVICE’S MEMORANDUM ON RECONSIDERATION

In accordance with Order No. 1301, the Postal Service hereby provides its reply to the comments of participants in response to the Postal Service’s Memorandum on Reconsideration.

I. THE COMMISSION’S LIMITED AUTHORITY TO ADJUST THE REVENUE REQUIREMENT DOES NOT SUPPORT RECOMMENDATION OF A 1.2 PERCENT PROVISION FOR CONTINGENCIES

The OCA and various intervenors who address the revenue issues raised on reconsideration outline an interpretation of the Commission’s authority that departs dramatically from the statutory scheme, as interpreted over thirty years by the Governors and the courts. Under these views, the determination of the revenue requirement, and especially the selection of a “reasonable provision for contingencies,” is the product of the Commission’s hearing process, pursuant to 39 U.S.C. § 3624. The parties commenting argue that, in that process, the Commission exercises the authority,

indeed the responsibility, to determine the Postal Service's revenue objectives. Specifically, the Consortium asserts that "determining the size of a 'reasonable' contingency is an integral part of the ratemaking responsibilities given by Congress to the Commission." Consortium at 2. They contend that the Commission carries out this responsibility, furthermore, by weighing and synthesizing evidence and argument submitted by the Postal Service and the parties opposed to the Postal Service's stated revenue goals. In the OCA's formulation, "[t]he Commission exercises its authority during the 'intermediate process' (i.e., Section 3624 proceedings) to evaluate the strength of the evidence submitted by the Postal Service and other participants and to make independent, substantive determinations based on the record." OCA at 8. In other words, in this view of the exercise of the Commission's authority over the revenue requirement, the Commission sits as judge of the Postal Service's revenue needs, including all of the financial and operational policy choices they embody, and has wide discretion to credit or discredit the Postal Service's estimates, as long as some evidence in the record supports the Commission's conclusions. These powers of decision, moreover, extend not only to the review of the accuracy of expense estimates,

2 The Commission's role as "judge" in this characterization is an explicit element of the OCA's interpretation:

Unlike the Postal Service, the Commission cited and described the record evidence it relied upon, setting forth its findings in a logical, orderly manner so that a reader could easily discern the reasoning path. The Commission's 40-page discourse on the contingency is a demonstration of the adjudicative process in its best sense: the evidence was painstakingly reviewed and weighed; the principles to be applied were articulated; those principles were applied to record facts; and the conclusions reached were clearly stated.

OCA t 11 (emphasis supplied)
but also to the subjective evaluation and determination of the fundamental policy choice regarding the assessment and acceptance of risk against the unforeseen, which is embodied in the provision for contingencies.

This encompassing view of Commission control over the revenue requirement is not without concession to some limitations. The rationality of this outline of the statutory ratemaking scheme is explained and reconciled with the actual language of the statute, as bearing a perfectly logical relationship to the other explicit authorities assigned to the Governors and the Postal Service in the statute. Citing the Commission's Opinion in this case, the OCA explains that the Commission's functions yield to the "primacy" of the Governors' role in revenue issues to the extent that the Commission's hearing process is sandwiched between the Postal Service's authority to initiate rate cases in 39 U.S.C. § 3622(a) and the Governors' authority to modify the Commission's recommendations in 39 U.S.C. § 3625(d). OCA at 7. The meat of the sandwich, however, is the Commission's power to decide how much revenue the Postal Service really needs to operate and carry out financial policy.


4 In the context of the contingency issue, the OCA appears to detract somewhat from this acknowledgment of Governor primacy by suggesting a clarification of the Postal Service's authority to initiate rate cases. OCA at 15. Contrary to section, 3622(a), which assigns that authority to the Postal Service in accordance with its assessment of need and public interest, the OCA states:

The nature of subsection (b)(3) and the importance placed upon it by Congress strongly indicate that rate increases are to be imposed upon the public only when absolutely necessary and upon particular classes of mail only when the Commission is satisfied that they have been caused, at least in part, by those particular classes. (continued...)
While the commenting parties do not raise the elements of this portrait of the balance of authorities here for the first time, their pleadings on reconsideration stand in stark contrast to the Governors' and the courts' interpretations or the Postal Reorganization Act (Act) since the beginnings of postal reorganization. In fact, in the formulations asserted on reconsideration, we appear to have come full circle back from the judicial rejection of these views in the early 1980s, when the Commission last attempted to dictate financial policy through cuts in the revenue requirement in a rate case. In this regard, it would serve little purpose to repeat in detail the arguments supporting the Governors' views that prevailed in court at that time and that have been reasserted many times subsequently. The Commission's interpretation of its own statutory prerogatives by now appears resistant to change in the face of the logic of these arguments, or the judicial conclusions that are consistent with them.

Furthermore, we have shown below that, even assuming a relatively wide scope for the Commission's assessment of the Postal Service's revenue requirement estimates, on the record of this case the Postal Service's proposed revenue requirement is strongly supported, and the Commission's Recommended Decision should be reconsidered.

4 (...)continued

Id.


We will, however, reemphasize here several salient deficiencies in the OCA's and the intervenors' contentions.

First, we note that the statutory construction of the Commission's authority put forth by the parties is almost entirely the product of inferences drawn from the relationships among various provisions of the Act, rather than explicit grants of authority in the statutory language. Thus, while section 3621 explicitly refers to the Governors' authority to fix rates and fees necessary to break even, the Commission's authority, in effect, to enforce breakeven through its limited ratemaking function is argued to derive from the general reference to "policies of this title" in section 3622. Furthermore, section 3624, which it is argued embodies the mechanism through which determination of the revenue requirement is made, nowhere refers to specific Commission authority with regard to any substantive element of any part of the Postal Service's Request. The argument assumes global Commission powers of decision, without regard to any of the limitations on its authority inherent in the statutory scheme and legislative intent. Specifically with regard to the contingency, the OCA posits that the Commission's authority to make that determination derives in part from its responsibilities to apply the principle of cost attribution in section 3622(b)(3). OCA at 14-15. The OCA seems to be arguing that the Commission has the responsibility to mitigate the size of the contingency, and therefore has the authority to determine the size of the contingency, because contingent expenses cannot be reliably traced to mail classes in advance. In this regard, we note that the same methodology for allocating the contingency as a

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7 We have elsewhere discussed the limitations of this analysis. See Initial Brief of the United States Postal Service, at II-20-22.
proportional burden among various mail categories has been followed from the beginning, and has seldom been a topic of controversy. Furthermore, there is no logical link between the Commission's limited function in allocating costs and designing rates and its purported authority to determine the overall level of costs. In the absence of an explicit grant of authority in the statute, the Commission's role in the statutory scheme cannot override the Governors' and the Postal Service's prerogatives embodied in other parts of the statute.

The same may be said of the Consortium's argument that the Commission's role in applying the factors in section 3622(b) indicates that it has control over the size of the contingency. Consortium at 9-10. The Consortium argues that the "complex balancing act" of applying the ratemaking factors can only be performed by the Commission, and, as a result, "only the Commission is able to assess what is a 'reasonable' contingency in light of both the Postal Service's needs and the public interest." This formulation ignores the fact that under the explicit terms of section 3622(a) it is the Postal Service, not the Commission, that determines when additional revenues are needed and whether a change in rates is in the public interest. As with the OCA's argument, the Consortium's more general formulation cannot override the important policy prerogatives reserved for the Postal Service and the Governors in the statutory scheme.

Second, the Consortium attempts to argue that the legislative history of the Postal Reorganization Act supports the assertion of Commission control over the revenue requirement. Consortium at 3. Citing statements made by sponsors of the legislation, the Consortium contends that these affirmations of the intended status of the
Commission as an independent agency, and the limitations embodied in the statutory procedure for modification by the Governors, indicate Congress' intent that the Commission should have control over elements of the revenue requirement through the hearing process and through its limited function of recommending specific rates and fees. Here again, the attempt to bootstrap plenary authority over the substance of the Postal Service's Request from the limited authority given the Commission in the statutory scheme must fail. Neither the Commission's independence nor the Governors' modification authority logically dictate that the Commission's role in reviewing the Request for purposes of recommending rates overrides the Postal Service's and the Governors' authorities. In particular, restrictions on the Governors' power to modify in no way compel the conclusion that the Commission enjoys the prerogative to make substantive determinations regarding the size of the revenue requirement, especially where they would conflict with the Postal Service's and Governors' policy prerogatives. The Consortium suggests that Congress would not have created the modification option unless it intended the Commission to be able to determine the Postal Service's revenue needs. However, while it is clear that the modification option is available to correct a situation where the Commission has improperly exceeded its authority by usurping the Postal Service's and the Governors' prerogatives to determine revenue needs, logically that is not the only circumstance in which it might be employed. It is just as reasonable to conclude that modification was intended to apply more commonly in situations where the Commission has erroneously,
or unreliably, estimated the revenue consequences of a particular rate design. In the absence of an explicit grant of authority in the statute, the existence of the modification option is unpersuasive as an indication of Congressional intent regarding the Commission’s authority to determine the contingency.

Focusing on the Act’s legislative history, we believe a more compelling indication that Congress did not intend to bifurcate authority over financial policy and revenue need is found in many references to unification of control as an overriding purpose of postal reorganization. Clearly, in passing the Act, Congress was attempting to move away from a set of circumstances that had hindered efficient postal operations. As stated in the report accompanying the House version of the legislation:

It has now become apparent that all the shortcomings of the Post Office Department are bound up in the fact that responsibility for managing the system is shared by a number of executive agencies and by several congressional committees. Therefore, the only solution to these problems is fundamental reform that puts complete responsibility in a single place, with appropriate safeguards against abuse of that responsibility and appropriate assurances of continued congressional surveillance.

Top management must be given authority, consistent with its responsibilities, to provide an efficient and economical postal system. Postal management has been severely and unjustly hampered in its efforts to administer the Department in a businesslike way.

An effective postal service needs an updated financial policy that is fully responsive to operating needs. The present financial arrangements are a hodgepodge of sometimes conflicting and often obstructive limitations.


A similar message was conveyed in the Senate Report:

The committee in no way deprecates the system of checks and balances established in the law over the years to insure that public policy as determined

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by Congress shall be followed by the Postmaster General. But it has found that, by the process of accumulation, the laws controlling the governance of the Department have become excessively restrictive and that it is not too soon for a complete break with the past. . . .

The areas of "no control," tending to foster drift and to inhibit innovation and imagination in the management of the Post Office even under the leadership of strong Postmasters General, can be overcome by four provisions of S.3842: (1) continuity of top management, (2) the authority to control postal revenue, (3) the authority to control costs, and (4) the authority to acquire funds outside the budget to modernize the postal plant.

S. 3842 is no halfway measure. Its objective is to establish a postal structure and a method of operating that will entrust management of the U.S. postal service, within broad policy guidelines designed to protect the ordinary mailer, to responsible public officials whose authority derives from the President.

S. Rep. No. 912, 91st Cong., 2d Sess. at 2-3 (June 3, 1970). We believe that these expressions of intent seriously undermine the arguments supporting Commission control over the revenue requirement.

Third, the Consortium cites dicta in several court cases to support its arguments regarding the Commission's authority over the contingency element of the revenue requirement. While we have discussed this and other caselaw extensively elsewhere, we emphasize one point here regarding the Second Circuit Court of Appeals' holding in Newsweek. Regarding the entire decision in that case, but particularly with respect to the contingency, the Commission has interpreted its holding very narrowly. It has often repeated the following conclusion regarding the limitations placed by Newsweek on its authority to review the revenue requirement:

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9 See Postal Service Initial Brief, Part II; Reply Brief of the United States Postal Service, at II-2-14.

we have concluded that the Commission has both the authority and the responsibility to make adjustments in the Postal Service’s proposed revenue requirement, so long as our adjustments are not arbitrary, our reasoning is fully articulated and based upon substantial evidence in the record, and where our adjustments have neither the intent nor the effect of causing more frequent rate filings nor constitute an intrusion into the policymaking domain of the board in accordance with the holding in Newsweek.

Id. at 25 (footnote omitted). This formula, furthermore, has frequently been recited by supporters of the Commission’s authority to adjust the revenue requirement, who emphasize the requirement of reasoned explanations of the Commission’s adjustments as a way to overcome the limitations imposed by the holding in Newsweek regarding the contingency. See Consortium at 7; ABA/NAPM at 4. In this regard, it is suggested that as long as the Commission engages in careful analysis of its reasons for reducing the contingency, and explains its approach and conclusions adequately, it can overcome the adverse result in Newsweek and demonstrate that its actions were not arbitrary.

While there is superficial support for this conclusion in the Commission’s and other advocates’ analyses of Newsweek, any attempt to apply the holding should start with the actual facts of that case and the court’s precise language. The court did find that the Commission’s reduction of the proposed contingency provision was arbitrary. What was before the court, however, was far from a superficial, unexplained analysis. Rather, the Commission’s discussion of its reduction of the contingency represented one of the most detailed analyses of the contingency that it has ever attempted, with heavy emphasis on an objective assessment under the so-called variance analysis. See PRC Op. R80-1, Vol. 1, at 18-40. Nevertheless, the court agreed with the Governors that the Commission’s adjustment of the contingency was arbitrary.
Newsweek at 1205. Furthermore, the court explicitly stated “we conclude that this decision also was an unlawful intrusion into the policy-making domain of the Board.” Id.

Any attempt to evade the importance of this holding by limiting it to the “disciplinary” nature of the Commission’s actions in Docket No. R80-1, moreover, must deal with another of the court’s conclusions in Newsweek, namely, that intent may not matter. The court concluded:

Whether or not it was the intent of the PRC to cause more frequent rate filings by eliminating nearly $1 billion from the Postal Service’s revenue requirements, the Board determined that the PRC’s action would necessarily have that effect.

Newsweek at 1204.

Fourth, the Consortium argues that the Governors’ protest against the Commission’s reduction of the contingency is inconsistent with “long-standing ratemaking practice.” Consortium at 9. The Consortium suggests that the Postal Service’s willingness to present testimony justifying the contingency provision in prior cases demonstrates that “the contingency has been understood to be within the Commission’s ratemaking authority and not within management’s discretion.” Id.

Nothing could be farther from the truth. Even a passing familiarity with the history of ratemaking under the Act would establish that the question of the Commission’s authority to reduce the revenue requirement has been a matter of serious contention from the very beginning. As the Governors’ Decision in this case shows, the Governors have never conceded that the Commission has the authority to infringe upon their management prerogatives through recommendations regarding reductions to the Postal Service’s revenue needs. The Postal Service, furthermore, has not accepted the
Commission's preferred approach to analyzing the reasonableness of the contingency, particularly with respect to quantitative variance analysis. On the contrary, if the history of ratemaking under the Act demonstrates anything, it demonstrates that the Commission's approval of the reasonableness of the proposed contingency provision is the norm. In the one instance in which the Commission chose to reduce the contingency through a detailed variance analysis, its decision was overturned as arbitrary.\(^{11}\)

Finally, both the Consortium and ABA/NAPM suggest that the Commission's action reducing the contingency provision in the instant case is authorized by the court's holding in *Association of American Publishers Inc. v. Governors of the U.S. Postal Service*, 485 F.2d 768, 773 (D.C. Cir. 1973)(AAP). Consortium at 15; ABA/NAPM at 2.

Under this argument, the Commission has the inherent authority to "split the difference" between two proposals on the record. This precedent in the current situation, however, is completely inapposite. The court's holding in AAP resolved a situation involving two costing studies, both of which were supported on the record, but neither of which was

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\(^{11}\) The OCA cites the Commission's observation regarding the nature of the record created in Docket No. R2000-1 on the contingency as a means of distinguishing the prior practice and precedent on this issue. OCA at 9-10. The OCA chides the Governors for choosing

to ignore the Commission's explicit declaration that, unlike prior cases where there was an "absence of participants' initiatives to explore the subject [of the contingency] on the record," in R2000-1 "participants have made voluminous presentations on the contingency provision, challenging the Service's proposal on a variety of grounds." PRC Op. R2000-1, ¶¶ 2150-51.

*Ibid.* at 10. This distinction is almost entirely invalid. Over the course of eleven omnibus rate cases, the contingency has been one of the most heavily addressed issues related to the revenue requirement in almost every case.
free from defects, not adjustment of a proposed contingency provision, which represents an important policy choice by the Board of Governors.

II. THE REASONABLENESS OF THE POSTAL SERVICE'S CONTINGENCY WAS FULLY SUPPORTED ON THE RECORD.

The Postal Service's support for its contingency presented on the record in this case differed neither in quantity nor in quality from the support it presented in past rate cases. In each of those but one, the Commission was able to conclude that the record supported the Postal Service's contingency provisions. In the one case in which it did not, the Commission was overruled by the courts. If one objectively compares the testimony presented by the Postal Service in this case with the testimony presented by the Postal Service in past cases, no difference in kind or amount can be found. The Commission's use of a lower contingency provision represents a substitution of its judgment for that of the Board of Governors. Even if it can be said that the record supported more than one reasonable conclusion concerning the contingency provision, it cannot be said that the Postal Service's contingency provision was not supported on the record or was unreasonable. As noted above, the Postal Service's judgment regarding this matter of fundamental financial policy is due deference, unless it is affirmatively shown to be unreasonable. As we discussed in our reconsideration

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12 The OCA alleges, incorrectly, that "all that the Postal Service provided for the Commission's consideration was a scant two pages by witness Tayman ...." OCA at 9. The Consortium chimes in with the criticism that "[w]itness Tayman's justification of a 2.5% contingency is limited to a mere 3 pages of his testimony...." Consortium at 13. These parties baselessly confuse quantity with reasonableness and apparently cannot even agree on quantity. In fact, the record is replete with written and oral testimony, direct and rebuttal, which provides substantial evidence in support of the Postal Service's contingency provision.
memorandum and in the briefs in this proceeding, the Postal Service's contingency provision was fully supported on the record by an examination of the Postal Service's financial condition, the state of the economy, and all other relevant factors. It is not true, as the OCA alleges, that the Postal Service did not present quantitative information. OCA Comments at 9. Both the Postal Service and the OCA presented forecasted inflation and other economic data; the same data were interpreted differently, with each reaching a conclusion based on judgment. The issue at hand is that the Commission should have not substituted its own judgment or that of experts in other industries for those of postal financial managers and the Board of Governors.

The Consortium argues that witness Tayman supported the Postal Service's contingency provision based on "entirely foreseeable factors that are not a valid basis for a contingency." Consortium Response at 13. This is untrue. The primary purpose of the contingency provision is to protect the Postal Service's finances against unknown adverse occurrences, since the Postal Service cannot accumulate profits, or change rates quickly in a financial crisis. Adverse occurrences include, in addition to events which are completely unforeseeable, the unforeseeable effects of known events, such as inflation, volume diversion, cost reduction program savings, and the labor contract. The Postal Service knows these things will happen and has estimated their effect; their actual financial impact, however, could turn out to be much different from that estimated in the revenue requirement. To characterize the financial impact of these events as "entirely foreseeable factors" is misleading, to say the least. For instance, a review of the PQ I RPW report indicates that the weakening economy and volume diversion are
having a more severe adverse impact on revenue than anticipated. The contingency provision must be sufficient to protect against such adverse affects.

The Commission and many participants have faulted the Postal Service for failure to rely on the variance analysis it presents or on some other quantitative analysis of the divergence of past estimates from actual results. As witness Strasser testified, there are many unknowns that cannot be determined by rigorous statistical analysis. Tr. 46-A/20193. Moreover, it is similarly illogical to believe that analysis of past divergences in volume trends can necessarily be assumed to apply when a still-evolving, new technology of potentially massive impact is in the picture, as is the case with the Internet.

The Consortium’s argument that “contingencies approved a decade or two ago in an era of volatile inflation, oil embargoes, high budget deficits, and political uncertainty, cannot be meaningfully cited under the present circumstances” is without merit as well. True, the volatile inflation that was most characteristic of that period ended. Was that predictable in advance or the result of trial and error in fiscal and monetary policy, the eventual success and timing of which could not have been known in advance? Can the

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13 In this regard, the Postal Service wishes to note that concerns expressed regarding reliance on extra-record evidence are misplaced. OCA Comments at 4-6, Consortium Response at 11. The Postal Service is certainly not urging the Commission to base its reconsideration on extra-record evidence. Facts such as the one noted above are presented simply to remind the Commission that evidence presented and arguments made by the Postal Service on the record may very well end up being proven true, and that it ought to approach and analyze the record keeping in mind the possibility and likelihood of serious adverse consequences resulting from such eventualities.
Consortium insure that no oil or other energy crisis will befall us in the future? Isn't such an event random and unpredictable? The notion of reduced risk from external variables is unfounded. Indeed, we are currently in a period of increasing economic weakness, high oil prices, energy shortages, tight labor markets, and volume diversion. Clearly, there are major uncertainties in the economy today and for the near future and the amount of uncertainty has increased since the last rate case. This was the essence of the testimony of Dr. Zarnowitz. Those who might dismiss his viewpoint as doomsaying would be well advised to read an article that appeared in the Washington Post on January 15, which included the following nuggets:

Citing the predictions of 50 private forecasters known as the Blue Chip Consensus -- "the experts who make a living doing this," as he put it — Clinton assured Americans that the economy would continue to grow this year at an annual rate of 2 percent to 3 percent.

What the president and his adviser failed to mention was that “the experts” have not predicted any of the nine recessions since the end of World War II.

Not the members of the Blue Chip Consensus or the Council of Economic Advisers. Not the crackerjack forecasting staffs of the Federal Reserve Board or the Congressional Budget Office.

And if, as a few renegades have begun to predict, the U.S. economy were heading into a mild recession this year, it would be one more forecast added to the dismal record.

"We really aren't very good at calling the turning points of the economy in either direction," said Murray Weidenbaum, top economic adviser in the Reagan administration.

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While high federal budget deficits appear to be behind us, at least for the immediate future, the same cannot be said for Postal Service net losses. It is not clear, moreover, what the Consortium means by “political uncertainty” and how that affects the Postal Service, but the question of legislative uncertainty remains a factor.
Allen Sinai of Decision Economics, a respected private forecaster, agreed. "It's probably only fair for forecasters to admit at times like this that we're simply not well equipped to predict turning points," he said. "A recession, by its nature, is a speculative call."

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"The reason we have trouble calling recessions is that all recessions are anomalies," said Joel Prakken, president of Macroeconomic Advisers of St. Louis, one of the nation's leading forecasting firms.

According to Prakken, every modern recession has been caused by a combination of overly aggressive interest rate increase[s] by the Federal Reserve, which weakens the economy, and some "external shock" that pushes it over the edge. Because such shocks -- the 1973 oil embargo, for example, or the 1990 Iraqi invasion of Kuwait -- are random and, by their nature, unpredictable, Prakken argues that it is virtually impossible to predict when a slowing economy would turn into a shrinking one.

Victor Zarnowitz, a longtime student of the business cycle, thinks much of the problem is that forecasters have become prisoners of an economic ideology that assumes too much rationality by economic factors. Thus, they spend too much time looking for recession indicators in official economic data, which often arrives too late to be of any use in forecasting, and not enough at the anecdotal evidence around them.

"It's easy to say that the bubble will burst sooner or later, but very difficult to say exactly when," said Zarnowitz, who now is a consultant at the Conference Board in New York.

Difficult, but not impossible, said Edward Leamer, director of the UCLA Anderson Business Forecast.

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...Leamer last month became the first Blue Chip Consensus forecaster to predict a mild recession in the United States this year.

"While the pattern is familiar, every recession has its own story," Leamer said. "You can't simply do a mechanical analysis of historical data."

Any economist such as Leamer who breaks from the consensus of the forecasting communities is well aware of the professional risks. Predicting recessions that never come is apt to earn an economist a reputation as crackpot or an unflattering moniker like "Dr. Doom." On the other hand, there
seems to be no professional penalty for missing a recession as long as you remain with the pack.

"If recessions were foreseeable, then they would be preventable," said Greg Mankiw, an economist at Harvard University. "Unfortunately, with our current stock of knowledge, we're not there yet." 

These experts are quoted here not as extra-record evidence proving the matters asserted, but simply because their basic arguments and conclusions are the same ones that the Postal Service has been making with regard to the contingency provision: The future, particularly adverse anomalies, are simply not predictable or subject to quantitative analysis. The Postal Service has taken the same viewpoint and it cannot simply be dismissed as unreasonable. Based on this viewpoint, the Postal Service concluded that a more traditional, but still relatively low, level of protection is necessary for the test year. The 2.5 percent contingency provision is a rational response to all the factors facing the Postal Service, as explained on the record of this proceeding. The level is completely reasonable when compared to the 4 to 5 percent contingencies of the 1970s and the 3 to 3.5 percent contingencies of the 1980s in the contexts of their times. Indeed, 2.5 percent is only slightly higher than the admittedly extraordinarily low levels of the 1990s. It is a rational judgment, explained on the record, and it should not

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15 Steven Pearlstein, *Tough Calls In Economic Forecasting—Seers Often Peer Into Cracked Crystal Balls*, Washington Post, Jan. 15, 2001, at A1 (emphasis added). The full article can be found at [http://www.washingtonpost.com/wp-dyn/articles/A60236-2001Jan14.html](http://www.washingtonpost.com/wp-dyn/articles/A60236-2001Jan14.html); it ought to be read by anyone concerned about the subject of the predictability of adversities, which is among the key issues in the instant controversy concerning the contingency provision.
be disturbed in the absence of some showing of error, as opposed to the substitution of others' judgment.

The Consortium distorts witness Tayman's testimony when it argues he "conceded" that "$450 million of the contingency was Intended to cover the fact that new rates are not expected to go into effect until several months into the Test Year..." Consortium Response at 13 n.8. An examination of the transcript pages cited by the Consortium, Tr. 2/561-63, indicates that witness Tayman testified that the implementation schedule meant that "a portion" of the test year contingency provision amounting to $450 million "would be consumed," i.e., would not actually be available in FY 2001, as a result of the implementation schedule. Witness Strasser made this point explicitly in his testimony. 16

The Postal Service's witnesses did not testify, as the Consortium would have it, that any particular portion of the contingency was intended to cover implementation after the beginning of the test year. In any event, an argument that postal management cannot take into account realities that will affect its actual financial state in the test year in determining the appropriate contingency provision is absurd. Such an argument is as equally untenable as an argument that an uncertain event with significant financial consequences anticipated to occur in the test year can properly be ignored because the Postal Service chose the test year, and the event will not reoccur after the test year. In fact, however, postal management would be remiss not to factor such an event fully into its assessment of the financial outlook, including the appropriate contingency level.

16 "Based on this timing alone, much of the test-year contingency will be consumed in FY 2001." Tr. 46-A/20199.
The Consortium’s Response distorts witness Strasser’s testimony in saying that he testified “that the Postal Service needs a higher contingency to restore equity.” Consortium Response at 14. Recovery of prior years’ losses has not been relied upon by the Postal Service as support for the contingency provision. Witness Strasser’s testimony was simply a correction of witness Rosenberg’s assertion that it is somehow improper to use contingency funds to restore equity. The Postal Service’s position is that, in the event—completely hypothetical in FY 2001—that part of the contingency were not spent, that amount would be, by definition, net income to the Postal Service, which, again by definition, would apply against prior years’ losses to reduce negative equity. There is nothing improper about this. The Postal Service is not, however, seeking to restore equity through the contingency provision. If it were, it certainly should have proposed a larger contingency amount.

Both the OCA and the Consortium then turn this argument on its head when they argue that prior years’ losses, rather than the contingency, is the appropriate mechanism to make up for forecast errors or the occurrence of unforeseen events. Consortium at 14; OCA at 10-11. They fail to explain why future ratepayers, who will continue to pay for past shortfalls, should be saddled in addition with current costs that could have been contemporaneously absorbed by an adequate contingency. Moreover, this argument fails to recognize that in the absence of large, unanticipated net incomes, prior years’ losses will never be completely paid off because they are amortized over nine years and continue to roll over from rate case to rate case. 17

17 This is not to say that the Postal Service does not hope for a time when the amount (continued...)
Postal Service would be roundly and deservedly criticized if it adopted such foolhardy financial policies as those suggested by the OCA and the Consortium with regard to the provisions for the contingency and for recovery of prior years' losses.

The OCA continues to peddle its flawed argument that the size of the contingency should be proportional to the size of the rate increase because the size of the increase is indicative of the amount of uncertainty. OCA at 15-16; Val-Pak at 5. To the contrary, it would be more accurate to say that the size of the increase indicates the amount of "certainty," i.e., what is predictable about the test year. It says nothing about what is unpredictable about the test year. It no less likely that an unknown adverse financial event could occur in a year where costs are predicted to fall than one where costs are predicted to increase. The Postal Service's position is based primarily, however, on the function of the contingency as protection of Postal Service finances as a whole. Potential adversities do not threaten only the amount of the rate increase, but the Postal Service as a whole. That is why the Kappel Commission originally, and both the Postal Service and the Commission ever since, have analyzed the contingency as a percentage of total costs.

The Governors attempted to illustrate this relationship by pointing out that an increase in rates could be justified solely to fund the contingency provision even if test

17 (...continued)
of equity left to be recovered becomes small enough to be recovered in one rate cycle.

18 In fact, a relatively small rate increase leaves the Postal Service more vulnerable, not less, to the effects of unpredictable adverse events. Accordingly, it would be more rational to argue that the size of the contingency should be inversely proportional to the size of the rate increase.
year before rates revenues and operating costs balanced. While the OCA seemed surprised and unsettled at the Governors’ suggestion, OCA Comments at 14-15, it is clearly supported by the express terms of 39 U.S.C. § 3621, which states:

Postal rates and fees shall provide sufficient revenues so that the total estimated income and appropriations to the Postal Service will equal as nearly as practicable total estimated costs of the Postal Service. For purposes of this section, “total estimated costs” shall include … a reasonable provision for contingencies.

Thus, if total estimated revenue in the test year before rates equaled total estimated operating costs, but did not equal total costs including a contingency provision, the statutory break-even standard would not be satisfied. Thus, requiring the contingency provision to be a relatively low percentage of the rate increase is inconsistent with the statute, which by its terms would allow for a contingency provision that equaled 100 percent of the rate increase. The OCA attempts to muddle these waters by arguing that section 3621 can’t mean what it says because a rate increase solely to fund a contingency would violate section 3622(b)(3). This argument ignores reality. The contingency percentage is applied on top of attributable costs and has never been treated as an attributable cost itself. The contingency is applied across the board to all

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19 As a further illustration, one might consider the hypothetical situation in which costs are expected to increase by 10% in the test year, but cost increases are estimated to be totally offset by cost reductions. The arguments advanced by the OCA and by Val Pak (at page 7) would have one believe that there is no risk in such a scenario, simply because the estimated net increase in expenses is zero. The fallacy in this thinking is that it seeks only to protect against test year expense mis-estimates and does not consider the possibility of unknown adverse events, or the possibility of revenue shortfalls. Looking at Postal Service finances as a whole, the base that must be protected is $136 billion, which is the total of both revenues and expenses. Looked at another way, a 2.5% contingency actually provides 1.25% of protection for expense overruns and a 1.25% contingency against revenue shortfalls either of which would have a serious adverse impact on the Postal Service’s financial position.
classes, subclasses, and services. Therefore, causation is not a consideration and the contingency is not governed by section 3622(b)(3).

The Consortium suggests that it was appropriate for the Commission to split the difference between the Postal Service’s testimony regarding the need for a contingency provision of 2.5 percent and the testimonies of intervenors supporting a 1 percent contingency. Consortium Response at 15. The Consortium cites a statement by the court in the APA case statement regarding the wisdom of King Solomon. Use of the court’s statement in the present case at least fails to recognize between the difference between the threat to split the baby, which stimulated truth-telling before King Solomon, and the actual splitting of a baby, resulting only in two bloody dead baby halves, which King Solomon would never have contemplated actually doing.

Even in cases where no actual baby is involved, splitting the difference is deemed wise only when no other solution can be discerned. There was no reason to split the difference in this case because the Postal Service’s contingency was supported on the record and is due deference.

Even when splitting the difference might seem to be the only reasonable path, there may be other, non-quantitative factors that need to be kept in mind. For instance, in the general context of the revenue requirement, the Commission ought to be conscious of the fact that the nature of the proceeding before it may not produce a balanced record. The Postal Service proposes what it believes to be the most reasonable and accurate case it can. Intervenors with various interests, primarily financial, attempt to show why the Postal Service may be wrong about this or that and present what they believe to be reasoned alternatives. In some areas, these
presentations balance each other out. Rate level and some rate design issues are
good examples of this. With respect to the revenue requirement, however, the
pressure is likely to be all in the same direction: reduction. There is rarely, if ever, any
countervailing concern on the part of any participant other than the Postal Service. For
instance, parties often argue that Postal Service cost estimates are too large. They do
not argue that cost reductions are too large. Even if they were to find an overestimate
in a cost reduction estimate, they would be likely to focus their attention on other issues
more favorable to their interests. The same is true of the Postal Service’s aggressive
revenue generation programs such as e-commerce, which also run in the direction of
reducing the overall size of a rate increase.\textsuperscript{20} Not one intervenor questioned the
prospects for producing this additional revenue, despite the uncertainty associated with
this program. Such uncertainty with respect to increased costs would not have gone
unchallenged for one minute. As a result, what appears to be a balanced conclusion
based on the record might very well be unbalanced and inequitable.

\begin{footnotesize}
\textsuperscript{20} The OCA misinterprets the Postal Service’s argument regarding the use by the
Commission of revenue from co-branded advertising, e-commerce, and retail sales.
OCA Comments at 20 n.24. The Postal Service did not say the Commission erred in
incorporating these estimates. The Postal Service stated that these revenues should
not have been counted as part of the increased revenue \textit{due to the Commission’s
recommended rates} as appears to be the case in Table 2-2 on page 74 of the Opinion.
The Postal Service also stated that the high-risk nature of these programs should have
been considered in analyzing the contingency amount.
\end{footnotesize}
III. THE FIELD RESERVE REPRESENTS A NON-CONTINGENT EXPENSE ELEMENT OF THE REVENUE REQUIREMENT ESTABLISHED ON THE RECORD

The arguments of the parties opposing the restoration of field reserve expenses are unfounded and are based on a complete misunderstanding of the reality of this situation. Val Pak alleges that the Postal Service uses the Field Reserve to pad the revenue requirement and further suggests that in the next rate case the Postal Service could put $2 billion or more into a field reserve to fund a backlog of pet projects. Val Pak at 5. This borders on an unfounded and inflammatory accusation that Postal Service managers are guilty of mismanagement and malfeasance. As the Postal Service has explained, postal managers use this budget technique to push field managers to achieve more savings than may appear possible. The alternative would be to issue field budgets based on the most likely scenario for breakthrough productivity savings, which would certainly result in no additional savings, higher costs, and therefore higher rates. Even if only a small portion of the Field Reserve winds up being saved as a result of setting overly aggressive field budget targets, there is benefit and this benefit accrues to the mailers. It is ironic that postal managers are accused of malfeasance for attempting to squeeze more savings out of the budget.

The OCA contends at page 12 of its Comments that the Field Reserve is part of the rate case contingency. This is simply not the case. The Field reserve is one of many components of the approved FY 2001 operating budget. The Postal Service routinely holds various costs in a servicewide finance number for allocation to organizational units during the budget year. This is a budget technique and a management prerogative to facilitate budget execution. Budget funds are routinely re-
programmed during the course of the year to facilitate the execution of the budget and facilitate the accomplishment of goals and objectives.²¹

A significant portion of the field reserve will probably be required to fund field budget shortfalls due to the aggressive nature of the cost reduction targets. To the extent that it appears these funds will not be needed for this purpose they will be re-programmed to fund other critical needs which had been temporarily deferred. This is nothing like the rate case contingency which is not a part of the Operating Budget. The OCA's treatment of the Field Reserve penalizes the Postal Service for taking an aggressive posture with regard to cost reduction savings. The safe approach would be to plan for smaller cost reduction savings which would be easier to achieve. The Postal Service would then have to request a larger rate increase. This would benefit neither the Postal Service, nor the mailers.

Both Val-Pak and the Consortium mistakenly base their arguments on a belief that the items for which any unspent field reserve funds would be used are capital investments. Val-Pak at 4; Consortium at 18. Val Pak alleges that witness Strasser erred when he testified that Field Reserve expenses could be spent on mail transport equipment or the information platform infrastructure because these are capital items which do not directly impact the expense budget. Quite the contrary. Mail transport

²¹ Witness Strasser's citation of an example of the routine use of this reallocation with respect to COLAs and health benefits was twisted by Val-Pak into an assertion by the Postal Service that it might need the field reserve for COLAs or health benefits. Val-Pak at 3. That was certainly not witness Strasser's testimony. He identified the specific items that the field reserve would be used for if the aggressive savings materialized. The reference to COLA's and health benefits was simply to show that this is a common budgeting technique for very real expenses.
equipment is the label used by the Postal Service to describe such things as mail bags and trays, which are expense items, not capital. Witness Strasser was also correct in referring to the expenses related to the installation and maintenance of the information platform infrastructure, since these are mainly contractual services and personnel costs.

IV. THE COMMENTS FILED BY THE CONSORTIUM OFFER NO VALID SUPPORT FOR THE COMMISSION'S IMPROPER TREATMENT OF SUPERVISOR COST ESTIMATES

On pages 18-20, the Consortium Memorandum attempts to refute the positions taken by the Postal Service in its December 20th Memorandum on the issue of supervisory cost savings. This attempt fails. The Commission should restore to the revenue requirement the amount improperly subtracted on the basis of alleged supervisory costs savings that, in fact, postal service witnesses testified will not occur in the test year.

In substance, the Consortium Memorandum offers two points. First, it quotes (at 19) a portion of the Commission's Opinion from Docket No. R97-1. That quotation, however, is essentially a recitation of the fact that the Postal Service offered no testimony on this matter in Docket No. R97-1. In this case, as noted in the December 20th Memorandum, the Postal Service explicitly addressed the matter in the direct testimony of its revenue requirement witness Tayman (USPS-T-9 at 14), and in the rebuttal testimony of witness Patelunas (Tr. 37/17142-45). As a result, regardless of their persuasiveness in Docket No. R97-1, the statements from the Commission's Opinion in that docket have no applicability to the record in this proceeding.

Second, the Consortium Memorandum seeks (at 19-20) to discount the testimony of witness Patelunas because he appears to lack first-hand knowledge of how changes
in operating conditions affect changes in supervision. This criticism is specious. Mr. Patelunas's testimonies over the course of this case covered an extremely wide variety of issues regarding test year costs and expenses. His expertise is well-documented. In this particular instance, however, he made no bones about the exact basis for his testimony. After citing the testimony of witness Buc (who likewise did not claim any first-hand knowledge on this issue) to the effect that if management changed the supervisory requirements in a new operating environment, Mr. Buc's necessary assumption that all things had been held equal would not apply, Mr. Patelunas stated:

I am informed by our program managers that this is in fact the case: most cost reduction programs change the operating environment and consequently, the Postal Service does not budget for proportional cost savings.

Tr. 37/17143. In relying on information provided by the program managers, who are the true experts based on their prior experiences and the hands-on analyses they perform to manage their programs, Mr. Patelunas was doing nothing more and nothing less than other analysts, working for the Postal Service, the intervenors, and the Commission, routinely do in thousands of instances. If the members of the Consortium had questions for Mr. Patelunas regarding the information he was provided by the program managers, they were free to pose those questions to him during oral cross-examination. A review of the transcript fails to reveal any instances in which they

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22 It is curious that the parties find the "second-hand" testimonies of witnesses Tayman and Patelunas entirely credible for purposes of establishing that cost reduction programs will reduce the workhours of craft employees, but unsatisfactory for purposes of establishing the effects of the same cost reduction programs on supervisor hours, when the basis for the testimonies (i.e., information provided by program managers) is the exact same in both instances.
availed themselves of that opportunity. Contrary to their untimely suggestions in their most recent pleading, his testimony was both reliable and persuasive.\(^{23}\)

Ultimately, it is ironic that the Consortium would choose to quote the statements from the Commission’s Opinion in the last case. Those statements do nothing more than illustrate quite vividly the complete change in circumstances between that case and this. What the Commission claimed to be lacking then as the basis for its actions was explicitly provided by the Postal Service in this proceeding. Specifically, in this case the Postal Service had the testimonies of witnesses Tayman and Patelunas which “discusses why the supervisory ratio should change under cost reduction programs,” the Postal Service thereby does “offer ... testimony on the issue,” and that testimony affirmatively explained in this case what the Commission in Docket No. R97-1 described as the Postal Service’s “failure to make a corresponding adjustment in supervisor’ work hours when craft employees' work hours are reduced” directly as a result of cost reduction programs. For these reason, as well as those explained in the Postal Service’s December 20th Memorandum, the Commission should restore the

\(^{23}\) In particular, there is no record basis for the Consortium’s claim (on page 20) that it is “unlikely” that supervisors supervise mail flow rather than people. Consider a supervisor in charge of three pieces of mechanized mail sorting equipment. Her responsibilities include making sure that each machine is adequately staffed, making sure that there is an efficient flow of mail to and from the machines, and addressing and resolving any problems which might arise in sorting the mail through her three machines. If a change from mechanization to automation (e.g., MPLSMs to BCSs) meant that her new machines needed substantially fewer employees to sort approximately the same volume (and thus had greatly enhanced productivity), it would not necessarily be unreasonable to expect that three machines is still a reasonable number of operations to be under her control, with the same responsibilities as before. The Consortium’s efforts to disparage the record testimony of Mr. Patelunas on this topic, upon which they also failed to question him during hearings, should be rejected.
amount of illusory test year supervisor cost savings that it has improperly removed from
the revenue requirement.

V. THE COMMISSION SHOULD ENDORSE THE POSTAL SERVICE'S
INTERPRETATION OF THE NEW LEGISLATION REGARDING NONPROFIT
STANDARD MAIL

In its December 20 Memorandum, the Postal Service explained why it believes that
the Nonprofit Standard rates recommended by the Commission may be based on a
misinterpretation of the new legislation governing such rates, and why that situation
might require redress. Postal Service Memorandum at 32-35. Two sets of responsive
comments were filed -- one by ANM and DMA, and the other by the OCA. The primary
thrust of both pleadings with respect to this matter was that, regardless of the merits of
the Postal Service's interpretation of the statute, the Commission should forgo
recommending any adjustment to the Nonprofit Standard rates at this time. While the
Postal Service disagrees with some of the reasoning offered by the parties to support
that conclusion, the result that they advocate, in terms of the lack of a compelling need
to recommend further Standard Mail rate adjustments exclusively on the basis of this
issue, appears to be acceptable under the totality of current circumstances. Obviously,
however, if the Commission is otherwise recommending adjustments to the Standard
Mail rates in response to the Postal Service's broader revenue concerns, the Postal
Service advocates that such adjustments be made in accordance with the correct
statutory interpretation.

It is important to recognize that ANM and DMA, parties that were involved with the
Postal Service in drafting the language of the joint proposal which eventually was
enacted into law, do not challenge the Postal Service's interpretation of the legislative
They state (page 2) that the “Postal Service’s statutory interpretation is not unreasonable, and the undersigned parties do not oppose its adoption in future cases.”

The OCA, however, identifies what it considers to be imprecision in the language of the statute that makes alternative interpretations of the statute possible, and goes so far as to suggest that this makes the Commission’s use of TYAR billing determinants reasonable. The OCA advises that the issue of statutory interpretation be left for another day. OCA Comments at 25-26.

The Postal Service strongly opposes that advice. Setting aside momentarily the matter of actual application of the new law to the existing situation, the Postal Service submits that the matter of statutory interpretation should be addressed and resolved. The new law was intended to be interpreted as stated in the Postal Service’s comments, and the validity of that interpretation should be acknowledged now. At the very least, when preparing its rate design for the next rate filing, the Postal Service would prefer to have an established consensus on the appropriate procedures to comply with the new legislation. Moreover, given the significance often attached to the contemporaneous construction of a statute, it is important that the postal agencies make clear their interpretation of the new provisions of section 3626, and that their interpretation be the correct one.

While the OCA has identified a curiosity in the wording of the new law which perhaps makes the provision in question seem less certain than might otherwise be the case.

Commentaries of persons intimately involved with drafting of legislation are entitled to weight in interpretation of a statute. Sutherland Statutory Construction § 48.12 (5th Ed).
case, the interpretation of the statute offered by the Postal Service is, in fact, the only one consistent with the legislative intent. Recall that the exclusive point of contention is the choice of billing determinants (TYBR or TYAR) to be used to calibrate to the 60 percent target for Nonprofit average revenue per piece versus Regular average revenue per piece. The Postal Service interprets new subsection 3626(a)(6)(B) to require TYBR billing determinants:

(B) For purposes of subparagraph (A), the estimated average revenue per piece for each regular-rate subclass shall be calculated on the basis of the expected volumes and mix of mail for each subclass at current rates in the test year of the proceeding.

No one disputes that the language “expected volumes and mix of mail ... at current rates in the test year of the proceeding” equates to TYBR billing determinants. The OCA, however, notes that subparagraph (B) makes this TYBR requirement explicit only with respect to “each regular-rate subclass.” It is true that if the phrase “regular-rate” had been omitted, or if that phrase had been followed by the phrase “and nonprofit,” any potential ambiguity in the literal language of the subparagraph would have been eliminated.

Nevertheless, even if some ambiguity exists at a theoretical level, the subparagraph is clear enough at a practical level. The exercise in question is to compare average revenue per piece estimates between commercial and nonprofit subclasses. Of the four possible permutations of billing determinants applied to the commercial/nonprofit subclasses (TYAR/TYAR, TYAR/TYBR, TYBR/TYAR, and TYBR/TYBR), the first two are clearly inconsistent with the plain language of the statute, which unequivocally requires the use of “current rates” (TYBR) for the
commercial subclasses. (Unfortunately, the first precluded option, using TYAR figures for both subclasses, appears to be the one employed by the Commission, and the OCA is simply in error to suggest on page 26 that the Commission's use of TYAR billing determinants is "reasonable" under any construction of the statute.) Therefore, only the last two options can be considered consistent with the "literal" language of the statute.

Of these, common sense precludes the third option, which would require a bizarre apples-to-oranges comparison of average revenues per piece using TYBR billing determinants for the commercial subclasses, but TYAR billing determinants for the nonprofit subclasses. The only sensible interpretation of the statute, therefore, is the fourth option -- calculating average revenue per piece estimates consistently using TYBR billing determinants both for the commercial subclasses, which the subparagraph literally requires, and for the nonprofit subclasses, which the subparagraph logically requires. Even the OCA appears to concede (on page 26) that this interpretation, presented by the Postal Service in its December 20th Memorandum, "makes sense."

Any doubt on this matter is easily resolved by reference to the legislative history.

The Senate report sets out the Congressional intent without ambiguity:

Under the special rule, rates will be set so that the estimated average revenue per piece to be received by the Postal Service from each subclass of Nonprofit Standard (A) mail will be equal, as nearly as practicable, to 60 percent of the estimated average revenue per piece to be received from the most closely corresponding regular rate subclass of mail. In making this calculation, the estimated average revenue per piece will be calculated on the basis of the expected volumes and mix of mail for each subclass at current rates in the test year of the rate proceeding.

S.Rep. No. 468, 106th Cong., 2d Sess. (Oct. 3, 2000) at 5 (emphasis added). These statements confirm that the calculations "for each subclass" should be made using
TYBR billing determinants. The imprecision supposedly causing the OCA’s concern is eliminated -- the statute contemplates a simple TYBR to TYBR comparison.25

Moving beyond mere issues of statutory construction, moreover, the OCA is equally off base to question the wisdom of this provision by characterizing it as “an instruction to ignore reality.” OCA Comments at 26. The intent was simply to establish a process that maintains the intended relative relationship between commercial and nonprofit rates. When the process was being designed by discussion and negotiation between the interested parties, it was agreed that the figure of 60 percent, when applied in the context of a target calculated using TYBR billing determinants, was satisfactory. Had the decision been made to use TYAR billing determinants, it is conceivable that a different target level might have been chosen. The statute should

25 While the above analysis is couched in terms of the standard canons of statutory construction, other facts merit mention, even though they have been alluded to above and the Commission is presumably already aware of them. Specifically, the language of the new legislation did not originate in Congress, but came directly from a proposal worked out by many interested parties. See Congressional Record for June 7, 2000 (S4669-70). Congress, in effect, accepted that proposal by passing it into law without modification. While the genesis of the stray phrase “regular-rate” in subparagraph 3626(a)(6)(B) may be unclear, it certainly occurred during the evolution of the proposal through discussion by the parties (i.e., not after the proposal had been forwarded to Congress), and the agreement to use before-rates billing determinants for all subclasses was simply not a point of contention during those discussions. While the parties perhaps failed to use the clearest possible language to express that agreement in the draft bill provided to Congress, their intent was clear in the statement of explanation which accompanied the draft bill. That statement, in turn, became the language in the Senate Report, quoted above. Taking the literal language of subparagraph (B), the context in which it was developed, and the statement of explanation included in the Senate Report, there is no credible basis to assert any legislative intent other than that the comparative calculations of average revenue per pieces were intended to be conducted with TYBR billing determinants for all subclasses.
not be viewed as "an instruction to ignore reality," but rather as a mandate to follow a set of prescribed procedures.

Both the comments of the OCA (at pages 26 and 27) and those of ANM and DMA (at page 3-4) seek to invoke the "as nearly as practicable" language of subparagraph 3622(a)(6)(A). While not totally unsympathetic to this approach, the Postal Service believes that some caution is warranted. The Postal Service understands the purpose of the "as nearly as practicable" language to be to recognize that as long as rates are rounded to some determinate level (e.g., tenths of cents), and as long as worksharing opportunities make relative as well as absolute rate levels important, there comes a point at which no acceptable tinkering with the rate schedules will result in movement closer to the exact target of 60.000... percent. Depending on a wide variety of circumstances, that point could come at, for example, 57 percent, or 61.3 percent, or 59.34 percent, or 60.04 percent, or any of an infinite set of other possibilities. Wherever that point might be, however, it is the one at which the target has been met "as nearly as practicable." Conversely, if reasonable adjustments could still be made in the rate schedules which would result in a percentage relationship materially closer to the target of 60 percent, the standard of "as nearly as practicable" has not been met.

Starting with a clean slate (i.e., rate design is still ongoing, and no new rates have been implemented), and comparing two otherwise acceptable sets of potential rates with materially different levels of convergence to the 60 percent target, the statute would appear to require selection of the one closer to the 60 percent target. The standard, after all, is not "approximately" 60 percent, but "as nearly as practicable" 60 percent. That situation, however, is not the one facing us in this instance. First of all,
we do not have a clean slate -- one set of new rates has already been implemented. Second, using the appropriate means of calibration (i.e., TYBR billing determinants), we do not know with certainty how close or how far we are from the 60 percent target. Consequently, we do not know whether it is possible to move materially closer to that target. On account of both of these factors, therefore, applying the "as nearly as practicable" standard is not as easy as might otherwise be the case.

In particular, the lack of a clean slate presents a further complication that is not discussed by either the OCA or ANM and DMA. Both sets of comments (OCA at 27, ANM and DMA at 2) indicate that the substitution of TYAR for TYBR billing determinants has caused a revenue shortfall from Standard Nonprofit rates of approximately $26 million. In fact, however, the discrepancy is merely in the ratio of average revenue per piece between commercial and nonprofit subclasses, and the problem could just as easily be characterized as a revenue surplus from commercial rates. Adjusting the rates for either type of mail in isolation, however, would not only affect the average revenue per piece ratios, but would also have consequences for overall breakeven. Reasonably assuming that whatever potential adjustments to be made would have to be overall net revenue neutral, the most likely steps taken to recalibrate to the 60 percent target correctly would be some increase in Nonprofit

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26 As the Postal Service acknowledged in its initial comments, the calculations it presented therein were not definitive because of complications arising from the matter of fee revenue. Of course, given some time, the fee revenue problem is certainly one which can be addressed and resolved.

27 Given the fact that the Commission got within one- or two-tenths of a percent using TYAR billing determinants, however, the possibility of the potential for material improvements using the TYBR figures cannot be dismissed out of hand.
Standard rates, and some decrease in commercial Standard rates. The downside to resolving the problem in this manner, however, is that the disruption of further new rate implementation would not be constrained to just one type of rates, and therefore both commercial and nonprofit mailers would all be affected.

With respect to the "cost" associated with the disruption of changing rates once again, ANM and DMA suggest (at pages 2-3) that the value of the burden imposed on the mailers and the vendors would be "far larger" than the $26 million that the Postal Service might obtain in additional revenue. The OCA comments (at page 28) also appear to suggest that the transactions costs might outweigh the revenue benefit. While the Postal Service is fully aware that there are significant administrative costs associated with rate changes, it is far from clear that they would approach a magnitude anywhere near sufficient to exceed a revenue increase of $26 million. If the sole issue were whether the Postal Service should be deprived of tens of millions of dollars in revenues merely to avoid such transactions costs, the Postal Service would be justified in maintaining its rights to receive the additional revenue. As noted in the preceding paragraph, however, the Postal Service in this instance would expect to obtain no net revenue from offsetting rate adjustments designed merely to move the ratios of average revenues per piece closer to 60 percent. Under such circumstances, the matter of

28 Alternatively, it would be theoretically possible to only adjust one of the two types of rates (either nonprofit or commercial Standard), hold the other type constant, and make the offsetting adjustment outside of the Standard class, but this would seem to be a particularly inefficient way to proceed.

29 That is, for example, more nearly the situation at this time with respect to Bound Printed Matter. The BPM situation is therefore clearly distinguishable from the problem posed by the new amendments to section 3626.
transactions costs does become more significant, and the Postal Service agrees it is a legitimate factor weighing against the need for rate adjustments that overall would be net revenue neutral. Also as discussed above, the significance of transactions cost is compounded by virtue of the fact that it would likely be all Standard mailers – commercial and nonprofit alike – that would be facing relatively slight adjustments in their rates.

Therefore, under the totality of these circumstances, the Postal Service reaches the following conclusions. First of all, regardless of whether it recommends any rate adjustments or not, Postal Service urges the Commission to acknowledge that the intent of the new legislation was to compare average revenues per piece calculated on the basis of TYBR billing determinants. Second, the Postal Service would not contest the suggestion of ANM and DMA that the Commission delay actual application of this construction of revised section 3626(a)(6) until the next time it recommends new rates for Standard mail. Given the position of those parties on the other issues pending before the Commission upon reconsideration, it is undoubtedly their view that such occasion should not arise before the next rate case. If compliance with the new legislation were the exclusive issue upon reconsideration, the Postal Service might share that view as well. The Postal Service, however, has simultaneously requested that the Commission restore hundreds of millions of dollars to the revenue requirement. If addressing those concerns requires the Commission to recommend new Standard Mail rates, or if the other circumstances arise in which Standard Mail rate levels are adjusted before the next rate case, the Postal Service believes it would be appropriate to use TYBR billing determinants to make the necessary calculations at that time.
VI. RATE DESIGN ISSUES

A. First-Class Mail

In comments filed by the Major Mailers Association (MMA Comments at 9) and jointly by the American Bankers Association and the National Association of Presort Mailers (ABA&NAPM Comments at 10), the suggestion is made that if the Commission should consider it necessary to make an upward adjustment of the First-Class Mail additional-ounce rate, it also should recommend extension of the Heavyweight Discount\textsuperscript{30} to presorted letters and flats weighing more than one ounce. In support of their proposal, ABA&NAPM invite the Commission attention to MMA Comments and their own Docket No. R2000-1 Brief filed on September 13, 2000. Neither MMA's Comments or the assertions in ABA&NAPM's Brief offer the Commission any basis for deviating from its explicit rejection of their Docket No. R2000-1 proposals to extend the Heavyweight Discount to letters weighing less than two ounces or to flats at any weight increment.

At page 7 of its Comments, MMA argues that

it \ldots [would be] patently unfair, at this juncture, to 'tinker' with the approved cost coverages, markups and markup indices. The appropriate place to consider such changes is in the Postal Service's next omnibus rate proceeding, where all relevant facts and circumstances can be considered.

It should be remembered that the recommended cost coverages have not been approved; the recommendations of the Commission have been allowed under protest.

\footnote{The discount currently applies to presorted First-Class Mail \textbf{letters} weighing more than two \textbf{ounces}.}
Moreover, material issues not yet resolved in Docket No. R2000-1 should be resolved in that docket, consistent with the statutory scheme established for doing so. Congress had the wisdom to establish procedures through which the Commission and the Governors could reconsider initial recommendations. It would be irresponsible for them to procrastinate simply because there will inevitably be another omnibus rate proceeding at some unknown point in the future. MMA cannot have it both ways, if “tinkering” is inappropriate, MMA should withdraw its proposals that the Commission “tinker” with the recommended Heavyweight Discount and the rate relationship between 5-Digit Automated and Carrier Route letters.

B. Bound Printed Matter

The Association of American Publishers (AAP), the Association for Postal Commerce (PostCom), and the Mail Order Association of America (MOAA) filed comments on January 12, 2001, responding to issues concerning Bound Printed Matter which were raised in the Postal Service’s December 20, 2000, Reconsideration Memorandum.

At pages 1-2 of its Comments, AAP argues that no adjustment should be made to correct the $30.6 million dollar shortfall in Bound Printed Matter revenues. AAP asserts that retention of the rates that have been allowed under protest “would cause the least amount of disruption to BPM mailers . . . .” AAP does not suggest that any particular degree of change is onerous, only that no change is less disruptive than some change. While there may be no disagreement on that point, it hardly serves as a

31 A position supported by both PostCom and MOAA.
compelling basis for preservation of the currently deficient Bound Printed Matter rates. Arguing for the status quo simply because the absence of any change would cause the least disruption is to argue that change should always be avoided, even when change is necessary to make the rates consistent with the Commission's intentions.\footnote{32}

PostCom (at 2-3), AAP (at 2-3) and MOAA (at 2) argue that adjustments to Bound Printed Matter rates could be avoided if the Commission assumes that the $30 million Bound Printed Matter revenue shortfall would be offset to some unspecified degree by undocumented extra-record projections in cost reductions resulting from expected volume shifts between Bound Printed Matter rate categories. Accordingly, the Postal Service cautions the Commission regarding reliance on such undocumented extra-record speculation.

In its comments at page 1, MOAA rehashes arguments explicitly rejected by the Commission in it Docket No. R2000-1 Opinion. The Commission specifically considered and rejected MOAA's plea that Bound Printed Matter be given a cost coverage similar to that for Periodicals. PRC Op. R2000-1, Vol. 1 at ¶5884. On reconsideration, the Postal Service is not requesting any modification of the 114 percent Bound Printed Matter cost coverage recommended by the Commission, merely that the recommended rates conform to that cost coverage target.

AAP argues that the Commission's reconsideration of the evidentiary record to correct mathematical errors would "require a more in-depth technical inquiry than the Postal Service's request and the procedures established for reconsideration afford."

\footnote{32}{The Postal Service would be surprised if mailers would adopt this approach if an error provided rates that were higher than intended by the Commission.}
AAP Comments at 3. The Postal Service only seeks the correction of mathematical errors which will ensure that Bound Printed Matter achieves the cost coverage the Commission found reasonable. Notwithstanding the efforts of AAP and PostCom to offer extra-record testimony via their Comments, no re-opening of the evidentiary record is necessary to make such corrections.

Finally, at page 3 of its Comments, PostCom argues for preservation of the status quo by asserting that "[t]he Postal Service has conceded that the BPM rates it proposed will result in 'rate shock' for at least some mailers. Tr. 13/5322, lines 1-6." At the cited passage, Postal Service witness Kiefer merely testified that there would be "some mailers who will still perceive some rate shock after our mitigation efforts . . . ." Throughout pages 5319–23, his testimony makes clear that he is discussing the likely perceptions of some mailers.

C. Parcel Post

Order No. 1301 lists the Commission's recommendation of the nonmachinable surcharge for parcel post among several issues identified in the Governors' Decision to be reconsidered by the Commission upon return of Docket No. R2000-1. Both United Parcel Service and Parcel Shippers Association (PSA) in their comments on reconsideration note the failure of the Postal Service to address this issue in its Memorandum filed on December 20, 2000. Each party, however, takes a different view of whether the matter should be reconsidered in light of the Governors' comments. UPS notes that, while the Governors discussed the issue, they did not explicitly request reconsideration. PSA, noting inclusion of the issue in Order No. 1301, argues that it should be reconsidered.
The Postal Service can confirm that reconsideration of the parcel post nonmachinable surcharge was not among the issues the Governors returned to the Commission for reconsideration. Throughout their Decision in this case, and in past cases where they have allowed the Commission's Recommended Decision under protest and returned matters for reconsideration, the Governors have consistently expressly requested reconsideration of those issues they have intended to return. Furthermore, the Postal Service asserts very strongly that the Commission, as it has in the past, should respect the limits of the Governors' Decision. Accordingly, the surcharge should not be reconsidered by the Commission.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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Chief Counsel, Ratemaking

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.

Daniel J. Foucheaux, Jr.