

**BEFORE THE  
POSTAL RATE COMMISSION**

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OFFICE OF THE ATTORNEY GENERAL

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**POSTAL RATE AND FEE CHANGES, 2001**

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**DOCKET NO. R2001-1**

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**REPLY BRIEF OF UNITED PARCEL SERVICE  
CONCERNING THE PROPOSED STIPULATION  
AND AGREEMENT OF SETTLEMENT**

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Pursuant to Presiding Officer's Ruling No. R2001-1/43 (January 31, 2002), United Parcel Service ("UPS") hereby files its Reply Brief Concerning the Proposed Stipulation and Agreement of Settlement in this case.

**STATEMENT OF POSITION**

As a signatory to the Settlement, UPS submits that the Commission should recommend the rates and fees proposed in the Settlement. Although UPS (and many other intervenors as well) could find fault with a number of the rates set forth in the Settlement and how they were developed, all but one of the parties have put those differences aside -- for now, at least -- to further their shared goal of facilitating the Postal Service's efforts to respond to recent extraordinary events and return to financial stability.

UPS is able to support the Settlement not only because of the unique circumstances now facing the postal community, but also because the Settlement rates comply with the most fundamental requirement of the Postal Reorganization Act: that the revenues for each class and subclass of mail cover its attributable costs using the

Commission's costing methods and make some contribution to the Postal Service's institutional costs. 39 U.S.C. § 3622(b)(3). See Library Reference USPS-LR-J-89 (showing that cost coverages exceed 100% for all classes of mail using the Commission's methodologies); USPS-T-29 (Robinson) at 12 n.7 (cost coverage for First Class workshared mail based on Commission methodology reflected in Library Reference USPS-LR-J-89); USPS-T-28 (Moeller) at 15-16 and n.11 (192.4% cost coverage for First-Class letters using Commission costing); Tr. 9/2523 (cost coverage for Outside County periodicals exceeds 100% based on Commission methodology); Tr. 10-C/3662 (institutional response). No participant suggests otherwise.

Only one party opposes the Settlement. APWU argues that the Settlement should be rejected because, it claims, the passthroughs of avoided costs used to determine First-Class Mail workshare discounts exceed 100%; it does not argue that any of the Settlement rates violate the requirement that the revenues for each subclass of mail must cover attributable costs and make some contribution to institutional costs.

UPS agrees with APWU that avoided cost passthroughs should not exceed 100%. UPS also agrees with many of the other principles espoused in the testimony of APWU's witness.<sup>1</sup> However, APWU's testimony does not provide a basis for rejecting the Settlement because it is clear on this record that the discounts APWU criticizes do not exceed properly measured avoided costs.

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1. PostCom, *et al.* is wrong when it states in its Initial Brief (at page 3) that "Equal Per-Unit Contribution Has No PRC Precedent," as APWU shows in its Initial Brief at 8-9, citing the Commission's Opinion and Recommended Decision in Docket No. MC95-1 (January 26, 1996) ("MC95-1") at ¶¶ 3070-73.

In light of this clear fact, the Commission should not venture into the thicket of deciding fundamental ratemaking principles of the type raised by APWU when, as here, that is not necessary to reaching a proper decision. That is especially so since, given the all but unanimous support for the Settlement rates, other parties have not addressed those issues fully.

### **ARGUMENT**

#### **A. Many of the Principles Advocated by APWU -- and Especially Its Argument That Passthroughs of Avoided Costs Should Not Exceed 100% -- Are Sound.**

UPS agrees with APWU that passthroughs of avoided costs used to determine worksharing discounts should not exceed 100%, and should generally be meaningfully below 100%. This principle is far from novel. It is the same approach that the Commission itself has followed, as APWU shows in its Initial Brief at 3, citing MC95-1 at ¶¶ 3068, 3076 (“From the beginning, [the Commission] has wanted to set the discount *no larger than* the clearly capturable avoided costs, so that the residual mailers would not experience a rate increase because some other mailers were encouraged to workshare”) (emphasis added), ¶ 3079. See also Opinion and Recommended Decision, Docket Nos. R97-1 (May 11, 1998), ¶ 5516, and R2000-1 (November 13, 2000), ¶ 5060 (referring to passthroughs greater than 100% as “unconventional”). Passthroughs no greater than 100% promote overall efficiency, MC95-1 at ¶¶ 3074, 3075, and are consistent with fairness and equity, *id.* at ¶ 3074.

In fact, the Commission has generally rejected proposals to pass through more than 100% of avoided costs. See, e.g., Docket No. R97-1 at ¶¶ 5521-22, 5526, 5530, 5561-62; Docket No. R2000-1, ¶¶ 5409, 5412. When the Commission has

recommended passthroughs that have exceeded avoided costs, it has done so to further specific policies or goals, none of which are implicated here. See Docket No. R97-1, ¶ 5635 (“to establish a meaningful differential between the basic Nonprofit ECR automation rate and the 5-digit automation rate”); Docket No. R2000-1, ¶ 5562 (to avoid “unduly burdensome” rate changes). Regardless of the merits of these specific exceptions, Commission policy has generally limited passthroughs to 100% or less.

Val-Pak is wrong in suggesting in its Initial Brief (at page 6) that passthroughs below 100% create cross-subsidy. The Commission has held that cross-subsidy exists when the rates for a service fall below its attributable (incremental) costs. R97-1 at ¶¶ 4001-26. As long as the total revenues for the “unbundled, upstream” services (Val-Pak Initial Brief at 6), *i.e.*, the nonworkshared portion of a service, cover the attributable costs of those services and make a contribution to institutional costs, there is no violation of the statutory costing requirement. Passthroughs less than 100% do not inevitably result in rates below attributable costs for “unbundled” services, as the entire history of the worksharing discounts recommended by the Commission shows.

In any event, in order to endorse the Settlement, the Commission need not reject the principles advocated by APWU, since the record clearly shows that the factual premise necessarily relied on by APWU -- that the discounts it attacks exceed properly measured avoided costs -- is incorrect.

**B. The Discounts Attacked by APWU Do Not Exceed Properly Measured Avoided Costs.**

APWU relies on the avoided cost calculations of Postal Service witness Miller (USPS-T-22), which in turn are based on the Postal Service’s costing methodologies, including the Postal Service’s mail processing volume variability factors. Tr. 12/4865-

70, 12/4903. When the Commission's costing methods (including its mail processing volume variability methodology) are used -- as they should be -- the passthroughs for the attacked discounts are substantially less than 100%. See Tr. 10-A/2862, 13/5164, MMA-SRT-1 at 7, Table 3 (Bentley). Thus, even though APWU is right on many of the principles, it is wrong on the facts.

The Postal Service erroneously states that the Settlement "encompasses the Postal Service's subclass costing presentation" and that "the Postal Service's estimates of volume-variable cost for the various subclasses . . . are not disputed in this proceeding." Initial Brief of the United States Postal Service at III-13, V-2. See also *id.* at IV-3 ("the settlement parties have agreed to accept witness Moeller's institutional cost allocations as fair and equitable"). On the contrary, the record contains ample evidence demonstrating that the Postal Service's testimony on mail processing volume variability, for example, is insufficient to overcome the Commission's long-held view that mail processing labor costs are essentially 100% volume variable. See, e.g., Tr. 11-A/3875-76 (examples of negative values for Total Piece Handlings in MODS data); Tr. 11-A/3878-3879 (examples of negative values for total pieces fed in MODS data); Tr. 11-A/3880-3881 (examples of negative values for First Handling Pieces in MODS data); Tr. 11-A/3882-3883 (MODS reporting negative workhours in accounting periods); Tr. 11-A/3884-3885 (examples of gaps in MODS data for sorting activities); Tr. 11-A/3887 (examples of inconsistencies in MODS data for TPF and TPH); Tr. 11-A/3888-3889 (examples of inconsistencies in MODS data for TPF and FHP); Tr. 11-A/3890-3891 (examples of zero TPF but positive workhours in MODS data); Tr. 11-A/3901-06, POIR No. 6, Item 11(a)-(r) (examples of MODS data problems).



The Commission need not reject its well-established conclusion on the variability of mail processing labor costs in order to uphold the Settlement. Indeed, since the Commission usually insists that avoided cost passthroughs be no larger than 100%, one could argue exactly the opposite in light of APWU's attack: it is only by adhering to its traditional approach to the attribution of mail processing labor costs that the Commission is able to reject APWU's attack without compromising its usual approach to worksharing passthroughs.

The parties have agreed in the Settlement that, "taken in their entirety," the "materials filed on behalf of the Postal Service" -- including designated written cross-examination of Postal Services witnesses -- "provide substantial evidence for" the Settlement rates. Stipulation and Agreement (February 13, 2002) at 3, ¶ 3. UPS was able to agree to the Settlement because, as noted above (at pages 1-2), the Settlement rates for each subclass cover attributable costs and make a contribution to institutional costs *under the Commission's costing methods*. In evaluating the Settlement, the Commission should continue to use its established costing methods, including its attribution of essentially all mail processing labor costs.<sup>2</sup> That is especially so here since, in light of the Settlement, the record is insufficiently developed to support a departure from the Commission's costing methods. *Motor Vehicle Mfrs. Ass'n of United*

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2. Paragraph 3 of the Stipulation does not, as the Postal Service seems to suggest (Initial Brief at V-40-41), prevent parties from relying on evidence that calls into question the validity of aspects of the Postal Service's direct case. As paragraph 9 of the Settlement states, the Settlement parties do not, by signing the Settlement, "agree with, or concede the applicability of, any ratemaking principle, [or] any method of cost of service determination . . . ." Thus, the Settlement parties remain free to make any arguments they deem advisable in support of the Settlement rates.

*States v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 42 (1983); *Global Crossing Telecommunications, Inc. v. FCC*, 259 F.3d 740, 746 (D.C. Cir. 2001) (“an agency changing its course by rescinding a rule,’ or departing from precedent ‘is obligated to supply a reasoned analysis for the change,’” quoting *State Farm*, 463 U.S. at 42).

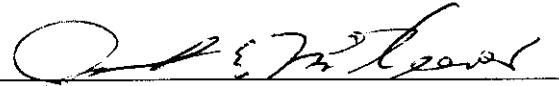
Before making any dramatic changes from its traditional costing and ratemaking approaches, the Commission must thoroughly examine all of the potential ramifications of such changes. Thus, the Commission should carefully refrain from deciding issues that it need not decide (including the transportation issues arising from the Postal Service’s contract with Federal Express, for example). See *MCI Telecommunications Corp. v. FCC*, 917 F.2d 30, 41 (D.C. Cir. 1990) (“An agency does not automatically have to reach every issue whose importance it had noted and on which it had conducted a hearing”). That includes the passthrough issues raised by APWU. The Commission is able to do that here because, as all but one party have agreed, the Settlement rates pass muster regardless of the costing methods any particular party favors.

### **CONCLUSION**

WHEREFORE, United Parcel Service respectfully requests that the Commission issue a decision recommending that the Governors of the United States Postal Service

adopt the rates and fees set forth in the Stipulation and Agreement filed on February 13, 2002.

Respectfully submitted,

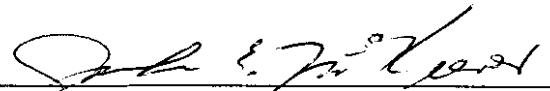
A handwritten signature in black ink, appearing to read "John E. McKeever", is written over a horizontal line.

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CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing Initial Brief of United Parcel Service Concerning the Proposed Stipulation and Agreement of Settlement by first class mail, postage prepaid, in accordance with Section 12 of the Commission's Rules of Practice.

  
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Dated: March 8, 2002  
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