

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

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COMPLAINT OF TIME WARNER INC. ET AL.  
CONCERNING PERIODICALS RATES

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Docket No. C2004-1

RESPONSES OF TIME WARNER INC. ET AL.  
WITNESS ROBERT W. MITCHELL TO MH/TW ET AL.-T1-19-24 AND 26-38  
(June 28, 2004)

Time Warner Inc., Condé Nast Publications, a Division of Advance Magazine Publishers Inc., Newsweek, Inc., The Reader's Digest Association, Inc., and TV Guide Magazine Group, Inc. (collectively, Time Warner Inc. et al.) hereby provide the responses of witness Mitchell (TW et al.-T-1) to McGraw-Hill interrogatories MH/TW et al.-T1-19-24 and 26-38, filed June 14, 2004.

MH/TW-T1-25 has been redirected to witness Stralberg (TW et al.-T-2).

Each interrogatory is stated verbatim and followed by the response.

Respectfully submitted,

s/ \_\_\_\_\_  
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## Responses of Witness Mitchell to MH/TW et al.-T1-19

**MH/TW et al. – T1-19:** With reference to your testimony at page 9 line 6 through page 11 line 6:

(a) Please confirm that inordinate increases in the attributed costs and rates of Periodicals mail have occurred since the early 1990s *despite* significantly increased use of pallets, increased dropshipping and increased worksharing of other types by Periodicals mailers during that period. If you do not confirm, please explain fully.

(b) Please provide your best estimate of the extent of increased use of pallets, increased dropshipping, and increased worksharing of other types by Periodicals mailers since 1990 (or for whatever years data may be available). Please specify the precise sources for your answer and provide any necessary calculations.

(c) Please confirm that the *inordinate increases* in the attributed costs and rates of Periodicals mail since the early 1990s have not apparently been caused by Periodicals mailing practices, but rather may largely be attributable to Postal Service choices or constraints, such as the apparent failure of the Postal Service to reduce sufficiently the number of its personnel assigned to process Periodicals mail after it had deployed expensive flats sorting machines (the so-called “automation refugee” problem), and/or Postal Service decisions to accord Standard mail priority use of flat sorting machines (relegating some Periodicals mail to more expensive manual handling that became even more expensive still due to the automation refugee problem). If you do not confirm, please explain fully.

(d) With reference to Graph 1 on page 10 of your testimony, please confirm that the trend of inordinate increases in the attributed costs and rates of Periodicals mail has held steady or accelerated for more than ten years, despite increased use of pallets, increased dropshipping, and increased worksharing of other types by Periodicals mailers during that period. If you do not confirm, please explain fully.

(e) Please confirm that an immediate effect of the proposed rate structure would be to significantly reduce the pooling and averaging of Periodicals mail costs for rate design purposes, resulting in a significant redistribution of revenue responsibility for costs among Periodicals mailers. If you do not confirm, please explain fully.

(f) Please confirm that the proposed rate structure would tend to result in significant rate increases for (among others) high-editorial/low-circulation national Periodicals, particularly to the extent that they are unable as a practical matter to palletize or dropship their mail, and would tend to result in significant rate decreases for high-circulation national periodicals, even if they simply maintain their current levels of palletization, dropshipping and other worksharing. If you do not confirm, please explain fully.

## Responses of Witness Mitchell to MH/TW et al.-T1-19

### RESPONSE

(a) Confirmed. That appears to be the case.

(b) According to PRC Library Reference 9 in Docket No. R2001-1, the proportion of pieces on pallets in Regular Periodicals is 69.1 percent (cell B136/cell B157 on the 'Test Year BR' sheet of the Outside County workbook). In Docket No. MC91-3, the Postal Service estimated the proportion of Regular pounds on pallets to be 25.9 percent (Workpapers of witness Robert W. Mitchell, USPS-T-3, showing 664,379,059 pounds on pallets and 1,901,127,243 pounds not on pallets). Keep in mind that some of the weight constraints on pallets were changed over this period.

The easiest way to develop figures for dropshipping and worksharing such as presorting is probably to compare the various volumes on pages 6 and 7 of Appendix G of the Commission's Opinion in Docket No. R2001-1 with corresponding volumes on page 7 of Appendix G of the Commission's Opinion in Docket No. R90-1. If the standard assumption is made that the zone distribution of editorial pounds is the same as the zone distribution of advertising pounds, the proportion entered in the DSCF has increased from 20.3 percent to 41.5 percent. Note should be made, however, of the fact that some portion of the DSCF-entered volume in each period was not really dropshipped, although the size of that portion is unknown. If the size of that portion were known, it could be made clear that the increase from 20.3 percent to 41.5 percent does not represent the increase in dropshipped volume or in worksharing. From the same source, the proportion of carrier route presorted pieces increased from 26.2 percent to 39.6 percent. Other proportions could be calculated.

Keep in mind that other things have been going on as well, such as the advent of barcoding by mailers, the addition of the DADC entry point, and improvements in the

## **Responses of Witness Mitchell to MH/TW et al.-T1-19**

signals sent. Also, there have been increases in the technical sophistication of mailers and improvements in technology, such as in co-mailing and the software available. For example, the computer programs that now routinely analyze transportation and dropship alternatives were in their infancy in 1990.

(c) The increases in Periodicals costs, to which you refer, have been a perplexing problem and have received considerable scrutiny. The explanations provided by the Postal Service have not been satisfying. Analysts have raised many questions, such as those you summarize, but conclusions have been difficult to verify. I can confirm that these questions have been raised and that further inquiry is needed.

(d) The graph on page 10 of my testimony focuses on rates under certain conditions, not on costs. However, there are costs behind the rates and I can certainly confirm that they have been increasing inordinately, as you suggest. I have not analyzed whether the pattern of increases exhibits the quality of acceleration, which would seem to require curves that are convex to the horizontal axis.

(e) Confirmed as to the first part. Your question has two parts, one relating to deaveraging and the other to the effects of the deaveraging. On the first part, it should be noted that some of the deaveraging merely improves on deaveraging done in the past, which is now understood not to have followed costs in a fair way. On the second part, many of the affected mailers will be able to make changes that will improve efficiency and reduce the effects.

(f) Not confirmed. I have not found it easy to select categories of mailers that would experience one level of effect instead of another. There may be an extent to which what you suggest is true, but I have also found factors like the number of pieces in a bundle and the number of bundles in a sack to have a substantial effect on the size

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of any resulting increase or decrease. In this regard, please see my response to Question 1 of POIR No. 1.

## Responses of Witness Mitchell to MH/TW et al.-T1-20

**MH/TW et al. – T1-20:** With reference to the statement at page 30 lines 13-15 of your testimony that “[s]ince mailers have *options* concerning not only what kind of container to use but also container makeup, these costs should be recognized in rates (emphasis added):”

(a) Please reconcile that statement with the statement at page 28 lines 8-10 of your testimony that “no argument is being made, and no position taken, that ... *all* mailers find themselves in situations where changes are feasible ...” (emphasis in original).

(b) Please state what percentage of outside-county Periodicals should, as a general matter in your view, “find themselves in situations where changes are feasible” and “have options” before Periodicals costs and rates can fairly and equitably be de-averaged in an effort to redistribute costs more precisely. Please explain your reasoning fully.

(c) Assuming that the proposed rate structure were to be adopted, please provide your best estimate of the respective percentages of outside-county Periodicals that would not in fact likely find themselves in situations where changes are feasible in order to (i) move significantly from sacks to pallets and/or (ii) increase dropshipping significantly. Please specify the precise sources and/or bases for your answers and provide any necessary calculations.

(d) Assuming that the proposed rate structure were to be adopted, please provide your best estimate of the percentage of outside-county Periodicals that may be threatened with or pushed into insolvency as a result of higher postage rates. Please specify the precise sources and/or bases for your answer and provide any necessary calculations.

(e) Please provide your best estimate of the price elasticity of demand associated with increases in postage rates for high-editorial/low-circulation Periodicals under the proposed rate structure. Please specify your sources precisely and provide any necessary calculations.

### RESPONSE

(a) I do not see that any reconciliation is needed. The statements to which you refer are not mutually inconsistent.

(b) I am not able to provide a proportion of the kind about which you ask. I believe it is clear, however, that the proportion of mailers who would find it in their best interests to make changes is substantial and that they exist in virtually every size

## **Responses of Witness Mitchell to MH/TW et al.-T1-20**

and zone category. The notion that the solution to an optimization problem would remain unchanged when virtually all of the input parameters change is not credible. Note also that the deaveraging proposed is fairer than the deaveraging it replaces.

(c) I am not able to provide estimates of the proportions in your question. Note, however, that there is a lot more to the proposed rates than pallets and dropshipping. For one thing, the dropship discounts are spread more evenly over potential dropship points in a way that recognizes the containers used and that recognizes costs more fairly. For another, the sizes of the bundles and the number of bundles per sack are shown to be quite important.

(d) I am not able to provide an estimate of a proportion of the kind you seek. I would note, however, contrary to what you may suspect, that I know of no evidence that any publications potentially finding themselves in an uncomfortable financial position would fit into any particular size category. I understand that the number of publications going into and going out of business each year is rather large. Publications exist in a competitive environment. Entry and exit decisions are made in large part on the basis of expected profitability. These decisions should be made on the basis of market-based rates for postal services, in kind with the other costs that publishers face.

(e) I am not able to provide estimates of the elasticities you seek. Some information in this regard is provided in my response to ABM/TW et al.-T1-64.

## **Responses of Witness Mitchell to MH/TW et al.-T1-21**

**MH/TW et al. – T1- 21:** With reference to your testimony at pages 37-39, and note 33 in particular, regarding the proposed discount of 10.1 cents per pound of editorial matter, in lieu of the current flat editorial pound charge, please confirm that if a high-zone mailer incurred total postage of 60 cents per piece prior to application of the proposed editorial pound discount, while a low-zone mailer incurred total postage of 25 cents per piece prior to application of that discount, and each piece weighed one pound and was 100% editorial, the proposed editorial pound discount would result in a greater than 40% reduction in postage for low-zone, low-cost mailer, but would result in a less than 17% reduction in postage for high-zone, high-cost mailer. If you do not confirm, please explain fully.

### **RESPONSE**

Confirmed. The phenomenon you outline, which is acknowledged in my testimony, is a consequence of the changes proposed, which are designed to achieve a range of objectives, and results from the fact that the editorial benefit as now given is highly skewed.

## Responses of Witness Mitchell to MH/TW et al.-T1-22

**MH/TW et al. – T1-22:** With reference to your testimony on page 39 lines 3-12, comparing the treatment of higher-zone publications under the current and proposed rate structures:

(a) Please confirm that under the current rate structure, the flat editorial pound charge mitigates, in proportion to editorial percentage of mailed Periodicals, the higher Postal Service transportation rates that would otherwise be charged higher-zone Periodicals, with the aim of thereby fostering widespread dissemination of editorial content. If you do not confirm, please explain fully.

(b) Please confirm that under the proposed rate structure, the pound charge for a 100% editorial publication mailed from zone 8 would increase from 19.3 cents per pound to 49.8 cents per pound. If you do not confirm, please explain fully.

(c) Please confirm that the assertion at page 39 lines 7-12 of your testimony that higher-zone publications would be “treated quite favorably” and receive a “high form of consideration” under the proposed rate structure means only that you did not mark up the proposed zone charges by 1.3% -- resulting, for example, in a proposed zone 6 charge of 36.2 cents rather than 36.7 cents. If you do not confirm, please explain fully.

(d) Please confirm that high-editorial Periodicals tend to lack the mail volume and density necessary to prepare their mail on pallets and/or dropship it, and could accordingly incur new sack charges ranging from \$1.53 to \$3.30 per sack under the proposed rate structure. If you do not confirm, please explain fully.

(e) Please confirm that there may be a significant number of high-editorial/low-circulation Periodicals for whom co-palletization and/or co-mailing may not be viable options presently or in the near future in view of the limited availability of efficient co-palletization and co-mailing services, the substantial capital and operating costs of those services, the delays in delivery time occasioned by those services, and/or other factors. If you do not confirm, please explain fully.

(f) Please confirm that the proposed rate structure is designed to send strong price signals to higher-zone/higher-editorial Periodicals to minimize their use of Postal Service transportation to the extent possible, and instead to utilize competing transportation providers to the extent that they are less expensive than Postal Service transportation. If you do not confirm, please explain fully.

(g) Please confirm that to the extent some mailers were eventually able to respond to such price signals and did manage in the future to switch to less expensive competing transportation, the unit costs of Postal Service transportation may increase even further for other mailers who are unable to

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do so, and who therefore remain dependent on Postal Service transportation. If you do not confirm, please explain fully.

### RESPONSE

(a) Your question has two parts. I can confirm that the flat editorial pound rate mitigates the extent to which higher-zone editorial matter contributes to additional (relative to zones 1&2) Postal Service transportation costs that it would otherwise be charged. In fact, it mitigates it to such a degree that the extent in question becomes zero.

I can also confirm that fostering the widespread dissemination of editorial content has been viewed as the aim of the flat editorial pound rate. As I discuss quite thoroughly in my testimony, however, I do not believe that the distribution of editorial content is any wider with the flat editorial pound rate than it would be without it. And because the maintenance of it requires that considerably less weight be given to other worthy rate-design objectives, the proposal is that it should be eliminated.

(b) Confirmed that the new pound rate shown in the proposed schedule is 49.8 cents per pound. But the piece in question will receive an editorial benefit of 10.1 cents per pound, which provides it with a net pound rate of 39.7 cents per pound. Also, the piece would pay a per-piece rate as well, so that the proportions involved in going from 19.3 to 39.7 are not indicative of the overall postage increase that applies.

(c) Confirmed, as far as it goes. I do not believe, however, that the current 1.3 percent markup is a permanent fixture. The basis of my choice of words, "high form," is that I believe the virtual most that any customer can ask for is that no more than the extra costs associated with his product be paid.

## **Responses of Witness Mitchell to MH/TW et al.-T1-22**

(d) Confirmed that some such publications could find themselves in that position, but I know of no evidence on the strength of it as a tendency. The per-sack charges would apply to all mail in sacks, not just to certain categories. Also, it should be noted that the per-sack charges are not a net addition to postage, because the associated per-piece and per-pound charges tend to be lower than those in the current rates.

(e) I can confirm that questions such as those you raise have been raised for publications of all editorial levels and are being considered. I cannot provide testimony on the extent of any capacity limitations in the printing industry or on the extent to which some printers might be lagging. I do know that if appropriate signals are not given in rates, progress in the printing industry will be stunted. On the question of capital and operating costs, there is a good deal of related work being done today, and I have no reason to believe that these costs have been found prohibitive. The question of delays has certainly been raised, but so has the opinion that lost time is made up in the end by improved service. See also the responses of witness Stralberg to ABM/TW et al.-T2-6 and MH/TW et al.-T2-3 and witness Schick to ABM/TW et al.-T4-6 and 51.

(f) The term “designed to” implies a preconceived goal or objective. I reject emphatically that this is the case. My goal has been to develop efficient, appropriate rates that send signals based on Postal Service costs to *all* mailers, not just to selected categories, and that honor accepted rate design conventions and practices. The information thus provided to mailers is more complete, more thorough, and more accurate than that which has been provided in the past. Mailers would be expected to respond to these rates in ways that improve efficiency, whether or not the extent of dropshipping is increased.

**Responses of Witness Mitchell to MH/TW et al.-T1-22**

(g) Not confirmed. See my response to MH/TW et al. – T1-3.

## Responses of Witness Mitchell to MH/TW et al.-T1-23

**MH/TW et al. – T1-23:** With reference to the experimental co-palletization dropship discounts for high-editorial/heavy-weight/small-circulation Periodicals recently proposed by the Postal Service in Docket No. MC2004-1:

(a) Please confirm that the proposed experimental discounts go a fair way toward meeting the objections raised to the current pallet discount at page 58 lines 33-5 of your testimony that “the discount is the same for a) heavy-weight and light-weight pieces and b) pieces transported a short distance and those carried long distances, even though the cost savings vary with both weight and distance.” If you do not confirm, please explain fully.

(b) Please confirm that the proposed experimental discounts, in conjunction with the current pallet discount, dropship pallet discount, and experimental co-palletization discounts from the outside-county Periodicals piece rates, reflect in principle a reasonable and measured alternative approach to achieving significant progress toward efficiency goals underlying the rate structure proposed by complainants here, but without the high degree of cost de-averaging and potentially severe rate impact upon high-editorial/low-circulation Periodicals that would flow from complainants’ proposed rate structure. If you do not confirm, please explain fully.

### RESPONSE

(a) Not confirmed. The discount proposed in Docket No. MC2004-1 builds on the existing pallet discount; it does not alter it or change any of its characteristics.

(b) Not confirmed. The concoction of discounts you list is highly and unjustifiably discriminatory, far from cost-based in a fair and defensible way, skewed toward apparent end results by their selection of cost bases that are misaligned with the mailer activity required, and will be little used. Although the cost reductions of the Postal Service should be greater than the rate reductions, sometimes much greater, and although the participating mailers may be helped without adverse effects on others (other than the possibility that some left-out or similarly situated mailer will view the discounts as unfair), they do not address any of the fundamental problems in Periodicals rates and will not generate meaningful increases in efficiency.

## Responses of Witness Mitchell to MH/TW et al.-T1-24

**MH/TW et al. – T1-24:** Please provide the following information or your best estimate, and specify the precise source of your answer and provide any necessary calculations:

(a) the number of outside-county Periodicals, non-profit Periodicals and classroom Periodicals, respectively; (b) the number of outside-county Periodicals that generally have approximately 70% or more editorial content, and the number that generally have approximately 85% or more editorial content; (c) the number of outside-county Periodicals that are weeklies or have higher frequency; (d) the average mailed circulation and average weight of outside-county Periodicals, and the ranges of the circulation and weight; (e) the average mailed circulation and average weight of those groups of Periodicals specified in subpart b above; (f) the number of outside county Periodicals that are “higher zone publications” as you use that term at page 39 line 4 of your testimony, and please provide your most precise definition of that term; and (g) the number of such higher zone publications in the groups of Periodicals specified in subpart b above.

### RESPONSE

(a) In Docket No. R2001-1, Postal Service witness Loetscher indicated that, mailed in the PERMIT System, there were 17,375 titles with a Regular permit (including Science of Agriculture), 8,315 titles with a Nonprofit permit, and 37 titles with a Classroom permit. The Outside County subclass includes Regular, Nonprofit, and Classroom. Response to CRPA-NFIP/USPS-T41-4. The PERMIT System covers about 95 percent of Periodicals revenue.

(b) In Docket No. R2001-1, witness Loetcher indicated that, mailed in the PERMIT System, 12,487 titles had from 0 percent to 10 percent advertising (average weight 4.64 ounces, volume 1,005,867,452, average circulation 80,553), 2,171 titles had from 10 percent to 20 percent advertising (average weight 6.38 ounces, volume 460,226,956, average circulation 211,988), and 1,941 titles had from 20 percent to 30 percent advertising (average weight 5.22 ounces, volume 573,401,204, average circulation 295,415). Table 1 of MPA/USPS-T34-2, Redirected from witness

## Responses of Witness Mitchell to MH/TW et al.-T1-24

Taufique. The average weight of Outside County Periodicals in FY 2000 was 7.53 ounces. I have not found data for 15 percent or less advertising.

(c) I do not know.

(d) Please see my answer to part "b" above. I do not know any ranges.

(e) Please see my answer to part "b" above.

(f) According to the Commission's Library Reference 9 in Docket No. R2001-1, 2.86 percent of all Outside County Periodicals go to zone 8, 3.06 percent go to zone 7, and 4.14 percent go to zone 6. The average haul for all entry points is 424 miles, which is between the average haul for zone 3 (302 miles) and zone 4 (593) miles. I usually think of higher-zone publications as those having a much higher than average proportion of their copies going to zones 6, 7, and 8.

(g) I do not know.

## Responses of Witness Mitchell to MH/TW et al.-T1-25

**MH/TW et al. – T1-25:** With regard to the proposed rate structure presented at page 43 of your testimony:

(a) Please explain whether it is anomalous that, alone among the container level and bundle level combinations, a 5-D bundle in a 5-D/CR container would pay no bundle charge.

(b) Please explain whether it is anomalous that (i) the charge for an origin-entered 3-D/SCF sack is lower than both the charge for an origin-entered ADC sack and the charge for an origin-entered 5-D/CR sack, while (ii) the charge for a DBMC-entered 3-D/SCF sack is identical to the charge for a DBMC-entered ADC sack and lower than the charge for a DBMC-entered 5-D/CR sack, while (iii) the charge for a DADC-entered 3-D/SCF sack is higher than the charge for a DADC-entered ADC sack and lower than the charge for a DADC-entered 5-D/CR sack, and (iv) the relationships among the corresponding pallet charges are identical to the above-described relationships among sack charges except that the charge for a DADC-entered 3-D/SCF pallet is higher than both the charge for a DADC-entered ADC pallet and the charge for a DADC-entered 5-D/CR pallet.

### RESPONSE

This question has been redirected to witness Stralberg.

## Responses of Witness Mitchell to MH/TW et al.-T1-26

**MH/TW et al. – T1-26:** With respect to the statement at page 27 lines 19-20 of your testimony that the proposed rates “preserve all applicable discounts:”

(a) Please confirm that the difference between the 5-digit Bar-Mach piece rate and the Carrier Route Basic rate under the proposed rates at page 43 of your testimony is 7.3 cents while the difference between the current 5-digit Automation flat rate and the current Carrier Route Basic rate is 6.3 cents. If you do confirm, please reconcile the differential with your above-quoted testimony. If you do not confirm, please explain fully.

(b) Please confirm that the difference between the SCF/3-digit Bar-Mach rate and the 5-digit Bar-Mach rate under the proposed rates is 3.6 cents while the difference between the current 3-digit Automation flat rate and the current 5-digit Automation flat rate is 5.7 cents. If you do confirm, please reconcile the differential with your above-quoted testimony. If you do not confirm, please explain fully.

### RESPONSE

(a) Confirmed. The question of which discounts are applicable is not an easy one. I preserved the carrier portions of the presort savings, as discussed on page 29 of my testimony, beginning at line 12, because no changes in the proposal affect them. The rest of the discounts are a little different. The proposal deaverages to recognize machinability and to provide an ADC presort level, which changes the structure of the discounts and the way they build on each other. The proposal also adjusts all costs to Commission costing, whereas the settlement rates are based on Postal Service costing. Under the latter costing, Commission Library Reference 9 in Docket No. R2001-1 shows that the carrier route passthrough (relative to the old 5-digit level, not barcoded) is 100 percent. It also shows, however, that the barcode discount for 5-digit pieces has a passthrough of 245 percent. Witness Stralberg develops a consistent set of costs for all of the new categories. In order to avoid distortions, I used all of them, except that the carrier portions discussed above were added in separately. This means that the proposed rates have a passthrough of 100 percent. Since the passthrough of 245 percent is therefore essentially backed

## **Responses of Witness Mitchell to MH/TW et al.-T1-26**

out, the interpretation of the comparison you cite is that the 5-digit, barcoded, machinable rate is higher, not that the carrier route rate is lower.

(b) Confirmed. The explanation follows along the lines of that in part “a.” Here, the current passthrough of the barcode discount for 3-digit pieces is 145 percent. When compared to the 245 percent noted above, this explains 1.2 cents of the difference (5.7 – 3.6) you cite.

## **Responses of Witness Mitchell to MH/TW et al.-T1-27**

**MH/TW et al. – T1-27:** Please explain fully what you mean when you refer to “unnecessary or inefficient transportation over long distances” at page 17 line 18 of your testimony.

### **RESPONSE**

In context, transportation that should be unnecessary would occur when, in order to obtain lower printing costs, a publisher of a local publication prints at a distant location despite the fact that his savings are less than the extra costs to the Postal Service of carrying the publication back to the publisher’s locality. Such transportation would also be inefficient. For additional discussion on this point, see my response to ABM/TW et al.-T1-61 (corrected).

## Responses of Witness Mitchell to MH/TW et al.-T1-28

**MH/TW et al. – T1-28:** Please specify the precise sources for the discussion rate history at page 8 line 2-5 and page 19 line 11 through page 20 line 15.

### RESPONSE

The best rate history is: UNITED STATES DOMESTIC POSTAGE RATES, 1789 TO 1956, Post Office Department, Washington, D.C., U. S. Government Printing Office, 1956. See page 63 for the legislation of 1879 and page 65 for the legislation of 1885.

The discussion on pages 19 and 20 draws more generally from historical literature, including that listed in footnote 9 on page 18 and footnote 10 on page 19 of my testimony, the report of the Penrose-Overstreet Commission (Report of the Postal Commission, Authorized by Congress to Make Inquiry Regarding Second-Class Matter, January 28, 1907, Government Printing Office, 1907), and the work of Richard B. Kielbowicz (see PRC Library References 1 and 2 in the instant docket and “Library Materials in the Mail: A Policy History,” Linda Lawson and Richard B. Kielbowicz, *The Library Quarterly*, Vol. 58, No. 1, January 1988, pp. 29-51).

## Responses of Witness Mitchell to MH/TW et al.-T1-29

**MH/TW et al. – T1-29:** Referring to your testimony at page 64, estimating Zone 8 postage of \$0.3416 for *The New Republic* under “current” rates, but applying the zoned rates to full weight (not just advertising weight) and applying a 10.1 cent per editorial pound discount in lieu of the flat editorial pound charge, please estimate (a) the zone 8 postage for *The New Republic* under the current rates including the flat editorial pound charge, and (b) the zone 8 postage under (i) current rates (including the flat editorial pound charge) and (ii) the proposed rates for a Periodical with the same relevant characteristics as *The New Republic* except that it has 100% editorial content and weighs one pound. Please set forth and explain your calculations any assumptions made.

### RESPONSE

(a) Consistent with the assumptions made on page 64 (in sacks, 3-digit barcoded, 3.3 ounces, 23 percent advertising), \$0.2869.

(b) Consistent with the same assumptions, except a weight of 1 pound and no advertising, \$0.4020.

## Responses of Witness Mitchell to MH/TW et al.-T1-30

**MH/TW et al. – T1-30:** Referring to your testimony at page 65 lines 12-13, estimating \$49.55 minus the cost of account maintenance as additional profit for a *New Republic* subscriber in zone 8, please specify the amount of the \$49.55 that is attributed to additional advertising revenue, and set forth and explain your calculations and any assumptions made in estimating such advertising revenue.

### RESPONSE

The figure of \$49.55 is a sum of 4 components, 2 of which are negative. Therefore, one cannot say how much of it is attributable to any one component. For example, if the sum were zero and the component of interest were \$5, it would not make sense to say that \$5 of the sum of zero is attributable to the component of interest. However, it can be said that if no advertising revenue were received for the extra copy, the figure of \$49.55 would decline to \$12.44. The difference between these two figures is \$37.11, which is the value of the second term on the right-hand side of equation (5) on page 63. The difference of \$37.11 is equal to  $n * k * P_{ADV} * Q_{ADV}$ .  $n$  = the number of copies per year = 44.  $k$  = an estimate of the average discount given on published advertising rates and is taken to be 0.5.  $P_{ADV}$  = the posted rate for a one-page advertisement in one copy, described in the first paragraph on page 65 of my testimony = 0.1024 \$/page.  $Q_{ADV}$  = the number of pages of advertising in one copy = 0.23 (the proportion of advertising) \* 3.3/16 (the weight of one copy in pounds) / 0.00288 (the number of pounds per one-sided page, described in the second paragraph on page 65 of my testimony).

## Responses of Witness Mitchell to MH/TW et al.-T1-31

**MH/TW et al. – T1-31:** Referring to your testimony at page 66 lines 12-13, estimating \$100.37 minus the cost of account maintenance as additional advertising profit for a *Pit & Quarry* subscriber in zone 8, please set forth and explain your calculations and any assumptions made in arriving at the \$100.37 figure.

### RESPONSE

The figure of \$100.37 is obtained from equation (5) on page 63 of my testimony.

The variables are defined and discussed therein. The second term, which is somewhat complex, is calculated just as described in my response to MH/TW et al. – T1-30, except that data for *Pit & Quarry* are used.  $P_{SUB}$  is the annual price of a subscription (assumed to be zero in this case) and  $MC_{PRT}$  is the marginal cost of printing another copy (estimated to be \$0.31, see page 66, line 10).

## **Responses of Witness Mitchell to MH/TW et al.-T1-32**

**MH/TW et al – T1-32:** Referring to your testimony at page 66, please state (a) the number and percentage of outside-county Periodicals that are controlled circulation or requester publications, and (b) the number of outside-county Periodicals that are 100% editorial in content. Please specify the precise sources for your answer and provide any necessary calculations.

### **RESPONSE**

(a) I have no way of estimating the proportion you seek.

(b) I have no way of estimating the proportion you seek. In Docket No. MC2004-1, Postal Service witness Taufique indicated that, based on PERMIT System data, 14,122 Outside County titles have less than 15 percent advertising.

## **Responses of Witness Mitchell to MH/TW et al.-T1-33**

**MH/TW et al. – T1-33:** Referring to your testimony at page 65 lines 10-11 and page 66 lines 9-10, please set forth and explain your calculations and any assumptions made in arriving at a 17 cents per copy marginal cost of printing for *The New Republic* while arriving at a 31 cents per copy cost of printing for *Pit & Quarry*.

### **RESPONSE**

Please see my responses to ABM/TW et al.-T1-99 and ABM/TW et al.-T1-101.

## Responses of Witness Mitchell to MH/TW et al.-T1-34

**MH/TW et al. – T1-34:** Referring to your testimony at page 65 lines 15-17, please state whether you would generally expect the cost of account maintenance to decline on a per account basis as circulation increased, and vice versa, and explain your answer fully.

### RESPONSE

As suggested on page 62 of my testimony, at line 9, the cost of account maintenance is a rather general term covering the costs of solicitation, billing, address-file maintenance, and renewal. (On the role of renewals, please see my response to ABM/TW et al.-T1-65.) I would not take the position that scale economies in these functions are nonexistent. But if there are such economies, the variable  $C_{AM}$  should be considered a marginal cost of account maintenance. To the extent that this marginal cost is lower than the unit cost you reference, recognizing it would increase the profit hit for dropping higher-zone subscribers. The fixed costs of account maintenance would simply be put in with the fixed costs of administration.

## Responses of Witness Mitchell to MH/TW et al.-T1-35

**MH/TW et al. – T1-35:** Referring to your testimony at page 65 lines 13-21:

(a) Please confirm that for a 100% editorial Periodical published weekly, offering an annual subscription for \$20 and having a circulation net of \$5.00, it would be profitable to drop a zone 8 subscriber under the proposed rate structure if it resulted in an increase of 10.1 cents per piece mailed to zone 8. If you do not confirm, please explain fully.

[b] (c) Please confirm that under the proposed rate structure, the pound charge for a one-pound piece mailed to zone 8 by a 100% editorial publication will increase by 20.4 cents (after applying the proposed 10.1 cents per editorial pound discount). If you do not confirm, please explain fully and show any necessary calculations.

(c) Please specify fully the basis, if any, for your statement I that “[a]s a proportion, circ net might be in the neighborhood of 50 percent.”

### RESPONSE

(a) Not confirmed. In the situation you specify, the publisher would find it profitable to drop all subscribers in all zones, and thereby go out of business.

(b) Confirmed.

(c) I have discussed the circ-net proportion with people in the industry and have been told that, as a rule of thumb, it is often in the neighborhood of 0.5 for consumer magazines, which qualify for Periodicals rates as General Publications. Actual values, of course, vary from magazine to magazine, and revenues and costs associated with newsstand sales and list rentals are sometimes included. The notion is reasonably simple. Subscription rates are expected to be an important part of the revenue received, and when additional subscribers contribute little or nothing to helping cover the fixed costs (of editorial creation, printing, and administration), there may be reason for concern. My testimony observes that a negative circ net “would be very unusual.” Page 66, line 1. None of my conclusions depend on circ net having a specific value.

## **Responses of Witness Mitchell to MH/TW et al.-T1-35**

The situation faced by Requester Publications, often referred to as controlled circulation publications, is quite different. Their costs are covered primarily by advertising revenues, and they usually expect subscription revenues to play little or no role. Their circ net, if calculated, could easily be negative. The application of my model to a Requester Publication is illustrated on page 66 of my testimony, beginning at line 3.

## Responses of Witness Mitchell to MH/TW et al.-T1-36

**MH/TW et al. – T1-36:** Referring to your testimony at page 67 line 5 and following regarding the “situation where the profit level of the publication is zero:”

(a) Please confirm that a publication is more likely to have a low, negligible or negative profit level to the extent that it has (i) low circulation relative to its fixed costs, (ii) low advertising content, (iii) high editorial content, (iv) high frequency (v) high weight per copy, (vi) is a start-up publication, and/or (vi) is a controlled circulation or requester publication. Please explain your answer fully.

(b) Please confirm that high-editorial/high-zone/low-circulation publications with low, negligible or negative profit levels may be threatened with insolvency by the proposed rate structure if they are unable to increase revenues or cut costs sufficiently to offset the increased postage. If you do not confirm, please explain fully.

(c) Please confirm that to the extent such a publication were to raise its subscription rate in an attempt to offset such increased postage, it would likely lose subscribers. If you do not confirm, please explain fully.

(d) Please confirm that to the extent such publication were unable to alter its mailing practices in order to offset such increased postage, it would have incentives to (i) reduce its editorial content in order to reduce costs and (ii) target its marketing on low-zone/low-cost subscribers rather than high-zone/high-cost subscribers. If you do not confirm, please explain fully.

### RESPONSE

(a) Not confirmed. My testimony focuses on tendencies, forces, and equilibrium situations. If the profit is above zero, the relevant profit figure would be a return on investment, not some absolute level, toward which most of the factors you list seem directed. When a publisher goes into business, he would be expected to take a longer-term view, have some vision, and know something about the likely circulation, the level of advertising, the kind and quantity of editorial content that will be created, the frequency of publication, and the weight per piece. The fact that at some point in time it might be a start-up publication does not change the publisher's vision. Investment decisions are not made on the basis of what the first year might look like. I know of no evidence or reasoning suggesting that profit levels (on a return on investment basis), are lower, are expected to be lower, or are desired to be lower for

## Responses of Witness Mitchell to MH/TW et al.-T1-36

controlled circulation publications. It is of course true that from any beginning position, changing the variables you list would affect profits, no matter how measured.

(b) Confirmed that *any* publication faced with low profit rates (not necessarily levels) and increases in factor prices, and with no alternatives to further adjust those levels, could become insolvent. I know of no evidence that high-editorial, high-zone, or low-circulation publications tend to be less profitable than others. It is certainly the case that many high-circulation publications have gone out of business. But even if there were evidence that a limited number of publications with low profit rates were threatened by a change being considered, I see no path that provides for judging their worth or parceling them out lower rates, or for having someone else subsidize them, and it would be decidedly inefficient to give all such publications low rates in order to preserve a few.

(c) Confirmed that this is likely to be the case more often than not. Note, however, that a loss of subscribers does not imply that subscription revenue will be lower. Also, adjustments in factors other than subscription rates are possible.

(d) Not confirmed. It is not necessarily the case that changing these factors in the way you specify would increase profits. On the question of solicitation, please see my response to ABM/TW et al.-T1-65. On the question of the profitability of what you call “high-zone/high-cost subscribers”, see Appendix A in my testimony.

## Responses of Witness Mitchell to MH/TW et al.-T1-37

**MH/TW et al. – T1-37:** Referring to your testimony at page 32 lines 10-12 that “[f]or zones 1&2 through 8, the number of [editorial] pounds is estimated in my workpapers by assuming that pieces entered in these zones have an average proportion of editorial content:” (a) please explain the basis for your assumption; (b) please explain whether it is likely that pieces entered in the higher zones in fact have a materially higher than average proportion of editorial content, and (c) if that were to be established, please state what effect it would have on your proposed zoned rates and explain your answer fully.

### RESPONSE

(a) Data are not available on the zone distribution of editorial content. The assumption to which you refer was made by the Postal Service in Dockets No. R77-1, R87-1, and R90-1. I agree that there could be differences, but it seems reasonable to believe that they are not large.

(b) The distribution needed would be pound-weighted, not piece-weighted. For example, a lightweight piece with a high proportion of editorial content entered in zone 8 would have very little effect on the distribution of the pounds. Despite the fact that Periodicals volume is a relatively small portion of total Postal Service volume, the numbers involved here are rather large and most of the important variables vary widely. That is, there are many Periodical titles, their weights vary substantially, their proportions of editorial content vary substantially, and their zone distributions vary substantially. In the face of large numbers and such diversity, it is often the case that summary distributions are not skewed. I have no basis for believing that the effect you suggest is likely.

(c) The magnitude of the effect on rates of the zone distribution of editorial being different from the corresponding distribution of advertising might not be significant. Suppose, as you suggest, the zone-8 pieces were found to have a higher-than-average proportion of editorial content. The total transportation costs that are recovered in the rates are determined by the actual distribution of editorial and

## **Responses of Witness Mitchell to MH/TW et al.-T1-37**

advertising combined. So, if there are more editorial pounds in zone 8 than in my analysis, the transportation costs developed and recovered in the rates are still at the appropriate level. To develop the differences in the zoned pound rates, these transportation costs are distributed to zones according to the number of pound-miles in each zone. Under your assumption, more costs would be distributed to zone 8 than in my analysis. Then, in order to get the cost per pound, on which the zone differences are based, this higher cost would be divided by a higher number of pounds, tending to yield approximately the same cost per pound as in my analysis.

Another way to look at this issue is to recognize that the current rate development procedure, used by the Postal Service and the Rate Commission in all rate cases, implicitly makes the same assumption that I make. The procedure can be done in one of two ways, which are equivalent. The first is to distribute total transportation costs on inflated pound-miles of advertising (inflated by the ratio of total pounds to advertising pounds, which is known). The second is to distribute the transportation costs for advertising on the pound-miles of advertising, with the transportation costs of advertising being determined by the product of total transportation costs and advertising pounds as a proportion of total pounds.

## Responses of Witness Mitchell to MH/TW et al.-T1-38

**MH/TW et al. – T1-38:** Referring to your testimony at page 19 lines 4-8 and page 69 lines 8-9 that “transportation costs today are a much smaller portion of total costs than they were in 1917,” please explain the extent to which that statement applies to *unit* costs of Postal Service transportation of Periodicals. Please specify the sources for your answer and provide any necessary calculations.

### RESPONSE

If one had transportation costs per pound-mile for 1917, either on a marginal basis or some kind of average total, I believe, adjusted for inflation, they would be much, much higher than corresponding figures today. Using the information in the 1917 literature I reference, however, I was not successful in developing such figures and therefore provided the analysis on page 19.

The transportation costs used in ratemaking, and specifically the ones used to develop the differences in the zoned pound rates, are volume variable (equivalent to marginal) costs. It is these costs, expressed on a pound-mile basis that would be most relevant in any comparison. Expressing these costs on a unit basis (usually meaning dividing by the number of pieces) would not be helpful.