POSTAL RATE COMMISSION

In the Matter of:	)	
	)	
COMPLAINT OF TIME WARNER, INC., ET AL., CONCERNING PERIODICAL RATES	)))	Docket No. C2004-1

Hearing Room
Postal Rate Commission
1333 H Street, N.W.
Washington, D.C.

Volume 3
Monday, July 12, 2004

The above-entitled matter came on for hearing pursuant to notice, at 9:30 a.m.

BEFORE:

HON. GEORGE A. OMAS, CHAIRMAN
HON. TONY HAMMOND, VICE-CHAIRMAN
HON. DANA B. COVINGTON, COMMISSIONER
HON. RUTH Y. GOLDWAY, COMMISSIONER

APPEARANCES:

On behalf of the United States Postal Service:

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APPEARANCES: (cont'd.)

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On behalf of the National Newspaper Association:

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C O N T E N T S

WITNESSES APPEARING:
JOHN STEELE GORDON
ROBERT W. MITCHELL

WITNESSES:	DIRECT	CROSS	REDIRECT	RECROSS	VOIR DIRE
John Steele Gordon					
by Mr. Keegan	608	--	770,785	--	--
by Mr. Straus	--	700	--	780	--
by Mr. Bergin	--	738	--	--	--
by Ms. Rush	--	740	--	--	--
Robert W. Mitchell					
by Mr. Keegan	790	--	--	--	--
by Mr. Straus	--	1132,1172	--	--	--

DOCUMENTS TRANSCRIBED INTO THE RECORD	PAGE
Corrected direct testimony of John Steele Gordon, TW et al-T-3	609
Corrected designated written cross-examination of John Steele Gordon, TW et al-T-3	630
Corrected direct testimony of Robert W. Mitchell, TW et al-T-1	792
Corrected designated written cross-examination of Robert W. Mitchell, TW et al T-1	870
Responses of Witness Mitchell to MH/TW et al.-T1-39	1119

E X H I B I T S

EXHIBITS AND/OR TESTIMONY	IDENTIFIED	RECEIVED
Corrected direct testimony of John Steele Gordon on behalf of Time Warner, Inc., et al., TW et al.-T-3	609	609
Corrected designated written cross-examination of John Steele Gordon, TW et al-T-3	630	630
Corrected direct testimony of Robert W. Mitchell on behalf of Time Warner, Inc., et al., TW et al-T-1	792	792
Corrected designated written cross-examination of Robert W. Mitchell , TW et al T-1	870	870
Responses of Witness Mitchell to MH/TW et al.-T1-39	1119	1119

1 P R O C E E D I N G S

2 (9:30 a.m.)

3 CHAIRMAN OMAS: Good morning. Today we are
4 continuing evidentiary hearings on Docket No. C2004-1
5 considering Complaint Concerning Periodical Rate
6 Filings filed by Time Warner, Inc.; Conde Nast
7 Publications, a Division of Advance Magazine
8 Publishers, Inc.; Newsweek, Inc., the Readers Digest
9 Association; and the TV Guide Magazine Group. For the
10 purposes of this case, these five Complainants are
11 known collectively as Time Warner, et al.
12 This morning we are scheduled to hear the
13 testimony of Time Warner, et al. Witness Gordon and
14 Mitchell. It had been my intention to have as much
15 outstanding material as possible included in today's
16 transcript, including designated institutional
17 responses.
18 This morning, Time Warner, et al. filed
19 additional institutional responses. I will defer
20 placing the institutional responses in the transcript
21 until the close of today's hearing. In the interim, I
22 have had copies of today's filings made available on
23 the table as you enter the hearing room. Before we
24 adjourn, I will entertain additional requests to
25 designate institutional responses.

1 No request to conduct additional cross-
2 examination of Witness Stralberg was received, so this
3 hearing will conclude the presentation of Complainant
4 Time Warner, et al.
5 This morning while the hearing is in
6 progress I will be issuing a procedural ruling that
7 will establish the scheduled dates for the remainder
8 of this case. As always, dates are subject to
9 adjustment for good cause shown.
10 It continues to be my intention to proceed
11 with this case in a prompt and measured fashion. When
12 the ruling is issued, I will see that copies are made
13 available in the hearing room for counsel to review.
14 Does anyone have a procedural matter to
15 discuss before we hear testimony today?
16 (No response.)
17 CHAIRMAN OMAS: Mr. Burzio, would you
18 introduce your witness, please?
19 MR. KEEGAN: Good morning, Mr. Chairman.
20 Timothy Keegan for Time Warner, et al. John Burzio is
21 getting time off for good behavior today, but not
22 entirely off.
23 CHAIRMAN OMAS: Mr. Gordon? Mr. Gordon,
24 would you stand and raise your right hand?
25 //

1 Whereupon,

2 JOHN STEELE GORDON

3 having been duly sworn, was called as a

4 witness and was examined and testified as follows:

5 DIRECT EXAMINATION

6 BY MR. KEEGAN:

7 Q Would you state your name and occupation,

8 please?

9 A My name is John Steele Gordon. I'm a

10 writer.

11 Q Do you have with you two copies of a

12 document that has been captioned TW et al-T-3, Direct

13 Testimony of John Steele Gordon?

14 A Yes, I do.

15 Q Is that your testimony in this case?

16 A Yes, it is.

17 Q Was it prepared by you?

18 A Yes, it was.

19 Q Would that be the testimony you would give

20 today if you were giving your testimony orally?

21 A Yes, it is.

22 Q Do you have any corrections or changes to

23 it?

24 A No, beyond what is indicated here.

25 MR. KEEGAN: There have been, Mr. Chairman,

1 two minor changes made in the record copies. One of
2 those is that several paragraphs were inadvertently
3 printed in italics, and those have been changed to
4 Roman font.
5 The other is that -- I apologize. That is
6 the only change.
7 CHAIRMAN OMAS: Thank you. Is there any
8 objection?
9 (No response.)
10 CHAIRMAN OMAS: Hearing none, I will direct
11 counsel to provide the reporter with two copies of the
12 corrected direct testimony of John Steele Gordon.
13 That testimony is received and will be transcribed
14 into evidence.
15 (The document referred to was
16 marked for identification as
17 Exhibit No. TW et al-T-3 and
18 was received in evidence.)
19 //
20 //
21 //
22 //
23 //
24 //
25 //

Postal Rate Commission 610
Submitted 4/26/2004 9:47 am
Filing ID: 40292
Accepted 4/26/2004
TW et al.-T-3

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

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

Docket No. C2004-1

DIRECT TESTIMONY OF JOHN STEELE GORDON ON BEHALF OF 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. CONCERNING COMMUNICATIONS IN THE TWENTIETH CENTURY

April 26, 2004

1 **DIRECT TESTIMONY OF**

2 **JOHN STEELE GORDON**

3 **CONCERNING**

4 **COMMUNICATIONS IN THE TWENTIETH CENTURY**

5

6 *Biographical Sketch*

7 John Steele Gordon was born in New York City in 1944 into a family long
8 associated with the city and its financial community. Both his grandfathers held
9 seats on the New York Stock Exchange. He was educated at Millbrook School and
10 Vanderbilt University, graduating with a B.A. in history in 1966.

11 After college he worked as a production editor for Harper & Row (now
12 HarperCollins) for six years before leaving to travel, driving a Land-Rover from New
13 York to Tierra del Fuego, a nine-month journey of 39,000 miles. This resulted in his
14 first book, *Overlanding*. Altogether he has driven through forty-seven countries on
15 five continents.

16 After returning to New York he served on the staffs of Congressmen Herman
17 Badillo and Robert Garcia. He has been a full-time writer for the last twenty years.
18 His second book, *The Scarlet Woman of Wall Street,* a history of Wall Street in the
19 1860's, was published in 1988. His third book, *Hamilton's Blessing: the*
20 *Extraordinary Life and Times of Our National Debt*, was published in 1997. *The*
21 *Great Game: The Emergence of Wall Street as a World Power, 1653-2000*, was
22 published by Scribner, a Simon and Schuster imprint, in November, 1999. A two-
23 hour special based on *The Great Game* aired on CNBC on April 24th, 2000. His
24 fourth book, a collection of his columns from *American Heritage* magazine, entitled
25 *The Business of America*, was published in July, 2001, by Walker. His history of the
26 laying of the Atlantic Cable, *A Thread Across the Ocean*, was published in June,
27 2002. His next book, *An Empire of Wealth: The Epic Story of American Economic*

Power, will be published by HarperCollins in October, 2004.

He specializes in business and financial history. He has had articles published in, among others, *Forbes*, *Forbes ASAP*, *Worth*, the *New York Times* and *The Wall Street Journal* Op-Ed pages, the *Washington Post*'s "Book World" and "Outlook." He is a contributing editor at American Heritage, where he has written the "Business of America" column since 1989.

In 1991 he traveled to Europe, Africa, North and South America, and Japan with the photographer Bruce Davidson for Schlumberger, Ltd., to create a photo essay called "Schlumberger People," for the company's annual report.

In 1992 he was the co-writer, with Timothy C. Forbes and Steve Forbes, of *Happily Ever After?*, a video produced by Forbes in honor of the seventy-fifth anniversary of the magazine.

He is a frequent commentator on *Marketplace*, the daily Public Radio business-news program heard on more than two hundred stations throughout the country. He has appeared on numerous other radio and television shows, including *New York: A Documentary Film* by Ric Burns, *Business Center* and *Squawk Box* on CNBC, and *The News Hour with Jim Lehrer* on PBS. He was a guest in 2001 on a live, two-hour edition of *Booknotes* with Brian Lamb on C-SPAN.

Mr. Gordon lives in North Salem, New York.

* * *

Nothing so characterized twentieth-century America as technological progress. Humankind first lifted off the ground under power in 1903. Only sixty-six years later we landed on the moon. In 1954 no manmade object had reached more than 272 miles above the earth. Today, the space craft voyager II is more than six billion miles from earth and still returning data. In 1900 life expectancy was forty-five

years, in 2000 it was seventy-six years and climbing rapidly.

But no aspect of this vast and on-going technological revolution has been more dramatic than communications. To be sure, the nineteenth century had seen a great improvement in communications. In 1800, most communities were isolated from each other and even the most electrifying news traveled very slowly. The Battles of Lexington and Concord in Massachusetts, which marked the beginning of the American Revolution, occurred on April 19th, 1775, but the news reached New York only on the 23rd. Williamsburg, Virginia, didn't hear it until April 28th, and London learned of the battles only on May 28th.

Two technological developments changed matters profoundly. The invention of rotary presses powered by steam in the 1820's allowed many more newspapers and magazines to be quickly printed at much lower cost. Much reduced in price, they became the daily habit of millions. As early as 1866, only thirty years after the first modern newspaper, the *New York Herald*, began publication, the *North American Review* had noted that "The daily newspaper is one of those things which are rooted in the necessities of modern civilization. The steam engine is not more essential to us. The newspaper is that which connects each individual with the general life of mankind."

The other nineteenth-century development was the first practical use of electricity when in 1844 Samuel Morse tapped out the famous words "What hath God Wrought!" in the Capitol Building in Washington and his partner Alfred Vail, in Baltimore, repeated them.

The telegraph spread with lightning speed, often using the pathways forged by the equally fast-spreading railroads. Only seventeen years after the first telegraph message, a line reached all the way to San Francisco. Five years after that, Cyrus Field had succeeded in laying the Atlantic Cable and Europe came within reach of instant communication for the first time. By the time Morse died in

1872, a message that would have taken six months a few decades earlier could be sent from San Francisco to India in a few hours.

In 1876 Alexander Graham Bell invented the telephone, which, unlike the telegraph, did not require skilled operators at each end. The telephone quickly spread through the business districts of major cities. It became possible to call between New York and Chicago in 1892, and by 1915 it was possible to call across the continent.

But the telegraph and telephone remained very expensive. When the Atlantic Cable opened for business in 1866, the price was a dollar a word with a fifteen word minimum, well over a week's wage for the average worker. Domestic telegraphy, while cheaper, was beyond the reach of most families except for the most important messages. The telephone, more expensive still, was found only in the more affluent private houses until after World War I, when about thirty-five percent of households had private telephones. In 1919 a long-distance call from New York to San Francisco cost $16.50 for three minutes, more than $150 in today's money. It would be 1946 before half the households in the United States had a phone.

Despite the development of the telegraph and telephone, by the early years of the twentieth century, the situation had not changed much since 1866. It was still newspapers (none of which circulated nationally) and, especially, magazines that bound the nation together by providing a common culture and a common source of information.

And because of the printing technology then available, publications had to be produced in one place. The linotype had been invented in 1884 by Ottman Merganthaler. By setting one line, rather than one letter, at a time, it allowed much faster typesetting. But it was still a cumbersome process, and newspapers and magazines had to be printed from metal type.

Thus it made sense for the Congress, in formulating the Post Office's

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mandate to hold this vast, sprawling country together by facilitating the distribution of printed matter, to set uniform postal rates for magazines, regardless of where they were printed or where they were sent, in 1876 and to maintain uniform rates for editorial matter when it zoned the rates for advertising matter in 1917.

But in the eighty-seven years since that decision, the technology of communications has changed more than it had in the previous eighty-seven. Indeed it has changed more than in the whole previous history of communications by means other than the human voice, a history that dates back to the dawn of the written word five thousand years ago.

The technology of printing, the oldest means of communication beyond the human voice and hand, has changed radically in the years since 1917. The teletypewriter, invented in 1913, came into widespread use in the years after the First World War. Attached to a linotype machine, it used a paper tape to control the composition, instead of linotype operators reading copy. A tape reader translated the punched code on the tape into electrical signals and these could be transmitted by wire to other linotype machines in other cities. For the first time this allowed newspapers to be printed in more than one city simultaneously.

Photo-composition machines dispensed with hot metal altogether and allowed type to be set by means of film, which was then used to make plates, from which the printing was done. As the cathode ray tube was developed for television, it was soon adapted for composing type. Coupled with a computer, the cathode ray tube allowed unprecedented ease in such matters as font selection, justification, and hyphenation–a great savings in labor.

Non-printing forms of communications technology advanced even more radically, introducing new means that were undreamed of in 1917. These new forms transformed the entertainment industry as well as the means by which the nation's politics are conducted. This, in turn, had profound effects on the printed

forms.

* * *

The first major change in non-printing technology was the radio. Transmitting voice (and, of course, music) by wireless had become possible by World War I, but it was only in the immediate post-war years that the technology became popular with more than technophiles. The first broadcast service was inaugurated in Pittsburgh in the fall of 1920 and carried the results of the presidential election that year.

The new service was an immediate hit and radio stations began to spring up all over the country. In 1925 the first radio advertising appeared, and in 1926 the first networks began to evolve. These new networks quickly developed national programming, heard simultaneously across the country. By 1929 there were more than six hundred stations in operation, radio signals reached nearly the entire country (today there are more than 10,700 radio stations in the United States), and nearly forty percent of all American households had radio sets, which were being manufactured at the rate of more than four million a year. A whole new group of celebrities emerged, such as Jack Benny and Fred Allen. Programs such as "The Shadow" and "Amos and Andy" became wildly popular and attendance at movie theaters dropped significantly on the nights when they were on.

More important, the new radio networks allowed the government to communicate directly and immediately with the citizenry when necessary. President Franklin Roosevelt's "fireside chats" began on Sunday, March 13th, 1933, only a week after his inauguration. The first one, urging the public to put its money back in banks once they began reopening the next day after the federal bank holiday, was listened to by millions, who accepted the President's assurances that the reopened banks would be safe. It proved a key moment in the nation's recovery from the

Great Depression.

The technology of radio was quickly pushed further and a workable television system was in place by the end of the 1930's, using a 525-line picture with thirty pictures per second, which was adopted as the American standard. The Second World War, of course, put television on hold, but restrictions on manufacturing sets were removed in 1946 and television quickly took off, thanks to such talent as Milton Berle.

In 1948, both major parties held their conventions in Philadelphia. The reason for that was simple enough: it lay in the middle of the coaxial cable that made simultaneous transmission throughout the northeast possible. Although there were still fewer than a million television sets in the country, the medium was already affecting American politics. Within a few years it would become the dominant medium in politics, which it has remained ever since. The country passed the million-set mark in 1949 and had ten million by 1951. By the end of that decade, over fifty million sets were in use, nearly one per household.

As with radio, television proved a powerful medium for binding the nation together. On March 31st, 1957, 107 million Americans–nearly two-thirds of the entire population–watched the premier of *Cinderella*, a musical written expressly for television by Rodgers and Hammerstein. It was, by far, the largest audience in history up to that time to watch a single event. But, six years later, a far larger audience, nearly the entire country not necessarily engaged in other matters, would watch the funeral of the assassinated President John F. Kennedy, providing a deeply needed national catharsis.

Emerging space technology quickly made even larger audiences possible. Communications satellites began operations in 1962, which allowed transmission of live television between Europe and the United States. In 1965, geosynchronous satellites, which hover over the same spot on the earth, were launched. This made

possible continuous live television throughout the world. The global village, first predicted by the philosopher Marshall McLuhan in 1960 but actually in development as far back as the Atlantic Cable, was now at hand. Today Americans can, and do, watch a war unfold in their living rooms.

With the spread of cable television, and, later, such satellite TV distributors as Direct-TV, the number of channels available has mushroomed. In the 1960's, most Americans had a choice of no more than three channels. Today, most markets are served by well over a hundred channels. This makes it possible for small groups interested in a particular subject, such as cooking, travel, sports, pets, nature, politics, history, and technology to find that subject treated on television on a dedicated channel. This is strikingly similar to the function that in 1917 was performed only by specialty magazines.

* * *

After World War II, a wholly new technology, quite undreamed of in the nineteenth century, began to develop, the computer. It has proved the most powerful invention at least since the steam engine two hundred years ago, perhaps since the development of agriculture ten thousand years ago. The first digital computer, called ENIAC for Electronic Numerical Integrator and Computer, was developed at the University of Pennsylvania in 1946, after three years of effort. With 18,000 vacuum tubes and miles of wire, it was the size of forty filing cabinets and was, by modern standards, glacially slow.

With the invention of the transistor in 1948, the size and cost of computers shrank quickly, and their use spread to many industries that had large data processing needs, such as banks and insurance companies. But they remained large, expensive and mysterious to the general public. Most people had never seen

a computer as late as 1970, because they were kept in special rooms, tended by men in white coats who spoke an arcane language.

The microprocessor changed everything. Essentially a computer on a chip of silicon, the microprocessor caused the cost of computing to plummet, along with the size of computers. Today the average American teenager has on his desk computing power that the Pentagon would have been hard pressed to afford forty years ago. Today computers are found, often many of them, in such devices as automobiles, television sets, telephones, wrist watches, and most household appliances. The world we live in today would not be possible without the microprocessor.

The computer greatly lowered the cost of such communications technologies as the telephone by taking over such functions as switchboards. The breakup of the monopoly on long distance service long held by AT&T, of course, also helped powerfully to lower prices. Fifty years ago, a long-distance call was expensive and people minimized their usage. Today they are so cheap that the government no longer even keeps statistics about how many are made. Many people today just play a flat monthly rate for all calls within the US and Canada.

The rise in international calls, where statistics are still kept, has been staggering. In 1950, about one million overseas calls originated in the United States. By 1970 the number was 23 million and a decade later over 200 million overseas calls originated in the United States. Today the number is over six billion calls and climbing rapidly.

Almost anyone can call whomever they please wherever they please whenever they please and not worry about the cost. And these calls can even be placed not just from home but from nearly anywhere. Half the people walking down the urban streets of America, it seems, are now on their cell phones. This is a situation almost unimaginable in the world of 1917, when fewer than thirty percent of

American households had any phone service at all.

* * *

This revolution in non-printing communications media, coupled with the revolution in printing technology, has had large effects on how printed material is created and distributed. In 1917 newspapers and magazines had to be printed where the type was set. But beginning with the teletypewriter, it became possible to set type and print simultaneously in more than one place. In 1917, there were no national newspapers. Today, it is possible—indeed it is commonplace—to have, the *New York Times* or the *Wall Street Journal* delivered to your doorstep in all the country's major cities and their suburbs.

Composition by computer and the distribution of digital images by electronic means allows magazines as well to be printed simultaneously in different cities and distributed from them. This has caused a major reduction in the transportation component in the cost of distributing Periodicals class mail, from over forty-four percent to less than fifteen percent.

* * *

But by far the most important communications medium to come out of the computer has not been improved telephony, but the Internet. It came into being as a result of the Cold War, when it was devised as a means of protecting communications against a nuclear strike. The hub-and-spoke model of telephone and telegraph networks were very vulnerable to being disrupted by an attack, for hitting the hub wiped out the whole network. So Paul Baran of the RAND Corporation suggested a "distributed network" with no hubs at all. Instead there

would be just an endless number of nodes, such as crossings in an urban street grid, that would allow traffic between computers to flow even if some of the pathways were blocked.

The ARPANET (for Advanced Research Projects, an agency set up by the Pentagon in the late 1950's) became operative in 1968, connecting a grand total of four computers, three in California and one in Utah. In the next fifteen years, a program for e-mail was devised, the TCP/IP program was written that allowed computers using different languages to "talk" with one another, and the domain name system was put in place, making it much easier for one computer to find another. By 1983 there were 563 computers on the net, mostly in universities, think tanks, and government agencies.

By 1990 there were 300,000 computers on the net and the number was doubling every three years. In 1992, an Englishman named Tim Berners-Lee created the first web browser and released it without copyright. This allowed users to search the web for sites dedicated to different subjects. The Internet was now complete and the world changed. Over seventy million American households (and uncountable millions of households around the world) are now connected by the Internet.

Almost forty million Americans now have high-speed access. This makes it possible to download complex material, such as photographs and even movies, in very little time. Thus magazines that could once only be delivered by mail, can now be delivered electronically at very little cost.

In the last ten years, the Internet, in addition to being a rapidly growing avenue of commerce that is remaking the business world has become a communications medium of unprecedented power. E-mail is now indispensable to the operation of major corporations and ordinary households alike. Newsgroups, loose associations of people interested in a common subject united by e-mail, now

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In the last ten years, the Internet, in addition to being a rapidly growing avenue of commerce that is remaking the business world has become a communications medium of unprecedented power. E-mail is now indispensable to the operation of major corporations and ordinary households alike. Newsgroups, loose associations of people interested in a common subject united by e-mail, now

number more than twenty-five thousand and are growing at the rate of several hundred a month. Weblogs ("blogs") now number in the tens of thousands, allowing people to become part of the public discussion of news events. Some, such as www.Andrewsullivan.com and www.overlawyered.com have become powerful voices. Other blogs function as letters-to-the-editor columns, only not under the control of the editors, exposing biases and sins of both commission and omission in major newspapers and magazines.

For the first time since the 1830's, it has become cheap to enter the news business. All one needs is a personal computer, an Internet Service Provider, and a webpage design. Some blogs have broken major news. The Drudge Report was the first to bring the Monica Lewinsky scandal, perhaps the biggest story to come out of Washington in the 1990's, to public attention.

Thanks to the Internet, the communications industry is in a state of flux it has not seen since the dawn of the industrial age made modern newspapers and magazines possible, perhaps since Gutenberg invented moveable type more than five hundred years ago.

But while we cannot see how this will all play out in the next few decades, we can know that the changes will be profound, affecting all forms of modern media.

* * *

With the addition of Hawaii and Alaska, the United States, geographically, is far larger and more far-flung than it was in 1917. But in a different sense it is far, far smaller. In 1917 it took three and a half days to travel from New York to Los Angeles. Today it takes five hours and at far lower cost. In 1917, a phone call to San Francisco cost nearly a week's wages for the average household. Today it is essentially free. In 1917, while news could reach across the country in seconds,

number more than twenty-five thousand and are growing at the rate of several hundred a month. Weblogs ("blogs") now number in the tens of thousands, allowing people to become part of the public discussion of news events. Some, such as www.Andrewsullivan.com and www.overlawyered.com have become powerful voices. Other blogs function as letters-to-the-editor columns, only not under the control of the editors, exposing biases and sins of both commission and omission in major newspapers and magazines.

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* * *

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images of great events could take days. Today, great events are broadcast live on dozens of TV channels. In 1917, people interested in an obscure topic had to rely on letters or small, expensive journals to communicate with others of similar interest. Today, no matter how obscure or arcane the topic, there is an Internet newsgroup devoted to it and everyone interested can learn of new developments in seconds.

Today the United States is tightly bound together by many forms of communications, many of them undreamed of in 1917. The United States, the third largest nation in the world in terms of geography, has become one vast neighborhood, where everyone can be "talked" to across the back fence. There is no longer the slightest chance that setting postal rates for editorial content in Periodicals class mail by zones to reflect actual costs would cause the country to be divided by these zones. That is a concern that belongs to an age long past.

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 § 12 of the rules of practice.

s/_____
Timothy L. Keegan

April 26, 2004
Washington, D.C.

1 CHAIRMAN OMAS: Mr. Gordon, have you had an
2 opportunity to examine the packet of designated
3 written cross-examination that was made available to
4 you in the hearing room this morning?
5 THE WITNESS: I have, Mr. Chairman.
6 CHAIRMAN OMAS: If questions contained in
7 that packet were posed to you orally today, would your
8 answers be the same as those you previously provided
9 in writing?
10 THE WITNESS: They would.
11 CHAIRMAN OMAS: Are there any corrections or
12 additions you would like to make to those answers?
13 THE WITNESS: Yes, Mr. Chairman. In my
14 response to ABM/TW et al-T-3-19, in the third to last
15 line the words "identify and" should be deleted and
16 the word "identity" inserted in their place.
17 In my response to NNA/TW et al-T-3-6, in the
18 second line there should be a comma after the word
19 "ways."
20 Those corrections have been made by hand in
21 the packet that I examined.
22 CHAIRMAN OMAS: Counsel, would you please
23 provide two copies of the corrected designated written
24 cross-examination of Witness Gordon to the reporter?
25 That material is received into evidence, and

1 it is to be transcribed into the record.

2 (The document referred to was

3 marked for identification as

4 Exhibit No. TW 35 al-T-3 and

5 was received in evidence.)

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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Complaint of Time Warner Inc. et al.
Concerning Periodicals Rates

Docket No. C2004-1

DESIGNATION OF WRITTEN CROSS-EXAMINATION
OF TW, CONDE NAST, NEWSWEEK, RDA, AND TV GUIDE
WITNESS JOHN STEELE GORDON
(TW et al.-T-3)

Party	Interrogatories
American Business Media	ABM/TW et al.-T3-1, 3-41, 43-51 NNA/TW et al.-T3-2, 11-12 USPS/TW et al.-T3-2-6, 9-10
United States Postal Service	ABM/TW et al.-T3-1, 19, 24-25 NNA/TW et al.-T3-2, 6, 9-10, 12 USPS/TW et al.-T3-1-8, 13

Respectfully submitted,

Steven W. Williams
Secretary

INTERROGATORY RESPONSES OF
TW, CONDE NAST, NEWSWEEK, RDA, AND TV GUIDE
WITNESS JOHN STEELE GORDON (T-3)
DESIGNATED AS WRITTEN CROSS-EXAMINATION

Interrogatory	Designating Parties
ABM/TW et al.-T3-1	ABM, USPS
ABM/TW et al.-T3-3	ABM
ABM/TW et al.-T3-4	ABM
ABM/TW et al.-T3-5	ABM
ABM/TW et al.-T3-6	ABM
ABM/TW et al.-T3-7	ABM
ABM/TW et al.-T3-8	ABM
ABM/TW et al.-T3-9	ABM
ABM/TW et al.-T3-10	ABM
ABM/TW et al.-T3-11	ABM
ABM/TW et al.-T3-12	ABM
ABM/TW et al.-T3-13	ABM
ABM/TW et al.-T3-14	ABM
ABM/TW et al.-T3-15	ABM
ABM/TW et al.-T3-16	ABM
ABM/TW et al.-T3-17	ABM
ABM/TW et al.-T3-18	ABM
ABM/TW et al.-T3-19	ABM, USPS
ABM/TW et al.-T3-20	ABM
ABM/TW et al.-T3-21	ABM
ABM/TW et al.-T3-22	ABM
ABM/TW et al.-T3-23	ABM
ABM/TW et al.-T3-24	ABM, USPS
ABM/TW et al.-T3-25	ABM, USPS
ABM/TW et al.-T3-26	ABM
ABM/TW et al.-T3-27	ABM
ABM/TW et al.-T3-28	ABM
ABM/TW et al.-T3-29	ABM
ABM/TW et al.-T3-30	ABM
ABM/TW et al.-T3-31	ABM
ABM/TW et al.-T3-32	ABM
ABM/TW et al.-T3-33	ABM
ABM/TW et al.-T3-34	ABM

ABM/TW et al.-T3-35	ABM
ABM/TW et al.-T3-36	ABM
ABM/TW et al.-T3-37	ABM
ABM/TW et al.-T3-38	ABM
ABM/TW et al.-T3-39	ABM
ABM/TW et al.-T3-40	ABM
ABM/TW et al.-T3-41	ABM
ABM/TW et al.-T3-43	ABM
ABM/TW et al.-T3-44	ABM
ABM/TW et al.-T3-45	ABM
ABM/TW et al.-T3-46	ABM
ABM/TW et al.-T3-47	ABM
ABM/TW et al.-T3-48	ABM
ABM/TW et al.-T3-49	ABM
ABM/TW et al.-T3-50	ABM
ABM/TW et al.-T3-51	ABM
NNA/TW et al.-T3-2	ABM, USPS
NNA/TW et al.-T3-6	USPS
NNA/TW et al.-T3-9	USPS
NNA/TW et al.-T3-10	USPS
NNA/TW et al.-T3-11	ABM
NNA/TW et al.-T3-12	ABM, USPS
USPS/TW et al.-T3-1	USPS
USPS/TW et al.-T3-2	ABM, USPS
USPS/TW et al.-T3-3	ABM, USPS
USPS/TW et al.-T3-4	ABM, USPS
USPS/TW et al.-T3-5	ABM, USPS
USPS/TW et al.-T3-6	ABM, USPS
USPS/TW et al.-T3-7	USPS
USPS/TW et al.-T3-8	USPS
USPS/TW et al.-T3-9	ABM
USPS/TW et al.-T3-10	ABM
USPS/TW et al.-T3-13	USPS

Response of Witness Gordon to ABM-T3-1

ABM/TW et al.-T3-1. In light of your testimony concerning changes in the communications media and elsewhere since 1917, and your conclusion that zoning the editorial pound rate will not "cause the country to be divided by these zones," please state whether you believe that Periodicals should be granted a postal rate preference to reflect the educational, cultural, scientific and informational value of Periodicals' editorial content and, (b) if so, setting forth all of the reasons why.

Response

I have not formed an opinion on the question.

Response of Witness Gordon to ABM/TW et al.-T3-3

ABM/TW et al.-T3-3. Please list the periodicals that you read on a regular basis.

Response

New York Times, Wall Street Journal, Time, Newsweek, The Week, Forbes, Gourmet, Cook's Illustrated, Astronomy, National Geographic, Audubon, Living Bird, Natural History, Martha Stewart Living, Naval History, American Heritage, Invention and Technology, Scientific American, PC World, PC Magazine, The American Genealogist, National Genealogical Society Quarterly, New York Genealogical and Biographical Record, New England Historical and Genealogical Register.

Response of Witness Gordon to ABM/TW et al.-T3-4

ABM/TW et al.-T3-4. Please examine the list of Periodical publications produced by American Business Media members, which is attached to these interrogatories, and identify: (a) which of these publications you read on a regular basis, (b) which of these publications you read occasionally, (c) which of these publications you read even once before April 26, 2004, and (d) which of these publications you believe are available on newsstands.

Response

a) None; b) Library Journal, Publisher's Weekly, Kirkus Review; c) none to my knowledge; d) I have no idea.

Response of Witness Gordon to ABM/TW et al.-T3-5

ABM/TW et al.-T3-5. Please list the specialized business publications not on the attached list that you read on a regular basis.

Response

None.

Response of Witness Gordon to ABM/TW et al.-T3-6

ABM/TW et al.-T3-6. Please list the specialized business publications not on the attached list that you read occasionally.

Response

None.

Response of Witness Gordon to ABM/TW et al.-T3-7

ABM/TW et al.-T3-7. Please list the specialized business publications not on the attached list that you read even once before April 26, 2004.

Response

None that I remember.

Response of Witness Gordon to ABM/TW et al.-T3-8

ABM/TW et al.-T3-8. Do you consider yourself an expert on the content of specialized business publications? If so, what is the basis for that expertise?

Response

No.

Response of Witness Gordon to ABM/TW et al.-T3-9

ABM/TW et al.-T3-9. Please confirm that, as of the date of this interrogatory, you have a website, www.johnsteelegordon.com.

Response

I so confirm.

Response of Witness Gordon to ABM/TW et al.-T3-10

ABM/TW et al.-T3-10. Please confirm that, as of the date on this interrogatory, the opening page of that website, after "John Steel Gordon, Author" and a quote from Oscar Wilde, contains the subhead "News."

Response

I so confirm.

Response of Witness Gordon to ABM/TW et al.-T3-11

ABM/TW et al.-T3-11. Please confirm that the "News" entries include primarily dates of speeches and appearances.

Response

I so confirm.

Response of Witness Gordon to ABM/TW et al.-T3-12

ABM/TW et al.-T3-12. Is the purpose of the "News" listing on your website: (a) to advise visitors to the website of upcoming events that they might attend or listen to, (b) to advise visitors to the website of past events, such as your speeches and radio appearances, or (c) something else? If something else, please identify the purpose.

Response

The purpose is to advise website visitors of upcoming events they might wish to attend or listen to.

Response of Witness Gordon to ABM/TW et al.-T3-13

ABM/TW et al.-T3-13. Please confirm that, as of the date on this interrogatory, after the word "News' on your website, the first date listed is Wednesday, July 1 (with no year) for the publication of the paperback edition of one of your books.

Response

That is what the site says. It is in error as July 1st, 2003, was a Tuesday.

Response of Witness Gordon to ABM/TW et al.-T3-14

ABM/TW et al.-T3-14. Please confirm that the most recent year in which July 1 fell on a Wednesday was 1998.

Response

I don't know.

Response of Witness Gordon to ABM/TW et al.-T3-15

ABM/TW et al.-T3-15. Please confirm that, as of the date of this interrogatory, (a) the "News" page on your website lists sixteen dates from July 1 to October 16, without a year, and (b) that the year is 2003.

Response

I so confirm.

Response of Witness Gordon to ABM/TW et al.-T3-16

ABM/TW et al.-T3-16. Please confirm that you have made appearances of the type listed on the "News" page of your website since October 16, 2003.

Response

I so confirm.

Response of Witness Gordon to ABM/TW et al.-T3-17

ABM/TW et al.-T3-17. Please confirm that you have scheduled appearances of the type described on the "News" page of your website during the remainder of this year.

Response

I so confirm.

Response of Witness Gordon to ABM/TW et al.-T3-18

ABM/TW et al.-T3-18. When did you last update the "News" section of your website?

Response

In the late summer of 2003.

Response of Witness Gordon to ABM/TW et al.-T3-19

ABM/TW et al.-T3-19. Please confirm that it is often difficult to assess the accuracy and timeliness of information found on websites.

Response

I can confirm that it is often difficult to assess the timeliness and accuracy of information found in any medium, including websites. However, this difficulty may often be easier to overcome for information found on a website than it would be if the same information were found in a print medium, because the internet often provides immediate access to parallel, redundant, or competing sources of the same information. Anyone who routinely uses the internet for research, or to keep up with developments in a business or profession, or just occasionally to seek the kind of information that would once have been sought out in an encyclopedia or a library, is familiar with the fact that using the internet substantially increases the number and variety of sources and the ease with which they can be located, accessed, reviewed, and evaluated. It is also usually easier in the case of internet sources than printed ones to discover the ~~identify and~~ identity of the source's sponsor, its institutional mission, and its affiliations and associations. Also, many web sites indicate the date on which they were updated.

Response of Witness Gordon to ABM/TW et al.-T3-20

ABM/TW et al.-T3-20. Please confirm that specialized business publications frequently summarize and authenticate information that is available elsewhere.

Response

That is my impression with respect to specialized business publications, as with respect to magazines, journals, newsletters, newspapers, and internet web sites generally.

Response of Witness Gordon to ABM/TW et al.-T3-21

ABM/TW et al.-T3-21. Please confirm that all qualified Periodicals carry a publication date.

Response

I am informed by counsel that all qualified Periodicals publications are required by Postal Service regulations to state a publication date. I do not know whether the regulations also require that the stated date of publication and the actual date of publication be the same, but it is my experience that publications often arrive in my mailbox or appear on the newsstand well in advance of the dates printed on their covers (and that the opposite occasionally occurs).

Response of Witness Gordon to ABM/TW et al.-T3-22

ABM/TW et al.-T3-22. Do you agree that most of specialized business publications operate with a high level of editorial integrity and that readers rely to a great extent on that integrity?

Response

I have no basis upon which to agree or disagree. Nor do I not know how one would go about discovering the answer to such a question.

Response of Witness Gordon to ABM/TW et al.-T3-23

ABM/TW et al.-T3-23. Is there any significance to the fact that the first and fourth full paragraphs on page 4 of your direct testimony are in italics?

Response

There is no significance. It was a typographical error.

Response of Witness Gordon to ABM/TW et al.-T3-24

ABM/TW et al.-T3-24. Do Periodicals today bind the nation together by providing a common source of information?

Response

Yes.

Response of Witness Gordon to ABM/TW et al.-T3-25

ABM/TW et al.-T3-25. Do specialized business periodicals today bind segments of the nation's businesses together by providing a common source of information?

Response

Yes.

Response of Witness Gordon to ABM/TW et al.-T3-26

ABM/TW et al.-T3-26. With reference to page 4, lines 22-23 of your testimony, why did the printing technology in the period referenced prevent a publication from being printed in, for example, New York and San Francisco? In other words, why couldn't the process be duplicated?

Response

It would have been prohibitively expensive to duplicate the process at different locations, as composition costs would have been the same at each location.

Response of Witness Gordon to ABM/TW et al.-T3-27

ABM/TW et al.-T3-27. Given the shortening of travel times between the coasts since the early twentieth century, wouldn't there have been more incentive to print at multiple locations then than there is now?

Response

Yes, but it was economically impossible.

Response of Witness Gordon to ABM/TW et al.-T3-28

ABM/TW et al.-T3-28. Please describe your knowledge of and experience in the publication printing business.

Response

My knowledge is that of an informed layman. My experience is non-existent.

Response of Witness Gordon to ABM/TW et al.-T3-29

ABM/TW et al.-T3-29. When you testify at page 5, lines 16-17, that "[f]or the first time, this allowed newspapers to be printed in more than one city simultaneously," do you mean that this development allowed printing at multiple plants cost-effectively?

Response

Yes.

Response of Witness Gordon to ABM/TW et al.-T3-30

ABM/TW et al.-T3-30. Can all Periodicals be printed cost effectively at multiple printing plants today? Please provide a full explanation of the bases for your response.

Response

I do not know.

Response of Witness Gordon to ABM/TW et al.-T3-31

ABM/TW et al.-T3-31. Is there any significance to the ellipses at line 3 of page 6 and line 14 of page 8?

Response

They are not ellipses (i.e., three spaced periods indicating omitted words within a quotation) but rather section breaks that are marked by three spaced asterisks centered on a line. See, e.g., Galactic Publications Book Service, "Submission Guidelines & Layout and Formatting Choices Overview" (<www.galacticpublications.com>).

Response of Witness Gordon to ABM/TW et al.-T3-32

ABM/TW et al.-T3-32. Your testimony at page 8, lines 5-12, suggests that cable television channels perform the same function today as specialty magazines performed in 1917. Is your reference to specialty magazines limited to consumer magazines, or is it intended to include business-to-business publications?

Response

My reference is to magazines devoted to subjects of the type listed in lines 10-11 of the same passage: "cooking, travel, sports, pets, nature, politics, history, and technology."

Response of Witness Gordon to ABM/TW et al.-T3-33

ABM/TW et al.-T3-33. Can you identify a single television channel, or a single television show on any channel, that regularly provides business information on the following subjects, each of which, and more, is covered by a publication produced by a single, medium-sized American Business Media member (Adams Business Media): (a) the beverage industry, (b) the fuel oil industry, (c) irrigation systems, (d) medical equipment design, (e) outdoor power equipment, and (f) specialty coffees?

Response

No.

Response of Witness Gordon to ABM/TW et al.-T3-34

ABM/TW et al.-T3-34. Please examine the attached list of American Business Media member publications and state which of them, if any, appear to contain information that is regularly available on television.

Response

I am unable to deduce from their titles alone what these publications may contain, and I am not familiar with the full range of materials regularly available on television.

Response of Witness Gordon to ABM/TW et al.-T3-35

ABM/TW et al.-T3-35. What is the source for your statement at page 10, lines 15-17, that the use of multiple printing plants has caused a drop in the transportation component from more than forty-four percent to less than fifteen percent?

Response

You have evidently misunderstood my meaning, for which I acknowledge that my imprecise choice of words is at fault. In the lines you cite, I concluded a section of the discussion by stating: "This has caused a major reduction in the transportation component in the cost of distributing Periodicals class mail. . . ." The intended antededant of the word *"This"* was the developments described in the preceding two paragraphs (ll.6-17), i.e., the "revolution in non-printing communications media, coupled with the revolution in printing technology" that occurred between 1917 and the present. However, *"This"* can just as easily be read--as you evidently did read it-- as referring only to the events described in the immediately preceding sentence.

Response of Witness Gordon to ABM/TW et al.-T3-36

ABM/TW et al.-T3-36. At the time you completed preparation of your testimony, did you know what time period was covered by the reduction in the transportation component from forty-four to fifteen percent?

Response

Yes.

Response of Witness Gordon to ABM/TW et al.-T3-37

ABM/TW et al.-T3-37. If you now know what time period was covered, please provide it and identify the source of your information.

Response

The period begins in approximately 1917, when Congress substantially increased second-class rates by introducing a zoned rate for the advertising portion of second-class publications while continuing to provide a low editorial rate which was unzoned. The impetus for this legislation was apparently the drain on the treasury caused by charging magazines and newspapers an unzoned rate so extremely low that it was tantamount to providing them with unlimited free transportation, which had the predictable result that second-class mail consumed transportation resources with ever-increasing profligacy. The end of the period is Fiscal Year 2000, the "base year" for the most recent omnibus postal rate case (see below).

My source was witness Mitchell's testimony, TW et al.-T-1, p. 18, l. 20--p. 19, l. 10, where he: (1) quotes a 1901 statement by President Roosevelt to the effect that second-class mail was operating at an annual deficit of $107 million (at a time when total *federal* outlays were only $525 million); (2) reports that "[f]ollowing a detailed and exacting study of all 1908 postal costs, the Hughes Commission found that 42.4 percent of second-class costs were for transportation"; and (3) based on PRC Library Reference 9 in Docket No. R2001-1, calculates that transportation costs "are now approximately 14.3 percent of Periodicals costs, and only about two-thirds of those are distance-related."

Response of Witness Gordon to ABM/TW et al.-T3-38

ABM/TW et al.-T3-38. Did your source for the statement that the transportation component has fallen from more than forty-four percent to less than fifteen percent also inform you of how much of that drop can be attributed to additional printing at multiple plants, how much was attributable to more drop shipping, how much was attributable to use of lower cost transportation by the Postal Service and how much was attributable to other factors? If so, or if you have obtained that information from another source, please provide that information and its source.

Response

No.

Response of Witness Gordon to ABM/TW et al.-T3-39

ABM/TW et al.-T3-39. How many Periodicals are in the United States mail?

Response

I do not know.

Response of Witness Gordon to ABM/TW et al.-T3-40

ABM/TW et al.-T3-40. How many Periodicals in the United States mail are printed at more than one printing plant?

Response

I do not know.

Response of Witness Gordon to ABM/TW et al.-T3-41

ABM/TW et al.-T3-41. How many publications in the United States mail with a total print run of less than 1,000,000 are printed at more than one printing plant?

Response

I do not know.

Response of Witness Gordon to ABM/TW et al.-T3-43

ABM/TW et al.-T3-43. If a publisher could lower its combined costs of postage and private transportation by printing at more than one plant, what considerations would lead that publisher to print at only one plant?

Response

I do not know.

Response of Witness Gordon to ABM/TW et al.-T3-44

ABM/TW et al.-T3-44. Do you know what costs must be duplicated if a publication is printed at more than one plant? If so, please identify them.

Response

The plates would have to be duplicated.

Response of Witness Gordon to ABM/TW et al.-T3-45

ABM/TW et al.-T3-45. You state at page 12, lines 8-9, that "it has become cheap to enter the news business." Isn't this statement directed more at the cost of distributing information, rather than at the cost of developing sophisticated and accurate editorial content?

Response

No. I believe that both costs have declined substantially in recent years.

Response of Witness Gordon to ABM/TW et al.-T3-46

ABM/TW et al.-T3-46. Has the "cheapness" of distributing information increased or decreased the need of businesses to distill and verify information that they receive?

Response

I believe that it has substantially decreased the cost and difficulty of distilling and verifying information and, for that reason, has increased the standard of performance that businesses must meet if they are to remain competitive.

Response of Witness Gordon to ABM/TW et al.-T3-47

ABM/TW et al.-T3-47. You testify at page 12, line 25, that it now takes five hours to travel from New York to Los Angeles. How is the speed of air travel relevant to the issues addressed in your testimony?

Response

The rate schedule set in 1917 was predicated on a country that was "three and a half days wide." The country today is only "five hours wide," so that the distance is effectively one-seventh as great and the nation much more integrated.

Response of Witness Gordon to ABM/TW et al.-T3-48

ABM/TW et al.-T3-48. At page 13, lines 4-5, you state unequivocally that "no matter how obscure or arcane the topic, there is an internet news group devoted to it and everyone interested in it can learn of new developments in seconds." Please identify an internet news group from which everyone interested can learn about the following topics, each of which is covered in depth by an American Business Media member publication: (a) commercial vehicle sourcing, (b) hotel management, (c) paperboard packaging, (d) spectroscopy, (e) urology, (f) engineered stone, (g) limousines, (h) injection molding, (i) commercial fishing, (j) urethane technology, (k) the kiosk business, (l) photonics (m) chain stores, (n) fertilizer technology, (o) medical practice in the federal government, (p) dairy herd management, (q) point of purchase marketing, and (r) private label merchandise.

Response

I do not know of any such newsgroups, which is not to say they do not exist.

Response of Witness Gordon to ABM/TW et al.-T3-49

ABM/TW et al.-T3-49. *Would it be prudent for an auto parts supplier to rely* equally on an internet news group and Automotive News for information about the auto industry?

Response

I have no opinion on whether an auto parts supplier should rely equally upon "an internet news group" and *Automotive News*. However, if the question is rephrased to ask if an auto parts supplier should rely equally on *the internet* and the magazine, the answer is unequivocally yes.

Response of Witness Gordon to ABM/TW et al.-T3-50

ABM/TW et al.-T3-50. Would it be prudent for a fire chief to rely equally on an internet news group and Fire Engineering for information on the latest in fire fighting equipment and techniques?

Response

See my response to ABM/TW et al.-T3-49.

Response of Witness Gordon to ABM/TW et al.-T3-51

ABM/TW et al.-T3-51. Would it be prudent for a physician to rely equally upon an internet news group and Mayo Clinic Proceedings, or Contemporary Pediatrics, or the New England Journal of Medicine for accurate medical information?

Response

See my response to ABM/TW et al.-T3-49.

Responses of Witness Gordon NNA/TW et al.-T3-2

NNA/TW et al T3-2 Do you believe Congress established uniform postal rates for magazines in whole or in part to establish a common culture across the American frontier?

RESPONSE

A common culture was certainly a major part of the goal to "bind the nation together."

CORRECTED 7/12/04

Responses of Witness Gordon NNA/TW et al.-T3-6

NNA/TW et al T3-6 *Do you believe each new medium developed in America has* displaced the media that preceded it? For example, did radio make magazines less important to the public? Please explain your response.

RESPONSE

I do not so believe. Each new medium caused the previous media to evolve in new ways, not to go extinct.

Responses of Witness Gordon NNA/TW et al.-T3-9

NNA/TW et al T3-9 Do you believe the Internet will displace all magazines within any time frame described in NNA/TW et al T3-8?

RESPONSE

No, I do not so believe.

Responses of Witness Gordon NNA/TW et al.-T3-10

NNA/TW et al T3-10 Do you believe the Internet will displace all newspapers within any time frame described in NNA/TW et al T3-8?

RESPONSE

No, I do not so believe.

Responses of Witness Gordon NNA/TW et al.-T3-11

NNA/TW et al T3-11 Have you conducted any studies or research or written any articles or books about the economic viability of Internet publications that do not depend upon print media in any way for sharing of fixed costs, sharing of content or sharing or marketing expenses? If so, please provide copies.

RESPONSE

No I have not.

Responses of Witness Gordon NNA/TW et al.-T3-12

NNA/TW et al T3-12 Do you believe the Postal Service has no role in "binding the nation together" with *information published in newspapers or magazines*

a. Today?
b. Next year?
c. In any time frame described in NNA/TW et al T3-8
d. Following implementation of any rates adopted as a result of this case?

RESPONSE

I believe the United States to be one of the most socially and culturally cohesive countries in the world and that, therefore, efforts by the Post Office to foster such cohesiveness are, at this point in our history, largely superfluous and economically unjustifiable.

Response of Witness Gordon to USPS/TW et al.-T3-1

USPS/TW et al.-T3-1. Have you testified previously as a witness on behalf of any party in any regulated industry? *If your response is yes, please provide the dates,* subject of your testimonies, parties you represented, and the entity before which you appeared.

RESPONSE

No.

Response of Witness Gordon to USPS/TW et al.-T3-2

USPS/TW et al.-T3-2. On page 13, lines 9-12 of your testimony, you state, "[t]here is no longer the slightest chance that setting postal rates for editorial content in Periodicals class mail by zones to reflect actual costs would cause the country to be divided by these zones." When did you first hear of, or become aware of, the concept of zoning of Periodicals rates for editorial content, in the postal ratemaking context? Please describe the circumstances as you remember them.

RESPONSE

I became aware of postal zones for periodicals in the spring of 2004, in consultation with James O'Brien of Time Warner.

Response of Witness Gordon to USPS/TW et al.-T3-3

USPS/TW et al.-T3-3.
(a) Do you agree that your testimony describes the impact that rotary presses, electricity, the telegraph, the telephone, printing technologies, the radio, the television, satellite technology, transistors, microprocessors, computers, personal computers, and the internet have all had on the American "neighborhood's" ability to communicate with each other? If not, please explain.
(b) Of the changes described in your testimony, please confirm that, as of today, the one technology that had the greatest impact on your "zoned editorial" conclusion (expressed on page 13, lines 9-12) is the use of personal computers and laptop computers to access the internet. If not confirmed, please explain.

RESPONSE

a) I agree.

b) All the technologies mentioned have had a major impact on communication.

Undoubtedly, computers and the Internet will have, in the fullness of time, the greatest impact, but the technology has not yet reached maturity or saturation, although the latter is happening rapidly.

Response of Witness Gordon to USPS/TW et al.-T3-4

USPS/TW et al.-T3-4. On page 4, line 27, through page 5, line 4 of your testimony, you state, "[t]hus it made sense for the Congress, in formulating the Post Office's mandate to hold this vast, sprawling country together by facilitating the distribution of printed matter, to set uniform postal rates for magazines, regardless of where they were printed or where they were sent, in 1876 and to maintain uniform rates for editorial matter when it zoned the rates for advertising matter in 1917." On page 12 lines 22-23 of your testimony, you state, "[w]ith the addition of Hawaii and Alaska, the United States, geographically, is far larger and more far-flung than it was in 1917."
(a) Are there any areas in this far-flung country where internet service/access is not available, is available to a limited extent, is of poor quality, and/or is cost prohibitive? If so, where?
(b) Are there any subsets of the population, demographically speaking, for which computer ownership and/or internet access is cost prohibitive? If so, please describe the affected groups.

RESPONSE

a) I am not aware of any such areas.

b) Few people today cannot afford a computer and nearly all libraries provide internet access at little or no cost.

Response of Witness Gordon to USPS/TW et al.-T3-5

USPS/TW et al.-T3-5. Have you conducted any market research studies, or are you aware of any such studies, that have measured consumer preferences for accessing publications online versus reading them in hardcopy form? If so, what were the conclusions of those studies?

RESPONSE

I am not competent to conduct market research studies, nor do I know of any on this subject.

Response of Witness Gordon to USPS/TW et al.-T3-6

USPS/TW et al.-T3-6. An August 2000 U.S. Census Bureau study can be accessed at the following website: http://www.census.gov/prod/2001pubs/p23-207.pdf. On page 2 of the study referenced above there is a heading entitled "[h]igh Income households are more likely to have computers or Internet access." Do you agree with this statement? If not, please explain why not.

RESPONSE

I agree with the statement.

Response of Witness Gordon to USPS/TW et al.-T3-7

USPS/TW et al.-T3-7. The Postal Service publishes a survey that it conducts each year, referred to as the Household Diary Study. A copy of the 2000 Household Diary Study was filed as a library reference in Docket No. R2001-1, and can be accessed at the following Postal Rate Commission website address: http://www.prc.gov/docs/27/27167/USPS-LR-J-104.pdf. Page 41 of the 2000 Household Diary Study states: "[i]ncome would seem to influence volumes since periodicals are typically received through a paid subscription (55 percent in 2000). Figure 5.1 shows that as income increases, Periodicals Volumes increase." Do you agree with this statement that as household income increases, the number of periodicals received per household per week increases? If not, please explain why.

RESPONSE

I do not have the knowledge that would allow me to agree or disagree with the statement.

Response of Witness Gordon to USPS/TW et al.-T3-8

USPS/TW et al.-T3-8. Throughout your testimony you describe how communications technologies have changed to an extent such that the United States has become "one vast neighborhood." On page 11 lines 21-22 of your testimony you state, "Thus magazines that could once only be delivered by mail, can now be delivered electronically at very little cost." If high income households are more likely to have computers and internet access, why do they also receive more periodicals in the mail than low income households, when a greater proportion of high income households could, at least in some cases, access those publications online?

RESPONSE

Your question seems to assume that high-income household do not receive more periodicals that are not currently available online than low-income households. I don't know of any reason to make that assumption. Putting that aside, I assume that many individuals have not yet adjusted or are in the process of adjusting to accessing periodicals online, and that many are only now discovering the online availability of periodicals to which they already have a mail subscription. Some, presumably, prefer to receive both forms, since there are places, such as beaches and bathtubs, where receiving a periodical in electronic form would be inconvenient at best. Some, of course, may simply prefer hard copy form.

Response of Witness Gordon to USPS/TW et al.-T3-9

USPS/TW et al.-T3-9. Are there types of publications which consumers are more likely to access online (assuming they are available) and types of publications which consumers would prefer to receive in hardcopy? If so, please describe the types of publications that consumers would prefer in each instance.

RESPONSE

Publications whose information is extremely time-sensitive would be better

distributed over the Internet. Otherwise I have no opinion.

Response of Witness Gordon to USPS/TW et al.-T3-10

USPS/TW et al.-T3-10. For publications that offer online alternatives, do the online editions of those publications offer 100 percent of the information that is in the hardcopy publication? If not, please estimate the percentage of the hardcopy information that is generally available in online editions of an average publication?

RESPONSE

I have no basis on which to generalize or offer percentages. I do know that some publications--such as The Wall Street Journal, The New Republic, National Review, and the Weekly Standard--provide more information in their online than in their hardcopy versions.

Response of Witness Gordon to USPS/TW et al.-T3-13

USPS/TW et al.-T3-13. Please confirm that the there are situations in which consumers are away from home and/or their computers, so that reading the online versions of publications is not possible, or is undesirable (e.g., commuting to work on mass transit, waiting for appointments, etc.). If not confirmed, please explain.

RESPONSE

I so confirm.

1 CHAIRMAN OMAS: Is there any additional
2 written cross-examination for Witness Gordon?
3 (No response.)
4 CHAIRMAN OMAS: This brings us to oral
5 cross-examination. Three parties have requested oral
6 cross-examination, American Business Media, McGraw-
7 Hill Companies and the National Newspaper Association.
8 Is there any other parties who wish or would
9 like to cross-examine Witness Gordon?
10 (No response.)
11 CHAIRMAN OMAS: Mr. Straus?
12 MR. STRAUS: Thank you.
13 CROSS-EXAMINATION
14 BY MR. STRAUS:
15 Q I introduced myself informally, Mr. Gordon,
16 but, for the record, I'm David Straus representing
17 American Business Media.
18 Let me ask you if you agree with the
19 following statement. "The educational, cultural,
20 scientific and informational value that periodical
21 publications provide today is no less than when
22 Section 3622(b)(8) was enacted in 1976."
23 A No. It's the same, I would think.
24 Q You agree with that statement?
25 A I agree with that.

1 Q When were you first contacted about
2 testifying in this case?
3 A Very late last year, I believe, or early in
4 January.
5 Q And what was your assignment at that time?
6 A It was to write a piece on the history of
7 communications technology and how it has changed over
8 the century or since 1917 basically.
9 Q That was it? Just how communications have
10 changed? Nothing about the flat editorial pound rate?
11 A I'm sorry? Say that again.
12 Q You weren't asked to say anything about
13 postage rates?
14 A No. It was mostly about the history of
15 communications and how they had changed. I mean, I'm
16 not an expert on postal rates.
17 Q Your testimony includes, for example, a
18 statement about why the percentage of costs
19 attributable to periodicals that are represented by
20 transportation --
21 MR. KEEGAN: Mr. Chairman, if Mr. Straus is
22 going to quote the testimony, I would appreciate it if
23 he could provide a reference.
24 CHAIRMAN OMAS: Mr. Straus?
25 MR. STRAUS: Sure. Page 10 of your

1 testimony, Lines 15 to 17.

2 BY MR. STRAUS:

3 Q There's a sentence there about the

4 percentage of costs attributable to periodicals that

5 are attributed to transportation. That has nothing to

6 do with change in communications, does it?

7 A Certainly it does because the cost of

8 communication is an important part of communication.

9 I mean, if it costs you $1,000 to make a phone call

10 across the Atlantic, you're probably not going to do

11 it.

12 Q You're not there talking about the overall

13 level of postage rates. You're talking about a

14 particular component of postage rates. The mailer

15 pays the rates rather than components, doesn't he?

16 A Well, yes.

17 Q We'll go on.

18 CHAIRMAN OMAS: Excuse me, Mr. Gordon. Will

19 you please pull the mike a little closer and talk a

20 little louder? Thank you.

21 BY MR. STRAUS:

22 Q Have you read the interrogatory responses of

23 the other Time Warner, et al. witnesses?

24 A No, I have not.

25 Q Sitting here today, do you have an opinion

1 on whether the educational, cultural, scientific and
2 informational value of periodicals justifies a rate
3 preference for periodicals?
4 A No. That is beyond my field of expertise.
5 Q Do you have an understanding of why others
6 have thought that the ESCI value should lead to a rate
7 preference?
8 A Yes.
9 Q And what is that understanding?
10 A According to what they said in 1917, that
11 this helped bind the nation together intellectually
12 and culturally. Therefore, it is a social good that
13 should be encouraged.
14 Q Is it your understanding that it is at least
15 in large part because of ESCI value that a periodical
16 pays lower rates than a catalog?
17 A I would believe so, yes.
18 Q A good deal of your testimony goes to
19 presenting your belief that let's say a good deal of
20 the information in periodicals is available on the
21 internet. Is that right?
22 A That's correct.
23 Q And would that same thing be true for
24 catalogs?
25 A Yes, I believe so.

1 Q Getting back to your explanation of why
2 others believe that ESCI value should lead to a lower
3 rate preference for periodicals, do you disagree with
4 that rationale?
5 A No.
6 Q You don't believe that it's superfluous and
7 unjustifiable for periodicals to enjoy lower rates
8 because they have editorial content?
9 A I think it is far less necessary now. I
10 think I'm not at all sure that it accomplishes or
11 helps to accomplish in any significant way the object.
12 Q Well, I think you just told me two things.
13 You said you don't think it's superfluous and
14 unjustifiable, but then I think you went on to say
15 that it's pretty much superfluous and unjustifiable.
16 Let me ask you again. Is a rate preference
17 for periodicals based on ESCI value superfluous and
18 unjustifiable?
19 A I think, yes, a rate preference is. I think
20 the object of binding the nation together
21 intellectually and culturally is a great social good.
22 Q But the rate preference for periodicals
23 doesn't contribute to that good?
24 A Not any more I don't think.
25 Q In response to American Business Media

1 Question 3, if you could turn to that please? We're
2 going to be going through a lot of these responses, so
3 I'll try to give you a heads up so you know where I
4 am.
5 There you gave us a list of the periodicals
6 that you read on a regular basis. Do you happen to
7 know how many of those have websites?
8 A No, I don't, but I would imagine most of
9 them except the very small genealogical magazines.
10 Q Do you visit those websites on a regular
11 basis?
12 A No, I don't. On an irregular basis, yes.
13 Q Why not?
14 A I find it unnecessary. I mean, I know where
15 they are. I have many of them in my list that I can
16 call up very quickly.
17 Q How many of these publications that you list
18 have content that's comprehensively covered in a
19 television show?
20 A A television show?
21 Q Yes.
22 A Are covered in a television show?
23 Q Yes. How many of these publications that
24 you read regularly have content that you can regularly
25 obtain on a television show?

1 A Not many of them, or none of them.
2 Q Why do you read *Publisher's Weekly*?
3 A I'm an author. It's a very important
4 magazine. I don't read it on a regular basis, but,
5 you know, they review my books, and I have a weakness
6 for reading those reviews.
7 Q What's the nature of the content of
8 *Publisher's Weekly*?
9 A Mostly of books that are coming out in the
10 next season or in the next few months.
11 Q Does it have a website?
12 A I'm sure it does. I've never been to it.
13 Q You've never been to its website?
14 A Not to *Publisher's Weekly*, no. You may have
15 to subscribe to it. I just don't know.
16 Q I'm going to hand you a copy of -- and I'm
17 sorry; I only have one copy -- the home page from
18 *Publisher's Weekly's* website that was printed out on
19 7-11-04.
20 Can you tell from that page, and I direct
21 your attention to the upper right, whether access to
22 the full content of the website requires a
23 subscription?
24 A So it seems to say. It's cut off on the
25 right, but you must be a sub -- to *Publisher's Weekly*.

1 Q Is that a pretty common restriction on
2 websites that duplicate or are in conjunction with
3 periodicals?
4 A I have no idea.
5 Q Do you read *Editor & Publisher*?
6 A No.
7 Q Why?
8 A I just don't find it necessary.
9 Q What's the *Curcas Review*?
10 A It also reviews books. I think it's mainly
11 used by libraries. It's much tougher than *Publisher's*
12 *Weekly* on authors.
13 Q Why do you read *Curcas Review*?
14 A Again, they review my books.
15 Q Are the reviewers whose reviews appear in
16 *Curcas Review* paid by authors or by publishers to
17 provide their opinions?
18 A I'd love to be able to pay a reviewer. No.
19 They're paid by *Curcas*, I assume. They're usually not
20 paid by publishers or authors.
21 Q Then you have some degree of confidence in
22 the integrity of *Curcas Review* that it's not going to
23 accept money for a favorable review?
24 A Oh, yes.
25 Q Have you ever read book reviews on

1 amazon.com?

2 A Yes.

3 Q Do you have the same degree of confidence

4 that the reviewers on amazon.com are totally

5 impartial?

6 A No, nowhere close to it.

7 Q And they're not nearly as well-qualified

8 either, are they?

9 A Well, we often don't know who they are.

10 Q I mean, it's not unknown for authors to

11 review their own books, and usually favorably?

12 A Or in my case the author's father.

13 Q Or the author's father.

14 We asked you in Question 7 -- well, let me

15 back up one step. In answer to Question 6, you say

16 that you've never read even occasionally any of the

17 thousand or more American Business Media publications

18 that were identified for you.

19 In Question No. 7 we asked you whether you

20 read any specialized publications even once before

21 April 26, and you said none that you remember. Have

22 you read any since then?

23 A No.

24 Q So it's fair to say then, isn't it, that

25 your opinion about the value and purpose and functions

1 that are served by specialized business publications
2 has been reached without reading a single one of them?
3 A Yes.
4 Q We asked you some questions about your
5 website. You recall those I'm sure. As of this
6 spring, according to your responses, you were advising
7 visitors on your website of what you called "upcoming
8 events," but all of them were at least six months old.
9 Isn't that right?
10 A That's correct.
11 Q Do you publish a hard copy newsletter of any
12 kind with the same type of information?
13 A No.
14 Q You do have events scheduled the remainder
15 of this year, do you not?
16 A Yes. I have a new book coming out in
17 October, so there will be a lot of them.
18 Q But your website hasn't been changed since
19 we first asked you about it, has it?
20 A No.
21 Q So your website still lists dates in July
22 without a year, so a reader could think that those
23 dates are referring to this July rather than last
24 July. Isn't that right?
25 A Yes. I have to confess, that is the case.

1 It is largely because I just have been finishing this
2 book, and dealing with the website and dealing with
3 the man who deals with the website drives me up a
4 wall.
5 Q And dealing with people like me who ask
6 you --
7 A No, no. You speak English. People who
8 design websites do not.
9 Q If the demand by your readers for
10 information about your upcoming appearances were
11 sufficient to justify your producing a monthly
12 newsletter that you sent to them by mail and you had
13 produced one in April of 2004 and had to send it out
14 to everybody, do you suppose you would have listed
15 last year's events, or would you have listed
16 accurately upcoming events?
17 A Certainly I would have accurately listed the
18 upcoming events. There wouldn't be much point to a
19 newsletter that told you about what happened last
20 year.
21 Q So someone who received that newsletter
22 would have been able to have a good deal of confidence
23 that the information is accurate?
24 A Yes.
25 Q But anyone who had such confidence in your

1 website would have had that confidence misplaced,
2 wouldn't they?
3 A That is correct. Many websites are dated.
4 This one does not happen to be. I think it's a good
5 idea to now when I do get around to revising it later
6 this summer it will have a date as to when this latest
7 revision was.
8 Q I don't want to beat a dead horse here, but
9 in your response to Question 19 you say that the
10 internet often provides immediate access to parallel,
11 redundant or competing sources of the same
12 information.
13 If I were to go to your website today and
14 figure out that those dates were a year old and I
15 wanted to go someplace else on the internet to find
16 that same information, would I be able to?
17 A Yes. Harper-Collins has a -- you can go to
18 I forget what it's called, Author Tracker or something
19 like that, that would bring it up to date.
20 Q Including your radio appearances and TV
21 appearances and the like?
22 A Yes.
23 Q In response to Question 19 again, you say
24 it's usually easier in the case of internet sources
25 than printed ones to discover the identity "and of"

1 the source's sponsor. I think you mean the identify
2 of the source's sponsor.
3 A Identity of.
4 Q Do you know what type of information is
5 found in the masthead of a periodical?
6 A Yes.
7 Q Is there any information there that tells
8 you who produces that periodical, the publisher?
9 A Yes. I mean, it gives the author, the
10 editors and the publishers and what have you.
11 Q Would your statement then not be true for
12 periodicals in terms of identifying the source's
13 sponsor?
14 A I think what I meant here was that it's
15 often very easy on the internet. They will give you
16 the source of the information so that you can check it
17 yourself, you know, the equivalent of a footnote.
18 Footnotes are very rare in magazines.
19 Q But that source could well be a periodical,
20 and you have the original source itself when you have
21 the periodical.
22 A Well, no, because if the periodical says
23 that two plus two equals six and it doesn't give you a
24 source for that where the reporter got the
25 information.

1 Q The website. I mean, if the website tells
2 you they got the information from the *New England*
3 *Journal of Medicine*, they don't tell you where the *New*
4 *England Journal of Medicine* got the information, do
5 they?
6 A No, but then you go to the *New England*
7 *Journal of Medicine*, and that being very scholarly
8 would give you that information.
9 Q But I still don't understand why it's easier
10 in the case of an internet source than a printed
11 source to identify the sponsor of the information.
12 A Because the *New England Journal of Medicine*,
13 I think, scholarly publications such as that, do give
14 very rigorous sources. Newspapers and magazines, you
15 know, of a popular nature usually do not.
16 Q Consumer magazines?
17 A Consumer magazines.
18 Q As a general proposition, is it easier and
19 less expensive to create a website or to create a
20 periodical?
21 A I believe it's much cheaper to create a
22 website. I've never tried to create a periodical.
23 People who are more talented at computers than I am
24 can create websites by themselves.
25 Q So it's pretty easy to throw pretty much any

1 kind of information up on the web?

2 A Sure, but also you can throw up any kind of

3 information in a periodical.

4 Q You have to have readers and advertisers in

5 most of them, don't you?

6 A You don't have to have the readers.

7 Q What are you going to do with it?

8 A What?

9 Q What are you going to do with it after you

10 print it?

11 A Well, you hope you have readers, but you

12 don't need the readers to produce it.

13 Q Is it your testimony and belief that because

14 of television and the internet periodicals are less

15 important today in terms of binding the nation

16 together than they once were?

17 A Yes.

18 Q Are periodicals no longer necessary for that

19 purpose?

20 A I didn't say that. I said they were less

21 important. They used to be the totality of means of

22 binding the nation together by information. They now

23 no longer are.

24 Q I hope you'll excuse my phrase here because

25 I don't know a better way to say it, but if there were

1 no periodicals would the nation be less bound together
2 than it is now?
3 A I suppose so, but not by a significant
4 matter. I mean, that's a theoretical question because
5 it's not likely to happen.
6 Q If you didn't like that theoretical, then
7 wait until the next one.
8 A Okay.
9 Q Let's assume that the cost of sending
10 periodicals to Alaska and Hawaii were prohibitive, and
11 publishers just didn't do it. Nobody would be willing
12 to pay the price of the periodical living in Alaska or
13 Hawaii.
14 If that were the case, would the residents
15 of Alaska and Hawaii be less integrated into the
16 fabric of the country than they are today?
17 A Only marginally I think because most
18 periodicals, certainly most major periodicals, have
19 websites. I mean, you can subscribe to the website of
20 the *Wall Street Journal* for less than you can
21 subscribe to the paper of the *Wall Street Journal*.
22 If for some reason it became prohibitive for
23 the *Wall Street Journal* to send the paper to Juneau,
24 the man in Juneau could subscribe to the *Wall Street*
25 *Journal* on line and read the entire paper every

1 morning even when it's too snowy for the paper to be
2 delivered.
3 Q Do all periodical related websites contain
4 all of the content of the parent periodical?
5 A I would not know that. I would imagine not,
6 but the major ones I believe do.
7 Q All of the content?
8 A I believe. Certainly in the case of the
9 *Wall Street Journal* it does. I don't think it has the
10 ads. I don't know because I usually read it in the
11 paper copy.
12 Q You've never read any specialized business
13 periodicals. You've never looked at any websites of
14 specialized business periodicals?
15 A No.
16 Q So you're saying then if *Soap Opera Digest*
17 and *Penthouse Magazine* couldn't find their way to
18 Alaska and Hawaii, that wouldn't be a concern to you?
19 A I think the public would survive it.
20 Q And if a firefighting magazine or a building
21 maintenance magazine or if *Editor & Publisher* couldn't
22 make their way to those states, that wouldn't matter
23 either?
24 A It would matter more than *Penthouse*.
25 Q But not much?

1 A I couldn't qualify if.
2 Q I think you already did.
3 I'm going to talk about the printing
4 business a bit because you do in your testimony. We
5 asked you about your knowledge and experience in the
6 periodical printing business.
7 You said you have no experience, but you
8 have the knowledge of an informed layman. I'm trying
9 to find out what the limits of that are.
10 What types of presses are used to print a
11 typical glossy magazine?
12 A I have no idea what the current ones are.
13 Q Are the same kinds of presses used for say a
14 four million press run as for a 40,000 press run?
15 A I don't know.
16 Q Specifically what changes have been made in
17 the printing industry to allow magazines to be printed
18 at more than one plant economically?
19 A Well, it's now very easy to transmit in
20 effect the plates. I mean, the information is then
21 turned into the plates and the plates can be made much
22 more cheaply than they could like in 1917 when it was
23 all hot metal.
24 Q What costs would still have to be duplicated
25 for printing at multiple plants?

1 A I mean, to the extent that I know it's the
2 press time and the setup would have to be duplicated,
3 but then --
4 Q The press time wouldn't be duplicated, would
5 it?
6 A No, but the setup would have to be
7 duplicated.
8 Q Does the term "make ready" mean anything to
9 you with respect to the printing business?
10 A No.
11 Q When you testified in your prepared
12 testimony that magazines can be printed in more than
13 one location, what was your understanding of the
14 extent to which they are?
15 A I know that some magazines and newspapers
16 are printed in more than one location.
17 Q My question was magazines.
18 A Magazines. I just know that some of them
19 are.
20 Q You knew that before you submitted your
21 testimony?
22 A Yes.
23 Q Which ones did you know are?
24 A Well, *Time* for instance.
25 Q Do you know how many magazines there are in

1 the country?

2 A Total number? No. I have no idea.

3 Q Do you know how many are printed at more

4 than one plant?

5 A No.

6 Q Have you looked at Mr. Stralberg's response

7 to American Business Media Question 42, which --

8 A No.

9 Q Well, it was redirected from you. You

10 redirected it to him.

11 A You'd have to tell me which one it is so

12 that I can --

13 Q It was Question 42 to you that was

14 redirected to Mr. Stralberg. It had to do with this

15 very question of the number of periodicals that are in

16 fact printed at multiple plants.

17 My question is have you taken a look at that

18 response?

19 A No, I have not.

20 Q Why couldn't you answer this question?

21 A Because I wouldn't have the faintest idea as

22 to what the total press run and number of printing

23 plants for each publication would be.

24 Q Do you have Mr. Stralberg's answer there?

25 A I'm not sure I ever saw it.

1 Q I'll show it to you.

2 A Wait. I have seen this.

3 Q Isn't it pretty apparent that he didn't have

4 the information and that he went and obtained it from

5 the Complainant?

6 MR. KEEGAN: Mr. Chairman, could the witness

7 have a moment to look over the answer?

8 MR. STRAUS: Sure.

9 MR. KEEGAN: And could you tell me again

10 what number it is?

11 MR. STRAUS: It was 42 to Gordon, redirected

12 to Stralberg.

13 (Pause.)

14 THE WITNESS: Well, it says the information

15 was provided to me, so I --

16 BY MR. STRAUS:

17 Q Well, it could have been provided to you as

18 well?

19 A It could have.

20 Q Do you see from his answer there how many

21 periodicals from the Complainants are printed at more

22 than one plant?

23 A Yes, I see them.

24 Q And how many are there?

25 A One, two, three, four, five, six.

1 Q Do you have any explanation for why if it's
2 economical to print at multiple plants only six out of
3 the 83 publications on that list are printed at
4 multiple plants?
5 A Well, it might be economical, or they might
6 have other reasons for not choosing to do so.
7 I mean, there often is what in economics is
8 called an installed base problem, and it's cheaper to
9 continue doing what you're doing rather than move to a
10 new technology or to a different technology up until
11 the old technology wears out.
12 I mean, if you've already paid for a press
13 there's no point in buying a new, better press until
14 that old one wears out, unless the new one is really
15 better and cheaper.
16 Q Are you suggesting that to print at multiple
17 plants would require the purchase of a new press?
18 A No, no. That was just an example. I'm just
19 saying that sometimes there is an installed base, and
20 there also is an inertia. People don't change the way
21 they're doing things unless there's a powerful reason
22 to do so.
23 Q If you can save a lot of money you might
24 want to do it, wouldn't you?
25 A Well, that would be a powerful reason to

1 overcome the inertia.

2 Q Let's take a look at one of the periodicals

3 that are actually published by the Complainants and

4 printed at a single printing.

5 Let me back up one second. Is there any

6 particular characteristic of those six that are

7 printed at multiple plants? Aren't they all weeklies?

8 A Yes, I believe so.

9 Q Don't you suppose then that maybe the

10 multiple printing plants have something to do with

11 avoiding time in transit rather than avoiding cost?

12 A It might.

13 Q *Vanity Fair* magazine prints a million and a

14 half copies -- you won't find it there -- and weighs

15 1.84 pounds. These are data taken from others of Mr.

16 Stralberg's responses. Just accept those for the

17 purpose of the question.

18 A million and a half copies, 1.84 pounds. A

19 very small portion -- that is, less than five percent

20 -- go to Zones 3 through 8, which means that Conde

21 Nast is dropshipping *Vanity Fair* magazine, so it's

22 paying to ship almost all of the copies weighing

23 nearly two pounds and has a million and a half copies.

24 We're talking about almost three million

25 pounds that they're paying to ship, rather than print

1 in multiple printing plants and avoid that shipping
2 expense. Does that tell you anything about whether or
3 not your theory is correct about being economical to
4 print at multiple plants?
5 A I would have to examine that in more depth
6 I'm afraid. It might. I understand what you're
7 getting at, but whether that's true or not I simply
8 have no idea at this point.
9 Q Please look at your answer to Question 32.
10 A Okay.
11 Q Is it fair to conclude from your response
12 that to the extent cable TV provides a reasonable
13 substitute for specialty magazines, it substitutes for
14 consumer magazines and not business publications?
15 A Certainly in the main, yes. Cable TV does
16 not provide a substitute for specific business
17 magazines.
18 Q In Question 33 we asked you if you could
19 identify a television channel or a TV show that covers
20 the subjects that are covered by one medium-sized
21 American Business Media member, and those subjects
22 were the beverage industry, the fuel oil industry,
23 irrigation systems, medical equipment design, outdoor
24 power equipment and specialty coffees.
25 Do you know whether any websites provide the

1 same type of in-depth information on these industries?
2 A I believe there are for some of them, yes,
3 but I do not know precisely.
4 Q How would you go about finding a website,
5 for example, on the beverage industry?
6 A You could Google for it.
7 Q And you would Google beverage?
8 A Sure. You'd get several thousand responses
9 very quickly.
10 Q How would you narrow those down so that you
11 could get the kind of reporting and editorial content
12 about the beverage industry that you would get in a
13 periodical devoted to the beverage industry?
14 A Well, for instance, *Automotive News*. If you
15 Google for it, you get -- what was it. Yes. In .15
16 of a second we got 532,000 hits, and the number one
17 was the website of *Automotive News*.
18 Q Was there any other website that had the
19 same kind of information that *Automotive News* carries?
20 A I did not go through the 532,000 hits.
21 Q Did you find any? Did you look at any?
22 A I did not, no.
23 Q Do you know what *Automotive News* covers?
24 A Automotive news.
25 Q But is it the kind of automotive news you'd

1 find in *Car & Driver* and *Road & Track* and *Auto Week*
2 and *Automobile*, or is it a different kind of news
3 about the auto industry?
4 A I'm afraid I have no idea.
5 Q I'm going to ask you now some questions
6 about your testimony at page 10, Lines 15 to 17, where
7 we attributed to you the statement that use of
8 multiple printing plants has caused a drop in the
9 transportation component from more than 44 percent to
10 less than 15 percent.
11 Now, I believe you deflected the question by
12 talking about using a vague reference that a high
13 school English teacher of mine said never to do
14 because it leads to confusion, but you never actually
15 gave an answer to the question, so I'll ask you again.
16 What is the source of that statement?
17 A Do you know which question?
18 Q I'm sorry. Question 35.
19 A Question 35. Do you mean the original
20 source of the 44 percent to less than 15 percent?
21 Q No. The source for the entire statement
22 that's quoted there, the statement: "This has caused
23 a major reduction in the transportation component cost
24 of distributing periodicals class mail."
25 I'm not asking for yet where the 44 percent

1 and the 15 percent came from. I'm asking for the
2 source of the statement what the cause was of that
3 change from 44 to 15.
4 A I'm afraid I don't know off the top of my
5 head. I'd have to go back and find out, you know, and
6 go look at the equivalent of footnotes to find that
7 out.
8 Q Well, we asked you in Question 35 what the
9 source was, and now I'm asking you the same question
10 again. The first time you didn't answer it. This
11 time you say you can't answer it?
12 A I can't answer it now, no. I didn't make it
13 up.
14 Q We attributed to you the statement that
15 multiple printing plants is the cause of the
16 reduction, and in this response you say no, that
17 wasn't your intent. You intended the cause of the
18 reduction to be not only multiple printing plants, but
19 the previous paragraph, which you said begins on Line
20 6. I think you meant Line 5, for the record.
21 If we look at that testimony at page 10, the
22 other thought that you'd like to get into now would be
23 a double cause; would be not only multiple printing
24 plants, but also the revolution in non-printing
25 communications media.

1 Can you tell me how a revolution in non-
2 printing communications media can lead to a reduction
3 in the percentage of periodical cost attributed to
4 transportation?
5 A No.
6 Q In Answer 35 you say you intended to say
7 that that too contributed to the reduction, and now
8 you can't tell me why it does?
9 A I'm afraid I'd have to study this more. I
10 cannot give you an answer to that off the top of my
11 head.
12 Q Do you think that a major factor in the
13 decline in transportation cost as a percentage of
14 total periodical cost might have to do with more
15 dropshipping by the publisher?
16 A It sounds reasonable, yes.
17 Q If publishers do their own shipping then the
18 Postal Service pays less transportation, doesn't it?
19 A Right.
20 Q In response to Question 36 we asked you a
21 question about the completion of your testimony. When
22 was your testimony completed? Do you recall?
23 A April, I believe. April 26.
24 Q I think that's when it was filed.
25 A Okay. Then it was sometime in April.

1 Q Within a couple of days of that?
2 A I would assume so. I can't remember now.
3 Q The source of the information, the cost
4 data, you give in response to Question 37 as Witness
5 Mitchell testimony. Do you see that?
6 A Yes, I do.
7 Q So you actually read Mr. Mitchell's
8 testimony before you prepared yours?
9 A Not before I prepared mine, no.
10 Q How could the testimony have been the source
11 for information in your testimony if you hadn't read
12 it?
13 A I'm sorry. It was not in my original
14 testimony. "If you know the time period covered,
15 please provide it and identify the source." I'm
16 providing it here, and this is the source. I had
17 Mitchell's testimony when I wrote the response.
18 Q The question was the source of your 44
19 percent and 15 percent, and they're in your written
20 testimony. They're not in your response.
21 A It was provided to me by --
22 Q If your source was counsel, there's nothing
23 wrong with that.
24 A Counsel, yes. I mean, I didn't have a clue
25 as to the answer, and then he gave me the answer.

1 Q No, no. I'm talking about the source of the
2 44, the source of the information on page 10 of your
3 testimony about comparing 44 percent to 15 percent.
4 You wrote that in April.
5 A Right.
6 Q You hadn't read Mr. Mitchell's testimony
7 when you wrote it?
8 A Right.
9 Q But Mr. Mitchell's testimony was
10 nevertheless the source for those numbers?
11 A It was provided to me by counsel.
12 Q Can we correct the answer to No. 37 to say
13 that counsel was your source for the information?
14 A All right. No problem.
15 Q All right. Now, the numbers you used are 44
16 percent and 15 percent. I'm not concerned with small
17 deviations, but I am curious.
18 If you look at the information in the second
19 paragraph in the response to 37, you quote a 42.4
20 percent number there that the Hughes Commission found.
21 The Hughes Commission also found that if you included
22 other transportation the cost was 66 percent. That's
23 also in Mr. Mitchell's testimony.
24 The Hughes Commission had two numbers, 42.4
25 percent and 66 percent. You used 44 percent. Can you

1 tell me where the 44 came from?

2 A It came from counsel.

3 Q So you don't know why the 42.4 or the 66

4 became 44?

5 A No.

6 Q I assume that since you haven't read Mr.

7 Mitchell's testimony, the answer you don't know, but

8 I'm going to ask you anyway.

9 Did Mr. Mitchell indicate at all that the

10 reduction in the transportation cost had anything to

11 do with multiple printing plants?

12 A I don't know.

13 Q In response to Question 41, you indicated --

14 I'm sorry; I'll give you a minute -- that you didn't

15 know how many publications in the United States with a

16 total print run of less than a million are printed at

17 more than one printing plant.

18 Did you try to find out that answer from

19 counsel or from another witness or from any other

20 source?

21 A No.

22 Q Please look at your answer to Question 46.

23 We asked you whether what you said, the cheapness of

24 distributing information, has increased or decreased

25 the need of businesses to distill and verify

1 information.

2 I don't believe your answer answers the

3 question. You say that it is easier to verify, but

4 you haven't said whether it's more or less important

5 to verify. Can you supplement that answer at all?

6 A Well, I don't think the cheapness is related

7 to the need.

8 Q Well, the cheapness creates a lot more

9 information. I think we may disagree on some things,

10 but we agree that there's a whole lot more information

11 available on people's websites, on blogs, on internet

12 news groups. There's just more information.

13 A Yes.

14 Q And that's because of the cheapness. Is

15 that right?

16 A That is correct.

17 Q And if someone is faced now with many, many

18 sources, some of which you've already said may be

19 unreliable such as individual websites to which not as

20 much attention is paid, my question is doesn't that

21 make it more important than it used to be to verify

22 sources because it's so cheap to distribute the

23 information?

24 A No. I think the need was always there.

25 There's now more information and, therefore, there's

1 more information to be checked.

2 Q Do you think there's more bad information

3 than there used to be? Let me state it a better way

4 because I know what your answer would be.

5 If in the old days you had a newspaper and

6 that was it and now you have a newspaper and 4,800

7 websites, don't you think that the percentage of

8 information that's unreliable is greater today than it

9 used to be?

10 A No. I think it's actually lower because a

11 lot of those 4,800 websites would be riding herd on

12 the newspaper.

13 In fact, every major newspaper today there

14 are websites, you know, pointing out the newspapers'

15 sins of omission and commission. I'm sure the editors

16 of the *New York Times* are not happy about that.

17 Q Well, when the *New York Times* makes a

18 mistake they correct it, don't they?

19 A Sometimes.

20 Q People that have websites with incorrect

21 information don't always correct it, do they?

22 A That is also correct. We've found out the

23 disagreement is to what is correct and what is not

24 correct.

25 Q We asked you in Question 47, and I'll pause

1 while the witness turns there, why the speed of flying
2 cross-country is relevant to your testimony. You
3 answered the question as asked.
4 Let me ask you a better question. Is it
5 relevant to the question of whether periodical rates
6 should be zoned or unzoned or the impact of
7 information in periodicals on the country?
8 A I think so because in 1917 the country was,
9 you know, as they described it, a vast, sprawling
10 country, and now it is just as vast, but it is far
11 less sprawling.
12 Q Are you suggesting that people on airplanes
13 carry the information with them from coast to coast
14 and distribute it when they get there?
15 A I don't mean that in a literal sense, no.
16 Q But are periodicals carried on airplanes by
17 the Postal Service?
18 A That sounds like an expensive way to
19 distribute periodicals, but I don't know.
20 Trucks move an awful lot faster now than
21 they did in 1917. In 1917, they didn't move over long
22 distances at all. Railroads did most of the --
23 Q Please look at the response to Question 48.
24 There I guess it's fair to say we're challenging your
25 statement that no matter how obscure or arcane the

1 topic, there's an internet news group devoted to it,
2 and everyone interested in it can learn of new
3 developments in seconds.
4 We asked you to identify internet news
5 groups that cover certain subjects covered by American
6 Business Media members like commercial vehicle
7 sourcing, paperboard packaging -- I'm skipping some --
8 spectroscopy, commercial fishing, kiosk business,
9 photonics, chain stores, dairy herd managements, and
10 we asked you to identify news groups for those.
11 You said you don't know of any, which is not
12 to say they do not exist. Did you try to find some?
13 A No, I did not.
14 Q Even though, as you said, it would only take
15 seconds to do so?
16 A Well, news groups don't often take more than
17 a second to find. You have to get the whole list of
18 them, and then it takes forever to scroll through
19 them. I don't believe you can Google for news groups.
20 Q So I've come up with some topics that are
21 really so obscure or arcane that you cannot find out
22 about them in seconds?
23 A I didn't try.
24 Q But you don't think you could?
25 A I don't think so, but who knows. I mean,

1 there are news groups for just about everything.
2 Q When we asked you about these subjects and
3 if they could be found in seconds, I would have hoped
4 you would have come up with a few.
5 A I don't think they could be found in
6 seconds. As I said, I know news groups are not so
7 easily found. As I said, you can't Google for them.
8 Q Please look at your response to 49 where we
9 ask you whether it would be prudent for an auto parts
10 supplier to rely equally on an internet news group and
11 on *Automotive News* for information about the auto
12 industry.
13 Your response is that people should rely
14 equally on the two. Is that right?
15 A No. I said equally if you rephrase it to
16 say on the internet, not on the internet news groups.
17 Q And you can say that categorically, without
18 ever having read *Automotive News*, that someone should
19 rely equally on the internet and on *Automotive News*?
20 A It's their website
21 Q Let's exclude *Automotive News'* own website
22 for a moment. How about other websites?
23 A Well, Google came up with 532,000 hits, and
24 I cannot testify as to the reliability of the other --
25 Q If you can't, then how can you testify that

1 people should rely equally on those 535,000 and on
2 *Automotive News* magazine?
3 A I didn't say that.
4 Q I'm quoting. "However, if the question is
5 rephrased to ask if an auto parts supplier should rely
6 equally on the internet and the magazine, the answer
7 is unequivocally yes."
8 So that answer depends upon *Automotive News*
9 having its own website?
10 A Not necessarily. I mean, you'd have to
11 examine the website, and any particular one you would
12 have to make up your own mind as to its reliability,
13 but can you rely on information derived from the
14 internet as much as you can from *Automotive News*? I
15 think the answer to that is yes.
16 Q Do you know anything about the reputation of
17 *Automotive News* and the auto industry?
18 A No. I have no idea whatever.
19 Q Would it matter to your answer to this
20 question?
21 A No, I don't think so.
22 Q So even if in the auto industry *Automotive*
23 *News* was perceived as by far the single best source of
24 information in the automobile industry, you'd still
25 say that people should rely equally on the internet?

1 A I said they can rely equally on the internet
2 because, for one thing, *Automotive News* is on the
3 internet.
4 Q No. You said "should." You didn't say
5 "can." Your answer uses the word "should." I don't
6 want you to misquote yourself.
7 Let's go on to Question 50. We asked you a
8 similar question with respect to a publication called
9 *Fire Engineering*, and your answer simply says see my
10 response before. It is the same.
11 So you're saying that not having seen *Fire*
12 *Engineering*, without knowing anything about the
13 reputation of *Fire Engineering*, you think that people
14 should rely equally on internet information and on
15 *Fire Engineering*; that the fire chief, for example,
16 should rely equally on them?
17 A I can say only in general people can rely
18 equally on the internet as on periodicals. As to fire
19 chiefs and *Fire Engineering* specifically, I have no
20 opinion.
21 Q In Question 51 we asked you the same
22 question about whether it would be prudent for a
23 physician to rely equally on an internet news group
24 and on *Mayo Clinic Proceedings*, *Contemporary*
25 *Pediatrics* or the *New England Journal of Medicine* for

1 accurate medical information.

2 I guess, Mr. Gordon, for your sake I hope

3 your doctor doesn't agree that the information on the

4 internet is just as good. I won't ask any more

5 questions.

6 A Of course, my doctor can go to *Mayo Clinic*

7 *Proceedings* on the internet.

8 Q But will he get all of the information there

9 that he gets in the periodical?

10 A I couldn't tell you that.

11 MR. STRAUS: I have no further questions.

12 Thank you, Mr. Gordon.

13 THE WITNESS: Thank you.

14 MR. STRAUS: Thank you, Mr. Chairman.

15 CHAIRMAN OMAS: Thank you, Mr. Straus.

16 Mr. Keegan, will you call your next witness

17 please?

18 Excuse me. Mr. Bergin? I'm getting carried

19 away here. Would you introduce yourself, Mr. Bergin,

20 please?

21 MR. BERGIN: Certainly, Mr. Chairman.

22 CROSS-EXAMINATION

23 BY MR. BERGIN:

24 Q Good morning, Mr. Gordon. My name is Tim

25 Bergin. I represent the McGraw-Hill Companies. I

1 just have some brief follow-up for you.

2 A Okay.

3 Q You indicated this morning, and correct me

4 if I'm wrong, that in your view preferential postage

5 rates play no role in contributing to the extent to

6 which publications help bind the nation together.

7 A I believe it's marginal at best at this

8 point.

9 Q What knowledge do you have of the role of

10 postage costs in the economics of small circulation

11 magazines that are mailed long distances?

12 A I have very little.

13 Q Any knowledge of the economics of start-up

14 magazines and the role that preferential postage rates

15 play to the viability of those magazines?

16 A No. I do not know them.

17 MR. BERGIN: In light of the cross-

18 examination by Mr. Straus, I have nothing further, Mr.

19 Chairman.

20 CHAIRMAN OMAS: Thank you, Mr. Bergin.

21 Ms. Rush?

22 MS. RUSH: Thank you, Mr. Chairman.

23 CHAIRMAN OMAS: Good morning, Ms. Rush.

24 MS. RUSH: Good morning.

25 CHAIRMAN OMAS: Would you introduce yourself

1 for the record?

2 MS. RUSH: I will.

3 CROSS-EXAMINATION

4 BY MS. RUSH:

5 Q Mr. Gordon, I'm Tonda Rush. I represent

6 National Newspaper Association. Our organization is

7 made up of mostly weeklies and small daily newspapers.

8 I read your book, Thread Across The Ocean,

9 and enjoyed it very much --

10 A I'm glad you did.

11 Q -- occasioned by your appearance here. I

12 assume from your context that you had access to the

13 Field family letters when you wrote the book or some

14 original materials from the Field family. As you did

15 that a couple of years ago, you may not recall.

16 A I did not use original materials in the

17 preparation of that book. It was almost all secondary

18 sources.

19 Q Did you use old newspapers and old

20 magazines?

21 A Yes, I did. I used like *Harper's Weekly*

22 back in the 1860s and the *New York Herald*, which was

23 the greatest newspaper in the world at that time.

24 Q Horace Greeley might not agree with that.

25 A No. My great-grandfather was his successor

1 as editor of the *Tribune*, so he probably wouldn't have
2 agreed either.
3 Q I'm just curious. Did you find those
4 sources on the internet, or were you required to get
5 them off microfilms and hard copy?
6 A I was able to get some of them off of hard
7 copy because I have access to hard copy of the
8 *Harper's Weekly* of the 1860s. As anybody has ever
9 done research with microfilm will testify, hard copy
10 is a lot nicer to deal with.
11 Q Easier to read. Okay. I'm curious about
12 your answers to a couple of NNA's first questions to
13 you, No. 1 and specifically No. 5 and No. 4.
14 Since you have some family history with the
15 *New York Herald*, your response to the question about
16 the *New York Tribune* now does not surprise me. You
17 said you really considered the *Tribune* more like a
18 magazine because it was a weekly publication sent
19 around the country. Have you done the research on
20 that?
21 A No. I meant the *Tribune* was a daily
22 newspaper in New York City --
23 Q Right.
24 A -- but the people who lived far away who
25 subscribed to the *New York Tribune*, they got in effect

1 a weekly digest, which would often arrive -- I think
2 it was printed on Saturday, and I believe it would
3 often arrive, you know, in Wisconsin say the next
4 Tuesday or Wednesday or whatever
5 Q So your characterization of it is not like a
6 newspaper was based upon its frequency or its
7 timeliness?
8 A Yes. I mean, a newspaper to me has the most
9 immediate news. Nowadays, of course, television has
10 to a large extent taken over that particular role. I
11 mean, we don't have extras in newspapers anymore.
12 Q That leads to my next question, which is
13 about your response to NNA's Question No. 5 in which
14 you said: "To me, a newspaper is something that is
15 published daily, except perhaps for Sundays, and
16 carries the very latest news." Was that your
17 testimony?
18 A Yes.
19 Q In response to my Question No. 4, and I
20 asked you about weekly newspapers, do you feel that
21 the weekly newspapers are not newspapers? Did you
22 disagree with my formulation in that question?
23 A Well, I think in very small towns where they
24 still have newspapers, I mean, they're as near as they
25 come to a newspaper. It's not economically possible

1 to publish every day and so they publish weekly. You
2 know, I guess maybe a newspaper is the most immediate
3 source for the news contained therein.
4 Q Would you expect those to be mostly local
5 news content publications?
6 A I would believe so, yes.
7 Q Do you subscribe to one?
8 A No.
9 Q Have you ever?
10 A No.
11 Q Have you ever lived in a small town?
12 A No. I was born and brought up in Manhattan.
13 Q Okay. May we just agree for purposes of
14 this discussion that at least those publishers
15 consider those products newspapers?
16 A Okay. Sure.
17 Q Okay. I just wanted to make sure we were
18 talking about the same thing here because many of my
19 questions are about smaller papers like that.
20 You said in your testimony beginning
21 basically on page 11 and pretty much through the end
22 quite a bit about how the internet has affected the
23 cost of the news business.
24 Would it be a fair statement that you
25 believe that the personal computer and the internet

1 have broken down the barriers to entry that relate to
2 the printing and the distribution?
3 A Yes, to a large extent. I mean, it's now
4 possible to create the modern equivalent of a
5 newspaper at very little cost.
6 Q And have you done any examination of the
7 penetration into American homes by internet access?
8 A Very little. I believe it's now 70 percent
9 of American homes have internet access.
10 Q Have you examined by any demographic
11 breakdown; for example, for the elderly?
12 A I believe it is the older you are the less
13 likely you are to have internet because the older you
14 are the less accepting of new technology you tend to
15 be, but there are plenty of elderly who are on the
16 internet. I can testify to that through my aunt.
17 Q African-American?
18 A Pardon?
19 Q African-American? Same answer or different
20 answer? More or less likely to be on the internet?
21 A Actually, the internet penetration among
22 African-Americans is growing faster than the general
23 population at the moment.
24 Q Any idea of absolute levels? Over 50
25 percent? Under 50 percent?

1 A I don't have those figures.
2 Q How about Hispanics?
3 A I believe they're slightly higher than
4 African-Americans, if I remember correctly.
5 Q I believe you said in response to one of the
6 questions, and I believe it was NNA's, that you
7 thought that most people had access to the internet
8 through libraries.
9 A Yes.
10 Q Do you believe that's true?
11 A I believe so.
12 Q Have you done any examination of the degree
13 to which any of these demographics -- the elderly, the
14 Hispanics or African-Americans -- actually do use the
15 library for internet access?
16 A No, I have not.
17 Q Have you developed any thoughts about what
18 percentage of a news product, whether it's a daily
19 newspaper, weekly newspaper, weekly news magazine,
20 would be devoted to the cost of acquiring and editing
21 the information, as opposed to the cost of printing it
22 and distributing it?
23 A Have I investigated that? No.
24 Q Would you assume it's a small number, a
25 large number, a medium sized number compared to

1 printing and distribution?

2 A I'm afraid I have no idea.

3 Q Writers do like to be paid. Do you agree?

4 A Yes.

5 Q Okay.

6 A No argument.

7 Q You said in response to ABM's Question No. 2

8 that you read regularly the *New York Times* and the

9 *Wall Street Journal*. Is that correct?

10 A I'm sorry? Say that again.

11 Q You read the *New York Times* and the *Wall*

12 *Street Journal*?

13 A Yes.

14 Q Those are two of the publications that you

15 read. Do you read them on line or in print?

16 A I usually read them in print, but sometimes

17 I have to read them on line because I live up in the

18 far northern suburbs of New York now, and while the

19 *New York Times* is supposed to be delivered at 6:30, it

20 sometimes shows up at 9:30.

21 Q So you read it on line?

22 A In that case I will go on line just to make

23 sure the world hasn't blown up.

24 Q Do you pay a subscription fee for the

25 internet access for those publications?

1 A Yes, I do.

2 Q Is it through the print product, or do you

3 have a separate subscription for those websites?

4 A They're separate.

5 Q Do you believe in those two cases that the

6 information you read on line is pretty much the same

7 as you'd see if you picked it up at a newsstand or if

8 it were delivered at 6:30 in your household?

9 A Yes, I believe so.

10 Q Does it seem to be written by the same

11 writers and the photographs taken by the same

12 photographers?

13 A Yes.

14 Q Would you expect that if those two papers

15 ceased to exist and they shifted their entire

16 operation on line that it would still be the same

17 amount and quality of information available to you?

18 A I couldn't tell you that. That would be

19 business decisions for them to make. I would hope it

20 would be the same.

21 Q That would be an economic question for them

22 to settle?

23 A Of course.

24 Q Okay. You made a reference to Matthew

25 Drudge. Do you consider the Drudge report a

1 journalist enterprise?

2 A Indeed.

3 Q Yes? Is it a subscriber product? Do you

4 have to pay to receive it?

5 A I believe it's free.

6 Q Any idea how the website supports itself?

7 A No, I'm afraid I do not.

8 Q Do you find the information there to be

9 equally reliable as what you would find in the *Wall*

10 *Street Journal* or the *New York Times*?

11 A No, but it's enough. It doesn't pretend to

12 be the same thing. I mean, what Matt Drudge is trying

13 to come up with, as he was perfectly willing to admit,

14 you know, is possibilities.

15 He gets the report from here, and he's

16 putting it on his website and saying this is something

17 to check into. He's not putting his imprimatur behind

18 it.

19 Q If those publications, the *New York Times*

20 or the *Wall Street Journal* or in fact any of the print

21 periodicals, ceased to exist would Matthew Drudge

22 still have a basis for his website do you think?

23 A He probably would have to -- well, there's

24 an infinity of sources for him. I mean, that's what

25 blogs do. I guess you could call him a blog.

1 On of my favorite blogs is Best of the Web
2 by James Toronto of the *Wall Street Journal*. It's
3 entirely from other -- it's the blog of blogs and his
4 comments.
5 Q Would it be fair to say that the blogs sit
6 on top of a pyramid that's based upon the printed
7 publications in some way?
8 A Some of them are, and some of them are not.
9 I mean, Andrew Sullivan has no -- I mean, he is a pure
10 blog. It's his information and his opinions, of
11 course.
12 Q So you would consider Matthew Drudge a
13 blogger you said?
14 A That's a news source as well.
15 Q Do you see the bloggers, if you can make a
16 generic characterization, primarily as journalists or
17 primarily as opinion writers?
18 A I think it varies from blog to blog.
19 Certainly a good many of them are opinion because
20 opinions are easier to come by than news.
21 Q I was interested in your TransAtlantic Cable
22 book, if I remember correctly. It's been a while
23 since I've read it, so forgive me if I've
24 mischaracterized it.
25 One of the earliest subscribers to the cable

1 was actually the Associated Press. Is that correct?
2 A Well, it brought I think it was the United
3 Press International into existence because the early
4 cable rates were so extraordinarily expensive. I
5 mean, Horace Greeley spent $5,000 to telegraph one
6 dispatch from the Franco-Prussian War, and $5,000 was
7 very serious money in 1870.
8 The newspapers got together to form the
9 United Press International so that they could share
10 this very expensive means of information.
11 Q Are you sure that you're talking about
12 United Press International and not the Associated
13 Press?
14 A I could be.
15 Q Are you familiar at all with the AP as it
16 exists today?
17 A Only as I read its dispatches in newspapers,
18 and I go to its website.
19 Q Do you find it is a basic source for much of
20 the material you see on the web?
21 A I imagine it would be, yes.
22 Q Do you have any idea how it's owned or how
23 it's operated?
24 A No, I do not.
25 Q Would it surprise you to hear that it's an

1 historic cooperative of newspaper publishers
2 basically?
3 A No, it would not.
4 Q You said in response to Mr. Straus' question
5 that you couldn't answer whether the content that you
6 find on line for a business publication would be the
7 same as what you would find in the print product.
8 Would that be true for a newspaper as well?
9 Have you examined newspaper websites to see if they're
10 posting the same things on line as they have in the
11 print product?
12 A The only ones I've done frequently are the
13 *New York Times* and the *Wall Street Journal*. As far as
14 I can tell, they're identical.
15 Q Are you aware of any internet websites that
16 would be considered basically local news websites when
17 you get outside the context of New York City and the
18 financial community? Have you ever looked at any that
19 are based primarily upon small town news or local
20 community news?
21 A The only one I'm at all familiar with, and
22 I'm not sure it rises to the level of a news group, is
23 in the town I live in in North Salem, New York.
24 One of the town council people has an email
25 list, and she sends around -- she's in the minority on

1 the town board. In fact, she is the minority on the
2 town board, and she doesn't feel that they're giving
3 proper information so she provides in effect her own
4 blog by email. It's a proto news group perhaps.
5 I wouldn't be surprised if there weren't
6 tens of thousands of other small towns in this country
7 that do exactly the same thing in their personal
8 capacity. Of course, the town also has its own
9 website and provides information, much of which she
10 regards as being less than totally accurate.
11 Q Would you regard her website as a
12 journalistic product?
13 A In a sense, yes.
14 Q Do you think it's detached and objective?
15 A I think with anything that's produced by
16 only one person is unlikely to be entirely detached
17 and objective, I mean, human nature being what it is.
18 Q Are you aware of any that are published by
19 local newspapers, any websites?
20 A Not that I'm aware of. I've never looked.
21 Q Could you accept for purposes of this
22 examination that many newspaper publishers do have
23 websites that contain some or all of their content?
24 A Sure.
25 Q Would it surprise you if any of them told

1 you that the primary economic support for the content
2 of the printed paper comes from advertising?
3 A No, that would not surprise me.
4 Q Are you at all familiar with the technology
5 called TiVO?
6 A Yes, recording TV programs. I have one.
7 Q I don't mean to make all of us sound age
8 challenged here. I have to admit I've never used it
9 myself.
10 A It's wonderful. Try it.
11 Q Can you explain how it works?
12 A It's a hard disk, and you record programs.
13 You can tell it to record this program at such and
14 such a time.
15 Compared to a VCR, it is heaven on earth.
16 You just go click, record this program, click, and it
17 does it. You don't have to go to MIT to find out how
18 to do it.
19 Q Are you familiar with a term that the
20 broadcasters are fond of using called ad zapping?
21 A Where you can zip through the ads? Right.
22 Q Right. TiVO does that for you? You can see
23 the program and omit the commercial if you want to?
24 A Well, unless I have yet to discover how to
25 do it, which is entirely possible. You can fast

1 forward through it --

2 Q Okay.

3 A -- and then stop it just in time hopefully.

4 Q If a print publisher told you that the

5 advertising on the internet website contains some of

6 the same problems for a print publisher, would that

7 surprise you -- that people have a tendency to sort of

8 zap through the advertising and go straight to the

9 content?

10 A No, that would not surprise me at all.

11 Q I realize you're not an economic witness,

12 nor am I an economist, so I won't take you very far

13 into this. Are you familiar with the concept of

14 incremental cost?

15 A Only vaguely.

16 Q If I said to you that the economics of

17 publishing involve creating one product that covers

18 basic overhead cost and that if you do that then it's

19 much cheaper to provide yet another ancillary product

20 to the side of that or on top of it, would that make

21 sense to you?

22 A Yes.

23 Q Would it make sense to you to find that a

24 newspaper might cover its basic overhead costs with a

25 print product and provide the website as an

1 incremental product?

2 A That would not surprise me, no, but we're in

3 the very early days of the internet. I mean, it's

4 evolving rapidly.

5 Remember, we went through a great bubble a

6 few years ago because people were selling ideas at

7 enormous prices on Wall Street, and many of them came

8 to grief. Now we're learning how to make money on the

9 internet.

10 Q That was exactly what I was about to ask

11 you, so I'm glad you raised that. Are you familiar

12 with any local news websites that actually do make

13 money?

14 A I'm not aware of any, but --

15 Q Have you talked to any publishers about the

16 likelihood of that happening in the near future?

17 A No.

18 Q Do you remember a Microsoft product called

19 Sidewalks that it rolled out in the mid 1990s with

20 local news content?

21 A No.

22 Q Does that bring any memory to mind?

23 A (Non-verbal response.)

24 Q As a writer, would it be fair to say that

25 when you do your research you like to rely upon a wide

1 variety of resources?

2 A Absolutely. One source is plagiarism. Two

3 sources is research.

4 Q Have you followed the discussions in

5 Congress this past year or so about concentration of

6 media ownerships and debates about the numbers of

7 broadcast stations that are owned in common and

8 broadcast/newspapers that are owned in common?

9 A Not in any depth. I've been aware of the

10 discussion going on.

11 Q Do you have a general sense that there is a

12 greater concentration of media ownership in the

13 country?

14 A In some senses, yes, but in other senses,

15 no.

16 Q If you confined it to print media, would you

17 say the answer is yes?

18 A I believe the number of newspapers is

19 declining in this country and has been for some time.

20 Q I believe I noticed in your autobiography

21 you went to school at Vanderbilt. Is that correct?

22 A That's correct.

23 Q You lived in Nashville for a while?

24 A That's correct.

25 Q Did you read any of the newspapers while you

1 were there?

2 A I read both the *Tennessean* and the *Banner*.

3 My cousin was the editor of the *Banner* when it folded.

4 Q So the *Banner* is gone?

5 A I believe so.

6 Q And the surviving newspaper is the

7 *Tennessean*?

8 A Yes.

9 Q Is it locally owned?

10 A I believe it's owed by is it the

11 Figgentolas? I forget.

12 Q Would it concern you if the economics of the

13 future meant that the printed publications found that

14 they could not make the internet sites profitable and

15 that they decided that print product was the only

16 likely viable economic model for themselves?

17 A Well, that's a theoretical because I don't

18 know that that will happen.

19 Q I'm not asking you to believe that it's

20 true. I'm just asking you to tell me would that

21 concern you if that were the case.

22 A Yes, it would.

23 MS. RUSH: I have no further questions, Mr.

24 Chairman.

25 CHAIRMAN OMAS: Thank you.

1 Is there any other party who wishes to
2 cross-examine Mr. Gordon at this time?
3 (No response.)
4 CHAIRMAN OMAS: Are there any questions from
5 the bench? Mr. Hammond?
6 VICE CHAIRMAN HAMMOND: I just wanted to get
7 a clarification off of one of your responses to Ms.
8 Rush's question when she was discussing weekly
9 newspapers. Did you say in response that you did not
10 consider weekly newspapers to be papers that contained
11 news?
12 THE WITNESS: Well, I guess what I should
13 say is there are two different kinds of weekly
14 newspapers. One is the weekly edition of a daily
15 newspaper such as the *New York Tribune*, and the weekly
16 edition was very widely disbursed whereas the daily
17 was not because it was impossible to get a daily
18 newspaper, you know, more than a few hundred miles
19 from New York City.
20 There are weekly newspapers in small towns
21 that have never been dailies that they are weeklies,
22 and they are the latest news available on the local
23 scene.
24 What constitutes a newspaper is that which
25 produces the very latest news, as opposed to a

1 magazine which is somewhat more interpretive. They're
2 merging, of course, because it used to be *Time*
3 magazine closed Friday afternoons. Now it closes, you
4 know, Sunday night or whatever it is.
5 VICE CHAIRMAN HAMMOND: So a small, weekly
6 newspaper could contain news?
7 THE WITNESS: Indeed. They do contain news.
8 VICE CHAIRMAN HAMMOND: Okay.
9 THE WITNESS: It's a question of, you know,
10 what is the definition of newspaper as opposed to
11 magazine. Of course, it's not black and white. It's
12 not two pigeon holes and shades of gray.
13 I think some weeklies such as the *New York*
14 *Tribune* weekly of the nineteenth century were
15 essentially magazines.
16 VICE CHAIRMAN HAMMOND: But today --
17 THE WITNESS: Today's weeklies are
18 newspapers. Sure.
19 VICE CHAIRMAN HAMMOND: Yes. They do
20 contain news?
21 THE WITNESS: Right.
22 VICE CHAIRMAN HAMMOND: Yes. Okay. Thank
23 you.
24 CHAIRMAN OMAS: Commissioner Goldway?
25 COMMISSIONER GOLDWAY: I must admit that it

1 was a pleasure to have some testimony written that was
2 the quality of well-written prose, as opposed to the
3 usual bureaucratic speech that we have to suffer
4 through. I appreciate that.
5 I also think that this is an interesting
6 opportunity for us at the PRC to think in terms of
7 larger policy issues than we often do, so I appreciate
8 your testimony and your willingness to tackle the
9 postal community and its arcane information. I thank
10 you for being here.
11 THE WITNESS: Thank you.
12 COMMISSIONER GOLDWAY: I do have a couple of
13 questions for you. You give a very fascinating list
14 of newspapers and magazines that you read. Clearly
15 you have wide interests.
16 THE WITNESS: I must confess, I was somewhat
17 appalled when I drew up the list and found out how
18 many I do subscribe to.
19 COMMISSIONER GOLDWAY: Birding and cooking
20 and traveling and all kinds of wonderful things.
21 I wonder when you think about the
22 implications of what the Complainants have asked for,
23 which is a shift in cost burden from one kind of
24 magazine to another, what you would feel like if you
25 could no longer get *National Geographic* because the

1 cost for delivery became too high and the subscription
2 rate became too high or the *New England Historical and*
3 *Genealogical Register*.
4 What's your sense about the priorities of
5 the magazines that you receive in terms of how you
6 would like them to be available to you?
7 THE WITNESS: Well, since I subscribe to
8 them I would like them to be available almost by
9 definition.
10 COMMISSIONER GOLDWAY: Is there a point at
11 which the subscription cost gets so high that you feel
12 that you can't subscribe to them?
13 THE WITNESS: I suppose there might be. On
14 the other hand, if the *New England Historical and*
15 *Genealogical Register* were to become prohibitively
16 expensive in paper, I would not mind reading something
17 like that on the web at all.
18 COMMISSIONER GOLDWAY: But the issue is
19 whether they can make enough money providing that
20 information on the web to still have it available for
21 you.
22 THE WITNESS: Of course, that particular
23 magazine does not depend on advertising except to a
24 very, very limited extent. Maybe two out of 48 pages
25 are advertising. Most of that the subscribers have

1 to --

2 COMMISSIONER GOLDWAY: So you think it would

3 still be a subscription magazine, just subscribe on

4 the web, and that would be the alternative?

5 THE WITNESS: Yes, I believe so.

6 COMMISSIONER GOLDWAY: The other concept

7 that I've been playing with in this is if we were to

8 change the rate structure, I think it's fair to say

9 that nationally distributed magazines would certainly

10 have a greater capacity for distributing their news

11 efficiently nationally, and some of the smaller

12 magazines would have some difficulty.

13 I'm wondering in the context of how we talk

14 about binding a nation together, the cultural and

15 educational vitality of the country, whether it's

16 better to have strong national presence of a few

17 magazines that speak out or whether it's better to

18 have a multiple of many different kinds of voices in

19 different ways and whether that's something that we

20 ought to consider when we look at the policy

21 implications of rates.

22 THE WITNESS: Well, I think that what's

23 important is not the magazine specifically. What's

24 important is the information and the ability of the

25 people to get that information in real time.

1 You know, if they can get it on the web I
2 think many people would be perfectly willing to get it
3 that way. I mean, as I talk about there's always an
4 inertia in the human affairs. People want to continue
5 doing things the way they've always done them.
6 There are many places where a hard copy
7 magazine is much more convenient than on the web. I
8 mean, laptops and beaches make a very poor
9 combination, but this is a matter of adjustment. This
10 has been happening ever since the birth of the world
11 economy, whenever that may have been.
12 In the late 1940s, many of the radio
13 programs migrated to television, and radio had to
14 fundamentally change its economic nature. Today the
15 radio business in the United States is far larger than
16 it was in 1946 before television began to compete with
17 it. It's just they had to evolve to face this new
18 situation, and they evolved very successfully.
19 COMMISSIONER GOLDWAY: So that sort of
20 supports my theory that human beings have an
21 insatiable appetite for information, and we'll find
22 subject matter to put in whatever communications
23 medium we have. If we have the access to it, we'll
24 find the content?
25 THE WITNESS: That is right, I think. On

1 the internet, especially with Google is one of the
2 great inventions of the internet era. I mean, it's
3 simply astonishing how fast it can process requests
4 and come up with a graded list of sites.
5 I mean, we Goggled on *Automotive News* and
6 came up with 532,000 references, which is really sort
7 of like Henry and the donut machine. There's too
8 many.
9 COMMISSIONER GOLDWAY: Too many, yes.
10 THE WITNESS: But they can narrow the search
11 if you learn how to Google. I bet there are courses
12 on Goggling 101.
13 COMMISSIONER GOLDWAY: When you were
14 preparing your book on The Economic Wealth of the
15 Great American Economy, which is due out -- I don't
16 have the title exactly right.
17 THE WITNESS: October.
18 COMMISSIONER GOLDWAY: October. Did you
19 focus on the importance of the communications industry
20 and in particular the print industry as dynamos for
21 the American economy, or do you see those as
22 secondary?
23 THE WITNESS: Not so much on the printing
24 industry, although I mention the newspapers coming
25 into the -- what we consider newspapers, modern

1 newspapers, as opposed to the old-fashioned newspapers
2 that Thomas Jefferson knew, which are a very different
3 beast.
4 How much that changed the country and how
5 quickly it did. I mean, as early as 1866 a magazine
6 called the *North American Review* said that the modern
7 newspaper was as essential to us as the steam engine.
8 In 1866, it was only 31 years after James Gordon
9 Bennett founded the *Herald*, so new technology becomes
10 essential very, very quickly. Also, of course, the
11 telegraph and then telephone and so on and so on.
12 I deal a great deal with that because, you
13 know, what makes an economy, the size of an economy,
14 is dependent upon how quickly things communicate. A
15 market can only be as big as the area within which
16 information is instant, and that's why on Wall Street
17 in the early days the messengers were called runners
18 because they were mostly young boys who did indeed run
19 between the Exchange and the brokerage houses and the
20 banks.
21 Now there are still a few runners left, but
22 they are mostly old, semi-retired men who sort of
23 shuffle along.
24 COMMISSIONER GOLDWAY: All right. Thank you
25 for your thoughts. I appreciate that.

1 THE WITNESS: Thank you.

2 CHAIRMAN OMAS: Commissioner Covington?

3 COMMISSIONER COVINGTON: Good morning, Mr.
4 Gordon. I echo what Commissioner Goldway stated in
5 regard to the preparation of your testimony. It was
6 pretty straightforward, and you brought out some major
7 points I think that we need to consider as we talk
8 about the future and the Postal Service's role of
9 continuing to bind the nation together.

10 I'm assuming that this is your first time
11 testifying before this Commission. Am I correct in
12 that?

13 THE WITNESS: It's my first time testifying
14 before any commission.

15 COMMISSIONER COVINGTON: Okay. Before any
16 commission. I noticed that previously in your young
17 career that you worked on Capitol Hill I believe for
18 Congressman Bodillo and Congressman Garcia.

19 THE WITNESS: I was in New York, not in
20 Washington. I was their press secretary in New York.

21 COMMISSIONER COVINGTON: But you were in the
22 district office?

23 THE WITNESS: No, not all that often
24 actually.

25 COMMISSIONER COVINGTON: Okay. What I

1 wanted to ask you is when you were I guess basically
2 selected to prepare testimony for us in this case, did
3 you have any idea or any concept of what a flat
4 editorial rate was or how uniform postal rates
5 interact with mailers of periodicals and/or media?
6 THE WITNESS: No, I had no idea whatever.
7 COMMISSIONER COVINGTON: Okay. I noticed
8 when Ms. Rush from the National Newspaper Association
9 was asking you about new technology I would imagine,
10 what do you see on the horizon in the future as far as
11 any changes that the print media can expect?
12 THE WITNESS: I'm not aware of any
13 particularly in the print media. I'm sure they'll be
14 coming fast and furiously as the computer continues to
15 evolve at an extraordinary rate.
16 COMMISSIONER COVINGTON: Okay. I would
17 imagine in your study and in your day-to-day activity,
18 you realize what an impact the internet has had I
19 guess basically from business to homes and vice versa.
20 Quite naturally, we're asked from time to
21 time to look at the impact that it's having on other
22 classes of mail, particularly first class mail. I
23 want to know just from your personal opinion how has
24 the internet actually affected you when it comes down
25 to going and getting those stamps at your local post

1 office there in North Salem, New York?

2 THE WITNESS: It's affected it quite a lot.

3 I use far fewer postage stamps today than I did 20

4 years ago. I mean, I pay most bills on line. I use

5 email. I used to write -- I keep them in a separate

6 folder on my computer. I have correspondence per

7 year. That folder gets smaller and smaller because I

8 use email more and more and more.

9 COMMISSIONER COVINGTON: I noticed that one

10 of the major points that you covered in the testimony

11 that you presented, you discussed how new technologies

12 have emerged from 1876 all the way up to 1917, which

13 actually I guess would go from the telephone, going

14 beyond the string and the two tin cans up to where we

15 are now, you know, with the internet.

16 I guess it's safe for us to assume that the

17 internet was one of the most I guess technologically

18 advanced mediums to come out, and I guess it's going

19 to be around and have a profound impact on our every

20 day lives.

21 I wanted to ask you one other question,

22 being I'm assuming the literary and journalistically

23 motivated professional that you are, the I guess

24 communications overall as far as the Postal Service.

25 If you remember, Mr. Straus alluded to ESCI, the

1 economical, cultural and scientific aspects.

2 As we proceed, I would imagine, with the

3 testimony and stuff here today, is there anything that

4 you think that the Commission would need to be aware

5 of as it relates to communication technology and/or

6 the print industry or anything that you think that we

7 should have a heads up on that could have an impact on

8 the Postal Service's economic well-being?

9 THE WITNESS: I'm not aware specifically, of

10 course, but I'm an historian so I'm paid to look

11 backwards more than forwards. People who get paid to

12 look forwards often get paid better than historians.

13 I have no specific information. I wish I

14 did. There might be a way to invest in it.

15 COMMISSIONER COVINGTON: There would be a

16 way to invest in it. Okay. Thanks, Mr. Gordon.

17 That's all I have.

18 CHAIRMAN OMAS: Mr. Keegan, would you like

19 some time with your witness?

20 MR. KEEGAN: Yes, Mr. Chairman. May we have

21 15 minutes?

22 CHAIRMAN OMAS: With that, we will take our

23 morning break as well, and we'll come back at 11:20.

24 (Whereupon, a short recess was taken.)

25 CHAIRMAN OMAS: I love the buzzer. Mr.

1 Keegan.

2 MR. KEEGAN: Thank you, Mr. Chairman.

3 REDIRECT EXAMINATION

4 BY MR. KEEGAN:

5 Q Mr. Gordon, would you please turn to your

6 response to ABM Number 37.

7 A Yes.

8 Q Actually, if you would go back one step to

9 ABM Number 36. You were asked in that question

10 whether at the time that you completed the preparation

11 of your testimony that you knew what time period was

12 covered by the reduction in the transportation

13 component from 44 to 15 percent, and you responded

14 yes. Is that still your response to that question?

15 A Yes, it is.

16 Q And if you would turn to your answer to

17 Number 37, you were asked there if you knew now what

18 time period was covered, and please provide it and

19 identify the source of your information.

20 And you provided some detailed information

21 from Mr. Mitchell's testimony. Did you have the

22 source information for what you wrote in your

23 testimony at the time that you wrote your testimony?

24 A Yes, I did.

25 Q Was putting that point in your testimony

1 expressly suggested to you by anyone?

2 A No.

3 Q During the oral cross-examination, I believe

4 you stated that the response to Number 37 was intended

5 to say that you know now what the source was, as

6 opposed to having known when you wrote your testimony.

7 Is that indeed the case or what is the

8 correct answer to that question?

9 A I knew it at the time that I wrote the

10 testimony. I am afraid that my mind doesn't contain

11 footnotes terribly well, and it was written several

12 months ago, and I simply didn't remember what

13 particular sources I had, or where each particular

14 fact came from.

15 And I now do remember receiving Mr.

16 Mitchell's testimony and reading it.

17 Q Okay. Thank you. Mr. Straus asked you

18 whether you have ever looked at a website for

19 specialized business publications, and you answered

20 that you had not. Have you ever looked at printouts

21 from websites for specialized business publications?

22 A Yes.

23 Q Did you in fact look at several of them

24 yesterday?

25 A Yes.

1 Q And what are those publications?
2 A Automotive News, Fire Engineering, Mayo
3 Clinic Proceedings, and the New England Journal of
4 Medicine.
5 Q And those are publications that you were
6 asked about in ABM Interrogatories?
7 A Yes.
8 Q Do you have the copies with you of the
9 printouts that you looked at?
10 A Yes, I do.
11 MR. KEEGAN: Mr. Chairman, with your
12 permission, I would like to distribute simply for
13 informational purposes copies to the Commission so
14 that they can follow along, and I have a copy for
15 counsel.
16 CHAIRMAN OMAS: Without objection.
17 BY MR. KEEGAN:
18 Q Would you turn to your response to ABM
19 Number 49, please. You were asked in that question
20 whether it would be prudent for an auto parts supplier
21 to rely equally on an internet news group, and
22 Automobile News for information about the auto
23 industry.
24 Was it your intention to suggest in this
25 testimony that internet news groups are a good or

1 reliable source of information for specialized
2 business information?
3 A No, I did not intend that.
4 Q In your response, you state that you have no
5 opinion on whether an auto parts supplier should reply
6 on an internet news group, but he should rely equally
7 on the internet on automotive news.
8 Has that opinion been changed, undermined,
9 or confirmed by looking at the website for automotive
10 news?
11 A It has been confirmed.
12 Q Does that website indicate that the content
13 of automotive news is available on a prescription
14 basis on-line?
15 A Yes, I believe it is available to anybody.
16 I don't believe there is a subscription charge.
17 Q Well, I direct your attention to the first
18 page of the photocopied materials from automotive
19 news. Is the first word on that page not
20 subscriptions?
21 A Yes, it is.
22 Q And the first paragraph on that page states
23 that you may subscribe, or you may follow the
24 instructions below to subscribe to any of these
25 publications.

1 A Yes, that includes access to premium on-line
2 services, although I am not sure what premium on-line
3 services constitutes.
4 Q Did you also have occasion in addition to
5 looking at the web pages of those five magazines to
6 looking at what Google turned up when you put the
7 names of those publications into a search?
8 A Yes.
9 Q You mentioned earlier that 532 thousand hits
10 came up when you put in automotive news, and you have
11 with you do you not the first page of those 532
12 thousand?
13 A Yes, I do.
14 Q If you would refer to that. There does not
15 appear on that page the item, Autocom News and
16 Reviews, the fourth item? Comprehensive news and
17 reviews of vehicles and other industry motor sports
18 and auto shows?
19 A Yes.
20 Q Does it appear on that page, Automotive News
21 Europe?
22 A Yes.
23 Q Automotive News, front page, from MSNBC?
24 A Yes.
25 Q Yahoo Auto and Truck Manufacturers Industry

1 News?

2 A Yes.

3 Q Advanced Automotive News?

4 A Yes.

5 Q And if you look at the right-hand side of

6 that page, do you see advertisements for additional

7 sources of internet information and other automotive

8 news?

9 A Yes. And those include Automotive News

10 World Analysis, Wards Automotive Yearbook, Asian

11 Automotive Industry, and other motor news itself?

12 A Yes.

13 Q And advertised as magazines at huge savings?

14 A Right.

15 Q Would you turn to the printouts for fire

16 engineering. Does the first page of that printout

17 indicate that fire engineering is available on a

18 subscription basis?

19 A Yes, it does.

20 Q And if you go to the page that you have that

21 shows the Google hits from putting in the search

22 request for fire engineering. The first response to

23 the -- the number one response to Google is Fire

24 Engineer Magazine is it not?

25 A Yes, it is.

1 Q But if you go down on the same page, which
2 contains 10 items, do you find structural fire
3 engineering research at the university?
4 A Yes.
5 Q Do you find Worster Polytech Institute News,
6 WPI Fire Protection Engineering?
7 A Yes, I do.
8 Q Do you find Fire Engineering and Civil
9 Engineering, and -- well, I'm sorry, the word is cut
10 off, but university is cut off, and I withdraw that
11 one.
12 If you would go then to Temporary
13 Pediatrics, and there is the first page of their
14 website, or the first page copied here, and one that
15 offers subscriptions?
16 A Yes, it is.
17 Q Do you have any indication that the material
18 provided to on-line subscribers is any less than that
19 provided to a printed edition subscriber?
20 A I don't believe so.
21 Q And if we go ahead to Mayo Clinic
22 proceedings, the then August subscription rates for
23 on-line subscription listed on the first page there?
24 Annual On-line subscription prices, U.S. dollars?
25 A Right, those annual subscription prices if

1 you subscribe on-line, but I am not sure that means
2 the subscription to the website. I think that you can
3 subscribe on-line to the printed edition, I believe.
4 Q I see. All right. If you would turn to the
5 pages for Google responses for Mayo Clinic
6 Proceedings. Is the fourth item on that page Mayo
7 Clinic Proceedings, Features and Primers on Medical
8 geonomics?
9 A Yes, it is.
10 Q Is the sixth item Mayo Clinic Proceedings,
11 printer friendly page, Mayo Clinic Proceedings, source
12 guide and help media, Mayo Clinic Proceedings, is a
13 peer review journal published at?
14 A Yes, it is.
15 Q And is the last item on the page, "Mayo
16 Clinic.com, Medical and Health Information and Tools
17 from?
18 A Yes, it is.
19 Q I am only assuming it is from the Mayo
20 Clinic given the title, but perhaps it is not.
21 A It refers you to their website, and so I
22 would assume so.
23 Q Yes. And last the New England Journal of
24 Medicine is the first page, and here also an offer of
25 a subscription?

1 A Yes. You can either subscribe to print and
2 on-line for $149, or just on-line, and no print issue
3 for $99.
4 Q Do you have any motion of why those
5 particular rates apply? Why $99 for the on-line
6 subscription, and $150 for the printed?
7 A Well, the on-line is no paper, no printing,
8 and no postage.
9 Q Would you draw from those subscription rates
10 the inference that an on-line subscriber would be
11 expected to get the bulk of the value of the editorial
12 content of the publication based on the prices that
13 one has to pay?
14 A I assume so.
15 Q And again if you go to the pages that Google
16 hits from putting in the search for the New England
17 Journal of Medicine. The first item you get on that
18 page is not for the publication itself, but news
19 results from the New England Journal of Medicine. Is
20 that right?
21 A Yes.
22 Q Did you look at a website or precast from
23 the website in additional to the New England Journal
24 of Medicine that calls itself, Latest News from the
25 New England Journal of Medicine? Do you recall that?

1 A I'm sorry, but could you ask that again?

2 Q Yes, I will. If you look again at the first

3 item on the Google page.

4 A Right.

5 Q And the result is for the New England

6 Journal of Medicine?

7 A Right.

8 Q And did you look at a printout of what you

9 get when you go to that site, the news results for the

10 New England Journal of Medicine?

11 A Did I look at it?

12 Q What is your recollection? I think it is

13 the next page that you have.

14 A Oh, right. Yes, I'm sorry. It produced

15 2,650 further sites.

16 Q And that is the site is it not that

17 exclusively devoted to recording and reprinting news

18 that is first printed in the New England Journal of

19 Medicine?

20 A I believe so.

21 MR. KEEGAN: Thank you. That's all that I

22 have, Mr. Chairman.

23 CHAIRMAN OMAS: Thank you, Mr. Keegan. I

24 take it that there is some recross, Mr. Straus?

25 MR. STRAUS: Yes, there is.

1 RECROSS-EXAMINATION

2 BY MS. STRAUS:

3 Q Mr. Gordon, Mr. Keegan gave you a stack of

4 printouts, and they are all dated yesterday aren't

5 they?

6 A Yes.

7 Q Did you ever look at anything that was the

8 equivalent to those printouts before you prepared your

9 testimony?

10 A No.

11 Q Before you answered the interrogatories?

12 A No.

13 Q After taking you through the publications

14 website, Mr. Keegan asked you to confirm that you had

15 looked at the printouts from Google. For example,

16 Fire Engineering. Did you open any of those websites

17 that Google referred to?

18 A No, I did not.

19 Q So you don't know whether those websites had

20 equivalent information or not do you?

21 A No.

22 Q And the same for Automotive News. You

23 didn't look at any of those websites either did you?

24 A No.

25 Q So you don't know if those websites have

1 equivalent information?

2 A No.

3 Q And the same would hold true for the Mayo

4 Clinic?

5 A It is true for all of them.

6 Q Okay. So for all of those examples, all you

7 know is that Google refers you to websites, and you

8 don't know what those websites contain?

9 A No, I do not.

10 MR. STRAUS: All right. Thank you. That's

11 all.

12 MS. DREIFUSS: Mr. Chairman, I had one

13 question on recross if that is all right.

14 CHAIRMAN OMAS: Yes, I was going to say Mr.

15 Bergin, do you have anything?

16 MR. BERGIN: No, Mr. Chairman.

17 CHAIRMAN OMAS: All right. Thank you.

18 BY MS. DREIFUSS:

19 Q On redirect examination, some of Mr.

20 Keegan's questions also bear on the questions of

21 Commissioner Goldway that were asked of you earlier.

22 He was asking you not so much about professional

23 journals, but about some of your particular interests,

24 such as birding. I gather that you subscribe to a

25 birding publication?

1 A Yes.

2 Q And a genealogical publication?

3 A Yes.

4 Q And she asked you if the periodicals price

5 seemed prohibitive, would you feel the lack of access

6 to those periodicals, and I believe your answer was

7 that you might very well be able to subscribe to them

8 on-line; is that correct?

9 A Yes.

10 Q I have a question that also brings in a

11 point that was discussed by Ms. Rush. She suggested,

12 at least in the case of consumer publications, that

13 internet penetration, and you gave this information,

14 too, that internet penetration is only about 70

15 percent is it not?

16 A Yes. And it is rising like about 25 percent

17 a year.

18 Q At the present time there may be subscribers

19 to some of these publications that provide revenues

20 for the non-printing and non-distribution costs of the

21 periodicals only as hard copy subscribers; isn't that

22 correct?

23 A I'm sorry, but could you say that again?

24 Q At the present time -- you said in the

25 future that there may be a higher internet penetration

1 than 70 percent, correct?

2 A Well, 70 percent of the American population

3 now has internet access in the home.

4 CHAIRMAN OMAS: Mr. Gordon, would you pull

5 your mike up closer, please?

6 THE WITNESS: Yes. I believe that the 70

7 percent refers to how many or what percentage of

8 American homes now have internet access in the home.

9 BY MS. DREIFUSS:

10 Q Right. But to the extent that periodicals

11 may in the short term actually have to resort to

12 distributing the information only on the internet, and

13 would not be able to absorb the printing and postage

14 costs to get information to readers.

15 And to that extent, that is 30 percent or

16 more of the population that does not have internet

17 access, and may very well be the hard copy subscribers

18 would not be providing those revenues to the

19 publications; isn't that correct?

20 A Yes, that is true, but that is looking at it

21 statically. I mean, the percentage of households in

22 the United States with internet access is growing

23 very, very rapidly. And that 70 percent is rising.

24 Somewhere I have them. Hold on a second.

25 (Brief Pause.)

1 THE WITNESS: I believe the figures that I
2 have is that -- and this is for 2002, and in September
3 of 2001, 143 million homes, about 54 percent of the
4 population was using the internet, an increase of 26
5 million in 13 months.
6 In September of 2001, 174 million people, or
7 66 percent of the population in the United States,
8 used computers. And those are 3 years old. So the
9 number of people who have internet access in their
10 homes is rapidly reaching saturation.
11 BY MS. DREIFUSS:
12 Q Do you know what that figure will be next
13 year?
14 A No, I do not.
15 Q Do you know what it will be 5 years from
16 now?
17 A No.
18 Q Do you think there still may be some
19 percentage that does not have internet access and
20 therefore would not be able to subscribe to the
21 publications on the internet?
22 A There certainly will be a percentage of
23 American households that will not have the internet,
24 but there are a percentage of American households that
25 do not have television, and the reason they don't

1 almost entirely is because they do not wish it.

2 Q Right. So there may be a percentage of

3 possible readers of publications who do not or will

4 not have internet access for those publications, but

5 might be willing to be hard copy subscribers; isn't

6 that correct?

7 A That is certainly true, but their

8 alternative was no magazine or internet magazine, and

9 they might very say, okay, I will get the internet. I

10 mean, the only people that would be affected by that

11 would be the people who would not under any

12 circumstances have internet in their homes.

13 MS. DREIFUSS: No further questions.

14 CHAIRMAN OMAS: Thank you. Are there any

15 additional recross? There being none --

16 MR. KEEGAN: Mr. Chairman, I'm sorry, but I

17 have very brief redirect.

18 CHAIRMAN OMAS: All right.

19 FURTHER REDIRECT EXAMINATION

20 BY MR. KEEGAN:

21 Q Mr. Gordon, would you take a look again at

22 Fire Engineering and look at the Google page that we

23 looked at previously.

24 A Okay.

25 Q Mr. Straus inquired whether you had actually

1 gone to any of the affiliated sites to find out what
2 was on them, and whether you had any basis on which to
3 think anything one way or the other about their
4 reliability, and I believe you said that you did not -
5 -
6 MR. STRAUS: I object to the question, as
7 the question does not --
8 MR. KEEGAN: I have not asked the question
9 yet.
10 MR. STRAUS: Well, I object to the
11 characterization of the previous testimony. The issue
12 was not the reliability of the information. It was
13 the content of the website and not the reliability.
14 BY MR. KEEGAN:
15 Q Fine. I will gladly amend the question as
16 Mr. Straus directs. If you take a look at that page,
17 and the sixth item on it, is it headed, "Structural
18 Fire Engineering Research At the University of" -- and
19 then it is blank?
20 A We are looking at the Google page?
21 Q Yes.
22 A Okay.
23 Q And do you see also the web address that is
24 associated with that site?
25 A Yes, it appears to be Sheffield University

1 in the U.K.

2 Q Have you ever heard of Sheffield University

3 in the United Kingdom?

4 A Oh, certainly.

5 Q Is it as far as you know a reputable

6 institution?

7 A Indeed.

8 Q If you go down two items from there, is the

9 next site -- is that site headed, "WPI Fire Protection

10 Engineering."

11 A Yes.

12 Q And does it go on to say, "Worster Polytech

13 Institute News, New Fire Safety Study Director

14 Appointed."

15 A Yes, I see that.

16 Q Have you ever heard of Worster Polytech

17 Institute?

18 A Yes, I have.

19 CHAIRMAN OMAS: Mr. Gordon, please pull the

20 mike and speak into the mike. Thank you.

21 THE WITNESS: I'm sorry.

22 BY MR. KEEGAN:

23 Q Is that to your knowledge a reputable

24 institution?

25 A Yes, it is.

1 Q If you go down to the next item, it is
2 headed is it not, "What is Fire Engineering?" And it
3 says, "The Institution of Fire Engineers. What is
4 Fire Engineering?" Is that correct?
5 A Yes.
6 Q All right. And can you infer anything about
7 that institution from the web address that is given
8 for it?
9 A It is an organization in the United Kingdom,
10 and I would imagine that it is a -- that we have
11 similar organizations in the United States. I mean,
12 they are not State sponsored, but they are
13 organizations, professional organizations.
14 Q Would you expect if you went to that site
15 that they would tell you what they are, and what the
16 organization is?
17 A I would certainly think so, yes.
18 Q And the last item on the page begins, "Fire
19 Engineering, Civil Engineering Department, University
20 of," and then it is blank. Can you infer anything
21 from the web address given for that site where that
22 information comes from?
23 A It appears to be Canterbury -- probably a
24 college or university in New Zealand. I mean, NZ, I
25 assume, is New Zealand. I have not heard of it, I'm

1 afraid.

2 Q Have you ever before yesterday or before Mr.

3 Straus' interrogatory, heard of Fire Engineering

4 Magazine?

5 A No, I had never heard of it.

6 Q Do you have any basis for any opinion one

7 way or the other on the quality or reliability of the

8 content in the Fire Engineering Magazine?

9 A No, I don't.

10 MR. KEEGAN: Thank you. That's all I have.

11 CHAIRMAN OMAS: Thank you. There being no

12 further cross-examination, that completes your

13 testimony here today, and we appreciate your

14 appearance, and your contribution to our record.

15 Thank you very much.

16 THE WITNESS: Thank you.

17 (Witness excused.)

18 CHAIRMAN OMAS: Mr. Keegan, would you please

19 call your next witness.

20 MR. KEEGAN: Time-Warner, et al., calls

21 Robert W. Mitchell.

22 Whereupon,

23 ROBERT W. MITCHELL

24 was called as a witness, and having been first duly

25 sworn, was examined and testified as follows:

1 DIRECT EXAMINATION

2 BY MR. KEEGAN:

3 Q Will you please state your name and

4 occupation?

5 A My name is Robert W. Mitchell, and I am an

6 independent postal consultant.

7 MR. KEEGAN: I beg your indulgence for a

8 moment, Mr. Chairman.

9 (Brief Pause.)

10 MR. STRAUS: It looks like we will finish

11 today.

12 CHAIRMAN OMAS: In fact, while Mr. Mitchell

13 prepares, I do want to just sort of give you an idea

14 of what we are going to try to do. I think we will

15 begin cross-examination with Mr. Mitchell, if he ever

16 gets set up, and we will go for approximately an hour,

17 and then we will take a lunch break if that is all

18 right with everyone here.

19 And then we will come back, and that will

20 sort of give us a mid-afternoon break or whatever. So

21 if everyone concurs, that is what we will do, and we

22 will try to break somewhere around 1:00 or so at a

23 good breaking point. Mr. Mitchell, are you ready?

24 THE WITNESS: I am very, very close. I

25 think we can proceed.

1 CHAIRMAN OMAS: Mr. Keegan.

2 BY MR. KEEGAN:

3 Q Do you have with you two copies of your

4 documents, captioned, "TW, et al., - 2-1, Direct

5 Testimony of Robert W. Mitchell on behalf of Time

6 Warner, Inc., et al."

7 A Yes, I do.

8 Q Was that testimony prepared by you under

9 your direction?

10 A Yes, it was.

11 Q And would that be the testimony that you

12 would give here today if you were testifying orally?

13 A Yes, it is. Should I point out that we have

14 made by hand a couple of corrections?

15 Q Yes, you should.

16 A Okay. Just for the record, on page 40, line

17 7, I refer to TRC library reference 8, and it should

18 be library reference 9 from a previous rate case. We

19 have corrected that in this copy.

20 And on page 64, there is a footnote, with

21 some page numbers from a transcript, and it is

22 Footnote Number 43. The page number in Part 2 of the

23 transcript should be 13361-78. The numbers that were

24 originally in this testimony were a typo that I made,

25 and it was not obvious until you checked it.

1 Q With those corrections that is your
2 testimony in this case?
3 A Yes, it is.
4 MR. KEEGAN: Mr. Chairman, I move that Mr.
5 Mitchell's testimony be accepted into evidence and
6 transcribed into the record.
7 CHAIRMAN OMAS: Is there any objection?
8 (No response.)
9 CHAIRMAN OMAS: Hearing none, I will direct
10 counsel to provide the reporter with two copies of
11 corrected direct testimony of Robert W. Mitchell.
12 That testimony is received and will be transcribed
13 into evidence.
14 (The document, previously
15 identified as Exhibit No. TW
16 et al. - 2-1, was received in
17 evidence.)
18 //
19 //
20 //
21 //
22 //
23 //
24 //
25 //

Postal Rate Commission 793
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TW et al.-T-1

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

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

Docket No. C2004-1

DIRECT TESTIMONY OF
ROBERT W. MITCHELL
ON BEHALF OF
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.
CONCERNING PERIODICALS
RATE DESIGN

April 26, 2004

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Direct Testimony

Of

Robert W. Mitchell

AUTOBIOGRAPHICAL SKETCH

My name is Robert W. Mitchell. I am a consultant on issues relating to postal rates. From 1992 until my retirement in 2002, I worked as Special Assistant to the Postal Rate Commission and, before that, as Special Assistant to the Chairman. From 1975 to 1992, I was a Cost Systems Analyst, a Planning Officer, an Assistant to the Assistant Postmaster General of Rates and Classifications, Manager of the Primary Rates Branch in the Office of Rates, and a Principal Economist at the United States Postal Service. I have worked on a wide range of rate issues, from costing to rate administration to rate design to regulatory policy. I have represented the Rate Commission and the Postal Service to mailers and postal groups. I was the Postal Service's witness on Periodicals and Standard Mail rates (then second and third class) in Dockets No. R87-1 and R90-1, and testified for the Postal Service in four other dockets. I have also been a consultant on rates to the nations of Dominica and The Gambia.

Prior to joining the Postal Service, I was an Assistant Professor of Business at the University of Wisconsin-Milwaukee, teaching Economic Theory and Managerial Economics. I have a Bachelor of Science in Mechanical Engineering from the University

of Cincinnati and an M. A. in Economics from Case Western Reserve University. While at Case, I passed my written and oral comprehensive examinations for the Ph.D. in Economics, with major areas in Economic Theory, Econometrics, and Industrial Economics.

I have written a number of articles and published papers, primarily on economic issues relating to postal rates, including: "Postal Worksharing: Welfare, Technical Efficiency, and Pareto Optimality," in *Emerging Competition In Postal and Delivery Services* (1999), and "Preparing the Postal Service's Rate Structures for Competition: A Study of How the United States Postal Service Might Adjust to Increased Competitive Pressure," in *Future Directions in Postal Reform* (2001).

Adjustments to this Testimony and its Workpapers

Certain adjustments to this testimony and its workpapers have been made since they were filed as proffered testimony and workpapers on January 12, 2004 and January 16, 2004, respectively. All adjustments made are listed below.

1. The headers originally on all pages have been removed.
2. The word "PROFFERED" has been removed from the title page.
3. The date on the title page has been changed.
4. This adjustment page has been added here, and so noted in the Table of Contents.
4. The page number of the second page of the Autobiographical Sketch is iii instead of ii.
5. Page 13, line 4, the word "is" has been added.
6. Page 20, line 18, an open single quote was added at the beginning of the line.
7. Page 36, line 20, "piece rate" was changed to "piece's postage."
8. Page 39 fn. 34, line 3, an extraneous "or" no longer appears.
9. Page 41, line 6, the period after the close parenthesis was added.
10. Page 41, line 10, the open parenthesis before "2" was added.
11. Page 43, a revised Rate Schedule has been inserted.
12. Page 45 fn. 39, line 2, an "s" was added to a word that is now "mailings."
13. Page 51, line 12, the comma after the word "above" was added.
14. Page 55, line 12, an unneeded space no longer appears after the word "Service."
15. Page 58, line 32, the period after the close parenthesis was added.
16. Page 66, line 6, the period after the close parenthesis was added.
17. Cost adjustments, supplied by witness Stralberg, were made to workpaper WP-Mitchell-3.xls, sheet 'BT inputs' cells Y67-AG84, now renamed WP-Mitchell-3F.xls. This change caused other changes in numbers calculated in the sheet.
18. Workpapers WP-Mitchell-1.xls and WP-Mitchell-2.xls have been renamed WP-Mitchell-1F.xls and WP-Mitchell-2F.xls, respectively. No adjustments in contents have been made.
19. Revised workpaper file names have been placed in appropriate places on pages 1, 2, 33 fn. 29, and 42.

I. PURPOSE OF TESTIMONY

The purpose of my testimony is to describe the deficiencies in Periodicals rates and to propose alternative rates, more consistent with the guidance in the Postal Reorganization Act, that recognize costs efficiently and give appropriate signals to mailers.

I contend that our current understanding of postal costs and mailer capabilities makes it clear that Periodicals rates are at variance with the Act's guiding background presumption in favor of efficient rates. I also contend that when a full record is developed, it will show that the unzoned editorial pound rate is not serving its intended purpose and is adverse to accepted principles of efficient rate setting.

My testimony has three main sections: (1) an analysis of the deficiencies of the current Periodicals rates (Section III); (2) a proposed alternative rate design for Periodicals that would take a long stride toward remedying those deficiencies, including a specific rate schedule and a detailed account of the development of the rates therein (Section IV); and (3) an explanation of the desirability of the proposed alternative rates, and their superiority to the current rates, in relation to the statutory ratemaking factors and other policy provisions of the Act (Section V).

In Appendix A, I develop a model of publisher decisions on whether a zoned editorial pound rate would provide reason to reduce or eliminate subscribers in the higher zones.

My workpapers consist of three spreadsheets and are contained in library reference TW et al. 2. WP-Mitchell-1F.xls is equivalent to the Commission's Library Reference No. 9 in Docket No. R2001-1, except that the billing determinants are for full-

weight zoning and three errors are corrected. WP-Mitchell-2F.xls contains the formulas to separate the letter-size pieces from the non-letter-size pieces; see sheet 'Ltr BD' in it. WP-Mitchell-3F.xls shows the development of the proposed rates.

II. SUMMARY OF TESTIMONY

Following is a summary of the three principal sections of this testimony.

Section III

Section III poses what seems, in the context of a complaint proceeding, the obvious threshold question: what is so wrong with current Periodicals rates as to justify a complaint proceeding seeking to effect their reform?

My answer to that question is essentially as follows:

1. Over a period that extends back into the 1980s, the increases in Periodicals rates have been greater than the increases in the Consumer Price Index, even after the reduced markups recommended by the Commission. The fact that this has been occurring makes it all the more important to search for other avenues of progress, on which this Complaint focuses.

2. Improvement in our understanding of costs in recent years has brought the existing deficiencies into clearer focus and has suggested new paths that cost recognition should follow. For example, the makeup of bundles, sacks, and pallets, including their entry points and associated interactions, are now understood to be important cost drivers, but these factors are all but neglected in rates. As a consequence, mailers often have no way of knowing or reason for caring that their decisions about mail preparation

1 and transportation are needlessly wasteful. If the factors that drive costs
2 were reflected in rates, mailers would respond accordingly.
3
4 3. Despite statutory language and legislative history that emphasize costs and
5 require recognition of the preparation of the mail, the Periodicals rate
6 structure still includes the highly inefficient unzoned editorial pound rate,
7 an outdated policy preference that thwarts adequate recognition of cost
8 incurrence. Maintaining this structure has interfered with the natural
9 forces that promote more efficient rates in every part of the Periodicals
10 rate design. For example, a variety of pound-oriented savings have been
11 converted into per-piece discounts in order to avoid undermining the
2 insensitivity of the editorial pound charge to actual cost incurrence.
13
14 4. If the pound rates for editorial matter were to vary with distance, the
15 marginal costs of printing and distributing would remain low relative to
16 revenues from advertising and subscriptions, even for the higher zones.
17 Therefore, publishers faced with zoned editorial pound rates would
18 continue to find it profitable to add higher-zone subscribers and would not
19 find reason to drop such subscribers or otherwise to limit the availability
20 of their publications based on the geographical proximity of the recipients.
21 An unzoned editorial pound rate is not required to make periodical
22 publications equally accessible in all areas or to promote the widespread
23 dissemination of editorial matter.

5. Because of the unzoned editorial pound rate, many local and regional publications that choose to print near their home base are unfairly charged elevated rates in order to support reduced rates for publications going greater distances.

Section IV

1. Section IV develops a schedule of rates designed to recognize costs efficiently and to give appropriate signals to mailers. The proposed rates are tied to the rates recommended by the Commission in Docket No. R2001-1; they preserve all discounts and rate structures to the maximum extent possible; they are revenue neutral; and they are based on the same volumes and billing determinants.

Section V

1. The proposed rates achieve improved consistency with the ratemaking factors set out in §§ 3622(b) and 3623(c) of the Act. They are more fair and equitable. Implicit cost coverages are more in line with principles of worksharing, efficient component pricing, and lowest combined cost.

2. Costs are recognized in the proposed rates in ways that are consistent with widely accepted rate-setting principles. The rates present mailers with the cost implications of their decisions and give them tools for dealing with

1 those implications in the form of incentives for more economical mailing
2 practices.
3
4 3. The proposed rates substantially improve the recognition of the effects of
5 the preparation of the mail on the Postal Service's costs. Specific
6 attention is paid to the handling and the makeup of bundles, sacks, and
7 pallets, and their associated entry points. Weight-related costs, however,
8 continue to be recovered in the pound charges, even when they are
9 incurred handling bundles.
10
11 4. The effects on mailers of any rate increases have been carefully
2 considered. The proposed rates move closer to rates that would be
13 generated by a competitive market at a measured pace that leaves room for
14 further improvement in the future. They would reduce cost averaging
15 across the subclass and increase the alignment of the rates of individual
16 mailers with the underlying Postal Service costs, but these steps are
17 tempered by consideration of potential impacts on individual mailers and
18 the desire to avoid undue burdens or extreme dislocations in intra-subclass
19 rate relationships. For example, no markups are proposed for the new rate
20 elements and higher-zone mailers would be faced with only the *additional*
21 costs associated with their mail. Also, many small publications will be
22 helped by the ADC presort level, the DBMC dropship rate, the recognition

of machinability, improvements in the pallet/sack differential, and improved dropship discounts for sacks.

5. The proposed rates are not unduly complex. They align with the operations that mailers perform in preparing mail and should be easy to understand. They avoid certain complexities in the current rates and diminish or eliminate a number of anomalies caused by the divergence of current rates from costs.

6. The proposed rates do not diminish the current recognition of the educational, cultural, scientific, and informational value of matter in Periodicals. The implicit cost coverages on editorial and advertising matter are not altered.

1 **III. WHAT IS WRONG WITH PERIODICALS RATES?**

2 Essentially, Periodicals (then denominated "second class") came into existence in
3 1879. In 1885, the rate was set at 1 cent per pound, independent of the distance
4 transported or the proportion of advertising. If a publisher failed to qualify for this rate,
5 he paid the third-class rate of 1 cent for each 2 ounces, fully 8 times higher. Clearly,
6 Congress intended not only to separate Periodicals for rate purposes but also to make the
7 rates extremely attractive.

8 Many adjustments in rates have occurred since that time, but Periodicals has
9 remained a separate class of mail throughout. Since the Postal Reorganization Act of
10 1970 (hereinafter Act), the rate level for Periodicals has been determined, except for
11 phasing provisions, by the application of a Commission-determined markup to
2 Periodicals costs. In a 1976 Amendment to the Act, Congress required that in selecting
13 markups, consideration is to be given to the "educational, cultural, scientific, and
14 informational [ECSI] value" of the mail matter conveyed. This consideration is
15 understood to apply in its strongest form to Periodicals.[1]

16 With this kind of history, one might expect Periodicals rates to be low and
17 attractive. But Periodicals rates are not low. They have been rising inordinately, and
18 their attractiveness is dwindling. One would be hard pressed to argue that this outcome is
19 consistent with what Congress expected. Something went wrong.

20 I do not contend that a few adjustments in the rates for Periodicals will solve all of
21 the problems. I do contend, however, that the current rates are inefficient to such a

[1] "Eligibility for the Periodicals class is conditioned, among other things, on a minimum amount of nonadvertising—or editorial—content. The presence of this type of content entitles all Periodicals mail to special consideration, given explicit statutory recognition of educational, cultural, scientific and informational value as a ratemaking criterion." PRC Op. R2000-1, p. 406, ¶ 5573 (footnote omitted).

degree that they do not conform to the policies of the Act and that improved rates that enhance efficiency will improve the lot of publishers. The purpose of this section is to explain some of the problems and to point to improvements. Then the next section discusses more specifically the improvements being proposed.

A. Periodicals Rates Have Been Increasing Too Rapidly

Particularly since the late 1980s, there has been concern that, due to rising costs, the rates for Periodicals have been rising inordinately rapidly. After years of efforts by mailers and the Postal Service to stem the rising costs, or even to agree about the reasons for the rise, the Commission said in Docket No. R2000-1:

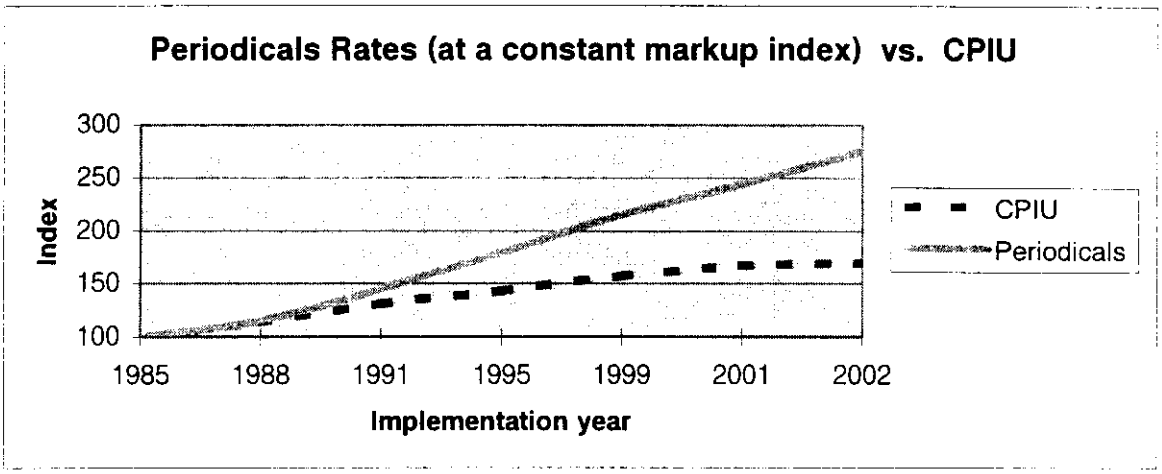
> The only conclusion is not comfortable: there are many reasons for believing that costs should have decreased; only a few factors that could be associated with increases; and a persistent net upward trend. It is clear that mailers and the Service must aggressively pursue the cost reduction opportunities identified on this record, and explore other aspects of the "operational realities" they face.

PRC Op. R2000-1, p. 412, ¶ 5593.

The extent of the problem is easy to illustrate. Graph 1 shows an index of Periodicals rates, at a constant markup index,[2] along with the Consumer Price Index, Urban (CPIU). The picture is disturbing. If no technological changes occurred and no scale economies were realized, and if factor prices increased in accord with inflation, then the index would be expected to increase with the CPIU.[3] As shown, however, the

[2] The notion of a markup index was introduced by the Commission in Docket No. R90-1 to help compare markups over time for specific subclasses when the average markup for all subclasses varies. The index is equal to the markup for a subclass divided by the average markup, both in percentage terms. If a rate were 6 cents and the cost were 4 cents, the markup would be 50 percent. If the average markup were 75 percent, the markup index would be 0.667 (50/75).

[3] Strictly speaking, this expectation requires an assumption that there have been no qualitative changes of significance in the product supplied by the Postal Service. If mailers switched to the use of pallets, for



Graph 1

Periodicals index has outstripped the CPIU, by a wide margin. Using the outcome of the 1984 rate case as a base, meaning that the indexes have a value of 100 in 1985, the Periodicals index increased to 275 while the CPIU increased to 170. The difference is substantial.

But the actual situation is worse than the picture. The Postal Service claims that important technological advances *did* occur during the period and that its total factor productivity (TFP) index increased 9.8 percent. It claims as well that it is realizing increasing returns to scale. In addition, some shifting to the use of pallets occurred, but a separate pallet rate did not exist.[4] This means that the most supportable expectation would actually be for the price index to be *below* the CPIU. Alternatively, if increases in real wages absorbed the gains from mechanization, palletization, scale, and other improvements, the rate index still should not exceed the CPIU. It is clear no such expectations have been borne out.

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example, but no separate cost-based pallet rate were reflected in the index (as was in fact the case during the period shown), one would expect the price index to *decrease*. Excepting pallets, it is not apparent that meaningful changes in the product have occurred. But if they have, possibly through the efforts of MTAC workgroups, the effect on the index would probably be to reduce rates, not to increase them.

1 This outcome is consistent with a phenomenon I have elsewhere referred to as
2 *negative technological change*. That is, mailers make cost-reducing adjustments (such as
3 the use of pallets), the Postal Service invests in advanced technology (such as flat sorting
4 machines and barcode readers), economies of scale are realized (consistent with the
5 Service's analysis of mail processing costs), and costs, corrected for inflation, do not
6 decline but *increase*.
7 By any measure, the situation is troubling. More effective measures to restrain
8 cost growth and to improve subclass efficiency are plainly needed. The most promising
9 measure—one that requires approval by the Commission—is to provide improved signals
10 in the rates for efficient conduct by aligning them more closely with Postal Service costs.
11
12 **B. Periodicals Rates Are Not Cost Based**
13 Under the Postal Reorganization Act of 1970, which supports recognition of costs
14 and of the preparation of the mail, a number of improvements have been made to the
15 Periodicals rate structure, all based on a record developed before the Postal Rate
16 Commission. In the first rate case, Docket No. R71-1, piece rates were introduced to
17 recognize that not all costs are pound related. The piece rates grew on a case-by-case
18 basis and now account for approximately 60 percent of Periodicals revenue; beyond this,
19 some evidence has been presented that the proportion should be even higher. It is clear,
20 then, that pound rates play a substantially lesser role than they did prior to reorganization;
21 indeed, the revenues obtained from the pound rates have gone from 100 percent down to
22 40 percent.

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[4] Note that since the Periodicals rate index is a constant-mix index, it is unaffected by volume shifts over the period among established worksharing categories. Changes in worksharing would, however, affect

1 In 1978, presort discounts were introduced, providing three separate presort tiers.
2 In 1985, dropship discounts (on a per-piece basis) were introduced for destination-SCF
3 entry. These discounts were subsequently expanded and refined to include both per-piece
4 and per-pound elements and to apply to destination area distribution centers and
5 destination delivery units. Saturation and high-density discounts were introduced in
6 1991, as were barcode discounts. In 2001 the number of presort tiers was expanded to
7 four. A pallet discount was introduced in 2002.

8 All of these changes improved the signals given to mailers, and they were all cost
9 based. As explained here and in other sections of my testimony, however, both the
10 quality of the signals and the extent to which costs are recognized are at this point
11 deficient. Our understanding of cost incurrence has improved substantially, especially in
12 recent years, as has the ability of mailers to respond to such incurrence. It is therefore
13 time to improve the signals and to take further steps in the direction of recognizing costs
14 in rates. Periodicals appears to be lagging other subclasses in this respect. There is little
15 question, for example, that some of the recent growth in the volume of parcel post has
16 been due to cost-based rate innovations, and Standard mail rates have been moving in the
17 direction of closer alignment with costs.

18 In times past, particularly when mailings were smaller and computers were rarer,
19 rate differences on the order of a cent per piece might not have been large enough to
20 evoke meaningful responses. But one of the realities of today's mailing environment is
21 that most mailers are reasonably sophisticated and have both the capability and the
22 willingness to analyze their operations and to respond to signals in rates. Today,
23 fractions of a cent can bring about meaningful alterations in the way mail is prepared,

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revenue-per-piece figures.

entered, and delivered. Even small changes in the parameters and constraints in mailing software can change the output in important ways, just by pressing the calculate button on a computer. When such capabilities on the part of mailers are neglected, and cost-based signals are not provided, the entire subclass suffers. It is important that we not let this continue to occur.

Disparities between costs and rates are in need of attention, despite the progress to date in the recognition of worksharing: (1) the *differences* among zones in the advertising pound rates are based on transportation costs only, and do not recognize that non-transportation costs also vary with distance; (2) the non-transportation portion of the dropship discounts (relative to zones 1&2), which is largely pound oriented, is given 50 percent on a per-piece basis; (3) many of the costs depend on the quantities and sizes of the bundles, sacks, and pallets in a mailing, but this fact goes largely unrecognized in rates; (4) the costs of handling bundles depend on the makeup (*e.g.*, ADC, SCF, 3-digit, or 5-digit) of their containers and where they are entered, but neither are these factors recognized in rates; (5) the one-half-cent per-piece pallet discount is based on a pound-oriented savings; and (6) the one-cent per-piece pallet discount is also based on pound-oriented savings and applies only to dropshipped pallets, although the savings exist for *all* pallets.

Many of these factors can be recognized in rates, and doing so would be in line with Commission emphasis in recent years on cost recognition, efficient component pricing, worksharing, and notions of lowest combined cost. Recognizing them would help the Postal Service to be a more effective delivery organization, and would improve the lot of mailers.

1 **C. Periodicals Rates Provide Poor Signals to Mailers**

2 Signals in prices are important throughout the economy. In fact, buyers (whether
3 firms or individuals) respond more strongly to price signals than to any other force I can
4 think of. Both firms and individuals watch out for their bottom line. The following story
5 may seem mundane and far removed from the economics of big business, but it is quite
6 relevant. I have a niece who lived in an apartment in Indianapolis for some years, and
7 had a cat. She told me that she left her kitchen faucet running slowly night and day, so
8 that her cat could get a drink. I asked her about her water bill. She said: "What
9 difference does it make? My water is included in my rent." Without appropriate signals,
10 people make inefficient decisions.

11 The current rates send underdeveloped signals to mailers, thus failing to provide
12 them with a reasonable and valuable avenue for responding to the high costs. It is
13 difficult to accept that putting mailers in this position is consistent with the ratesetting
14 guidance contained in the Act.

15 The following observations indicate the importance of signals generally and the
16 inadequacy of the signals given by the current rates.

17 Our understanding of cost incurrence and how it should be reflected in rates
18 progresses as we make advances in cost analysis. For many years, attention centered on
19 whether costs were piece-oriented or pound-oriented, with some recognition of cubic
20 measures in parcel post.[5] If only reality were so simple. More recently, attention has

[5] The reasoning has been that a marginal cost can be partitioned into a piece-related cost and a pound-related cost. If the number of pieces increases, say, 10 percent and the number of pounds remains the same (which requires a decrease in the per-piece weight), the piece-cost will increase 10 percent and the pound-cost will remain unchanged. Alternatively, if the number of pounds increases 10 percent and the number of pieces remains the same (which requires an increase in the per-piece weight), the pound-cost will increase 10 percent and the piece-cost will remain unchanged. It is not necessarily the case, however, that such a

1 focused increasingly on cost drivers and on linkages among cost drivers and volume.[6]
2 Part of the interest in cost drivers derives from the increased use of mechanization and
3 automation by the Postal Service. For example, with bundles now being sorted on small
4 parcel and bundle sorters (SPBSs), the cost of sorting bundles is virtually independent of
5 the weight of the bundles and the number of pieces in them. Similarly, with the use of
6 sack sorters and lift trucks, the costs of sorting sacks and pallets are virtually independent
7 of the nature of their contents.[7] Moreover, the processing these receive depends on their
8 makeup and their entry point. When these factors are not recognized in rates, mailers
9 cannot be expected to understand or respond to the costs of handling their mail. The rates
10 being proposed, by taking significant steps toward recognizing these factors, would
11 increase the efficiency with which mail is prepared and handled.
12 The current relationship between rates and actual processing is disjointed and
13 sometimes perverse, as James O'Brien explained in his testimony in Docket No. R2000-
14 1. (Tr. 24/11166). For example, the same carrier-route bundles receive different
15 processing and incur different costs depending on whether they are on 5-digit pallets or 3-
16 digit pallets. Yet, these pieces pay the same rates. Faced with such signals, mailers

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partitioning is always possible. That is, it is not always the case that the cost function, even for marginal cost in a relevant range, can be described well by an equation of the form MC = a * pieces + b * pounds.

[6] For example, see Michael D. Bradley, Jeff Colvin, and John. C. Panzar, "Issues in Measuring Incremental Cost in a Multi-function Enterprise," pp. 3-21, in *Managing Change in the Postal and Delivery Industries*, ed. Michael A. Crew and Paul R. Kleindorfer, 1997, Kluwer, Boston. Also see "Technical Report #1: Economic Analysis of Data Quality Issues," especially Chapter 2, *Data Quality Study*, prepared for the United States Postal Service, Contract No. 102590-97-B-1972, April 16, 1999. The Commission has emphasized reliance on cost drivers as well. In a discussion of transportation costs, for example, it said: "This step is viewed as relating to the behavior of pricing in the transportation markets in the sense that the cost at which transportation can be procured is related to the cubic-foot-miles of capacity involved; in the parlance used in recent years in such analyses, cubic-foot-miles of capacity is called a 'cost driver' of transportation costs." PRC Op. R2000-1, p. 169, para. 3250.

[7] One dimension of scale economies is that a larger-scale operation might have heavier bundles, sacks, and pallets. These economies cannot be realized if inappropriate signals are given to mailers.

1 cannot be expected to consider the cost implications of the preparation decisions they
2 make.

3 As another example, consider the tradeoff between bundles and sacks. In some
4 cases, mailers have a choice between preparing one 24-piece bundle and 24 sacks
5 containing one piece each, which would be sorted individually and taken intact to the
6 carrier. Processing the sacks is vastly more expensive than processing the bundle, but the
7 rates are the same. If the mailer, given appropriate signals, values the sacks and is
8 willing to pay for their handling, the outcome is not inconsistent with efficiency.
9 Alternatively, the mailer could decide that the return from using the sacks is not worth the
10 cost. But neither of these is happening, as the result of improper pricing signals.

11 Before Docket No. R90-1, the rates for Standard mail were uniform nationwide.
2 In that case, consistent with principles of efficient component pricing, lower rates were
13 allowed for mail entered at destination BMCs, SCFs, and delivery units. Going into the
14 case, the Postal Service estimated that 14.6 percent of Standard mail was dropshipped.
15 Today, 73.3 percent of it is dropshipped, and the efficiency of the class has increased
16 dramatically. Changes of this magnitude point to the efficacy of signals in rates in
17 promoting more efficient mailer behavior.

18 The difference between 14.6 percent and 73.3 percent represents an enormous
19 waste of resources, at the expense not of the Postal Service, since it is entitled by law to
20 charge rates that achieve breakeven, but of Standard mailers themselves. Until the advent
21 of correct price signals, however, they were helpless to do anything about it. Periodicals
22 mailers are currently in much the same situation.

1 It is not reasonable to expect publishers, or printers, or anyone else to consider
2 costs that do not affect their bank accounts. So, if the Postal Service charges no more to
3 deliver to more distant locations, it is unreasonable to expect printing bids to reflect the
4 additional transportation costs that the Postal Service incurs, or to expect the publisher to
5 recognize those costs.[8] In the extreme, if service were not an issue and rates were not
6 dependent on distance, all printing could be done in Guam and the publisher could not be
7 faulted for making a bad decision. But publishers collectively would nonetheless suffer
8 from such decisions, because *all* of the handling and transportation costs for Periodicals
9 *are* attributed to Periodicals, even if they are not transcribed into rates that recognize
10 actual handling and distance. If all publications were printed in Guam, handling and
11 transportation costs for Periodicals, and, accordingly, all Periodicals rates, would be
12 exceedingly high, although no publisher or printer would be right to regard his own
13 choices as the reason for those high rates.
14 The implications are clear. In order for publishers and/or printers to make
15 efficient decisions about distribution methods and/or printing locations, and thereby to
16 bring about efficient, low-cost postal services, postal rates must reflect the Postal
17 Service's costs. The extent to which they do so currently is limited. Insofar as
18 unnecessary or inefficient transportation over long distances is concerned, the problem is
19 two-fold. First, due to the unzoned editorial pound rate, the postage paid does not reflect
20 the higher *transportation* costs associated with the higher zones. Second, as Periodicals

[8] I am assuming that postage costs are included in printer's bids. Another possibility is for the printer to bid without postage and then somehow pass the postage through to the publisher. Either way, the publisher should be considering the postage.

rates have been developed thus far, neither does the postage paid reflect the higher *non-*transportation costs associated with the higher zones.

Recognition of the importance of rates as signals for efficient behavior is not new. In Docket No. MC95-1, where automation and bulk bypass were issues, the Commission said that "[r]ates send economic signals to mailers," that it "remains committed to adapting mail classifications and . . . rates to the demonstrated cost savings resulting from automated processing," and that its decision would "encourage mailers to provide mail that is compatible with automated processing and the bulk bypass of processing." PRC Op. MC95-1, pp. I-9-10, ¶¶ 1023-24. Rates that are better aligned with preparation options and their associated costs, as proposed in this Complaint, would undoubtedly have an effect on mailer decisions, whether it be on the sizes of the bundles, the containers selected, the makeup and contents of the containers, or the entry points. Mailer responses to these signals would make Periodicals more efficient as a subclass. One of the purposes of this case is to help make that happen.

D. Zoning the Editorial Pound Rate Will Not Reduce the Widespread Availability of Periodicals and Will Treat Local and Regional Publications More Fairly

1. History and purpose of the unzoned editorial rate

In the decades before the 1917 legislation on rates (40 Stat. 327, 328), several postmasters general expressed concern that the extraordinarily low rate at which second-class material was being carried (one cent per pound irrespective of distance) was a serious drain on public revenues.[9] "In 1901, Postmaster General Smith reported that the

[9] In 1901 President Roosevelt noted that second class "composed three-fifths of the weight but paid only about $4 million of the more than $111 million it cost to operate the postal service." *A Study of the Intent of Legislation on Second-Class Mail*, Rita L. Moroney, Research Administrator/Historian, United States

1 Government paid not less than 5 cents a pound for transportation of second-class matter
2 and at least 2 cents a pound for handling."[10] Transportation costs at that time, at least
3 relative to other postal costs, were obviously very large.

4 Following a detailed and exacting study of all 1908 postal costs, the Hughes
5 Commission found that 42.4 percent of second-class costs were for transportation (a
6 proportion that increased to 66.5 percent if costs characterized as "other transportation"
7 were added).[11] In contrast, transportation costs are now approximately 14.3 percent of
8 Periodicals costs, and only about two-thirds of these are distance-related.[12] If these
9 proportions are indicative, the importance of transportation costs then was at least three
10 times what it is now, and maybe higher than that.[13]

11 Despite the desire of the Post Office Department and two successive presidents
2 (Roosevelt and Taft) to do something about the situation, opposition from the
13 beneficiaries of the existing rate prevented anything from being accomplished until 1917,
14 when a Congress in urgent need of revenues to fund America's participation in World
15 War One acted to improve the alignment of second-class rates with costs.[14] After

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Postal Service, July 1977, p. 39. The magnitude of the sums involved can be inferred from the fact that total federal outlays in that year were $525 million. *Political Facts of the United States: 1789*, ed. Erik W. Austin (Columbia U. Press, 1986), p. 450.

[10] *Quoted in* The Report of the Commission on Second-Class Matter, Appointed Pursuant to the Joint Resolution of Congress, Approved March 4, 1911), *contained in* Message of the President transmitting The Annual Report of the Postmaster General for the Fiscal Year ending June 30, 1911 and The Hughes Commission Report, February 22, 1912, p. 65 (hereinafter Hughes Commission Report).

[11] Hughes Commission Report, at 127.

[12] Calculated from PRC Library Reference 9, Docket No. R2001-1. Only the distance-related transportation costs affect the relative levels of the zoned pound charges.

[13] Operations then and now may be comparable in terms of average haul. The Hughes Commission Report shows an average haul for subscriber second class of 602 miles, *id.* at 84, and the Postal Service's CRA for Fiscal Year 1989, the last year average haul figures were developed, shows an average haul for Regular second class of 724 miles. Similar figures can be developed, however, from the Periodicals billing determinants and the average hauls by zone. Doing this for the test year in Docket No. R2001-1 yields 464.8 miles for all of Outside County.

[14] The magnitude of the unexpected financial burden imposed on the federal government by World War One is indicated by the growth in total federal outlays from $713 million in 1916, to $1.95 billion in 1917,

1 extensive negotiation and compromise, a zoned rate structure was adopted for advertising
2 matter carried in second-class publications, with a lower, unzoned rate for editorial
3 matter.

4 The decision not to apply the zone rates but to arrange a low, clearly subsidized
5 rate for editorial matter was a compromise reached after publishers argued that applying
6 the zone rates uniformly would have deleterious effects on the distribution of
7 publications. The extremely low, unzoned rates for publications that had existed since
8 1885 had generated a powerful political constituency fiercely devoted to their
9 preservation, particularly the many highly successful nationally circulated publications
10 that tended to be edited and produced in the nation's great cities and to be transported
11 throughout the country virtually free of charge, courtesy of the Post Office. *The Saturday*
12 *Evening Post* and *The Ladies Home Journal* are familiar examples. It is therefore not
13 surprising that the arguments against zoning focused on the high costs of transportation
14 and raised the specter of a nation divided into separate regional publishing zones because
15 of cost prohibitive rates for mailing to subscribers in remote parts of the country.

16 When it last reviewed the question of zoning the full weight of publications, the
17 Postal Rate Commission emphasized similar concerns: "Witness Kielbowicz concludes:
18 'Public information found on the pages of periodicals should be just as accessible to the
19 residents of Washington State as to the residents of Washington, D.C.'" PRC Op. R90-1,
20 p. V-120, ¶ 5277. The *MOAA* court recognized that a concern of this kind, rooted in the
21 "rather broad anti-Balkanization principle" (2 F.3d 408, 436 (D.C. Cir. 1993)) expressed

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$12.7 billion in 1818, and $18.4 billion in 1919. After 1919, federal outlays would not top the $10 billion mark again until 1941. *Political Facts of the United States: 1789*, p. 451.

1 in the Act's definition of the Postal Service's purpose as "bind[ing] the Nation," prompted
2 the Commission's decision to maintain the unzoned editorial pound rate.
3 I do not see that a risk of publishing zones exists today. For one thing,
4 transportation costs are much lower than they were in 1917, making it highly unlikely
5 that publishers would find it profitable to drop subscribers in the higher zones.[15] And
6 even in the unlikely event that zoning of the editorial pound rates were to cause some
7 zones to be disfavored or dropped by some publications,[16] it is hard to see how, given all
8 of the other sources of information and avenues of communication now available, the
9 effect on the unity or cohesion of the nation could be significant.
10 Another factor that needs to be considered is the *funding* of the unzoned editorial
11 rate. Since the advertising rate appears to have been set at a level approximate to its
12 costs, any remaining shortfall in revenue had to be covered as part of the federal budget.
13 For all practical purposes, this continued until Reorganization in 1970. The situation
14 now, however, is that any relief in rates provided to one group of mailers is made up by
15 higher rates for other groups. Therefore, any evaluation of the effects of the unzoned
16 editorial rate on "bind[ing] the Nation" must include its effects on publications that are
17 disadvantaged by it, which would include all lower-zone publications. One well defined
18 group having this characteristic, as discussed further below, is local and regional
19 publications. The expectation would certainly be for them to print near their areas of

[15] For a detailed analysis of why zoning the editorial rate would be unlikely, in current circumstances, to alter the overall geographical pattern of publication distribution, or to diminish the "widespread dissemination of information," *see* Appendix A.

[16] It should not go unnoted that providing a subsidy to a wide group of publications in order to achieve certain behavior on the part of a small portion of that group is an extremely inefficient way to bring about a desired end, and should be avoided.

1 delivery, which leads currently to rates elevated by the benefit given to higher-zone
2 publications.
3
4 2. Impact of the unzoned editorial rate on local and regional publications
5 According to *The Magazine Handbook*, published by the Magazine Publishers of
6 America,[17] there were 17,321 different magazine titles published in the year 2002.
7 *Handbook*, p. 4. In Docket No. R2000-1, the Postal Service indicated that there were
8 9,679 Nonprofit permits and 22,798 Regular permits, with an overlap of 1,218.[18] These
9 numbers are large enough to contain subgroups of considerable size, an important one
10 being local and regional publications. Some of these publications are represented on the
11 Mailers Technical Advisory Committee by the City and Regional Magazine Association,
12 which has existed for 25 years and whose 87 member magazines have circulations
13 averaging in the range of 25,000 to 50,000. Most of the copies are delivered within a
14 given metropolitan area, and very few use In-County rates.[19]
15 The local and regional category includes publications devoted to particular
16 industries or professions, such as the eleven different construction magazines published
17 by McGraw-Hill, including *California Construction News*, *Colorado Construction*,
18 *Louisiana Contractor*, and *New York Construction News,*[20] publications centered on
19 individual cities, such as *Chicago*, *Cincinnati*, *Indianapolis Monthly*, and *Kansas City*
20 *Home Design*, state travel magazines, such as *Ohio* and *Wisconsin Trails*,[21] college

[17] *The Magazine Handbook* is available on MPA's website:
http://www.magazine.org/Government_Action/2408.cfm
[18] *See* Docket No. R2000-1, interrogatory response CRPA/USPS-T38-3, Tr. 17/6959.
[19] *See* http://www.citymag.org.
[20] *See* the McGraw-Hill web site http://regionalpublications.construction.com/.
[21] *See* http://www.magazinetime.com/categories-regional---local-mid-west.html.

1 alumni magazines,[22] regionally and locally oriented religious publications, and various
2 publications that cater to geographically concentrated ethnic communities or interest
3 groups, such as *The Baltimore Afro-American*.

4 Around the subclass average, a publication's implicit cost coverage is a function
5 of its proportion of advertising content, among other things. This reflects the recognition
6 of ECSI value. In order to abstract from this effect, and to allow balanced comparisons, I
7 assume that all local and regional publications have an average proportion of advertising
8 content. It follows that if they were average in other respects as well, their cost coverages
9 would all be equal to the average for the subclass. But these publications are not average
10 in other respects. Importantly, their final delivery occurs primarily in limited
11 geographical areas, regardless of where they are printed. I know of one city magazine
12 that is entered in zones 1 and 2. Ninety-four percent of its copies stay within those two
13 zones.

14 Another factor affecting publications' implicit cost coverages is their postal zone,
15 with respect to which local and regional publications may be viewed as falling into one of
16 two camps. Camp 1 is composed of publications printed in close proximity to their final
17 delivery area. These publications have short hauls and relatively high cost coverages.
18 They represent what would seem the natural and expected model for publications with
19 geographically concentrated subscriberships. Camp 2 is composed of publications
20 printed some distance from their delivery area and then carried to the delivery area by the
21 Postal Service. These publications have a substantial haul and relatively low cost
22 coverages.

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[22] The graduates of larger, more prominent schools that draw students from across the nation may be distributed widely, but there are thousands of smaller schools that draw largely from their own states and

1 Camp-2 publishers have made decisions to print some distance from their home
2 base. There is no reason to believe that these decisions were not rational, given the rates
3 they see. But these rates do not show them the full costs of their decisions and thus they
4 cannot be expected to make efficient decisions. Because the increase in postal rates
5 attendant to a decision to print at a distant location is less than the associated increase in
6 postal costs, Camp 2 publishers have unknowingly made decisions that imposed extra
7 costs on someone else. Camp-1 publishers, who are printing in close proximity to their
8 delivery area, are paying these extra costs, and thus are helping to finance longer-distance
9 mail.

10 Camp 1 publishers should not be discriminated against, and Camp 2 publishers
11 should not be blinded to the resource implications of their decisions. Both should be
12 given cost-based signals and then allowed to choose where to print. Those who decide to
13 print locally should not be required to pay elevated postal rates to help support publishers
14 who make different decisions or who mail more broadly.

15 The discussion thus far has assumed that local and regional publications have an
16 average degree of advertising content. This assumption is important to thinking clearly
17 about implicit coverages, cost-based rates, and the signals sent to mailers. But when one
18 begins to look at real situations and actual decisions, it is evident that the proportion of
19 advertising content is actually quite important. Consider, for example, a local publication
20 with little or no advertising, whose increase in postage with distance is therefore
21 negligible. The current rate structure puts the Postal Service in the position of saying:
22 "You can print your publications 3,000 miles from where your subscribers live if you
23 wish. We will carry it back at no additional charge. All of your freight will be paid by

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communities, and whose graduates tend to remain much closer to home.

1 other mailers." This is an extreme example of inappropriate signals in rates. In the case
2 of a *nationwide* publication distributed from one location, *some* of the copies will be
3 carried a considerable distance at no additional charge; in the case of a *local* publication
4 printed far from home, *all* of the copies will be carried a considerable distance at no
5 additional charge.

6 Publications whose subscribers are concentrated in limited geographic areas exist
7 naturally, because of who they are, and are not the result of plucking unusual
8 observations from the tail of a distribution. There is nothing random about them, and
9 they are not part of some kind of continuum that warrants averaging for rate purposes.
10 The local and regional grouping represents a legitimate focus and warrants attention. I do
11 not contend that this group should be singled out for any kind of preferred treatment, but
2 it certainly deserves to be treated fairly.

1 **IV. RATE DESIGN**

2 The rates developed in this section are for the Outside County subclass and are
3 aimed specifically at the weaknesses discussed in earlier parts of my testimony. In a
4 general sense, the costs of the mail are recognized in the rates, consistent with accepted
5 rate-design principles, in such a way that mailers are able to decide whether the value
6 they receive from higher-cost services is greater than the value they receive from lower-
7 cost services, after considering any costs they might incur to prepare their mail in one
8 way or another. Unless mailers are presented with the cost consequences of the decisions
9 they make, and unless they are given choices concerning preparation alternatives, it is not
10 possible for them to make decisions that result in the efficient use of the nation's
11 resources.[23] It is certainly the case that neither the Postal Service nor the Rate
12 Commission knows either the value that individual mailers receive from their use of the
13 mail or these mailers' costs of various preparation alternatives. But even if these values
14 and costs were known and understood, it would still not be possible to use them
15 effectively, on a mailer-by-mailer basis. Mailers, however, can do just that, given cost-
16 based rates.

17 More specifically, the rates developed here zone publications' full weight,
18 recognizing transportation costs according to the way they are incurred, and at the same
19 time recognizing alternatives associated with the preparation and usage of bundles, sacks,
20 and pallets. Mailers have alternatives in all of these areas, and it is accordingly important
21 that the cost-consequences of these alternatives be reflected in the rates. The non-

[23] Note that the postal costs associated with mailer decisions are costs not to the Postal Service only, but to the nation as well. It is not possible for the Postal Service to use resources to process and deliver the mail without the remainder of the nation giving up the use of those resources and the output associated with that

1 transportation portion of distance-related costs is reflected by allowing the charges for
2 containers to vary with the point of entry. As explained further below, for example, a 5-
3 digit sack entered at an origin facility receives more handling than the same sack entered
4 at a destination facility, such as an SCF.[24] Similarly, a 5-digit bundle in an ADC sack
5 receives more handling that the same bundle in a 5-digit sack.

6 In line with precedent, but with one modification, the degree of presortation is
7 recognized. The flow models developed by the Postal Service, which underlie the current
8 rates, give separate recognition to, among others, pieces sorted into mixed ADC bundles,
9 ADC bundles, and 3-digit/SCF bundles. Therefore, in order to follow costs, these three
10 presort levels are proposed. There is no change in recognition of sortation to the 5-digit
11 and the carrier-route levels, the latter including high density and saturation. For all
12 sortation levels except the carrier-route level, machinability is recognized, in addition to
13 the current recognition of prebarcoding. Note that the inclusion of SCF bundles in the
14 existing 3-digit category is consistent with the cost analysis on which the current rates are
15 based. For this reason, the costs behind the current rates are not well aligned with the
16 definition of the categories.[25]

17 While recognizing the distinctions necessary to allow mailers to make efficient
18 decisions, the rates developed preserve to the maximum extent possible the
19 recommendations of the Commission in Docket No. R2001-1. Specifically, the rates
20 preserve all applicable discounts, are based on the same costs and the same cost studies,

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use. When viewed in terms of other output forgone, the cost of inefficiently using resources for postal output becomes real indeed.

[24] Throughout my testimony, and in the proposed rate schedules, "origin" entry refers to entry at an office or other facility that is upstream of the destination BMC.

[25] There was no record evidence concerning this issue in R2001-1 and no indication that anyone focused on the problem. Now that it is clear, however, there is no reason not to recognize the issue in the rates. Indeed, costs are not available to properly support the former presort structure.

1 are revenue neutral, are based on the same volumes and billing determinants, and result in
2 the same cost coverage. Neither the In-County nor the Ride-Along rates are affected.
3 Existing palletization discounts are eliminated as separate rate categories, but the costs
4 avoided due to palletization are recognized more thoroughly and more uniformly via the
5 per-sack and per-pallet charges that vary by container type and entry point. As explained
6 below, three rate-design errors are corrected, one of which the Settlement Agreement
7 could have recognized.

8 An overview of the rates developed here should note that no argument is being
9 made, and no position taken, that any mailers *should* change the way they are preparing
10 their mail or that *all* mailers find themselves in situations where changes are feasible or
11 costless. Similarly, no position is taken that any mailers, given the rate signals and the
2 alternatives they currently face, are making poor preparation decisions. However, a
13 position *is* taken that mailers should be given cost-based signals in rates, and it *is*
14 believed that many mailers will then find it in their best interests to make changes.
15 Furthermore, the position *is* taken that these changes will improve the general situation of
16 Periodicals mailers as a class and the efficiency of Periodicals mail as a subclass.

17 The remainder of this section deals with specific topics important to the design of
18 the rates being proposed.

19 **Per-Piece Charges.** The per-piece costs, along with the associated volumes, are
20 provided by witness Stralberg, TW et al.-T-2. The volumes reconcile with those of the
21 Commission, as contained in PRC LR-9, Docket No. R2001-1. The top presort tier is for
22 pieces sorted into mixed ADC (MxADC or MADC) bundles. Within this tier, barcoding
23 is recognized, as in the current rates. Also, recognition is given to the machinability of

1 the pieces. Machinable pieces can be processed on the AFSM-100 and non-machinable
2 pieces (usually processed on the FSM-1000) cannot. The breakout, then, is non-
3 machinable (Non), machinable (Mach), barcoded non-machinable (Bar-Non), and
4 barcoded machinable (Bar-Mach).

5 Beyond this first tier, the tiers are ADC, 3-d/SCF, 5-d, and carrier route. Within
6 carrier route, high density and saturation are recognized, with discounts equal to those in
7 the current rates. The 3-d/SCF tier is slightly different from the current 3-digit tier, in
8 that it includes pieces sorted into SCF bundles.[26] This is done because the flow models
9 on which the current 3-digit discount is based include the costs for SCF pieces in the
10 costs for the 3-digit tier. One could argue, then, that the existing tiers are not defined
11 according to the costs behind them.

12 In Docket No. R2001-1, the rates recommended for barcoded pieces and carrier-
13 route presorted pieces recognized the associated *carrier* savings. Those savings were
14 derived from the carrier costing system and are not included in the costs developed by
15 witness Stralberg. In order to be consistent with the Commission's recommendations,
16 those savings are added to the differences derived from witness Stralberg's figures. The
17 savings for barcoded pieces are found in PRC LR-9, Discounts! cells D32-D53 (0.633
18 cents) and for carrier route in Discounts! cells D32-D59 (2.983 cents). Because the high
19 density and saturation rates are found by applying Commission discounts to the carrier-
20 route rate, no adjustments in them are required.

21 **Per-Bundle Charges.** The handling received by bundles depends on the makeup
22 of the bundles (whether they are mixed ADC bundles, ADC bundles, 3-d/SCF bundles, 5-

1 digit bundles, or carrier-route bundles) and the level of the container on (or in) which the
2 bundles reside. For example, a 5-digit bundle on an ADC pallet receives bundle sorts
3 before it is broken, while a 5-digit bundle on a 5-digit pallet does not. Within limits
4 allowed by Postal Service regulations, mailers have options concerning the sizes and the
5 makeup of bundles. Since the cost of bundle handling is relatively independent of both
6 the weight of the bundles and the number of pieces in the bundles, it is clear that makeup
7 can affect Postal Service costs. The charges shown are per bundle, depending on the
8 level of the bundle and its container.

9 **Per-Sack and Per-Pallet Charges.** Sacks are the traditional container for mail
10 and are handled in various ways. Pallets are more recent and are handled with lift trucks,
11 although pallet jacks are sometimes used. Intuitively, a cost is incurred each time a sack
12 or a pallet is handled, and this cost is relatively independent of both the weight of the
13 container and the number of pieces on (or in) it. Since mailers have options concerning
14 not only what kind of container to use but also container makeup, these costs should be
15 recognized in rates.

16 Sacks and pallets incur costs up to the point where their contents are removed and
17 processed further. Clearly, a container entered far from its destination receives more
18 handling than a container entered at its destination. Also, a container should not be
19 entered further downstream than its makeup. For example, an ADC container should not
20 be entered at a destination SCF, as it would then have to be hauled upstream to the ADC
21 for processing. The costs developed by witness Stralberg recognize the containers' levels
22 and entry points.

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[26]The Postal Service is expected to clarify preparation guidelines concerning 3-digit and SCF bundles. At the present time, there are relatively few SCF bundles. It may be that mailers will be required to exhaust

Because of their role in dropshipping activities, specific recognition in the proposed rates is given to the destination BMC, the destination ADC, the destination SCF, and the destination delivery unit (commonly DBMC, DADC, DSCF, and DDU, respectively). Facilities not qualifying as one of these are categorized as "origin" facilities. These include stations, branches, post offices, annexes, SCFs, P&DCs, ADCs, and OBMCs.[27] Costs do vary according to which of these facilities are used, but they are averaged, as in the current rates. Most mail is entered at larger facilities, and mailers often respect Postal Service preferences on entry arrangements. The respective entry points are recognized in the proposed rates for mixed ADC, ADC, 3-d/SCF, and 5-d/CR containers.

Zoned Pound Rates. The zoned pound rates are developed according to Commission procedures of long standing, with the modification that they apply to the publications' full weight. As usual, only the transportation costs are used in this development, separated, as typically done, according to whether they are distance-related, with the result that the *differences* in the zone rates reflect 100 percent of the variable transportation costs between any two zones for which the difference is calculated. Importantly, the higher zones do not pay any additional institutional costs relative to the lower zones. The scheme is as follows: DDU entry pays no transportation costs; DSCF entry and above pay non-distance-related transportation costs; and DADC and above pay distance-related transportation costs.

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the preparation of 3-digit bundles before preparing SCF bundles.

[27] In Docket No. R97-1, DBMC and OBMC facilities for Periodicals were referred to as Transfer Hubs. See Response of USPS to ABM interrogatory No. 6, Tr. 19A/8430. For dropship and other entry purposes, it is assumed that the Postal Service will specify the appropriate facilities for Periodicals, along with any submission requirements.

1 The first step in distributing the transportation costs is to develop a set of billing
2 determinants appropriate to zoning the full weight. This provides, for each entry point,
3 the weight in pounds of both the advertising and the editorial matter. Much of the
4 development needed was done by the Postal Service in Docket No. R2001-1 and is
5 contained in PRC LR-9. The calculations were done by recognizing that, even though the
6 *pounds* of editorial for DDU and DSCF entry are not reported separately, there has been a
7 *per-piece* discount for these entry points. Therefore, the number of pounds can be
8 estimated by multiplying the number of pieces by the per-piece weight. The Postal
9 Service also estimated the number of pieces entered in the DADC, so that the weight at
10 this entry point can also be calculated. For zones 1&2 through 8, the number of pounds
11 is estimated in my workpapers by assuming that pieces entered in these zones have an
12 average proportion of editorial content. The average proportion on a pound basis is used
13 for this calculation, not the piece-weighted average.
14 Normally, 100 percent of the distance-related transportation cost is distributed to
15 the zones, according to the proportion in each zone of total pound miles.[28] That is, 100
16 percent of the distance-related transportation cost is distributed on 100 percent of the
17 weight. Per-pound transportation costs by zone are then obtained by dividing the cost for
18 each zone by the total pounds in each zone. The *differences* among the zones in these
19 per-pound costs are preserved for advertising matter while, in order to cover other pound-
20 related costs and the benefit given to editorial matter, the absolute levels are increased.
21 Equivalently, 44 percent (approximating the proportion of the total weight that is
22 advertising) of the distance-related transportation costs could be distributed on 44 percent

[28] The average haul in miles for each zone is contained in PRC LR-9, which includes an average haul for DADC entry.

1 of the weight, and the *differences* would not affected. In Docket No. R2001-1, however,
2 the Postal Service distributed 50 percent of the distance-related transportation cost on 44
3 percent of the weight, thus obtaining inflated differences among the zones and inflated
4 pound rates for higher-zone mail. When asked about this procedure in a Presiding
5 Officer's Information Request (POIR), witness Taufique responded that "[d]istributing
6 approximately 44 percent of the transportation cost to the calculation of advertising
7 pound rates is more appropriate than the 50 percent allocation in the context of the Postal
8 Service proposal." Response of witness Taufique to Question 3, POIR No. 5, Tr.
9 11C/4512. Strangely, this error was not corrected in the Settlement Agreement. The
10 problem, however, goes somewhat beyond the Commission's question and Taufique's
11 response. According to Taufique's workpapers, only 40.47 percent of weight entered at
2 the DADC and above is advertising. Thus, 40.47 percent of the transportation cost
13 should be distributed to the advertising weight. In order to reduce the burden on higher-
14 zone mailers, indeed to reduce their rates so that they are aligned more fairly with costs,
15 this error is corrected in the rates being proposed.[29]

16 Two other errors of the Postal Service in Docket No. R2001-1 are corrected. As
17 shown in PRC LR-9, Pound Data_Adv!, cell E57, the Postal Service withheld a portion
18 (0.4 cents per piece) of the DSCF pound-rate discount from DSCF-entered mail.[30]
19 Correcting this error improves the alignment of rates and costs and is consistent with past
20 Commission recommendations. Also, on the same spreadsheet (see cells D58 and D59),
21 the Postal Service divided the transportation costs by only 75 percent of the weight of

[29] As developed in my workpaper WP-Mitchell-1F.xls, correcting this error would have resulted in a zone-8 pound rate for advertising of 56.6 cents per pound instead of the current 63.8 cents.
[30] Specifically, the reference to cell E49 should be removed from cell E57.

1 Science-of-Agriculture publications. Since the transportation costs are caused by the full
2 weight carried, the 75-percent restriction should be removed.

3 **Dropship Discounts.** In the current rates, dropshipping is recognized in several
4 ways. First, the pound rates for advertising are reduced according to the zone of entry,
5 including separate pound rates for DADC, DSCF, and DDU entry. Second, per-piece
6 discounts are offered for pieces entered at DADC, DSCF, and DDU locations. Third, an
7 increased pallet discount of one cent per piece is provided to dropshipped pallets. And
8 fourth, a special discount is added for a limited class of co-palletized pieces that are
9 dropshipped. All of these are based, in one way or another, on Postal Service savings.
10 However, not all of the savings for dropshipping are recognized. Specifically, no pound-
11 rate discount is provided for editorial, and no discount is provided to account for non-
2 transportation cost differences between the zone of otherwise entry and zones 1&2, the
13 latter being different for sacks and pallets. In addition, some of the discounts that *are*
14 given are not well aligned with costs.

15 The rates being proposed recognize dropship savings in both transportation and
16 non-transportation costs, in fairer, more balanced, and more appropriate ways. First, the
17 transportation savings are recognized in the zoned pound rates, which are proposed to
18 apply to the full weight of the mailing. Second, both the per-sack and the per-pallet
19 charges vary with the makeup of the container and, more importantly, with the entry
20 point of the container. Third, the per-bundle charges vary with the makeup of both the
21 bundle and the associated container. The rate schedule recognizes that a mixed ADC
22 container would not normally be dropshipped, and that an ADC container may or may
23 not be dropshipped. When the options are offered in this way, the question of

1 dropshipping is integrated with other alternatives mailers have, all of which have cost
2 consequences.

3 **Pallet Discounts.** As reviewed partially above, the current rates contain an
4 overlay of three pallet discounts. First, a one-half-cent per-piece discount is provided to
5 all pieces on approved pallets. Second, an additional one-cent per-piece discount is
6 provided to all pieces on dropshipped pallets. Third, effective April 20, 2003, as a result
7 of Docket No. MC2002-3, an even further discount of either one cent per piece or 0.7
8 cents per piece is provided, in order, for DSCF and DADC entry of qualifying *co-*
9 palletized pieces.

10 Generally, these discounts reflect costs in an uneven way and do not present
11 mailers with a true reflection of the cost consequences of their decisions. For example,
2 the savings on which the one-cent-per-piece discount (No. 2 in the previous paragraph) is
13 based exist whether or not the pallet is dropshipped, yet the discount is given only if the
14 pallet is dropshipped. This presents an unnatural incentive to remove potentially
15 attractive pallets from the Service's transportation system. Similarly, the savings on
16 which the co-palletization discount (No. 3 in the previous paragraph) is based exist for
17 both sacks and pallets, whether co-palletized or not, but the discount is given only for co-
18 pallets. In addition, on a per-piece basis, the cost of handling pallets as they move across
19 the country is less than the corresponding cost of handling sacks, but these differences are
20 not recognized at all. Finally, many, perhaps most, of the pallet savings are pound-
21 oriented; yet the discounts are given on a per-piece basis.

22 The recognition of pallets in the rates being proposed is uniform and cost-based,
23 as well as much simpler. It occurs implicitly through the per-sack and the per-pallet

1 charges that vary by container makeup and entry point. Mailers can make choices based
2 on container preferences, in view of the cost consequences of those decisions. At the
3 same time, the Postal Service will receive suitable compensation for handling containers,
4 including on its transportation equipment. No perverse incentives are provided.

5 **Recognition of Editorial Content.** In the past, editorial content[31] has been
6 recognized in rates in two ways. First, editorial matter in all zones and at all entry points
7 has paid a pound rate that has generally been set at 75 percent of the pound rate for
8 advertising going to zones 1&2. Second, since Docket No. R84-1, a per-piece editorial
9 discount has been provided, which now equals 7.4 cents times the proportion of editorial
10 content. If a piece has 70 percent editorial content, a per-piece discount of 5.18 cents (7.4
11 * 0.70) is allowed.

2 The funding for these lower rates has been provided by increasing *all* Periodicals
13 rates, both pound and piece rates, both advertising and editorial. In support of the
14 unzoned editorial pound rate, all of the pound rates for advertising have been increased.
15 When the editorial rate was then set at 75 percent of the increased zones 1&2 rate, the
16 editorial rate became higher as well. In support of the per-piece editorial discount, the
17 piece rates have been increased. If an average piece had 50 percent editorial, for
18 example, all piece rates would be increased by 3.7 cents (0.5 * 7.4), and then the piece
19 with 70 percent editorial would receive the 5.18-cent discount. The net reduction in the
20 piece's postage would be 1.48 cents (5.18 – 3.70). This reduction becomes an add-on for
21 pieces with a lower-than-average proportion of editorial content. Although the form of

[31] A definition of advertising is contained in the DMCS, which refers to content that does not qualify as advertising as non-advertising. Informally, non-advertising is often referred to as editorial. My testimony refers frequently to editorial content.

1 the per-pound editorial benefit is different in the rates being proposed, the funding
2 mechanism is the same.

3 Because of the lower rates provided to editorial matter, the cost coverage on
4 editorial matter has been considerably lower than the cost coverage on advertising matter.
5 As reference points, these "implicit" coverages can be calculated easily from the current
6 rates and the billing determinants behind them. Two packages of mail can be considered,
7 each identical in every way to the nation's total Periodicals mailings for one year, except
8 that one is all editorial and the other is all advertising. The revenue for these two
9 packages can be calculated at current rates. The two revenues can be compared to the
10 costs for the year, it being the case that the costs of handling editorial and advertising are
11 the same. When this is done, it turns out that the current cost coverage on editorial is
2 84.7 percent and the corresponding coverage on advertising is 129.5 percent.[32] On
13 average, the coverage is 101.3 percent. PRC Op. R2001-1, Appendix G, Schedule 1.

14 In the rates being proposed, these coverages on advertising and editorial matter
15 are maintained. Substantial deference is therefore provided to the educational, cultural,
16 scientific, and informational value of Periodicals, as required by § 3622(b)(8) of the Act
17 and as reflected in current rates. The current per-piece editorial benefit is maintained.
18 The per-pound benefit, currently skewed by distance, is provided in the form of a new
19 discount equal to 10.1 cents per pound of editorial matter. Arranging the editorial benefit
20 in this way does not favor some (longer-distance) editorial matter over other (shorter-
21 distance) editorial matter.

[32] These cost coverages are calculated before accounting for the benefit for the preferred categories, which generally lowers the coverage by about one-half percentage point.

1 It is reasonable to ask why it would not be better to arrange a per-pound editorial
2 benefit by allowing a suitable percentage reduction to the total pound charges. This
3 would provide a discount proportionate to postage and, therefore, generally,
4 proportionate to costs incurred.[33] Such a proposal, however, fails on two counts. First,
5 the higher-zone publications, which would have the higher pound charges and therefore
6 the higher discounts, have not been charged any additional institutional costs. Therefore,
7 even at subclass coverages some distance above those that currently exist, these
8 publications, after the percentage discount, would be paying below-cost rates. Second,
9 and perhaps more importantly, the zone charges are recognized in the dropship discounts,
10 and giving a percentage postage reduction would effectively reduce those discounts to
11 levels below avoided costs. The end result, then, would violate the principles of cost-
12 based rates, lowest combined cost, and efficient component pricing, which are critical to
13 bringing about efficient mailer decisions.
14 The damage that would be done to discounts by a uniform percentage reduction
15 for editorial can be illustrated easily. Assume the base rate is 20 cents and the
16 worksharing activity saves 4 cents. The rate for workshared pieces should then be set at
17 16 cents. If both workshare and non-workshare mailers were given a discount of 10
18 percent, the non-workshare mailers would be paying 18 cents (20 cents less 10 percent of
19 20 cents) and the workshare mailers would, similarly, be paying 14.4 cents. The
20 difference between 18 and 14.4 is 3.6 cents, less than the savings of 4 cents (20 cents less

[33] The argument in favor of a percentage discount would be that it is somehow unfair for highly workshared publications to be given a percentage reduction for editorial content that is larger than the percentage reduction given to less workshared publications. But, as explained in the text, this argument runs up against difficulties.

1 4 cents = 16 cents; 16 cents less 10 % of 16 cents = 14.4 cents). The signal, then, would
2 be inappropriate.

3 **Deference to Higher-Zone Material.** The unzoned editorial pound rate has
4 clearly provided considerable deference to higher-zone publications, depending, of
5 course, on their proportions of editorial content. Indeed, they are generally carried below
6 cost. It is reasonable to ask how these higher-zone publications would be treated under
7 the rates being proposed. The answer is that they would be treated quite favorably. By
8 design, the higher-zone publications would pay only the *additional* costs associated with
9 distant entry, and no additional fixed costs. Relatively speaking, then, their rates would
10 tend to exceed their marginal costs by less than the rates of other mailers, and rates equal
11 to marginal costs are generally understood to be ideal. The result is a high form of
12 consideration.

13 **Proportion of Revenue from the Pound Rates.** The proportion of Periodicals
14 revenue obtained from the pound rates has declined over time to a current level about 40
15 percent. To some extent, this proportion has been as much an input to rate design as an
16 endogenous figure based on costs and billing determinants. The procedure has been to
17 begin with a revenue requirement for the subclass (equal to total cost multiplied by the
18 cost coverage), and to obtain 40 percent of that requirement from the pound rates.
19 Conversely, 60 percent of the requirement is obtained from the piece rates.[34]

[34] When the procedure is mapped out in detail, account is taken of Ride-Along revenue and fees, plus the contingency and a small adjustment factor. Note that the proportion of revenue from the pound rates should be expected to change with the average weight per piece and therefore or should have been affected by the merger into Outside County of Nonprofit and Classroom. The result should also be affected by the discount received by Nonprofit and Classroom.

Of the revenue obtained from the pound rates, about 36 percent is accounted for currently by transportation costs.[35] The remainder, to the extent that the rates are cost-based, is accounted for by non-transportation costs that are pound-oriented.[36] To build these non-transportation costs into the pound rates, as well as to recover the revenue loss associated with the unzoned editorial pound rate, the usual procedure has been to develop first-cut pound rates based on transportation costs alone, and then to add an additional amount (23.8 cents per pound in PRC LR-~~8~~7, R2001-1) onto each zoned rate. Doing this does not affect the zone differences of the first-cut rates.

In the rates being proposed, some of these non-transportation costs (currently viewed as pound oriented) are covered by the per-bundle, per-sack, and per-pallet charges, as the associated costs are affected in some degree by weight. Therefore, in order to maintain an appropriate level for the pound rates, I adopted a reduced proportion for the pound rates, consistent with witness Stralberg's conclusion that about 30 percent of the costs are pound-oriented, and obtained 70 percent of the revenue from the per-piece, per-sack, and per-bundle charges. In effect, this assumes that 10 percentage points of the revenues formerly obtained from the per-pound rates should be obtained from the per-piece, per-bundle, per-sack, and per-pallet rates. This tie to the current rates seems reasonable.

Letter-Size Pieces. The Outside County subclass contains a number of letter-size pieces (hereinafter letters). Most of them, if not all, are prepared in trays, and any associated use of bundles, sacks, and pallets is undoubtedly quite different from the use of same by flats. Because of the differences in the way letters are handled and the

[35] Transportation costs are 14.3 % of total costs: 14.3% divided by 40% = 35.75%.
[36] One could argue that about 1.3 % of the pound revenue is a contribution to institutional costs.

1 associated inapplicability of the proposed charges for bundles, sacks, and pallets, it is
2 proposed that letters continue to pay the current rates.
3 Making this provision for letters requires an estimate of the amount of revenue
4 they generate, so that the remainder of the revenue requirement can be obtained from
5 non-letters. Postal Service Library Reference J-53 (R2000-1) shows that 4.3793 percent
6 of the total volume is letters. (See cell Class! G74 in spreadsheet SHP03U_1.xls.). A
7 partial breakdown of this proportion is contained in the billing determinants, which
8 provide the number of barcoded letters at each of the non-carrier-route presort levels.
9 The following assumptions were then made: (1) that there are no high density or
10 saturation letters; (2) that no pallet discounts are given for letters; (3) that no letters have
11 Ride-Along attachments; (4) that the ratio of letters to flats in the carrier-route category is
2 the same as the corresponding ratio for *all other* letters; (5) for the per-piece editorial
13 benefit and the per-piece discounts for DDU, DSCF, and DADC, that the number of
14 letters is equal to the billing determinant figure for these categories multiplied by the
15 proportion of letters in the subclass; (6) that letters are distributed among the zones in the
16 same proportions as the flats; (7) that letters in the Regular and the Classroom categories
17 weigh 2.5 ounces each; and (8) that letters in the Nonprofit category weigh 2.0 ounces
18 each.
19 Next, in order to complete the estimate, the ratio of barcoded letters to total
20 barcoded pieces was calculated for each of the non-carrier-route presort tiers, a factor was
21 applied to each of these ratios (the same factor for each ratio), and the result was applied
22 to the number of *non-barcoded* pieces in each tier. This factor, which was selected so
23 that the total number of letters came out at the correct level, turned out to be 48.13

1 percent. Thus, if 6 percent of the barcoded pieces in the basic presort tier are letters, then
2 the estimate is that 2.88 percent (6% * 0.4813) of its non-barcoded pieces are letters. It
3 makes sense that the proportion of letters in the non-barcoded categories is lower than in
4 the barcoded categories, because: a) the incentive for letters to barcode is larger than the
5 incentive for flats, and b) the equipment necessary to barcode letters is cheaper and more
6 readily available. The calculations leading to the estimate of letter revenue are shown on
7 sheet Ltr BD! of file WP-Mitchell-2F.xls, in my workpapers.

8 **Nonprofit and Classroom Publications.** In P.L. 106-384, Congress amended
9 the Revenue Forgone Reform Act (RFRA) (P.L. 103-123) to require that Nonprofit and
10 Classroom Periodicals be given a 5 percent discount on their total postage bill, excepting
11 postage due to the advertising pound rates or for commingled pieces. This provision is
2 accommodated in the rates being proposed.

13 **Science-of-Agriculture Publications.** As provided in RFRA, Science-of-
14 Agriculture (SoA) publications pay pound rates on their within-zones-1&2 advertising
15 equal to 75 percent of the corresponding rate for Outside County publications. Under the
16 proposed rates, this provision is satisfied. In general, SoA publications will benefit from
17 the proposed rates, since they have a short average haul. The proportion of SoA
18 publications going to zones 1&2 (and closer) is 73 percent, compared to only 59 percent
19 for all Outside County publications. The corresponding proportions for zone 3 and closer
20 are 90 percent and 68 percent. Also, SoA publications are highly presorted, 59.4 percent
21 to carrier route, compared to a subclass average of 42.1 percent. In effect, under the
22 unzoned editorial rate, SoA rates have been increased to help pay the costs of higher-zone
23 publications, even though SoA publications are predominately lower-zone.

1 **Schedule of Rates.** The complete schedule of rates, consistent with the

2 development described above, is shown below.

3

4 **Proposed Rate Schedule – Outside County Periodicals – Non-Letters**

PERIODICALS RATES									
Per Piece		Per Bundle		Per Sack		Per Pallet		Per Pound	
Bundle Level Piece Description		Container Level Bundle Level		Sack Level Entry Point		Pallet Level Entry Point		Distance (Zone) From Entry Point	
Bundle/ Piece	$/Pc	Container/ Bundle	$/Bundle	Sack/ Entry Pt.	$/Sack	Pallet/ Entry Pt.	$/Pallet	Entry Zone	$/Pound
Mx. ADC		**Mx. ADC**							
Non	0.440	MADC	0.260	**Mx ADC**		**ADC**			
Mach	0.310	ADC	0.320	Origin	1.53	Origin	40.44	DDU	0.145
Bar-Non	0.386	3-D/SCF	0.340			DBMC	26.90	DSCF	0.166
Bar-Mach	0.264	5-D	0.370	**ADC**		DADC	13.67	DADC	0.174
ADC				Origin	3.25			Z 1&2	0.191
Non	0.321			DBMC	2.37			Zone 3	0.206
Mach	0.275	**ADC**		DADC	1.29	**3-D/SCF**		Zone-4	0.244
Bar-Non	0.290	ADC	0.100			Origin	40.02	Zone-5	0.301
Bar-Mach	0.241	3D/SCF	0.170	**3-D/SCF**		DBMC	26.90	Zone-6	0.362
SCF/3-D		5-D	0.200	Origin	3.22	DADC	25.72	Zone-7	0.436
Non	0.307	CR	0.210	DBMC	2.37	DSCF	13.67	Zone-8	0.498
Mach	0.260			DADC	2.02				
Bar-Non	0.280			DSCF	1.29				
Bar-Mach	0.230	**3-D/SCF**				**5-D**			
5-D		3-D/SCF	0.110	**5-D/CR**		Origin	42.39		
Non	0.233	5-D	0.180	Origin	3.30	DBMC	30.46		
Mach	0.210	CR	0.190	DBMC	2.78	DADC	24.58		
Bar-Non	0.225			DADC	2.10	DSCF	17.05		
Bar-Mach	0.194			DSCF	1.73	DDU	1.57		
CR Basic	0.121	**5-D/CR**		DDU	0.93				
CR HD	0.089	5-D	0.000						
SAT	0.081	CR	0.080						
Piece Sorting Delivery		Bundle Sorting		Sack Handling/Sorting Sack Opening Sack Return		Pallet Handling Pallet Opening Pallet return		Transportation Bulk Handling Some Piece Sorting Delivery	

Per-pound Editorial Discount, cents per editorial pound	10.1
Per piece editorial discount, cents times editorial percent	7.4
Per-piece charge for qualified Ride-Along pieces, cents	12.4

5

1 **V. COMPLIANCE WITH REORGANIZATION ACT**

2 In addition to certain general policies, the Act identifies two specific sets of
3 factors that should be included in considerations leading to rates. One set is found in §
4 3622(b) and the other in § 3623(c). Although there is overlap, the former set is specified
5 as applicable to changes in rates and fees, and the latter set as applicable to "changes in
6 the mail classification schedule." § 3623(b). In practice, the former set has received its
7 greatest scrutiny in regard to selecting markups for the various subclasses and services,
8 consistent with breakeven, as is typically done in omnibus rate cases. They are
9 important, then, as much or more in a relative sense as in an absolute sense.

10 The rates being proposed are guided by an interest in giving mailers more
11 appropriate signals. The belief is that such signals will bring about more efficient
12 decisions, which will improve the efficiency of the class, the lot of the mailers, and the
13 contribution that periodicals make to the nation. Practically speaking, the rates being
14 proposed recognize more effectively the costs of bundles, sacks, and pallets, and
15 associated interdependencies, including entry points, in a way that aligns operationally
16 with decisions mailers make. To an extent, then, the changes focus on the implicit
17 markups of mail categories (some of which may be viewed as new), a process the
18 Commission has indicated is at the heart of rate design.[37] [38] No changes in subclass
19 markups are proposed.

[37] The phrase "implicit coverage" (or "implicit cost coverage") is used in rate proceedings to refer to cost coverages calculated for categories or other groupings of mail that fall *within* subclasses. Such coverages are usually expressed in percentage terms. The numerical value of an implicit coverage is not necessarily *implied* by anything other than that the numerator is the revenue of the category and the denominator is the corresponding cost. In percentage terms, the implicit *markup* equals the implicit coverage minus one hundred percentage points.

[38] See PRC Op. R2000-1, p. 390, ¶ 5533, where the Commission said: "Rate design for a subclass can be thought of as setting the implicit percentage markups for each rate category."

Periodicals has long been regarded as the class with the most complex rate structure. To the extent that this is true, it has been because of: a) the way in which rates differ for editorial and advertising content and b) an interest in being at the forefront of recognizing costs in rates.[39] At any particular time, however, cost recognition is limited by the data that are available, the analysis that has been done, and our understanding of the mail and its markets. Especially with the improved flow models now being used, our perspective is much better than it was even a few years ago. Accordingly, this case can be viewed as a significant step in the appropriate recognition of costs and in bringing Periodicals into suitable alignment with the criteria in the Act.

It is not necessary to decide which set of criteria is most applicable to the changes being proposed. Both sets are important in their own right and should be included, as applicable, in all rate considerations. They are considered here. My discussion of these criteria should not be viewed as legal opinion, as I do not claim expertise in that area. It *is* my opinion, however, that the criteria primarily employ practical language and economic terms of art, and that most, if not all, refer to concepts that are susceptible to being understood by economists and rate practitioners. It is from this perspective that I testify.

Section 3622(b) identifies nine specific criteria, listed below:

1. the establishment and maintenance of a fair and equitable schedule;

2. the value of the mail service actually provided each class or type of mail service to both the sender and the recipient, including but not limited to the collection, mode of transportation, and priority of delivery;

[39] Another point worth noting is that since all periodicals are required to have a frequency of publication and a list of subscribers or requesters. Periodicals mailings are to a considerable extent repetitive. Thus, once mailing arrangements are made, any associated efficiencies can be realized over and over.

3. the requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributed to that class or type plus that portion of all other costs of the Postal Service reasonably assignable to such class or type;

4. the effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters;

5. the available alternative means of sending and receiving letters and other mail matter at reasonable costs;

6. the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service;

7. simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees charged the various classes of mail for postal services;

8. the educational, cultural, scientific and informational value to the recipient of mail matter; and

9. such other factors as the Commission deems appropriate.

Section 3623(c) identifies six specific criteria that are to be included in the consideration of classification changes. They are:

1. the establishment and maintenance of a fair and equitable classification system for all mail;

2. the relative value to the people of the kinds of mail matter entered into the postal system and the desirability and justification for special classifications and services of mail;

3. the importance of providing classifications with extremely high degrees of reliability and speed of delivery;

4. the importance of providing classifications which do not require an extremely high degree of reliability and speed of delivery;

5. the desirability of special classifications from the point of view of both the user and of the Postal Service; and

6. such other factors as the Commission may deem appropriate.

Sections 3623(c)(3) through (c)(4) do not apply to this proposal. Also, § 3622(b)(5), focusing on alternatives, does not apply. The remainder of the criteria are considered.

Sections 3622(b)(1) and 3623(c)(1), Fairness and Equity

In both sections, criterion number one indicates that consideration should be given to the fairness and equity of the rates. Although fairness and equity are sometimes viewed as existing in the eye of the beholder, and therefore as matters of opinion, there are several generally accepted notions that are usually thought of as being indicated. First, fairness and equity require that similarly situated mailers be treated similarly. I believe the rates being proposed move strongly in the direction of meeting this requirement. In accordance with widely accepted rate-design principles, they recognize similarities and differences in bundle preparation, sack usage, and pallet usage. They also recognize similarities and differences in entry patterns, entry points, and distance transported. In addition, they reduce the extent to which mailers will find their rates influenced in undesirable ways by the practices of dissimilarly situated mailers whose rates do not reflect cost incurrence.

Another reflection of fairness and equity involves the extent to which the rates reflect costs. On this point, the Commission has explained:

> The Commission begins the rate design process assuming equal implicit markups. This is a neutral starting position which seems to be implied by § 3622(b)(1), a fair and equitable schedule. It is consistent with the Commission's general policies that the rates for each rate category be above cost; that rates reflect the costs developed in the record; and that rate design results in identifiable relationships between rate categories. Equal implicit

> markups, however, are only a starting place, and often may not be practical or appropriate.
>
> The Commission bases worksharing discounts on avoided costs. Basing discounts on avoided costs does not result in equal implicit markups, rather it results in equal per-piece markups. It also results in worksharing mail having higher implicit markups than mail which is not workshared and the most heavily workshared pieces *(i.e.* those with the largest discount) having the highest implicit markups.
>
> This approach to worksharing discounts is called "efficient component pricing" (ECP) in the economic literature. The theory requires the discount to be 100 percent of the cost savings. The Commission tries to achieve 100 percent passthrough of the worksharing savings, but again it frequently may depart from this standard for a variety of reasons. An important virtue of ECP is that the mailer will perform the workshared activity *(e.g.* presort) when he can do so at a lower cost than the Postal Service. This leads to productive efficiency *(i.e.* the most efficient provider does the work resulting in the lowest cost to society). Because ECP also lowers the real cost of mailing, volume should increase in response to lower effective prices.

PRC Op, R2000-1, p. 390, ¶¶ 5533-35.

The rates being proposed reflect costs fairly and lead to implicit markups that are consistent with notions of efficient component pricing and the appropriate recognition of worksharing activities. The costs of bundles are recognized in the rates for bundles, according to their makeup and the processing they receive. And the costs of sacks and pallets are recognized in their rates, according to the way incurred. In all cases, the makeup of the containers is recognized, consistent with their entry point. The converse of developing implicit markups in this way is that it is fair for mailers to face in rates the costs of their own mail and their own preparation decisions, and that it is fair for mailers to see in rates a reflection of the resources absorbed by their mail.

There are three more notions of fairness that warrant note. First, it is fair to give mailers tools for responding to the situations they face, and for influencing the market

1 into which they are essentially locked.[40] As explained earlier in my testimony,
2 Periodicals mailers have faced substantial rate increases for nearly two decades. They
3 have sought options for cooperating with the Postal Service in ways that would help both
4 sides. They have been willing to invest of themselves and make changes, if only given
5 the options and the appropriate signals. They have found themselves *with* the motivation,
6 but *without* the tools. The proposed rates provide mailers with a broader range of signals
7 relating to costs and resource usage. The rates place a little more of the outcome in the
8 hands of the mailers themselves, so they can do more than stand and watch. I believe this
9 is an inherently fair thing to do.
10 Second, to mailers that dropship, it is fair to provide a rate reduction equal to the
11 Postal Service's associated cost reduction. The existing rates are deficient in this regard;
2 the proposed rates are not. Costs mailers incur preparing and submitting their mail may
13 be irrelevant to determining economically efficient rate levels, but they are not irrelevant
14 to fairness. They point as well to the importance of assuring that accepted rate-design
15 principles are honored, such as those associated with efficient component pricing.
16 Besides, it seems unfair on its face for the Postal Service to find itself in the position of
17 saying: "We understand that you may dropship in order to meet subscriber needs and to
18 achieve a viable product, and we are giving you that option. But when you do it, your
19 reduction in rates will be considerably smaller than our reduction in costs, so that we will
20 be extracting a higher per-piece contribution than before, and your implicit markup will
21 be elevated far more than might be expected under accepted worksharing principles.

[40] The Private Express Statutes, as I understand they are interpreted, do not prevent rivals from competing with the Postal Service for the delivery of periodicals. However, the mailbox rule places a severe constraint on potential (and actual) private operators. If it were not for that rule, I am confident that private operators would be delivering a substantial portion of periodicals today.

1 Furthermore, we are going to use that extra contribution to help provide lower rates (in
2 many cases below-cost rates) to mailers who do not dropship."
3 Third, it is an axiom of regulatory theory that the rates that would be generated by
4 the forces of a competitive market, were such a market possible, are fair and equitable
5 rates, and that regulation should tend to replicate such rates, where feasible. It seems
6 clear that competitive rates would be based on the costs of providing the service and that
7 the rates for mail entered at the destination would be based on the costs to accomplish
8 delivery from that point. Periodicals rates at the present do not meet this test, while the
9 proposed rates do.
10 **Sections 3622(b)(2) and 3623(c)(2), Value**
11 These sections refer in one way or another to the value of the mail matter and the
12 mail service to the sender and the recipient. The rates being proposed, along with the
13 associated rate structure, are designed specifically to allow mailers to focus on the value
14 they place on various kinds of service, and at the same time, on the costs to the Postal
15 Service and to the nation of providing those services. Consider sacks, for example. The
16 cost of handling a sack is relatively independent of the amount of mail in the sack. This
17 means that a sack could have one 5-pound bundle or several bundles totaling 30 pounds.
18 Under the proposed rates, the mailer using sacks can focus on the value of using the sack,
19 with various contents. If the sack is the preferred alternative and is worth the cost, the
20 mailer will use it, and will pay for the resources required. Importantly, and fairly, no
21 other mailer will be required to help finance that decision. On the other hand, if the
22 mailer decides on a different alternative, he will be able to evaluate that alternative in
23 view of its costs and the value placed on it.

1 Considerations of value are unique to each mailer. Neither the Postal Service nor
2 the Rate Commission can presume the value that various mailers place on various
3 alternatives. But when the cost of each service is reflected in the rates, each mailer can
4 make his own assessment, given his own value determinations. Nothing is wrong with a
5 mailer using a higher-cost service, as long as he is charged for that service. The Postal
6 Service, under these conditions, incurs the costs and passes them on to the mailer.
7 Neither the Postal Service nor the mailer would be better off if the mailer chose a
8 different service and the Postal Service's costs were lower.

9 **Section 3622(b)(3), Costs**

10 This section has been interpreted, for the most part, to require that *subclasses* of
11 mail recover their costs, with appropriate cost coverages. But, as the Commission noted
12 in Docket No. R2000-1, quoted also above "[r]ate design for a subclass can be thought of
13 as setting the implicit percentage markups for each rate category." Op. p. 390, ¶ 5533.
14 Clearly, the interest in tracing costs goes well below the subclass level as, I believe, it
15 should. Indeed the contribution that the classification approach makes to the setting of
16 appropriate rates is that it helps provide a fair path to establishing rates for particular
17 mailpieces that recognize their costs and other appropriate factors. If the cost coverages
18 on particular mailpieces were found to be substantially higher than the coverage for the
19 subclass as a whole, or even if substantially lower, including the possibility of coverages
20 below 100 percent (indicating below-cost rates), a case could be made for inquiry into
21 whether the pieces are appropriately classified and rated. Much of the history of
22 ratemaking under the Reorganization Act has involved questions of whether new rate

categories (within subclasses) should be established and of how these categories should be priced.

The Commission has often shown an interest in the cost coverages on particular groups of mail within subclasses. For example, after considering the coverage on Standard mail above and below the break point, it concluded:

> The Commission hopes that reliable information on implicit markups may make it possible to calculate the total amount of revenue that should be obtained from pieces above and from pieces below the break point. This would be an important contribution to ensuring that intra subclass rate relationships for Standard Mail are fair and equitable. The separate issue of the best way to design rates for the pieces above and below the break point might also be addressed by studying implicit markups.

PRC Op. R2000-1, p. 392, ¶ 5540.

Similarly, in regard to the Residual Shape Surcharge in Standard, on the same record, the Commission said:

> Several objections raised on this record were also presented and resolved in Docket No. R97-1. In essence, these include arguments that there is no cost coverage requirement below the subclass level; that costs should not be "blended"; and that other mailers have not objected to "averaged" costs. The Commission has once again considered the validity of these arguments, but finds no sound reasons to depart from its previous conclusions. In general, the Commission continues to believe that overall considerations of fairness and equity and an interest in cost-based rates overcome opponents' objections.

PRC Op. R2000-1, p.357, ¶ 5436.

The rates being proposed are designed to track costs within the subclass, and to do so in a way that aligns with decisions mailers must make about their mail. They are in line with interests the Commission has expressed in cost-based rates and in implicit markups.

1 In addition to a general interest in tracking costs and in giving mailers appropriate
2 signals concerning the resource requirements of *their* subclass, improvements are made in
3 three specific categories within Periodicals that now have what may be called *deviant*
4 cost coverages. First, as discussed in the Rate Design section above, Science-of-
5 Agriculture publications have a much lower average haul than the Periodicals subclass.
6 They are, therefore, paying rates that are elevated in order to help finance discounts for
7 higher-zone mail. It would seem more reasonable for them to receive their
8 congressionally provided discount from a cost-based rate than from one that is elevated.
9 This end is achieved in the proposed rates.
10 Second, a more general perspective on the extent to which the Periodicals rates
11 track (or do not track) costs is provided by a comparison with In-County rates. Under
12 RFRA, the markup on In-County is one-half the markup on Outside County. The latter
13 being 1.3 percent, it follows that the former is 0.65 percent. Therefore, for all practical
14 purposes, both sets of rates are at cost. All In-County publications are entered at what is
15 essentially their destination. Therefore, the rate for DSCF-entered In-County
16 publications is an at-cost rate. We know, then, that if Outside County rates were cost
17 based, the rate for DSCF entered Outside County pieces would be near the corresponding
18 In-County rate, for there is little reason to believe that the costs of handling the pieces
19 would be different. It turns out, however, that the Outside County rate is in the
20 neighborhood of twice the In-County rate. This suggests that the low-zone rates for
21 Outside County Periodicals are elevated above costs to a degree that cannot be called
22 anything but excessive, and therefore that higher-zone periodicals have rates that are
23 substantially below costs.

1 Third, as discussed in Section III-D, local and regional publications as a group,
2 entered in their associated areas, are paying rates that are elevated to help provide lower
3 rates for higher-zone mail. And if these publications are printed and entered at distant
4 locations, they pay rates that do not recognize the Postal Service's additional costs, and
5 they thereby impose additional costs on other mailers. Nothing in this pattern of charges
6 relates the rates to the costs incurred. In fact, these publishers are part of the group
7 discussed in the previous paragraph, which is paying excessive rates, a situation
8 addressed by the proposed rates.

9 **Section 3622(b)(4), Effects of Rate Increases**

10 It has been common in rate proceedings to set rates in such a way as to temper the
11 effects on mailers that receive substantial increases. On the other hand, it is important to
12 take meaningful steps toward improved and meritorious rate positions.

13 The proposed rates will have effects on mailers and some of them may be viewed
14 as substantial, meaning, of course, that the mail involved has been the beneficiary for
15 some time of rate preferences. But the impact is limited. For one thing, the amount of
16 revenue obtained from the bundle, sack, and pallet charges, is only about 21 percent of
17 the total revenue requirement, and no markup is proposed on these charges. For another,
18 some of the effects are due to improvements in the piece charges, in that ADC
19 preparation is no longer averaged with mixed ADC and non-machinability is recognized.
20 Many small mailers will benefit from these changes. In addition, it may be important to
21 mailers of smaller quantities that a new DBMC dropship discount is proposed, that the
22 pallet discounts are not restricted to dropshipped mailings, and that improved dropship
23 discounts are proposed for pieces in sacks.

1 More importantly, however, the proposed rates focus on a range of cost-driving
2 factors over which mailers have control and to which mailers would be expected to
3 respond. In general, Periodicals mail is prepared using computers and commercially
4 available software. In using such, inputs and constraints must be selected, like sack
5 weight, pallet weight, bundle weights, and preferences relating to sack and bundle
6 makeup. In addition, mailers will face improved signals relating to machinability and
7 barcoding. If the reality of the costs behind these signals is hidden by excessive
8 tempering, mailers will not understand the cost consequences of their decisions and
9 efficient changes will not be made.

10 **Section 3622(b)(6), Preparation**

11 This criterion requires that consideration be given to the "degree of preparation of
12 [the] mail . . . by the mailer and its effect upon reducing costs to the Postal Service."
13 The importance of this criterion, and the role it has played, is great. It has been the basis
14 and justification for a wide and still evolving range of worksharing discounts, which have
15 set the United States apart from most countries of the world.[41] In addressing, as it does,
16 the general issue of "preparation," its importance goes beyond issues of worksharing *per*
17 *se* and to issues of the nature of the mail itself, for the preparation of mail involves
18 decisions on bundles, containers, and entry points. These issues are addressed
19 specifically by the rates being proposed.

20 One of the great failures of the current rates is the extent to which they do not
21 allow mailers to see the cost effects or the efficiency implications of the decisions they

[41] See: Elcano, Mary S., German, R. Andrew, and Pickett, John T., "Hiding in Plain Sight: The Quiet Liberalization of the United States Postal System," in Michael Crew and Paul Kleindorfer, *Current Directions in Postal Reform*, pp. 337-52, 2000, Kluwer, Boston. Also, the Commission said: "The concept

1 make. Mailers cannot be expected to do what is best when they are given financial
2 incentives to do something different. Yet these same mailers are forced to live with the
3 cost implications of their decisions, because the rates they pay are ultimately based on
4 costs.

5 One could argue that mailers are hamstrung; they want to do something to help,
6 but are given no guidance. The proposed rates break through this blindness and allow
7 them to consider the efficiency improvements that are possible by aligning preparation
8 decisions with the value of the service and its associated costs. Mailers will be expected
9 to do nothing more than watch out for their own best interests, and at the same time reap
10 the efficiency benefits of being able to balance the benefits and the costs. The overall
11 efficiency of the Periodicals subclass should increase.

12 **Section 3622(b)(7), Simplicity**

13 This section is referred to, in shorthand, as focusing on simplicity and complexity.
14 But it goes on to highlight the importance of "identifiable relationships between the rates
15 . . . charged." It is true that one could argue for simplicity at any cost. In fact, a postal
16 official, not especially knowledgeable in rates, once asked me: "Why don't we just
17 charge them all a quarter and get it over with?"

18 As rates become simpler, however, fairness declines, the efficiency of the
19 subclass declines, costs get ignored and become inflated, mailers are given poor signals
20 concerning what is best to do, and rates increase. To their credit, Periodicals mailers
21 have not generally argued for simplicity. They use computers to prepare their mail and
22 are able to respond to the signals in rates.

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of worksharing has been widely applied and is credited with helping the Service to attract expanding volumes of mail and to improve its productivity." PRC Op. MC95-1, p. III-26, ¶ 3068.

1 The rates being proposed may appear complex, but they are orderly and
2 identifiable. Also, they are not adorned with special discounts, restrictions, or
3 surcharges. There are per-piece charges, per-bundle charges, per-sack charges, and per-
4 pallet charges. The charges depend in clear ways on the makeup and entry point of the
5 containers. The purpose of the charges is clear. The options of the mailers are also clear.
6 And, the charges are for things that mailers know and understand: mailers understand
7 presorting, barcoding, and machinability; mailers know how many bundles they have and
8 their makeup; mailers understand their usage of sacks and pallets; and mailers are keenly
9 aware of their entry points. Indeed, one of the great advances of recent years has been
10 the development of dropship software and the integration of such programs into trucking
11 operations.

12 Part of the attractiveness of the proposed rates is their freedom from the
13 complexities caused by the split nature of the pound rates that now exist. Under the
14 unzoned editorial pound rate, the rates are skewed away from costs in a way that presents
15 an endless array of anomalies and administrative difficulties. Several examples will
16 illustrate this point. First, printers see dropship discounts that depend on the proportion
17 of editorial content. Accordingly, two publications, identical except that one has more
18 editorial than the other, might have to be scheduled and handled differently. This causes
19 disparity in printing practices, for no apparent reason.

20 Second, discounts are difficult to arrange. In connection with the non-
21 transportation savings for DSCF and DDU entry in Docket No. R2000-1, witness
22 Taufique said:

23 The allocation of these non-transportation cost savings to pounds
24 and pieces is one area where my proposal differs from the R97-1

> Commission methodology. Instead of a 50/50 split, the Postal Service is proposing a 75 percent allocation of these cost savings to piece-related discounts and only 25 percent to pound-related rate reduction for DDU and DSCF entry. . . . On the pound side the value of this discount diminishes because less than half of all the pounds actually pay the zoned advertising pound rates. The piece discount provides a more efficient vehicle to provide dropship incentives because the value of the discount applies to every piece regardless of the proportions of editorial and advertising contents.

USPS-T-38, pp. 9-10.

In support of its decision to continue its R97-1 method, the Commission observed:

> It would seem, however, that if the savings are the same for a container with many light-weight pieces as for a container holding fewer heavy-weight pieces, then the savings are, in fact, pound oriented. If, under these conditions, the discount is given on a per-piece basis, the container with many lightweight pieces will receive a discount larger than the Postal Service's savings and the container with fewer heavy-weight pieces will receive a discount smaller than the savings. The incentive thus provided would be for mailers of lightweight pieces to dropship and receive an excessive discount.

PRC Op. R2000-1, p. 437, ¶ 5684.

Third, there are complexities in the current pallet discount. In its Opinion in Docket No. R2001-1, the Commission observed that the "consideration of pallet discounts in previous cases has raised the possibility that associated savings, in terms of transportation, may have a pound orientation and may vary with distance." (p. 109, ¶ 3177). But it proceeded to recommend the per-piece pallet discount contained in the Settlement Agreement. Under that arrangement, 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. There is no way that mailers can rationalize discounts of this kind. The proposed rates turn these anomalies into understandable relationships.

Section 3622(b)(8), ECSI Value

The educational, cultural, scientific, and informational value of the materials in the Periodicals subclass is recognized in two ways. First, the overall subclass is given a low cost coverage of 101.3 percent. Second, the implicit coverage on editorial matter is 84.7 percent and that on advertising matter is 129.5 percent. These are values that characterize the current rates, per the Commission's recommendation in Docket No. R2001-1, and it is not proposed that they be changed.

The proposed rates, if approved, will meet the statutory criteria, send effective pricing signals to mailers, help to align mail preparation with mail processing, and increase the efficiency with which mailer needs are met.

1 **Appendix A – A Model of Publishers' Decisions**

2 Paraphrasing Kielbowicz slightly, additional light can be shed on the possibility
3 that the information on the pages of periodicals might become less accessible to residents
4 of Washington State than to the residents of Washington, D.C. by considering the
5 conditions that might lead to reduced accessibility. Specifically, it seems to me that in
6 order for information to be less accessible in the further zones than in the closer zones,
7 one of two possibilities would most likely have to occur. The first possibility is that a
8 publication might zone its subscription rates. The second is that a publisher might decide
9 to offer the publication to the closer zones only, to which the postage is lower.[42]

10 The possibility that a publisher would, given a zoned editorial pound rate, decide
11 to adopt a subscription scheme under which the higher zones are charged more than the
12 lower zones is, I think, remote. The primary reasons for this remoteness are
13 administrative difficulties and customer confusion (and, maybe, customer anger). One
14 example would be that travelers purchasing a newsstand copy could not be told as easily
15 what the subscription rate might be in their hometown. Also, both gift subscriptions and
16 subscriber relocations would be more difficult. In addition, publishers view themselves
17 as having competitors in the further zones and tend to feel that an increase there would
18 impair their competitive position. Interestingly, support for my conclusion was provided
19 at a recent postal meeting wherein one publisher explained that he once tried such a
20 scheme and found it to be a disaster.

21 The second possibility, concerning a publisher disenfranchising further-zone
22 subscribers, is at the heart of questions the Commission raised about accessibility, and the

[42] Other possibilities might be concocted, such as a change in the publisher's basic business model. But most of these changes would be second-order in character and would most likely affect all zones.

court's notice of an anti-Balkanization principle. If a publisher were to decide to cancel all subscriptions from the higher zones, and to refuse to accept new subscriptions from those zones, then it might be the case that potential subscribers in those zones would be cut off from the information in the publication. Of course, such a cut-off, shown below to be unlikely, would be total only if the publication were unavailable in libraries, or on newsstands, or on the Internet.

In order to investigate whether it would be likely that publications would drop subscribers in the further zones, the following model focuses on the determinants of their profitability. Once the model is developed, the effects on profits of dropping subscribers in zone 8 can be examined.

The profit of a publication (Π) is equal to its total revenue (TR) minus its total cost (TC):

(1) $$\Pi = TR - TC$$

The total annual *revenue* of a publication is equal to the subscription revenue plus the advertising revenue, which can be expressed as follows:

(2) $$TR = V * P_{SUB} + n * V * k * P_{ADV} * Q_{ADV}$$

where: V = the volume of one issue = the number of subscribers

P_{SUB} = the average price of a one-year subscription

P_{ADV} = the posted rate for a one-page advertisement in one copy

Q_{ADV} = the number of pages of advertising in one copy

k = a reduction factor from the posted advertising rate to account for discounts, commissions, and sales fees

n = the number of issues per year

The total annual *cost* of the publication is equal to the cost of creating the editorial material (C_{ED}, for one issue) plus the cost of printing ($C_{PRT\text{-}AVG}$, the average per piece for one issue) plus the cost of mailing ($C_{MAIL\text{-}AVG}$, the average per piece for one issue) plus the average cost of account maintenance (C_{AM}, for one subscriber for one year, includes solicitation and billing and renewal) plus the cost of administration (C_{ADM}, for the publication for one year, assumed relatively fixed with respect to volume), as follows:

(3) $$TC = n\,(C_{ED} + V * C_{PRT\text{-}AVG} + V * C_{MAIL\text{-}AVG}) + V * C_{AM} + C_{ADM}$$

The average cost of printing one issue can be viewed as having a fixed component (FC_{PRT}) and a marginal component (MC_{PRT}), so that $C_{PRT\text{-}AVG} = FC_{PRT}/V + MC_{PRT}$. The total postage for one issue ($V * C_{MAIL\text{-}AVG}$) can be expressed in terms of zones as follows: $V_{SCF} * C_{SCF} + V_{1\text{-}2} * C_{1\text{-}2} + V_3 * C_3 + \ldots + V_8 * C_8$. The subscripts indicate DSCF or zone of entry, assuming no DDU or DADC entry. The total volume, V, shown above, is simply the sum of the subscripted volumes. Substituting, a detailed expression for the profit is obtained:

(4) $$\Pi = (V_{SCF} + V_{1\text{-}2} + V_3 + \ldots + V_8)\, P_{SUB} + n\,(V_{SCF} + \ldots + V_8)\, k * P_{ADV} * Q_{ADV}$$
$$- n\, C_{ED} - n\, FC_{PRT} - n\,(V_{SCF} + \ldots + V_8)\, MC_{PRT}$$
$$- n\,(V_{SCF} * C_{SCF} + V_{1\text{-}2} * C_{1\text{-}2} + \ldots + V_8 * C_8)$$
$$- (V_{SCF} + V_{1\text{-}2} + \ldots + V_8)\, C_{AM} - C_{ADM}$$

The partial derivative of profit with respect to zone-8 indicates the increase in profit from adding a subscriber in zone 8, or the decrease in profit from dropping such a subscriber:

(5) $$\partial \Pi / \partial V_8 = P_{SUB} + n * k * P_{ADV} * Q_{ADV} - n * MC_{PRT} - n * C_8 - C_{AM}$$

This equation is perfectly general. It says that if a subscriber is added in zone 8, the revenue for the year will increase by the subscription price plus the advertising revenue. These are the first two terms. Then, with negative signs, it says the cost will increase by the marginal cost of printing another copy, the cost of mailing a copy to zone 8, and the average cost of maintaining a new account, multiplied by the number of issues where needed. It can be seen that if the last three terms, which include the postage to zone 8 as the second term, are high, possibly because of high postage to zone 8 when the full weight of the publication is zoned, there is the possibility of the addition to profit being negative.

Some idea of the orders of magnitude involved in equation (5) can be obtained by thinking about a specific publication. Since it has been discussed in previous cases, I selected *The New Republic* (*TNR*) magazine for this purpose. The subscription price for

CORRECTED 7/12/04

TNR, according to its website (www.tnr.com) is $39.95 per year. The lowest rate I could find on the Internet was $34.95 per year (at www.magazinecity.net). In order to be conservative, I used $34.95 as an average. *TNR* is a weekly magazine, with 44 issues per year. Thus, n = 44.

Mailing information, last provided in Docket No. R90-1 by witness Dearth, shows the average weight of *TNR* to be 3.3 ounces and the average proportion of advertising to be 23 percent.[43] A set of full-weight-zoned rates to go with this information is easy to develop and, for the subclass, does not result in a rate increase. It results only in a set of rates that is more cost based than the existing rates, with the same revenue. This is done by applying the current advertising pound rates to the full weight, instead of to just the advertising weight, and then returning any excess revenue through a per-pound discount on editorial pounds.[44] In this way, the average benefit to editorial matter is not changed. Based on the Commission's workpapers in Docket No. R2001-1, applying the advertising pound rates in this way results in additional revenue of $243,753,950, which, after rounding, is equivalent to 10.1 cents per editorial pound. Thus, after applying the advertising pound rates to the full weight of publications, a new discount is applied, equal to 10.1 cents per editorial pound. Under these rates, assuming the pieces are presorted to the 3-digit level, barcoded, and not on pallets, the postage for sending a copy to zone 8 is $0.3416.

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[43] See answers of Jeffrey Dearth of interrogatories of ABP, 1-18, Docket No. R90-1, Tr. 27 part 2/~~13661-778~~ 13361-78. The zone distribution of pieces was provided as: SCF – 3677, z1-2 – 10,110, z3 – 20,221, z4 – 22,978, z5 – 10,110, z6 – 4,595, z7 – 1,838, z8 – 18,383.

[44] Developing full-weight-zoned rates in this way, instead of developing them from scratch, adds to the conservatism of the analysis of this appendix since, as explained in Section IV, there is an error in the development of the current rates that artificially elevates the zone-8 pound rate.

1 From the web site, I also calculated a price for advertising of 0.1291 $/page
2 (assuming the ad is in 2 colors and is run 6 times). To check this, I calculated a similar
3 figure for *Business Week* and obtained 0.1024 $/page. In order to be conservative, I used
4 the lower of these two figures, and neglected the fact that advertising sold in less than
5 full-page increments is sold at a higher price. To account for discounts, commissions,
6 and sales charges, I used a value for k of 0.5. There is no way of knowing what the
7 correct factor is.
8 To obtain the quantity of advertising, I applied the weight of 3.3 ounces and the
9 advertising proportion of 23 percent to a weight figure of 0.00288 pounds per page,
10 which recognizes that each sheet of paper has two sides.[45] To go with these figures, the
11 marginal cost of printing is estimated to be $0.17 per copy.
12 Putting these figures into equation (5) shows that the additional profit from a
13 subscriber in zone 8 is $49.55 – C_{AM}. This means that as long as the cost of account
14 maintenance is less than $49.55, it will be profitable to add a subscriber in zone 8 or,
15 alternatively, that it will not be profitable to drop a subscriber in zone 8. The cost of
16 account maintenance is an average annual figure that includes the cost of obtaining and
17 renewing subscribers, billing, keeping records, and maintaining address files. The
18 difference between the realized subscription price ($34.95) and the cost of account
19 maintenance is known in the publishing industry as circ net, short for circulation net, and
20 is frequently expressed as a proportion of the subscription price. As a proportion, circ net
21 might be in the neighborhood of 50 percent. Since a negative circ net ($34.95 – $49.55)

[45] This figure was obtained by weighing an issue of *Business Week* magazine (8.5 ounces) with 184 pages.

1 would be very unusual, it appears that adding a subscriber in zone 8 would be
2 profitable.[46]

3 This analysis does not depend on a publication having paid subscribers. To get a
4 ballpark result for a controlled circulation publication, I looked at *Pit & Quarry,* a
5 monthly magazine. According to ABP's initial brief in Docket No. R90-1, it weighs 6
6 ounces. (p. 18). Its web site (www.pitandquarry.com) shows a subscription rate of
7 $39.00 per year for unqualified subscribers, but I assumed an average of zero. A
8 circulation of approximately 24,000 is shown. The full-page advertising rate for a color
9 ad run 6 times is $6,740, which gives a P_{ADV} of 0.2808 $/page. I assumed 50 percent
10 advertising, a marginal printing cost of 31 cents per copy, and 0.00288 pounds per page
11 (as above). Assuming 3-digit presort and barcoding, the postage for a piece going to
12 zone 8 is 46.63 cents. The implied increase in profit for a subscription in zone 8
13 (equation 5) is $100.37 – C_{AM}. In other words, as long as the cost of account
14 maintenance for one subscriber is less than $100.37 per year, which is almost certainly
15 the case, it is profitable to add subscribers in zone 8.

16 It may be noted that *Pit & Quarry* has been publishing since 1916. Without
17 question, as far as I know, it makes a major contribution to its industry and is an
18 important publication. On the other hand, it views itself as existing in a competitive
19 marketplace. Its website shows a "competitive analysis" with comparisons to two other
20 magazines, *Rock Products* and *Aggregates Manager*. It emphasizes that *Rock Products*
21 has lost 3,245 qualified subscribers (15 percent of its circulation) in the last year.

[46] At a subscription rate of $19.98, exactly one-half the published rate, the cost of account maintenance would have to be $34.57 for zone 8 subscribers to be unprofitable. The conclusion in the text is unaffected.

There is another way, perhaps even more revealing, of bounding these estimates. If the profit level of a publication were extremely high, one would expect healthy subscription and advertising rates relative to costs, and that subscribers in all zones would be profitable. If there were a chance that a subscriber in zone 8 would be unprofitable, it would seem most likely in a situation where the profit level of the publication is zero. Therefore, it is illuminating to constrain the estimate of equation (5) such that the profit shown in equation (4) is zero. If this is done, by substituting the required relationship from equation (4) into equation (5), it turns out that the added profit for a subscriber in zone 8 is:

(6) $$\partial \Pi / \partial V_8 = n * C_{ED}/V + n * FC_{PRT}/V + C_{ADM}/V + n * C_{MAIL\text{-}AVG} - n * C_8$$

For *TNR*, the cost of sending a copy to zone 8 has already been calculated as \$0.3416. The average cost of sending copies in the mail ($C_{MAIL\text{-}AVG}$) can be calculated using the above assumptions and the zone distribution provided by witness Dearth. The result is \$0.2878. Thus, the last two terms in equation (6) are 44 * (0.2878–0.3416) dollars, or \$–2.37. Therefore, in order for the additional profit from adding a subscriber in zone 8 to be negative, it must the case that the sum of: a) 44 times the per-copy editorial cost, b) 44 times the average fixed cost of printing a copy, and c) the annual cost of administration per subscriber, is in total less than \$2.37. I indicated above that the marginal cost of printing a copy is estimated to be about \$0.17. The corresponding average cost is about \$0.33, which means that the average fixed cost of printing (FC_{PRT}/V) is about \$0.16. This means that the term n * FC_{PRT}/V by itself is 44* 0.16 =

1 $7.04. Since the second term is $7.04, the sum of the first three terms on the right is
2 certainly more than $2.37. The conclusion is that it is profitable to add subscribers in
3 zone 8.

4 Just as was done for equation (5), this equation can be evaluated, at least roughly,
5 for *Pit & Quarry* magazine. Some of the required figures are given above. I assumed an
6 average postage equal to that for zone 4, which is 34.52 cents per piece, and an average
7 fixed cost for printing of 30 cents. The equation shows the addition to profit for an
8 additional subscriber in zone 8 to be $12 * C_{ED}/V + C_{ADM}/V + \$2.15$.

9 The explanation for these results is reasonably simple, perhaps intuitive. The first
10 term on the right of equation six ($n * C_{ED}/V$) exists because the revenues (from
11 subscriptions and advertising) must be large enough to cover, among other costs, the cost
12 of creating the editorial content, but this cost does not depend on volume, so, to be
13 profitable, additional subscriptions do not need to contribute to this cost. The second
14 term on the right ($n * FC_{PRT}/V$) exists because the revenues must also be large enough to
15 cover the fixed costs of printing, but neither does this cost vary with volume, so, to be
16 profitable, additional subscriptions do not need to contribute to it either. The third term
17 on the right (C_{ADM}/V) exists because the revenues must be large enough to cover the
18 administrative costs of publishing, but these costs too are fixed, so, to be profitable,
19 additional subscriptions do not need to contribute to them. In effect, the revenue from the
20 new subscriptions is the same as the revenue from the existing subscriptions, but it needs
21 to cover only the low marginal cost of printing, the additional postage (which is
22 somewhat higher than average, due to it being in zone 8), and the additional cost of
23 maintaining another account, which is the same as the cost of maintaining the existing

1 accounts. The new subscriptions, although they provide revenue just like the other
2 subscriptions, do not have to contribute to the cost of creating editorial, the fixed cost of
3 printing, or the administrative costs. Under these conditions, they are bound to be
4 profitable. Subscriptions will be accepted from zone 8 subscribers and there is no
5 incentive to disenfranchise persons living there. The higher postage costs in zone 8,
6 when the editorial matter is zoned, are not high enough to overcome the fact that so many
7 costs are fixed.

8 One of the factors contributing to this outcome is that transportation costs today
9 are a much smaller portion of total costs than they were in 1917. Due to piece rates, the
10 source of about 60 percent of Periodicals revenue, pound rates play a much smaller role
11 in determining postage charges than they did in 1917. The increase in postage, even for
12 zone 8, that would be occasioned by zoning publications' full weight is much smaller
13 than it would have been in 1917, and, since deferential rates are now financed by other
14 rates within the same subclass, would be partially offset by lower pound charges in the
15 lower zones.

16 This result is directly responsive to the Kielbowicz concern for the residents of
17 Washington State. The analysis shows that his standard is met just as well with zoned
18 editorial pound rates as with unzoned editorial pound rates. No subscriber will be
19 disenfranchised by zoning the full weight of publications.

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 § 12 of the rules of practice.

s/_____
Timothy L. Keegan

April 26, 2004
Washington, D.C.

1 CHAIRMAN OMAS: Mr. Mitchell, have you had
2 an opportunity to examine the packet of designated
3 written cross-examination that was made available to
4 you in the hearing room this morning?
5 THE WITNESS: Yes, I have.
6 CHAIRMAN OMAS: If the questions contained
7 in that packet were posed to you orally today would
8 your answers be the same as those previously provided
9 in writing?
10 THE WITNESS: Yes, they would, but is this
11 the time to point out a couple of typographical errors
12 that we found?
13 CHAIRMAN OMAS: Yes. If there are any
14 corrections or additions that you would like to make?
15 THE WITNESS: In the hopes of improving the
16 literary content of my responses, we have found a
17 couple of typographical errors that I would like to
18 point out. The first one is in the response to ABM
19 13, and that is an ABM question to me, and I am
20 leaving off the USPS-/TW et al., or whatever it is,
21 but in effect I think it is clear.
22 In ABM 13 to me, there is an Attachment A,
23 and on page 7 of Attachment A, line 4, there is a
24 space right in the middle of the line where the number
25 one-half should appear. It should refer to one-half

1 ounce pieces, and the original was okay, but when we
2 went into the conversion to PDF file, it left off the
3 one-half and put in a hyphen.
4 So it should refer to one-half ounce pieces.
5 The second one is in ABM 30. On line 3, the word "be"
6 -- B-E -- should be inserted after the word "not"
7 there.
8 The third one is in ABM 59, on line 3, and
9 the third word should be "consistent." And as it was
10 filed originally, I think the word was "consist." So
11 it was an obvious error. The fourth one is in NNA 20,
12 and in NNA 20, the third to the last line, we need to
13 insert the word, "the" -- T-H-E, before the word,
14 "black." And we need to change the word while, W-H-I-
15 L-E, to the word, "white", W-H-I-T-E, which I think
16 anyone would have guessed when they were reading it.
17 I would also like to say in case anyone has
18 sensitivities along these lines that several of my
19 interrogatory responses have subscripts in them, and
20 subscripts are usually in smaller type than the text.
21 And for some reason, when we converted to
22 PDF, the subscripts came in full-sized type. To me it
23 looks awkward. For some reason, that did not happen
24 in my testimony, but did happen in some interrogatory
25 responses.

1 So I just wanted you to know that I made all
2 the subscripts in smaller type than the original. And
3 I think that is all.
4 CHAIRMAN OMAS: Counsel, would you please
5 provide two copies of the corrected designated written
6 cross-examination of witness Mitchell to the reporter.
7 That material is received into evidence and it is to
8 be transcribed in the record.
9 (The document, previously
10 identified as Exhibit No. TW
11 et al.- 2-1, was received in
12 evidence.)
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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Complaint of Time Warner Inc. et al.
Concerning Periodicals Rates

Docket No. C2004-1

DESIGNATION OF WRITTEN CROSS-EXAMINATION
OF TW, CONDE NAST, NEWSWEEK, RDA, AND TV GUIDE
WITNESS ROBERT MITCHELL
(TW et al.-T-1)

Party	Interrogatories
American Business Media	ABM/TW et al.-T1-1-2, 4-22, 24-28, 30-34, 36-57, 60, 62-63, 65-76, 81-90, 92-97, 99-103 NNA/TW et al.-T1-19 USPS/TW et al.-T1-5, 10-11, 13-15
American Postal Workers Union, AFL-CIO	ABM/TW et al.-T1-38-39, 42-43, 64, 83, 94 APWU/TW et al.-T1-1-3 MH/TW et al.-T1-2, 7, 9, 19-20, 23-24, 26 NNA/TW et al.-T1-2-3, 6, 8, 11 OCA/TW et al.-T1-2, 6 USPS/TW et al.-T1-10, 13, 15
Magazine Publishers of America	ABM/TW et al.-T1-13, 20, 24, 36-37, 57, 59-60, 72, 86 MH/TW et al.-T1-1, 3, 9, 29 NNA/TW et al.-T1-4-5, 7, 11, 19, 21, 28, 35
McGraw-Hill Companies, Inc., The	MH/TW et al.-T1-1-12, 14-24, 26-32, 34-37 POIR No. 1, Question 1
Office of the Consumer Advocate	POIR No. 1, Questions 3 and 4

United States Postal Service

ABM/TW et al.-T1-13-14, 16, 18, 21-22, 26, 30, 32, 35, 37, 40, 42-44, 48-53, 58, 60-61, 71, 75, 79-80, 83-84, 86, 90-93, 99, 102
APWU/TW et al.-T1-1-2
MH/TW et al.-T1-31
NNA/TW et al.-T1-1-15, 18-20, 22-23, 26-30, 32-36
OCA/TW et al.-T1-1, 5
USPS/TW et al.-T1-1-11, 13-15

Respectfully submitted,

Steven W. Williams
Secretary

INTERROGATORY RESPONSES OF
TW, CONDE NAST, NEWSWEEK, RDA, AND TV GUIDE
WITNESS ROBERT MITCHELL (T-1)
DESIGNATED AS WRITTEN CROSS-EXAMINATION

Interrogatory	Designating Parties
ABM/TW et al.-T1-1	ABM
ABM/TW et al.-T1-2	ABM
ABM/TW et al.-T1-4	ABM
ABM/TW et al.-T1-5	ABM
ABM/TW et al.-T1-6	ABM
ABM/TW et al.-T1-7	ABM
ABM/TW et al.-T1-8	ABM
ABM/TW et al.-T1-9	ABM
ABM/TW et al.-T1-10	ABM
ABM/TW et al.-T1-11	ABM
ABM/TW et al.-T1-12	ABM
ABM/TW et al.-T1-13	ABM, MPA, USPS
ABM/TW et al.-T1-14	ABM, USPS
ABM/TW et al.-T1-15	ABM
ABM/TW et al.-T1-16	ABM, USPS
ABM/TW et al.-T1-17	ABM
ABM/TW et al.-T1-18	ABM, USPS
ABM/TW et al.-T1-19	ABM
ABM/TW et al.-T1-20	ABM, MPA
ABM/TW et al.-T1-21	ABM, USPS
ABM/TW et al.-T1-22	ABM, USPS
ABM/TW et al.-T1-24	ABM, MPA
ABM/TW et al.-T1-25	ABM
ABM/TW et al.-T1-26	ABM, USPS
ABM/TW et al.-T1-27	ABM
ABM/TW et al.-T1-28	ABM
ABM/TW et al.-T1-30	ABM, USPS
ABM/TW et al.-T1-31	ABM
ABM/TW et al.-T1-32	ABM, USPS
ABM/TW et al.-T1-33	ABM
ABM/TW et al.-T1-34	ABM
ABM/TW et al.-T1-35	USPS
ABM/TW et al.-T1-36	ABM, MPA

ABM/TW et al.-T1-37	ABM, MPA, USPS
ABM/TW et al.-T1-38	ABM, APWU
ABM/TW et al.-T1-39	ABM, APWU
ABM/TW et al.-T1-40	ABM, USPS
ABM/TW et al.-T1-41	ABM
ABM/TW et al.-T1-42	ABM, APWU, USPS
ABM/TW et al.-T1-43	ABM, APWU, USPS
ABM/TW et al.-T1-44	ABM, USPS
ABM/TW et al.-T1-45	ABM
ABM/TW et al.-T1-46	ABM
ABM/TW et al.-T1-47	ABM
ABM/TW et al.-T1-48	ABM, USPS
ABM/TW et al.-T1-49	ABM, USPS
ABM/TW et al.-T1-50	ABM, USPS
ABM/TW et al.-T1-51	ABM, USPS
ABM/TW et al.-T1-52	ABM, USPS
ABM/TW et al.-T1-53	ABM, USPS
ABM/TW et al.-T1-54	ABM
ABM/TW et al.-T1-55	ABM
ABM/TW et al.-T1-56	ABM
ABM/TW et al.-T1-57	ABM, MPA
ABM/TW et al.-T1-58	USPS
ABM/TW et al.-T1-59	MPA
ABM/TW et al.-T1-60	ABM, MPA, USPS
ABM/TW et al.-T1-61	USPS
ABM/TW et al.-T1-62	ABM
ABM/TW et al.-T1-63	ABM
ABM/TW et al.-T1-64	APWU
ABM/TW et al.-T1-65	ABM
ABM/TW et al.-T1-66	ABM
ABM/TW et al.-T1-67	ABM
ABM/TW et al.-T1-68	ABM
ABM/TW et al.-T1-69	ABM
ABM/TW et al.-T1-70	ABM
ABM/TW et al.-T1-71	ABM, USPS
ABM/TW et al.-T1-72	ABM, MPA
ABM/TW et al.-T1-73	ABM
ABM/TW et al.-T1-74	ABM
ABM/TW et al.-T1-75	ABM, USPS

ABM/TW et al.-T1-76	ABM
ABM/TW et al.-T1-79	USPS
ABM/TW et al.-T1-80	USPS
ABM/TW et al.-T1-81	ABM
ABM/TW et al.-T1-82	ABM
ABM/TW et al.-T1-83	ABM, APWU, USPS
ABM/TW et al.-T1-84	ABM, USPS
ABM/TW et al.-T1-85	ABM
ABM/TW et al.-T1-86	ABM, MPA, USPS
ABM/TW et al.-T1-87	ABM
ABM/TW et al.-T1-88	ABM
ABM/TW et al.-T1-89	ABM
ABM/TW et al.-T1-90	ABM, USPS
ABM/TW et al.-T1-91	USPS
ABM/TW et al.-T1-92	ABM, USPS
ABM/TW et al.-T1-93	ABM, USPS
ABM/TW et al.-T1-94	ABM, APWU
ABM/TW et al.-T1-95	ABM
ABM/TW et al.-T1-96	ABM
ABM/TW et al.-T1-97	ABM
ABM/TW et al.-T1-99	ABM, USPS
ABM/TW et al.-T1-100	ABM
ABM/TW et al.-T1-101	ABM
ABM/TW et al.-T1-102	ABM, USPS
ABM/TW et al.-T1-103	ABM
APWU/TW et al.-T1-1	APWU, USPS
APWU/TW et al.-T1-2	APWU, USPS
APWU/TW et al.-T1-3	APWU
MH/TW et al.-T1-1	McGraw-Hill, MPA
MH/TW et al.-T1-2	APWU, McGraw-Hill
MH/TW et al.-T1-3	McGraw-Hill, MPA
MH/TW et al.-T1-4	McGraw-Hill
MH/TW et al.-T1-5	McGraw-Hill
MH/TW et al.-T1-6	McGraw-Hill
MH/TW et al.-T1-7	APWU, McGraw-Hill
MH/TW et al.-T1-8	McGraw-Hill
MH/TW et al.-T1-9	APWU, McGraw-Hill, MPA
MH/TW et al.-T1-10	McGraw-Hill
MH/TW et al.-T1-11	McGraw-Hill

MH/TW et al.-T1-12	McGraw-Hill
MH/TW et al.-T1-14	McGraw-Hill
MH/TW et al.-T1-15	McGraw-Hill
MH/TW et al.-T1-16	McGraw-Hill
MH/TW et al.-T1-17	McGraw-Hill
MH/TW et al.-T1-18	McGraw-Hill
MH/TW et al.-T1-19	APWU, McGraw-Hill
MH/TW et al.-T1-20	APWU, McGraw-Hill
MH/TW et al.-T1-21	McGraw-Hill
MH/TW et al.-T1-22	McGraw-Hill
MH/TW et al.-T1-23	APWU, McGraw-Hill
MH/TW et al.-T1-24	APWU, McGraw-Hill
MH/TW et al.-T1-26	APWU, McGraw-Hill
MH/TW et al.-T1-27	McGraw-Hill
MH/TW et al.-T1-28	McGraw-Hill
MH/TW et al.-T1-29	McGraw-Hill, MPA
MH/TW et al.-T1-30	McGraw-Hill
MH/TW et al.-T1-31	McGraw-Hill, USPS
MH/TW et al.-T1-32	McGraw-Hill
MH/TW et al.-T1-34	McGraw-Hill
MH/TW et al.-T1-35	McGraw-Hill
MH/TW et al.-T1-36	McGraw-Hill
MH/TW et al.-T1-37	McGraw-Hill
NNA/TW et al.-T1-1	USPS
NNA/TW et al.-T1-2	APWU, USPS
NNA/TW et al.-T1-3	APWU, USPS
NNA/TW et al.-T1-4	MPA, USPS
NNA/TW et al.-T1-5	MPA, USPS
NNA/TW et al.-T1-6	APWU, USPS
NNA/TW et al.-T1-7	MPA, USPS
NNA/TW et al.-T1-8	APWU, USPS
NNA/TW et al.-T1-9	USPS
NNA/TW et al.-T1-10	USPS
NNA/TW et al.-T1-11	APWU, MPA, USPS
NNA/TW et al.-T1-12	USPS
NNA/TW et al.-T1-13	USPS
NNA/TW et al.-T1-14	USPS
NNA/TW et al.-T1-15	USPS
NNA/TW et al.-T1-18	USPS

NNA/TW et al.-T1-19	ABM, MPA, USPS
NNA/TW et al.-T1-20	USPS
NNA/TW et al.-T1-21	MPA
NNA/TW et al.-T1-22	USPS
NNA/TW et al.-T1-23	USPS
NNA/TW et al.-T1-26	USPS
NNA/TW et al.-T1-27	USPS
NNA/TW et al.-T1-28	MPA, USPS
NNA/TW et al.-T1-29	USPS
NNA/TW et al.-T1-30	USPS
NNA/TW et al.-T1-32	USPS
NNA/TW et al.-T1-33	USPS
NNA/TW et al.-T1-34	USPS
NNA/TW et al.-T1-35	MPA, USPS
NNA/TW et al.-T1-36	USPS
OCA/TW et al.-T1-1	USPS
OCA/TW et al.-T1-2	APWU
OCA/TW et al.-T1-5	USPS
OCA/TW et al.-T1-6	APWU
USPS/TW et al.-T1-1	USPS
USPS/TW et al.-T1-2	USPS
USPS/TW et al.-T1-3	USPS
USPS/TW et al.-T1-4	USPS
USPS/TW et al.-T1-5	ABM, USPS
USPS/TW et al.-T1-6	USPS
USPS/TW et al.-T1-7	USPS
USPS/TW et al.-T1-8	USPS
USPS/TW et al.-T1-9	USPS
USPS/TW et al.-T1-10	ABM, APWU, USPS
USPS/TW et al.-T1-11	ABM, USPS
USPS/TW et al.-T1-13	ABM, APWU, USPS
USPS/TW et al.-T1-14	ABM, USPS
USPS/TW et al.-T1-15	ABM, APWU, USPS
POIR No. 1, Question 1	McGraw-Hill
POIR No. 1, Questions 3 and 4	OCA

Response of Time Warner Inc. et al. Witness Robert W. Mitchell to Interrogatory of American Business Media

ABM/TW et al.-T1-1. Please provide a narrative detailing Mr. Mitchell's experience in or with the periodical publishing industry, including employment by periodical publishers or analysis of that industry.

Response:

For the past twenty-five years, the design and analysis of Periodicals rates and classifications has been among my major areas of responsibility: from 1979 to 1992 at the United States Postal Service as an Assistant to the Assistant Postmaster General of Rates and Classifications, Manager of the Primary Rates Branch in the Office of Rates, Principal Economist, and as the Postal Service's witness on Periodicals rates in Dockets No. R87-1 and R90-1; from 1992 until 2002 at the Postal Rate Commission as Special Assistant to the Chairman and Special Assistant to the Commission; and from 2002 until the present as a private postal consultant.

During these years I developed knowledge and understanding of the periodical publishing industry in many ways, including talking to mailers and publishers, observing their operations, fielding their inquiries, following newsletters and other widely circulated media (including newspaper, television, and radio reports), reading magazines such as *Folio* and *Mailing Systems Technology*, working with information sources such as *The Magazine Handbook* and the Household Diary of the Postal Service, reading testimony and briefs in cases before the Postal Rate Commission (including those of ABM, formerly ABP), and interactions with colleagues at the Postal Service and the Commission.

Initially, my work at the Postal Service centered primarily on issues relating to costing and corporate planning. Beginning in 1979, while working for the Assistant Postmaster General of the Rates and Classifications Department and in the now-defunct Office of Rates, I began working seriously and in detail on issues relating to Periodicals (then second-class) rates, including detailed attention to the workpapers supporting rates, which were then done by hand, to appropriations requests, and to

possible changes in the structure of the rates. One of the earlier issues that received a great deal of my attention was the destination SCF discount proposed by the Postal Service in Docket No. R84-1. Questions existed about the nature of the cost study that was to be done, what special information was needed, and how the rate proposal should be designed.

Prior to my testimony on second-class rates in Docket No. R87-1, I computerized all of the supporting workpapers. This allowed considerably more inquiry than was possible previously. Specifically, we were able to assess the effects of changes and to ask classic "what if" questions. During this period, I prepared a number of studies of alternative rate structures. I do not have copies of these studies, in part because I tried to avoid taking internal documents when I moved to the Rate Commission in 1992. During this period of time, the rates people at the Postal Service worked in limited degree with the marketing people, who resided in a separate department under a separate Senior Assistant Postmaster General, but did not work much with mailers.

Following Docket No. R87-1, I took the lead in working more with the Marketing Department and in communicating more with mailers on rate issues. I felt that the more I understood mailer's situations and interests the better, and that mailers deserved but were not getting good answers to rate questions. I spoke at many second-class meetings, including those at Postal Forums, and found mailers both large and small saying: I have wondered about such and such, and have asked about it many times, but I have never been able to get a clear answer. It was in order to answer some of these questions that several managers and account representatives in the Marketing Department kept asking me to go with them to meetings.

In Docket No. R84-1, the piece rate for basic presort increased 75.7 percent. In Docket No. R87-1, it increased again by 30.1 percent. Both of these increases were virtually an order of magnitude greater than the average increase for the subclass and were also greater than the Postal Service proposed. The Commission recommended

them in order to bring rates into closer alignment with costs and to send correspondingly appropriate signals to mailers. It was about such changes that mailers asked. If rates people are going to be involved in these kinds of changes, they need to face the mailers paying the rates, listen to their concerns, and provide explanation. Incidentally, I found in some cases that mailers had focused on specific rate cells instead of the postage for their entire mailing.

My interest in talking with mailers continued while I was working for the Rate Commission, from 1992 through 2002. I believe that the Postal Service and the Rate Commission, as independent agencies charged with achieving fair and balanced rates, have the same goals. I understand that the Commission makes rate decisions based on a record developed in a proceeding that is open to the public, but I have always felt it helpful to be able to approach that record with a good understanding of mailers and the mailing industry.

Over the years, I have addressed and talked with many mailers, at Postal Forums, Postal Customer Councils, focus groups, and meetings sponsored by industry and trade associations, including the Magazine Publishers of America, the Association of Paid Circulation Publications (now Periodicals Publications Association), the American Business Press (now American Business Media), the Coalition of Religious Press Associations, the Alliance of Nonprofit Mailers, the National Newspaper Association, the International Regional Magazines Association, the Graphic Communications Association (now IDEAlliance), the Agriculture Circulation Association, the Classroom Publishers Association, the Red Tag News Publications Association, the Direct Marketing Association, the Newspaper Association of America, the Independent Free Papers of America, and the Envelope Manufacturers Association. I have tried to recall meetings with specific publishers, apart from widely attended meetings, and recall meetings with representatives of Dow Jones, McGraw-Hill, The Hearst Corp., National Geographic, and Highlights for Children. I have also talked with managers from Brown

Printing Company, Postal Logistics Inc., and Farrington, visited a number of printing plants, including World Color Press (now Quebecor World), Quad Graphics, and Judd's Press (now part of Perry-Judd's), and accompanied members of the Rate Commission on a number of visits to facilities of printers and publishers, including Rodale Inc. (including *Prevention* and *Runner's World*), Time Inc., RR Donnelley, and the Billy Graham Evangelistic Association (*Decision Magazine*). I attended a presentation made at the Commission by Reader's Digest. I have visited a number of Postal Service facilities, some more than once, including Atlanta, St Louis, San Diego, Baltimore, Richmond, Gaithersburg, Philadelphia, Northern Virginia, the Newark BMC and international hub, the Northwest hub in Minneapolis, Carol Stream, the Washington BMC, Washington, Charlottesville, and various destination delivery units. I was an invited speaker at an MPA meeting last year, for which they paid my transportation expenses.

I began working as a consultant to Time Inc. in November 2002. My only other Periodicals-mailer client is Scholastic, but I have not worked with them on Periodicals issues. My other clients, to the best of my knowledge, have no involvement with Periodicals mail.

Response of Time Warner Inc. et al. Witness Robert W. Mitchell to Interrogatory of American Business Media

ABM/TW et al.-T1-2. Please describe in detail all of Mr. Mitchell's experience that is relevant to his discussion in Appendix A of the sources of and possible variations in revenues received (a) by *Pit & Quarry* and (b) by publications similar to *Pit & Quarry.*

Response:

It is not the purpose of my Appendix-A model to analyze the sources of revenue or the possible variations in revenue of any particular publication or type of publication. Rather, my model is designed to focus on a very specific question: given a publication with a distribution and an ease of accessibility by actual and potential readers, is it reasonable to expect that the publisher would change that distribution and ease of accessibility given a change from flat editorial rates to zoned editorial rates, and no other changes? This question is importantly related to the question of widespread dissemination. If no publisher, given such a change in rates, would change his distribution or the ease of accessibility of his publication, then it is difficult to see how such a change in rates could affect the extent to which the publication is disseminated widely.

To be useful, a model need not develop an answer in exactly the way a particular firm would develop an answer for itself. Economic models seek to identify and put dimensions on the basic forces acting on firms, including their goals, and to answer questions or study implications. The contribution that such modeling efforts can make is not reduced by the fact that actual firms go about their decision-making in a myriad of different ways. For example, most models of competition among firms suggest that profit-maximizing firms tend to operate at a point where their marginal cost is equal to their marginal revenue. Yet almost no one argues that firms focus their strategic efforts on developing estimates of their marginal revenue.

Before I built the model in Appendix A, I had given a great deal of thought to the factors associated with whether the rates for editorial matter are zoned. I understood clearly that the marginal cost of printing another copy is small and that the cost of

preparing editorial matter would not increase if another copy were to be printed. I also understood how postal rates vary by zone with and without editorial zoning. It seemed apparent that no publisher would refuse a subscriber in a higher zone.

The purpose of my model is to help explain the role of the various factors involved: a low marginal cost of printing, a fixed cost of preparing editorial content, and an adjustment in postal rates, depending on the zone and the proportion of advertising, and to help put dimensions on the various interrelationships. The model deals systematically with the forces important to publishers' decisions on zones and the availability of their publications.

Reaching conclusions for particular publications requires publication-specific information. Some of this information is available. Some is viewed by publications as proprietary but can be estimated. In order to supplement information readily available, I made certain estimates. My conclusion for *Pit & Quarry* on page 66 of my testimony is: "In other words, as long as the cost of account maintenance for one subscriber is less than $100.37 per year, which is almost certainly the case, it is profitable to add subscribers in zone 8." I did not testify concerning the actual costs of account maintenance, costs that clearly must cover subscriber acquisition, record keeping and related operations, and attempts to obtain renewal. I do not know what steps *Pit & Quarry* takes in any of these areas.

The result found, however, is so strong that it would be unaffected by refinements in my estimates. In cases like this, results are generally described as robust. Nevertheless, this does not end the steps that can be taken. If *Pit & Quarry*, or any similar publication, were to provide information specific to that publication, the results could be more finely tailored.

My response to ABM/TW et al.-T1-1 provides additional information relevant to this question.

Response of Witness Mitchell to ABM/TW et al.-T1-4

ABM/TW et al.-T1-4. You state in response to ABM/TW et al.-T1-1 that you read Folio and Mailing Systems Technology. Please identify at least one website and one internet news group from which the same quality and quantity of information concerning the periodical industry can be obtained.

RESPONSE

Folio maintains a web site of its own, which appears to make its articles available, including from back issues, and also provides search capabilities. *Mailing Systems Technology* maintains a site with a Message Board and a Buyer's Resource. ABM has a web site and allows interested persons to sign up for E-News. MPA has a web site providing multiple opportunities for interaction. I have no reason to believe that any of these are not high in quality, and the quantity of information in the articles I looked at appears to be the same as the quantity in the physical publication.

I wrote one article for *Mailing Systems Technology* that was a summary of a paper that is available in its entirety on the Postal Rate Commission's web site. I have also been a resource to *Folio* for articles on rates. The information I provided them, as well as much of the information apparently provided by others, was available in other places in similar quality and often-greater quantity. The sites of the Association of Postal Commerce, the Alliance of Nonprofit Mailers, and the Postal Rate Commission come to mind. Another site containing a number of papers, speeches, and presentations is www.postalinsight.pb.com; and yet others would be www.postalwatch.org, www.DMNews.com, and www.majormailers.org. In most cases, the quantity of the information in these sources is greater than the quantity that might be reported in a magazine.

Response of Witness Mitchell to ABM/TW et al.-T1-5

ABM/TW et al.-T1-5. Have you ever been an employee of, as opposed to a consultant for, a periodical publishing company? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-6

ABM/TW et al.-T1-6. Have you ever provided services related to the production of a periodical to a publishing company? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-7

ABM/TW et al.-T1-7. Have you ever sold advertising for a periodical publisher? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-8

ABM/TW et al.-T1-8. Have you ever purchased advertising from a periodical publisher? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-9

ABM/TW et al.-T1-9. Have you ever been employed, as an employee or a consultant, in the advertising business? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-10

ABM/TW et al.-T1-10. Have you ever arranged for the printing of a periodical? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-11

ABM/TW et al.-T1-11. Have you ever arranged for the transportation of a periodical? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-12

ABM/TW et al.-T1-12. Have you ever arranged for the distribution of a periodical? If so, provide the details.

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-13

ABM/TW et al.-T1-13. *In the speeches and meetings described in your response to* ABM/TW et al.-T1-1, did you ever address the zoning of the editorial pound rate or other issues that have been raised by complainants in this proceeding? If so, please make copies of those speeches or notes from those meetings available, if you still have them.

RESPONSE

I have been able to identify two presentations that apply. The first was to a meeting organized by the Envelope Manufacturers Association on May 8, 2003 and the second was to an MPA meeting on June 16, 2003. Slides from both presentations are appended as Attachments A and B. The oral portions of my presentations were not read.

Attachment A to Response of Witness Mitchell to ABM/TW et al.-T1-13
Slides for presentation to Envelope Manufacturers Association, May 8, 2003

HORSE DESIGNED BY COMMITTEE

A. CHANGE IS ON THE AGENDA

1. **Activity due to Transformation Plan, Bush Commission, Further Automation, and Network Realignment.**

2. **Product Redesign will get more emphasis.**

3. **Considerable attention is being given to issues like Standardization, Worksharing, Downstream Access, Niche Classifications, and Negotiated Service Agreements.**

B. MY BIASES

1. **Rate improvements should be a central part of any strategy for the future.**

2. **USPS will be better able to make these rate changes if it understands its costs.**

3. **Cost based rates serve the markets more effectively than rates that are not cost based, and they contribute to the vitality of the Postal Service.**

4. **Mailers respond to rate signals MIGHTILY.**

! **Facilitated by high volumes.**

! **Facilitated by mailer sophistication.**

C. CURRENT RATE SITUATION NOT PARTICULARLY GOOD

1. **In the past, we have tended to refine certain rate areas but leave major glitches in others.**

2. **Some worksharing signals are very troublesome.**

Principal cause – Rate Averaging.

3. **Some recent weaknesses are apparent.**

! **A Niche Classification case was filed recently with no cost information at all.**

! **An NSA was filed without firm-specific costs.**

D. EXAMPLES – I

1. **First-Class Mail**

! **Almost no separate rate recognition for letters, flats, & parcels.**

! **Additional postage for additional weight is too high.**

! **No destination entry discounts.**

! **Poor signals on postage sales.**

24 cents per Dollar of sales at Window

E. EXAMPLES – II

1. **Periodicals**

! **Inadequate recognition of machinability.**

! **Poor dropship signals.**

! **Poorly constructed pallet discounts.**

2. **Standard Mail**

! **Poor dropship signals.**

! **Too far from 100% passthrough on worksharing discounts.**

! **Pound charges too high.**

! **Minimum-per-piece rate causing difficulties.**

F. RATE AVERAGING and WORKSHARING

1. **Dropshipping in Standard Mail**

   From New York to Los Angeles

! **1 Truck of 1/2-Ounce Pieces**

! **6 Trucks of 3-ounce Pieces**

Y **Same Dropship Discount**

Y **Adverse Selection**

2. **More Dropshipping Standard Mail**

   Two New York Mailers.

! **One with mail for Chicago**

! **Another with mail for Los Angeles**

Y **Same Dropship Discount**

Y **Adverse Selection**

G. EFFECTS OF IMPROVEMENT

1. More complex rate structures.

! Additional rate elements and zones.

! Could see something like: Charge per sack, charge per pallet, charge per bundle, charge per piece, and charge per pound, plus presortation differences and dropship differences.

2. Some rates ↑ and some rates ↓

! But all mailers would see opportunities to make efficient changes in what they are doing.

3. What should mailers do?

! Support changes that make sense.

! Work with the Postal Service on changes that make sense.

H. TO MAKE PROGRESS

1. **USPS must do studies to support changes.**

a. **They are under investing in analysis. The needs include mailer-specific costs.**

b. **The studies are needed now. They would be needed even more if USPS were fully privatized. The need is not due to the demands of the regulatory framework.**

2. **USPS must play the leadership role.**

c. **The changes cannot be made by the Rate Commission.**

d. **USPS cannot bow to political pressure.**

e. **USPS cannot make the changes needed if it wants full agreement before it proposes them.**

f. **Rate Commission must be prepared to make tough decisions.**

Attachment B to Response of Witness Mitchell to ABM/TW et al.-T1-13
Slides for presentation to Magazine Publishers of America, June 16, 2003

ECSI Value, Binding the Nation, And the Flat Editorial Pound Rate

A Little History and a Few Observations

1. **The rate for 2c had been 1 ¢/lb since 1885, regardless of distance or advertising content. There were no piece rates. It was recognized that this rate was highly subsidized by the Government.**

2. **Transportation costs in this period were very large relative to other costs. Many analyses showed that costs were 6-10 ¢/lb, particularly for long distances. Over a period of 20 years, there were many arguments to increase 2c rates.**

3. **In 1917, using the War Revenue Act as a vehicle, the House proposed to zone the full weight of 2c.**

4. **There were arguments that magazines and daily newspapers were our great mediums of exchange, that sectional publishing zones would be created, that 3 distinct zones of thought and feeling would be created. Basically, I think, the argument was that some existing publishers would stop sending to the distant zones. I have not found arguments about publishers going out of business.**

5. **There was concern about private profits being made on the subsidized 2c rates, particularly on advertising. A tax was considered on publisher's profits over $4,000.**

6. **In a compromise, the Senate created the flat editorial rate. In the final step of the 1917 Bill, editorial became 1.5 ¢/lb and zone 8 became 10**

¢/lb, 6.7 times greater. Still no piece rates, until 1971. Periodicals with 5% or less advertising were treated as though they had no advertising – I don't know when this stopped. Nonprofit rates were created by exempting nonprofits from the new rates and creating a rate for them of 1 1/8 ¢/lb, unzoned. Congress zoned advertising for Nonprofit in 1967.

7. The final 1917 rates had the flat editorial rate set at 75% of the zones 1-2 advertising rate. This specific 75% relationship has been honored until the Postal Service proposal in R2001-1. In that case, it proposed an 81.1% proportion. The settlement changed it to 77.8%.

8. Inherited in 1970, were the following rates: editorial 3.4 ¢/lb and zone 8 advertising 17.0 ¢/lb, 5 times greater, with no piece rates.

9. R71-1, starting with the Temporary rates, piece rates came into existence. In 1971, 2.4% of the volume was in zone 8 and 65.5% was in zones 1-2.

10. Congress amended the Reorganization Act in 1976 to say that ECSI value should be considered in setting rates. Book publishers had gone to court in 1974 to argue that their rates were too high. The judge said their remedy, if there is one, would have to come from Congress. It was understood, but may not be written anywhere, that ECSI value applies to Books and Periodicals.

11. R84-1. The per-piece editorial discount came into existence. The Rate Commission cut it from whole cloth because it felt the role of pound rates was being diminished. This discount has grown since.

12. **R2000-1, before the modification, zone 8 pound rate = 3.1 times the flat editorial rate. Volume: 2.8% in zone 8 and 60.5% in zones 1-2 & closer.**

13. **The cost coverage on Periodicals was 101%. Note two things. 1) The coverage on editorial was 82.3% and the coverage on advertising was 125.6%. Thus, editorial is being handled well below cost. 2) If the per-piece editorial discount did not exist, the coverage on editorial would have been 92.7% and the coverage on advertising would have been 110.8%. Thus, the per-piece editorial benefit is well over half the total benefit being given to editorial, relative to advertising. Observation: In 1917, all of the editorial benefit was on the pound rates and the benefit was highly skewed toward distance. Now, less than half of the editorial benefit is given in the pound rates, and this limited portion is mildly skewed toward distance.**

14. **In the court case following R90-1 (MOAA or Dow Jones), the Commission's justification for the flat editorial pound rate was reviewed. The court said: it is perfectly obvious that the ECSI value of local (low-zone) publications is just as important as the ECSI value of nationwide (high-zone) publications, so ECSI value cannot be used to support a decision to continue the flat editorial rate. This is very important.**

15. **The court let the Commission's decision stand because the Commission had argued, mostly in earlier decisions, that the flat editorial rate plays an important role in <u>binding the Nation together</u>. The court referred to this as an anti-Balkanization principle. The court repeated a Commission characterization of the choice as being between <u>economic</u> considerations and <u>public policy</u> considerations.**

16. **I believe this leaves us in the following situation. 1) ECSI-value considerations support a low cost coverage on periodicals, and further support a relatively lower cost coverage on editorial and a relatively higher cost coverage on advertising (although there is no coverage split built into In-County rates). 2) The justification for the flat editorial rate rests on weight given to any role it plays in <u>binding the Nation together</u>.**

Response of Witness Mitchell to ABM/TW et al.-T1-14

ABM/TW et al.-T1-14. Please explain the nature of your assignments from Time Inc., beginning in November, 2002.

RESPONSE

I have provided advice to Time Inc. on a broad range of postal issues, from rates to legislation, usually in response to a specific request for my opinion from Time Inc. management (although I have commented on some issues on my own initiative), sometimes in writing and sometimes orally only. I have attended and participated in several meetings of Time Inc. and Time Warner managers, postal counsel, and postal consultants concerning postal matters. We began discussing deficiencies in Periodicals rates in the first part of calendar 2003. Much of my work since July, 2003 has been in connection with the instant Complaint case.

Response of Witness Mitchell to ABM/TW et al.-T1-15

ABM/TW et al.-T1-15. Please define "efficient" as you use that word at page 1, line 8.

RESPONSE

The term in question appears in the first sentence of a two-sentence paragraph in a general statement of purpose of testimony. The full sentence is: "I contend that our current understanding of postal costs and mailer capabilities makes it clear that Periodicals rates are at variance with the Act's guiding background presumption in favor of efficient rates."

The Act creates an expert Commission and provides certain guidance to the ratesetting process, including that consideration is to be given to the costs, the value of the service provided, the alternatives available, the degree of preparation of the mail, and such other factors as the Commission may wish to consider. I believe Congress expected that the Commission would draw on the literature available in the regulatory area and that the result would be good rates. In other words, I think one would be ill advised to argue that Congress expected less than state-of-the-art work. At this point, "efficient" is synonymous with good rate setting. Given our current understanding of postal costs (including cost drivers) and mailer capabilities, I believe the rates are unacceptably far from being well set.

Response of Witness Mitchell to ABM/TW et al.-T1-16

ABM/TW et al.-T1-16. Is it "efficient," is it "inefficient," or is it neither to charge lower postage to a Periodical than to a catalog with identical physical characteristics? Explain.

RESPONSE

At an early stage in the consideration of your question, one would ask about the relative costs involved, which would depend on more than just the "physical characteristics" of the mailpieces, and might be affected by the service provided. Also, some concepts of efficiency would require that consideration be given to the *value* of the service provided, a notion that is more easily considered for a subclass than for a piece. The consideration of externalities can also be important, as Congress seems to have anticipated when it specified that ECSI value should be recognized. If my neighbor's welfare is improved when I receive a periodical, but not when I receive a catalog, a step to encourage the realization of that welfare could easily involve a lower rate for the periodical, on the grounds that such a rate arrangement is more efficient.

If all periodicals could choose to use the catalog rates, and they can, then, except for considerations of service and maybe prestige, setting Periodicals rates above the applicable catalog rates would result in a Periodicals subclass with no volume, hardly what one would hope to achieve by creating a special and separate subclass for periodicals.

In general, we do not have absolute measures of efficiency, and comparisons of the efficiency levels of different subclasses cannot generally be made. Usually, observations on efficiency are made in the context of a characteristic of a rate structure or a change being considered. One might say that a particular

characteristic is inefficient or that a particular change will improve efficiency. So focused, measures of the effects of a change can sometimes be developed.

Response of Witness Mitchell to ABM/TW et al.-T1-17

ABM/TW et al.-T1-17. When you compare periodicals rates with inflation since the 1980s, at page 3, lines 10-12, are you using average rate per piece or some other measure of periodicals rates?

RESPONSE

Page 3, lines 10-12, to which you refer, is part of a summary section. It summarizes Section III.A., which begins on page 9. As explained further on the latter page, the rate index is a quantity-weighted price index, using base period weights in each omnibus rate case, linked together, and corrected to a constant markup index. Therefore, it is not based on average revenue per piece figures for the subclass, which I take your "average rate per piece" to be. The average revenue per piece is not a "measure of [the level of] periodicals rates," and cannot be used to develop such a measure.

Response of Witness Mitchell to ABM/TW et al.-T1-18

ABM/TW et al.-T1-18. During the period references at page 3, lines 10-12, did periodicals mailers take steps that should have reduced Postal Service periodicals costs, such as barcoding, palletizing and dropshipping?

RESPONSE

Yes. But note that to the extent that the postage reductions were equal to the cost reductions, these steps would not cause rates to decrease.

Response of Witness Mitchell to ABM/TW et al.-T1-19

ABM/TW et al.-T1-19. What is your explanation for the fact that cost-reducing measures by periodicals mailers do not appear to have reduced periodical processing costs, at least to the extent that they should have?

RESPONSE

Using the results of the cost-avoidance studies and the shifts in billing determinants, one can calculate the reduction in Postal Service costs that should have occurred, *ceteris paribus*. But since we do not know what the costs would have been without the billing determinant shifts, it is not possible to tell whether the cost-reducing measures had the expected effects. However, nothing I am saying here should be taken to detract from my concern that the increases in Periodicals costs have been too large.

Response of Witness Mitchell to ABM/TW et al.-T1-20

ABM/TW et al.-T1-20. Is your reference at page 4, line 2, to "mailers" intended to include all mailers?

RESPONSE

Yes. If the factors that drive costs are reflected more completely in rates, all mailers will face a changed set of signals and will make decisions based on them. This is not to say that all mailers will choose to make changes or that they will make them immediately.

The rationale for improved information in rates is not that the signals involved will bring about some sort of uniformity in behavior. Rather, it is that in all decisions relating to mail preparation and entry attention will be given in appropriate ways to the value received by the mailers and the costs involved, including costs to the mailer and to the Postal Service. If the proposed rates are implemented, all mailers will face a new rate structure and all mailers will see postage differences associated with alternatives that had no (or different) postage differences associated with them before. Were this to occur, I would expect many changes. And note that every change is an efficiency improvement in that the postage savings to the mailer (also equal to the Postal Service savings), including consideration of changes in value (which the mailer knows and the Postal Service does not), is larger than the cost to the mailer of making the change. (Changes involving higher postage are also possible, in which case the postage increase is less than the cost savings to the mailer of making the change.)

Response of Witness Mitchell to ABM/TW et al.-T1-21

ABM/TW et al.-T1-21. Is the First-Class rate inefficient?

RESPONSE

No absolute measure of the efficiency of a subclass is available; and if one were, it would not be possible to specify a level (or range of levels) that is efficient and another level (or range of levels) that is inefficient. Within the context of considering a specific change, one might conclude that making the change would be an efficiency improvement. Similarly, one might conclude that a particular characteristic of a subclass's rate structure is inefficient, due either to agreement that the signals it sends are perverse or in comparison to some alternative.

Based on this reasoning, First-Class rates cannot be called efficient. For example, charging the same rate for a 2-ounce letter and a 2-ounce flat is inefficient by almost any criterion. The signals sent by such a rate arrangement are perverse. I do not mean to suggest, however, that factors such as ease of administration are not important considerations.

Response of Witness Mitchell to ABM/TW et al.-T1-22

ABM/TW et al.-T1-22. Is the Standard rate inefficient?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-21, Standard rates cannot be said to be efficient. For one thing, most of the changes being proposed in this docket would apply well to Standard.

Response of Witness Mitchell to ABM/TW et al.-T1-24

ABM/TW et al.-T1-24. Please explain the term "economical mailing practices" on page 6, lines 1-2.

RESPONSE

In context, a mailing practice becomes more economical if the mailer makes a change such that: (a) the decrease in postage under cost-based rates (which also equals the decrease in the costs of the Postal Service and in the costs of the nation), including the value of any changes in the level of service received, is less than the cost to the mailer of making the change (which could be zero – especially if no information about the effects of the change has ever been given in rates before); or (b) the increase in postage under cost-based rates (which also equals the increase in the costs of the Postal Service and in the costs of the nation), including the value of any changes in the level of service received, is less than the cost savings to the mailer of making the change.

Response of Witness Mitchell to ABM/TW et al.-T1-25

ABM/TW et al.-T1-25. Do the proposed rates provide penalties for those who cannot engage in what you call "more economical mailing practices" as well as incentives for those that do?

RESPONSE

The term *penalty* suggests a burden imposed as punishment for a blameworthy act. It is misleading to apply that term to the proposition that a rate ought to recognize the costs of the mail involved. No penalties are contained in the proposed rates. You may be confused by the fact that in moving from the current rates (which are not cost based) to the proposed rates (which are cost based in substantially greater degree), some mailers will see rate increases.

It is irrational not to assume that all mailers have made decisions concerning what is best for them under the current rate structure. That is, they have considered a wide range of alternatives, focused on their interests, their capabilities, and the rates associated with those alternatives, and have selected what is optimal. When all of these rates change, and new alternatives are introduced as well, it is virtually inconceivable that no changes will be made. But if there are mailers who see the optimal solution as unaffected by changes in virtually all of the inputs and "cannot" see that changes are indicated, they would be under no obligation to reconsider. Their rates would be fairly based on the costs their mail incurs and their mail should be delivered effectively.

Do not be deceived into believing that mailing practices do not evolve over time. Even if changes are not made immediately, the new rate structure will inform decisions made in the future, such as those involving basic business models, mechanization, and printing locations. All of these take time and all should be made in full view of the cost implications involved. And don't forget that the future we all

look forward to is influenced substantially by the innovative spirit of businesses and entrepreneurs. Predictions of future paths are often wrong. It is important that we allow this process to occur within a framework that not only reveals opportunities but also reflects the costs involved.

Response of Witness Mitchell to ABM/TW et al.-T1-26

ABM/TW et al.-T1-26. With reference to your testimony on page 6, lines 11-12, that the effects of your proposed rates on mailers "have been carefully considered," please state in detail (a) by whom they have been considered, (b) when they have been considered, and (c) how they have been considered?

RESPONSE

I considered them. Witness Stralberg considered them. Jim O'Brien considered them. We discussed them in limited ways with others, including counsel. Consideration began in early calendar 2003. Detailed consideration began in July of 2003. We considered and refined the proportion of the revenue to get from the piece rates. We considered the pound rates and whether pound-related costs were in the bundle costs. We considered the structure for the rates. We calculated rate increases for mailings with various characteristics. We looked at the rate differences and compared them to existing rate differences. We looked at the effect of changing the number of pieces per bundle and the number of bundles per sack and the weight and makeup of the pallets. We considered whether the signals were at the appropriate level to send information to mailers about what the cost implications of their decisions really are.

Response of Witness Mitchell to ABM/TW et al.-T1-27

TW et al.-T1-27. Why is it important or beneficial that periodicals rates move closer to those that would be generated by a competitive market, as you imply at page 6, lines 12-13?

RESPONSE

It is generally accepted that rates that would be generated by competitive markets are appropriately cost-based and send signals to buyers and potential buyers that lead to efficient resource allocation and the maximization of consumer utility.

Response of Witness Mitchell to ABM/TW et al.-T1-28

ABM/TW et al.-T1-28. Why isn't there a competitive market?

RESPONSE

The reason is not that the current rates are low and efficient or that appropriate signals are being sent in the rates. Rather, the reason competitors do not exist today is that the mailbox rule prevents effective delivery. If it were not for the mailbox rule, there would be competitors for periodicals delivery today, and they would be carrying, I believe, virtually all of the well-prepared, machinable pieces with barcodes.

Response of Witness Mitchell to ABM/TW et al.-T1-30

ABM/TW et al.-T1-30. Please explain how your proposed rates move "at a measured pace," as stated on page 6, line 13.

RESPONSE

The question of how to go about moving to improved rates is always a difficult one. If the rate differences were only a portion of the cost differences, the information sent to mailers in the rates would not be a reflection of the cost differences and would not allow appropriate comparisons to be made of current and alternative positions. Under such conditions, movement toward preferred positions can be slow or non-existent. Mailers who could make efficient changes might not, mailers making such changes might do so in an incomplete or unbalanced way, and mailers planning for the future would not have the guidance they need.

Further discussion of the movement of the proposed rates can be found in the section beginning on line 9 of page 54 of my testimony. For a discussion of certain aspects of the outcome of Docket No. R84-1, which changed the proportion of revenue obtained from the piece rates, see paragraph 6 of my response to ABM/TW et al.-T1-1. A similar situation occurred in Docket No. R90-1, in which some of the Standard rates increased 42 percent, and some Standard Nonprofit rates increased 51 percent.

Response of Witness Mitchell to ABM/TW et al.-T1-31

ABM/TW et al.-T1-31. You state at page 6, lines 16-21, that the impact of your proposal is tempered by the fact that there are no markups for the new rate elements. (a) Markups over what? (b) What markups are proposed for the other rate elements?

RESPONSE

(a) Markup over cost. (b) Since there are no markups for the new rate elements, the contribution of the subclass is obtained from the piece and pound rates, which leaves the markups where they are now, thus minimizing the effects of the change.

Response of Witness Mitchell to ABM/TW et al.-T1-32

ABM/TW et al.-T1-32. Will all small publications be helped by what you describe at page 6, line 22 to page 7, line 1 as "recognition of machinability"?

RESPONSE

One cannot say that all small mailers will be helped by the recognition of machinability. I believe, however, that the publications of many small mailers are machinable. Also, I believe all mailers should be provided information relating to the cost differences associated with machinability. No pieces should be non-machinable if the extra value associated with sending such pieces is less than the value of the extra resources drawn by the Postal Service from the nation in order to handle those pieces. Pieces seeing an increase due to this recognition are those that are now being provided below-cost rates, corrected for ECSI value.

Response of Witness Mitchell to ABM/TW et al.-T1-33

ABM/TW et al.-T1-33. How will small publications be helped by what you describe at page 7, line 1, as "improvements in the pallet/sack differential"?

RESPONSE

The current pallet/sack differential is biased in the direction of dropshipping – if you don't dropship, you don't get the pallet discount, even though the savings are there. The proposed rates are not infirm in this regard. Also, under the proposed rates, sacks get dropship discounts that are fairly based on costs, just as do pallets, and the pallet/sack differential becomes small or non-existent when sacks are used effectively. Sacks should not be discouraged unnecessarily or unfairly.

Response of Witness Mitchell to ABM/TW et al.-T1-34

ABM/TW et al.-T1-34. Will all small publications be helped by what you describe at page 7, line 2, as "improved dropship discounts for sacks"?

RESPONSE

Blanket and all-inclusive statements such as the one you suggest cannot generally be made. I see no reason, however, to exclude sacks from dropship discounts, especially since some mailers dropship them by air. They certainly deserve rates that recognize their costs. Also, many sacks are entered near their destination, quite naturally, because the mailers reside there. I see no reason not to give them fair rates.

Response of Witness Mitchell to ABM/TW et al.-T1-35

ABM/TW et al.-T1-35. Please provide your understanding of the extent that sacks are drop shipped and the reasons underlying that understanding.

RESPONSE

A sack entered at a destination facility could have been dropshipped (i.e., transported some distance by the mailer or his agent) or could be entered there because the mail was printed there. The Postal Service does not interrogate mailers to see how far they may have driven. Whatever the reason for a sack being entered at a destination office, I believe it should be provided a fair rate.

I do not know the extent to which sacks are dropshipped. It is well known that some sacks are dropshipped by small and large mailers, by air, for service reasons, using aircraft that cannot handle pallets. It should not be necessary for the volume of these sacks to reach some critical mass in order for them to receive fair rates. Further, this volume might grow under improved rates.

Response of Witness Mitchell to ABM/TW et al.-T1-36

ABM/TW et al.-T1-36. You testify at page 8, lines 2-7, that Congress initially set periodicals rates to be "extremely attractive." Is it still important that periodicals rates be attractive, and if so why?

RESPONSE

Congress still thinks it is important, and so do I. It has singled out periodicals for separate and special rate treatment by specifying that their ECSI value must be recognized. It is not clear to me how this provision would be honored if Periodicals class rates were to come out higher than some other applicable rates.

Response of Witness Mitchell to ABM/TW et al.-T1-37

ABM/TW et al.-T1-37. You refer at page 8, lines 12-15 to congressional recognition of the ECSI value of periodicals. (a) Do improvements in printing and information technology, along with the availability of cable television and the internet, substantially diminish the need to recognize the ECSI value of periodicals? (b) If not, why not?

RESPONSE

(a) I do not see why they would. (b) In my mind, the most appropriate way to think about the recognition of ECSI value is to consider the externalities involved. I do not see how these would be affected by printing technology or cable television.

Response of Witness Mitchell to ABM/TW et al.-T1-38

ABM/TW et al.-T1-38. What percentage of the periodicals mailed today have circulations less than 250,000?

RESPONSE

I have no way of knowing.

Response of Witness Mitchell to ABM/TW et al.-T1-39

ABM/TW et al.-T1-39. What percentage of the periodicals mailed today have circulations less than 100,000?

RESPONSE

Please see my response to ABM/TW et al.-T1-38.

Response of Witness Mitchell to ABM/TW et al.-T1-40

ABM/TW et al.-T1-40. If your proposed rates increase rates for most periodicals, would that make the periodicals rate less attractive?

RESPONSE

No. The level of attractiveness would seem most likely to be taken as some kind of summation over volume of the difference between an applicable alternative rate and the Periodicals rate. Since the rates being proposed are revenue neutral, I don't see why this would change. Or, in the alternative, one might look at the difference between a representative alternative rate and a representative Periodicals rate.

The focus on alternatives is in order because it is difficult to evaluate a rate in isolation. Corrected for their proportions of editorial content, a finding that the rates for some periodicals are more attractive than the rates for others (i.e., some are further below the alternative rates than others) would seem to imply that something is out of balance. Were this imbalance to be corrected, it is difficult to see that any attractiveness measure would be affected in a meaningful way.

Response of Witness Mitchell to ABM/TW et al.-T1-41

ABM/TW et al.-T1-41. You state at page 11, line 12, that periodicals rates are not cost based. Are they market based?

RESPONSE

The term "market-based" has no generally accepted meaning. Accordingly, I have no idea what it is that you want to know. However, I usually think of the term in one of two ways. The first relates to whether demand is recognized when the rates are set, which might lead in the extreme to different rates for each mailer, depending on his willingness (or ability) to pay. This is not done in Periodicals. The second relates to whether the rates are structured similarly to rates that would be generated by a competitive market or in a way that would be competitive in such a market. As discussed further in my response to ABM/TW et al.-T1-28, I do not believe that Periodicals rates are market-based in this sense either.

Response of Witness Mitchell to ABM/TW et al.-T1-42

ABM/TW et al.-T1-42. Are First-Class rates cost based?

RESPONSE

The term "cost-based" has no generally accepted meaning and is used to mean different, sometimes mutually contradictory, things. Occasionally, the context is helpful. I use the term to mean that the costs of the mail in question are known and acknowledged, and that a decision on some defensible basis is made on what the markup over that cost should be. Defined in this way, I do not find First-Class rates to be cost based.

Response of Witness Mitchell to ABM/TW et al.-T1-43

ABM/TW et al.-T1-43. Are Standard mail rates cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is no.

Response of Witness Mitchell to ABM/TW et al.-T1-44

ABM/TW et al.-T1-44. Are parcel rates cost based?

RESPONSE

Please see my response to ABM/TW et al.-T1-42. Numerous changes have been made in recent years in parcel post rates, and substantial cost evidence was developed and relied on in support of each change. However, I am not prepared to evaluate whether all relevant costs have been recognized or whether the markups are defensible.

Response of Witness Mitchell to ABM/TW et al.-T1-45

ABM/TW et al.-T1-45. Is the existing periodicals pallet discount cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is no.

Response of Witness Mitchell to ABM/TW et al.-T1-46

ABM/TW et al.-T1-46. Is the existing periodicals drop shipped pallet discount cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is no.

Response of Witness Mitchell to ABM/TW et al.-T1-47

ABM/TW et al.-T1-47. Are the periodicals advertising pound rates cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is that the *differences* in the advertising pound rates (which are in principle preserved in the proposed rates) are cost-based in degree, since they recognize transportation costs but not non-transportation costs, but that the *levels* of the advertising pound rates are not well related to costs.

Response of Witness Mitchell to ABM/TW et al.-T1-48

ABM/TW et al.-T1-48 Are the periodicals carrier route discounts cost-based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is yes.

Response of Witness Mitchell to ABM/TW et al.-T1-49

ABM/TW et al.-T1-49 Is the periodicals 3-digit presort discount cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is yes.

Response of Witness Mitchell to ABM/TW et al.-T1-50

ABM/TW et al.-T1-50 Is the periodicals barcode discount cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is yes.

Response of Witness Mitchell to ABM/TW et al.-T1-51

ABM/TW et al.-T1-51 Is the periodicals DDU entry discount cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is that it is cost-based in limited degree, due to the circumstances discussed in my response to ABM/TW et al.-T1-23 and to the flat editorial pound rate.

Response of Witness Mitchell to ABM/TW et al.-T1-52

ABM/TW et al.-T1-52 Is the periodicals DSCF entry discount cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is that it is cost based in limited degree, due to the circumstances discussed in my response to ABM/TW et al.-T1-23 and to the flat editorial pound rate.

Response of Witness Mitchell to ABM/TW et al.-T1-53

ABM/TW et al.-T1-53 Is the periodicals DADC entry discount cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is that it is cost based in limited degree, due to the circumstances discussed in my response to ABM/TW et al.-T1-23 and to the flat editorial pound rate.

Response of Witness Mitchell to ABM/TW et al.-T1-54

ABM/TW et al.-T1-54. Is the periodicals letter/flat differential cost based?

RESPONSE

The Periodicals rate structure does not have a letter/flat differential.

Response of Witness Mitchell to ABM/TW et al.-T1-55

ABM/TW et al.-T1-55. In your proposal, are the editorial pound rates cost based?

RESPONSE

Based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is yes.

Response of Witness Mitchell to ABM/TW et al.-T1-56

ABM/TW et al.-T1-56. In your proposal, is the differential between the editorial pound rates and the advertising pound rates cost based?

RESPONSE

There is no differential between the editorial pound rates and the advertising pound rates in my proposal. See the "Proposed Rate Schedule" on page 43 of my testimony. Since there is certainly no difference in the cost of handling editorial and advertising matter, based on the reasoning provided in my response to ABM/TW et al.-T1-42, my answer is yes.

Response of Witness Mitchell to ABM/TW et al.-T1-57

ABM/TW et al.-T1-57 (corrected). Please confirm that, based upon your statement at page 11, lines 19-22, that pound rates play a "substantially lesser role" than they did prior to reorganization, the contribution to "inefficiency" of a flat editorial rate has also declined substantially. If you cannot confirm, please explain why.

RESPONSE

Not confirmed. The importance of pound rates playing a lesser role is that there is no longer a need to subsidize higher-zone distribution, because charging rates that cover costs will not affect that distribution.

Neither the absolute level of the pound rates nor their proportion of total postage (both of which have been reduced by the evolution of the piece rates) is as important to efficiency as are the differences of the pound rates across zones. In 1970, the zone-8 rate was 17.0 cents (per pound) and the zones-1&2 rate was 5.2 cents, differing by 11.8 cents. In the current rates, the corresponding difference is 30.0 cents. Moreover, mailers now are much more responsive to signals in rates than they were in the past. Part of the gain resulting from improved signals lies in the response of mailers.

Response of Witness Mitchell to ABM/TW et al.-T1-58

ABM/TW et al.-T1-58. With reference to your testimony at page 16, lines 3-6, please give the details, and an example, of when a mailer has a choice between preparing one 24-piece bundle and 24 sacks containing one piece each, and state the frequency with which mailers actually choose to mail one-piece sacks.

RESPONSE

I do not know the frequency of one choice vs. another and have no idea what the volume of single-piece (or meager-piece) sacks might be; but given the level and behavior in recent years of Periodicals costs, I am concerned that they might occur all too often. The problem is that mailers are given no information in rates that might help them focus on the cost implications of their decisions or on the alternatives available.

The classic situation might be a supplemental mailing of 24 pieces going to widely dispersed addresses. The pieces could be prepared in a 24-piece mixed ADC bundle and placed in a mixed ADC sack, or they could be placed in 24 5-digit sacks that would travel unopened to the respective DDUs. Supplemental mailings (including special-edition mailings) tend to be frequent and expensive. It seems likely that they all pay rates that are substantially below costs. Mailers should consider whether alternatives are available, including the possibility of integrating such mailings with a main file. Without appropriate signals, they will not do so.

Response of Witness Mitchell to ABM/TW et al.-T1-59

ABM/TW et al.-T1-59. You state at page 16, line 8, that if a mailer is willing to pay the cost of handling 24 sacks with one piece, "the outcome is not inconsistent with efficiency." Is it consistent with efficiency?

RESPONSE

To the extent that *postal rates* can have an effect on efficiency, which I believe is the only issue of efficiency before the Commission, "if a mailer is willing to pay the cost," it is consistent with efficiency for 24 pieces of mail to be handled in 24 sacks, or to be carried by 24 couriers in 24 chauffeured limousines. The point is that there is nothing wrong with preferring to use a sack, even one that is virtually empty, as long as the mailer pays rates that recognize the associated costs.

The problem is that, under the current rate structure, a mailer could choose a high-cost (to the Postal Service and the nation) service when the value (to the mailer) of the service is less than the cost imposed. Further, the mailer might do this without being aware of the costs being imposed and without knowing that a burden is thereby being placed on someone else.

Response of Witness Mitchell to ABM/TW et al.-T1-60

ABM/TW et al.-T1-60. You state at page 16, lines 18-19, that there was an "enormous waste of resources" resulting from the fact that 14.6% of Standard mail was dropshipped before 1990, but 73.3% is now. (a) What resources were wasted? (b) In each situation, didn't the mail have to be transported by someone? (c) Is it your testimony that Postal Service transportation is inherently less efficient than private transportation? (d) If so, why? (e) If not, why is it necessarily less efficient for mailers to pay the Postal Service to transport their mail than it is for them to pay private carriers to transport their mail?

RESPONSE

One of the reasons, of course, for proposing the dropship discounts in Standard (then third-class) mail was to give fair and competitive rates to mailers whose mail was destination-entered naturally, because the mail was printed in the destination city. It certainly didn't make sense for such a mailer to have the option of having the mail printed in a distant city and turned over to the Postal Service to carry back at no additional charge. But when I developed those dropship discounts, neither I nor anyone I talked to at the Postal Service had any idea how much mail would become dropshipped, though some of it involved little more than shifting control of a plant-load contract to the mailer.

The general idea in worksharing is to give a discount equal to the Postal Service's savings and to let the mailer decide who should do the work. There is no reason for the Postal Service to want to get out of the transportation business. Indeed, part of its assignment and part of the concept of a national postal service relates to its ability to amass large volumes of mail and to provide efficient transportation. Nevertheless, the rates need to reflect the costs of this provision.

When the mailer chooses to do the transporting, it is generally because he can do it at a lower cost than the Postal Service, understanding as well that there could be value in any improvement in service. This value, plus the difference between the

cost to the Postal Service and the cost to the mailer is net gain, much like stemming the waste of resources. It is important to keep in mind that once the mailer takes control, he has options that the Postal Service does not have and he has incentives to innovate and to do things that he will not do for the Postal Service. For example, he might coordinate various mailings, schedule production in a different way, handle risk in a different way, and work with the trucking companies in a different way. Also, the value of any improved service is not realizable at all under Postal Service transportation.

Response of Witness Mitchell to ABM/TW et al.-T1-61

ABM/TW et al.-T1-61 (corrected). (a) Please state the basis for your assumption at page 17, footnote 8, that postage costs "are included in printer's [sic: printers'] bids." (b) did you ask witness Schick, from QuadGraphics, or any other printer if this assumption is correct? (c) If so, what was the response?

RESPONSE

I made the assumption because, whether the postage is in the printer's bid or not, I think it highly likely that the burden of paying the postage falls on the publisher instead of the printer. I have not discussed this with witness Schick or any other printer, at least not in recent years.

The point is very simple. Suppose you live in Cleveland and are the publisher of *Cleveland Supercity* magazine. And suppose further that nearly all of the copies go to subscribers who reside in the general vicinity of Cleveland. Now consider getting your magazine printed and mailed. Suppose a printer nearby will print it for 20 cents (per copy) and a printer at a distant location will print it for 19, neither including postage. The postage if printed and entered nearby is 30.0 cents (per piece), and the postage if printed and entered at the distant location is 30.6 cents. You will gain 0.4 cents (per piece) by having it printed at the distant location. But if the extra cost to the Postal Service of having your publication entered at the distant location is 2 cents, allowing you to have it printed and entered there is a really bad deal for other mailers and for the nation, and wastes energy besides. The rates need to reflect the Postal Service's costs. Without that information in the rates, you cannot and will not make the correct decision.

Response of Witness Mitchell to ABM/TW et al.-T1-62

ABM/TW et al.-T1-62. Who were the "beneficiaries of the existing rate" to whom you refer at page 19, line 13.

RESPONSE

The publishers mailing publications for 1 cent per pound or fraction thereof, regardless of distance or editorial content. The term "beneficiary" seems in order since that rate, close and even more-so far, was way below cost. The likelihood of a zoned rate structure that lowered their total postage bill was zero. One cannot blame them for clinging to a low local rate and for wanting it to apply to all distances, regardless of the cost to what was then, in effect, the Federal Government.

Response of Witness Mitchell to ABM/TW et al.-T1-63

ABM/TW et al.-T1-63. Please explain the role of the complainants in the "negotiations and compromise" to which you refer at page 19, line 15, through page 20, line 3.

RESPONSE

The negotiations at issue took place in 1917. I do not know whether any of the complainants even existed at that time.

Response of Witness Mitchell to ABM/TW et al.-T1-64

ABM/TW et al.-T1-64. Do you believe that if periodicals rates were established without regard to their ECSI value, and if as a result the markup over attributable costs were to increase to the average system markup, there would be any effect on the flow or availability of information in the United States?

RESPONSE

In Docket No. R2001-1, Postal Service witness Tolley estimated the own-price elasticity of Regular Periodicals to be –0.17, substantially lower in absolute value than most other categories. This means that a 10 percent increase in rates would be estimated to cause a reduction in volume of 1.7 percent, *ceteris paribus*. This is a market relationship and would not apply to individual publications or groups of publications. Elasticities probably say more about quantities than about availability. Anyone placing a meaningful value on the information in a periodical would not likely be one to see the effects of any volume decline.

Asking about the effects of an increase in the average rate for Periodicals, however, is quite different from asking about the effects of changing to the rates in our proposal. The proposed rates are revenue neutral and with any mailer response at all, the average postage paid by mailers will decline. This is equivalent to a rate decrease. Also, it is a general presumption that cost-based rates serve markets more effectively than other rates, as the MOAA court apparently had in mind when it said that "the divergence from cost principles has the probable tendency of increasing overall costs of distribution, and thereby reducing the market-clearing level of distribution." (2 F.3d 408, 436 (D.C. Cir. 1993))

Response of Witness Mitchell to ABM/TW et al.-T1-65

ABM/TW et al.-T1-65. You testify at page 21, lines 4-5, that publishers should not find it profitable to drop subscribers in distant zones. Might publishers in that situation tend to devote more of their marketing resources on the less costly zones?

RESPONSE

Persons desirous of obtaining subscriptions are not affected by solicitation practices; they see the publications at a newsstand, they hear about them from a friend, they hear about them through an agent (including national promotions of large groups of magazines and the promotion packages I get continually in my credit card statements), and they seek them out in other ways. Also, persons on well-suited or high-quality lists will be profitable targets no matter where they reside. The question you raise might apply at the margin to low-quality lists. If a publisher had a list (or some other channel) that was viewed as likely to draw a low response, he might decide that a return exists for using the list in a low-postage area but not in a high-postage area, although this may represent a level of fine-tuning not achievable. But the more likely situation would probably involve deciding whether to mail to the same list a second or third time. It is relatively common to mail again to the same list, particularly if a prior solicitation yielded an encouraging response. In this case, a potential subscriber in a distant zone might be solicited twice and then not called again. It is difficult to argue that such a potential subscriber has not been given ample opportunity to subscribe.

Part of the solicitation process involves securing renewals. At a spring 2004 IDEAlliance meeting, the Director of Postal Affairs of Reiman Publications said that Reiman makes 13 attempts to obtain renewals. She didn't say so, but if she had said that she makes only 12 attempts in high-zone areas, I would have understood. But the situation here, should it exist, is not troubling. After 6 or 8 attempts by the

publisher, it would seem that the subscriber has had every reasonable opportunity to re-subscribe, and that the publication is as available to him as anyone could desire. Further, if the value placed by him on the publication is at any meaningful level whatever, he would have re-subscribed long ago.

Response of Witness Mitchell to ABM/TW et al.-T1-66

ABM/TW et al.-T1-66. You testify at page 21, lines 5-9, that even if zoning the editorial rate caused some areas to be disfavored, "it is hard to see," given all of the "other sources of information and avenues of communication now available," that there would be adverse consequences. Please examine the list of American Business Media member publications provided as an attachment to American Business Media's first interrogatories to witness John Steele Gordon and identify those whose content is available in reasonably equivalent depth and reliability from "other sources of information and avenues of communication."

RESPONSE

Your question misrepresents my testimony. I did not state that " 'it is hard to see,' given all of the 'other sources of information and avenues of communication now available,' that there would be adverse consequences." I stated that "it is hard to see how, given all of the other sources of information and avenues of communication now available, *the effect on the unity or cohesion of the nation could be significant*" (emphasis added).

I am not competent to identify the member publications of American Business Media whose content is currently available from other sources. I assume, however, that if their content is *valuable*, potential recipients should be willing to cover the costs of sending it. Many if not most of the publications on your list are apparently sent to profit-making businesses that would be expected to use the information to make more profit, sometimes by putting competitors out of business. I do not see why the transportation and delivery of magazines to them should be subsidized.

Response of Witness Mitchell to ABM/TW et al.-T1-67

ABM/TW et al.-T1-67. What mailers now pay the institutional costs that periodicals mailers would pay if their rates were not restrained to reflect their ECSI value?

RESPONSE

If the contribution to institutional costs of the Periodicals subclass were to increase, it is not possible to say which rates would decrease. Similarly, if the contribution to institutional costs of the same subclass were to decrease, whether due to a decision to recognize ECSI value or some other reason, it is not possible to say which rates would increase.

Response of Witness Mitchell to ABM/TW et al.-T1-68

ABM/TW et al.-T1-68. (a) Are you opposed to the low, single-digit cost coverage that Periodicals have enjoyed for several years? (b) If so, why? (c) If not, why not?

RESPONSE

I am not opposed to the cost coverage about which you ask. I view it as selected in part in response to a troubling situation surrounding Periodicals costs. This situation is addressed in my testimony and undergirds the need for the changes being proposed.

Response of Witness Mitchell to ABM/TW et al.-T1-69

ABM/TW et al.-T1-69. Where are the publications listed at page 22, lines 17-20, printed?

RESPONSE

I do not know.

Response of Witness Mitchell to ABM/TW et al.-T1-70

ABM/TW et al.-T1-70. Please identify the city magazine discussed at page 23, lines 11-13, and state where it is printed and whether it is drop shipped.

RESPONSE

When I worked for the Postal Service, I found myself able to obtain mailing statements quite easily, either through the Postal Service or from mailers. I recall one printer handing me consolidated mailing statements for 50 publications. Since then, it has not been so easy. In the summer of 2003, before I began to outline or develop my testimony, I did a number of Internet searches for local and regional publications. I was already familiar with the *Washingtonian* and the *Baltimore Magazine*. I found that there are quite a large number of similar magazines. I then inquired to see if I could get a mailing profile for any of the city magazines. One source referred me to another source, who was willing to satisfy my curiosity on the condition that I not use the name of the magazine or the printer. I can tell you, however, that it is entered into the Postal Service at a point not substantially distant from where it is printed.

Response of Witness Mitchell to ABM/TW et al.-T1-71

ABM/TW et al.-T1-71. You say at page 24, line 22, through page 23, line 1, that the present periodicals rate structure amounts to the Postal Service saying to a local publication with little or no advertising that it will transport it for free and that all of the freight will be paid by other mailers. (a) Please identify ten such publications. (b) what other mailers will pay the freight costs? (c) Does the Postal Service give the same message to, for example, Capital One with respect to its First-Class credit card solicitations?

RESPONSE

I have no way of identifying publications that might fit subject model. But identifying such publications would not make less troublesome the situation surrounding the signals being sent. The signals are real, and the opportunity exists to have other mailers pay the costs thus caused. Within the framework of a fixed cost coverage and fixed billing determinants, the costs are covered by *other* Periodicals mailers. When a mailer shifts toward being printed further away, the Postal Service's costs increase more than its revenues, with the implication that the rates for *all* Periodicals will have to be increased in the next rate case. The situation is undesirable.

I do not know how Capital One selects its printing locations for its First-Class solicitations. To the extent that it is a national mailer from one printing location, however, the opportunity to increase its average haul is substantial. That is, the First-Class rate structure gives such mailers the option of increasing their average haul and having their mail transported the greater distance at no apparent additional charge, by air. It is difficult to argue that the signals involved are anything but inefficient, and it seems doubtful that ease of administration and use are important issues for the bulk categories of First Class.

Response of Witness Mitchell to ABM/TW et al.-T1-72

ABM/TW et al.-T1-72. (a) *Please identify each periodical published by the* complainants that have "subscribers in limited geographic areas," as you use that phrase at page 25, line 6. (b) How many subscribers in limited geographic areas receive those periodicals? (c) what percentage do such copies represent of the total copies of all of the publications of the complainants?

RESPONSE

The discussion on page 25 relates to local and regional publications whose entire print-run would be distributed predominantly in a specific geographic area. The *Indianapolis Monthly* would be an example. It does not refer to broadly distributed magazines that may prepare local editions by selective binding, such as *Time's* Chicago Metro edition or *TV Guide's* 150 local editions. None of the complainants publish local or regional publications.

Response of Witness Mitchell to ABM/TW et al.-T1-73

ABM/TW et al.-T1-73. (a) Have you been retained in this case to represent the interests of regional or local publications? (b) If so, provide the details.

RESPONSE

No. I have been retained in this case to provide expert testimony on matters of rate design, not as a representative of any interest or party.

Response of Witness Mitchell to ABM/TW et al.-T1-74

ABM/TW et al.-T1-74. Please estimate the percentage of periodical pieces entered in zones 1 and 2 today that are drop shipped into those zones.

RESPONSE

I have no way of developing such an estimate for today or for any representative period, even if it were clear how to define dropshipment. Since I do not believe the Postal Service interrogates mailers concerning how far they may have driven their trucks, I would think that a special survey might be needed to approach the question.

Note that the attractiveness of zones 1&2 as a dropship point might increase under the proposed rates, since the pallet discounts implicit in the proposed Rate Schedule do not require DADC/DSCF entry. This feature could be of interest to smaller mailers.

Response of Witness Mitchell to ABM/TW et al.-T1-75

ABM/TW et al.-T1-75. Why have you chosen not to zone the Ride-Along rate?

RESPONSE

I have not given any consideration to zoning the Ride-Along rate, possibly because the revenues from it are handled as an appendage to the billing determinants. However, I would not be opposed to considering it. The first step might be to see if any supporting data are available.

Response of Witness Mitchell to ABM/TW et al.-T1-76

ABM/TW et al.-T1-76. You state at page 28, lines 8-11, that you are not suggesting that all mailers can make the changes that would enable them to avoid large rate increases if the proposed rates were adopted. Please identify the types of mailer that would not be able to make such changes.

RESPONSE

I don't believe one can identify types that would not be able to make changes. Virtually all mailers face alternatives surrounding sack makeup, sack weight, bundle makeup, bundle thickness, pallet makeup, minimum pallet weight, and entry points. They also face questions about how to handle supplemental mailings and special editons, whether to barcode, and whether to make their pieces machinable. On many of these questions, the current rates send mailers inadequate information and leave them in the dark.

Response of Witness Mitchell to ABM/TW et al.-T1-79

ABM/TW et al.-T1-79. What percentage of the pieces produced by the complainants cannot be processed on an AFSM 100?

RESPONSE

No records exist that would allow calculation of the percentage of complainants' pieces that can or cannot be processed on an AFSM-100. Machinability sometimes varies from issue to issue, depending on weight and other factors, and the decision on what goes on the AFSM-100 is normally made by Postal Service machine operators.

However, for the purposes of the analysis performed by witness Stralberg in response to ABM/TW et al.-T1-3, the following publications were assumed to be non-machinable on the AFSM-100: *Time for Kids*, *In Style*, *Vanity Fair,* and *Modern Bride*.

Response of Witness Mitchell to ABM/TW et al.-T1-80

ABM/TW et al.-T1-80. Please explain why you propose dropship discounts for mail deposited at a destination BMC.

RESPONSE

Some background on this question is provided in footnote 27 on page 31 of my testimony. It appears that the term "transfer hub" is no longer being used and that facilities once so designated are now referred to as BMCs. The notion is reasonably simple. A BMC is positioned and connected to serve a broad territory efficiently, a territory that would generally receive substantial volumes of mail. Even a relatively small mailer could have a great deal of volume for such a large area. It seems likely that many mailers might find it effective to take mail to DBMCs and that the Postal Service could process it from there quite well. Costs and volumes are available for DBMC-entered mail. We believe that DBMC entry is an option that should be available.

The general idea behind the Postal Service's plant loading program is that mail can be taken directly to a downstream facility, avoiding as much local handling as possible. DBMCs would seem to be an important option in this program. If the Postal Service is not reaching them, I believe it should be. Our proposal is to bring this same option to mailers.

Response of Witness Mitchell to ABM/TW et al.-T1-81

ABM/TW et al.-T1-81. Please explain why DSCF entry pieces would pay no distance-related transportation costs under your proposal.

RESPONSE

DSCF-entered pieces pay no distance-related transportation costs now. I have made no changes in this regard but have simply followed current practice. The intra-SCF portion of segment 14 transportation costs is not large and is not treated as distance-related. It is paid equally by all mail since all mail originates and destinates in some SCF. No attempt is made to charge mail according the number of miles it travels within an SCF area on contract transportation.

Response of Witness Mitchell to ABM/TW et al.-T1-82

ABM/TW et al.-T1-82. (a) What types of periodical mail benefit from the adjustment at page 33, lines 16-20, to increase the passthrough of DSCF pound-related costs to 10%? (b) what types of periodical mail would pay more as a result of this adjustment?

RESPONSE

No passthrough has been increased to 10 percent. The effects of the adjustments discussed on page 33 are outlined in my response to Question 4 of POIR No. 1.

Response of Witness Mitchell to ABM/TW et al.-T1-83

ABM/TW et al.-T1-83. What percentage of the complainants mail is entered at the DSCF and what percentage is entered at the DSCF or DDU?

RESPONSE

The percentages of mail entered at the DSCF and the DDU, in order, by complainant are: Time Warner 69.17 percent and 0.03 percent; TV Guide 88.28 percent and 1.32 percent; Newsweek 72.44 percent and 0.74 percent; Condé Nast 66.50 percent and 0.94 percent; and Reader's Digest 65.05 percent and 0.00 percent.

Response of Witness Mitchell to ABM/TW et al.-T1-84

ABM/TW et al.-T1-84. (a) Should all Postal Service workshare discounts be equal to avoided costs? (b) If not, under what circumstances should the discounts depart from avoided costs?

RESPONSE

Consistent with the Reorganization Act, a broad range of factors is considered when rates are set. Blanket rules are dangerous and can be counterproductive.

Generally, at least in situations where externalities do not exist, economic efficiency requires that costs be acknowledged and that markups be consistent with the elasticities and cross elasticities. Setting rates in this way has been shown to be equivalent to a breakeven version of rates that would be generated by a competitive market.

In some cases, mailers move from one rate to another by worksharing, which means they do a piece of work that the Postal Service would otherwise do. Then the Postal Service integrates the pieces into the mailstream at what is often referred to as further downstream. For example, a mailer (or an agent of a mailer) might sort pieces into trays or transport them to a destination area. In other cases, moving from one rate to another involves altering Postal Service costs by doing something that may be different from what the Postal Service would otherwise do, such as by sorting addresses on a computer, using an address file to spray on a barcode, changing the shape or processing category of a piece, adjusting the weight of a piece, or printing a piece near its destination (whether or not the mailer resides near the destination). Mail entered near the destination is often referred to as dropshipped, even when no special transportation activities have been performed. Some of these matters are discussed in more detail in my paper: "Postal Worksharing: Welfare, Technical Efficiency, and Pareto Optimality," in *Emerging*

Competition In Postal and Delivery Services, edited by Michael A. Crew and Paul R. Kleindorfer, Boston, Kluwer Academic Publishers, 1999, which is available on the Commission's website.

In situations where mailers have the option of taking steps that reduce the Postal Service's costs, including worksharing activities, interest sometimes centers on setting the rates so that the mailer performs those steps in cases where the cost to the mailer (less any concomitant increase in the value of the service received) is less than the cost savings to the Postal Service. The goal here would be one of technical efficiency or lowest combined cost, adjusted for value. Setting rates in this way is generally taken to require setting the difference between the two rates, which is sometimes referred to or displayed as a discount, equal to the unit incremental cost avoided when the mailers move from one rate to the other, although the change in cost for pieces at the margin can also be important.

But there is more to ratesetting than notions of technical efficiency and lowest combined cost. Reality may not fit the scheme contemplated by the worksharing concept. Avoided costs can be difficult to estimate. Interest can center on a desire to deaverage rates in order to meet competition, reflect costs, and improve the allocation of resources. Concepts of fairness can be important. The economic efficiency of the rates may receive attention. Mailer sensitivity to the rate differences can vary, causing differences in the cross elasticities. In addition, the behavior of rates and costs over time can raise questions of continuity and the effects on mailers.

The avoided cost guideline about which you ask has been important in the past and will undoubtedly be so in the future. But many other factors can also be important. Furthermore, there are definitional problems that would influence where the rule

would be applied, such as what worksharing really is and how avoided costs should be defined.

Response of Witness Mitchell to ABM/TW et al.-T1-85

ABM/TW et al.-T1-85. At page 39, lines 7-9, you state that higher zone publications would pay only the additional costs associated with distant entry and no additional fixed costs. (a) By "fixed costs," are you referring to institutional costs? (b) If not, to what are you referring?

RESPONSE

Yes. Fixed costs are a residual found by subtracting the attributable costs from the total costs, and are sometimes referred to in postal parlance as institutional costs.

Response of Witness Mitchell to ABM/TW et al.-T1-86

ABM/TW et al.-T1-86. Do the rates you propose produce "equal implicit markups," as you refer to that term at page 47, line 28 to page 48, line 1 (quoting from the Commission)?

RESPONSE

If equal implicit markups is taken to mean equal implicit percentage markups over costs, no, consistent with the further explanation provided by the Commission in the same passage. To the extent that the rate structure being proposed is aligned with the important cost drivers, and if account is taken of the benefit given to editorial matter, the rates being proposed produce equal per-piece markups.

Response of Witness Mitchell to ABM/TW et al.-T1-87

ABM/TW et al.-T1-87. If the Postal Service were to begin delivery point sequencing of all flats, and if as a result the value of carrier route presort were to disappear, should the carrier route discount be immediately and completely eliminated?

RESPONSE

If the Postal Service sees an acceptable ROI for delivery point sequencing of all flats, one would expect the cost of 5-digit flats, which would cost the mailer less to prepare than carrier route flats, to be lower than the cost of carrier route flats. Under these conditions, the rates for 5-digit flats should decline to the point of being lower than the rates for carrier route flats (without the carrier route rates rising), and mailers would move voluntarily to the 5-digit category. It would not matter whether the carrier route discount were eliminated.

Response of Witness Mitchell to ABM/TW et al.-T1-88

ABM/TW et al.-T1-88. At page 49, lines 5-6, you state that periodicals mailers find themselves with the motivation but not the tools to change the way they prepare and present mail. Did you mean to say that they have the tools but not the motivation?

RESPONSE

It is clear that the signals and the information in the rates are deficient, which detracts from incentives that could be provided. But I see mailer motivation more broadly; I see mailers saying: "I want to be involved; I am willing to help; we are all in this together; just point me in the right direction."

Response of Witness Mitchell to ABM/TW et al.-T1-89

ABM/TW et al.-T1-89. (a) In setting rates, if the Commission should find that, for example, publishers of small weekly periodicals have no choice but to mail their product in 5-digit sacks in order to obtain reasonable service, and that such sacks tend to be low volume, should the Commission take that finding into consideration in assessing your proposal? (b) If so, how?

RESPONSE

What we have is a mailer saying: "If I prepare my mail in a way that imposes extra costs on the Postal Service and the nation, I believe I can achieve in some cases a one-day improvement in service levels, which is of considerable value to me, but I should receive a subsidy for doing this, and the extra costs I cause should be paid by some other publishers." Even if there were evidence that the other publishers had excess profits, or at least higher profits than the publisher causing the extra costs, and there is not, it is difficult to see that rates should be skewed in favor of the cost-causing mailer.

Periodicals should be processed on the evening received by the sectional centers and taken out the next day for delivery. If the behavior of the Postal Service is inconsistent with operating guidelines and with the service standards for the subclasses, the situation needs to be fixed. At the present time, however, I believe many mailers see 5-digit sacks as providing a degree of service improvement that they do not really provide. Additional testing needs to be done.

Response of Witness Mitchell to ABM/TW et al.-T1-90

ABM/TW et al.-T1-90. If the Commission should find that some of the higher costs of what complainants deem "inefficient" mail result from Postal Service concentration on efficient processing of the remainder of the mail, such as, for example, added costs that result from the elimination of sack sorters, should the Commission take that finding into consideration in assessing your proposal? (b) If so, how?

RESPONSE

The question of whether mail is inefficient does not hinge on the characteristics of the mail *per se*, the way the Postal Service processes it, or how productive the mailer is in preparing it. Rather, it hinges on its postage relative to its costs (with associated implications for efficient resource allocation) and on whether there are changes that could be made in the way the mail is prepared that would allow cost savings (to the Postal Service and the nation) that are greater than the cost to the mailer of making the changes, including the value of service changes. Of course, there could also be changes that increase Postal Service costs and decrease mailer costs more. Therefore, there is no particular sense in which inefficient mail has higher costs than any other mail.

To deal with your question, assume there are two categories of mail, *A* and *B*. In the first case, *A* is entered upstream and *B* is entered downstream, and let's follow your suggestion that *A* is on some basis inefficient. Your suggestion is that the Postal Service concentrates on and lowers the costs of *B* but does nothing unique to *A*, possibly causing the cost of *B* to decline 10 percent. As I see it, *A* also receives downstream processing. Accordingly, in view of its upstream processing, its costs might decline 5 percent, and the absolute magnitudes of the cost reductions would be the same. These costs should be recognized in ratesetting. The fact that the cost of processing *A* is higher than you might wish is no different from any other

area or product in the Postal Service whose costs someone feels should be lower, but are not.

In the second case, assume that *A* is in sacks and *B* is on pallets, that they are processed in parallel, and that the cost of *A* is 10 cents and the cost of *B* is 7 cents. As I understand your question, you posit that the Postal Service might concentrate on processing pallets and remove the sack sorters, and that the cost of *A* might increase to 12 cents. The reality of the 12-cent cost does not depend on where the Postal Service was concentrating when it occurred. Unless sack sorters are no longer the lowest-cost way to handle sacks, it does not seem in order that they be removed. Nevertheless, the 12-cent cost, should it exist, should be recognized, the characteristics of the situation at hand should be studied, and a decision should be made whether elimination of the sack sorters is consistent with efficient and economical management. The decision cannot be made until the homework is done.

Response of Witness Mitchell to ABM/TW et al.-T1-91

ABM/TW et al.-T1-91. (a) Do you agree with the manner in which the Commission treats the Alaska air costs? (b) If so, why? (c) If not, why not?

RESPONSE

I believe that the Commission regarded Alaska air costs as a special case, for policy reasons that are grounded in the Act. While I respect that decision, I cannot agree that volume-variable costs are properly characterized as "institutional" rather than "attributable," at least as those terms are understood by economists. I believe the decision can more properly be characterized, from an economist's point of view, as a policy-based exception to the attribution requirement of § 3622(b)(3).

Response of Witness Mitchell to ABM/TW et al.-T1-92

ABM/TW et al.-T1-92. (a) Assume that some machinable periodicals are sometimes processed manually so that greater volumes of Standard mail can be processed on machines and that, as a result, Standard mail costs in a facility are reduced by $2,000,000 while periodical costs are increased by $1,000,000. Would you make any attributable cost or rate modification to reflect this situation? (b) If so, why? (c) If not, why not?

RESPONSE

The situation you posit appears due to capacity limitations and could be the result of poor planning or flawed investment decisions. Whatever the cause, the first step is to perform the cost analysis. If it is the case that the rate of utilization of capacity is 100 percent, the marginal cost of Standard involves processing a piece manually just as does the marginal cost of Periodicals. Therefore, proper costing does not generate the dilemma that appears to exist in your question.

In the end, the costs of the Postal Service are what the costs of the Postal Service are. One cannot pretend that the resource implications of one volume vs. another are different from reality. If fairness adjustments are to be made, it is better to make them in the markups than in the costs, the latter being a relatively unexplored area.

Response of Witness Mitchell to ABM/TW et al.-T1-93

ABM/TW et al.-T1-93. You state at page 54, lines 13-15, that the rates you propose will adversely affect some, but that "the impact is limited." To support this assertion, you state that "only" 21% of the revenue is from bundle, sack and pallet charges and that "no markup is proposed from these charges." (a) Please describe in detail and provide the results of any analysis you have made to examine the impact of your proposed rates on individual publications. (b) Please confirm that, under your proposed rates (and without any change in mailing), the postage costs for some publications would increase by more than 50%.

RESPONSE

Without billing determinants for individual publications, the approach I used is to study representative situations. I can give you some examples.

Virtually all publications have a zone distribution, the final postage being a weighted average. Accordingly, select zone 5 as being representative of non-dropshipped publications. Further, assume 10 percent advertising, in sacks, machinable, barcoded, ADC presort, in an ADC container, origin-office entry, 3 ounces, 7 pieces per bundle, and 3 bundles per sack. The pieces in this situation receive an increase of 28.36 percent. If the number of pieces per bundle is changed to 12, the increase becomes 4.74 percent, and if a further change is made to 5 bundles per sack, the increase becomes negative, the postage declining 7.37 percent. I found the number of pieces per bundle and the number of bundles per sack to be quite important.

Increases of the magnitude you cite can occur for mail that is heavily subsidized currently and that makes no changes to its mailing practices. If, in the example just given, the pieces are changed to nonmachinable, nonbarcoded, 14 ounces, 4 pieces per bundle, and 3 bundles per sack (implying 12 pieces per sack), the increase becomes 49.07 percent.

Response of Witness Mitchell to ABM/TW et al.-T1-94

ABM/TW et al.-T1-94. With respect to the quotation in footnote 41, has worksharing of periodicals helped the Postal Service improve its productivity?

RESPONSE

Worksharing generally involves the mailer purchasing a different mix of services from the Postal Service than was purchased before. Except for scale effects, which would be long-term and second order, and for the possibility that the marginal cost curves might not be completely horizontal, the productivity of no potential service should change and, accordingly, neither should any measure of the Postal Service's overall productivity. However, it should be noted that worksharing can allow a mailer to avoid purchasing a service that is of lesser value, that is unproductive, or that the mailer can produce more efficiently.

Response of Witness Mitchell to ABM/TW et al.-T1-95

ABM/TW et al.-T1-95. Do you agree that, for some publications, the cost of obtaining a *new* subscriber exceeds the incremental revenue associated with that subscriber in the first year?

RESPONSE

Yes, that is relatively common. The hope is that renewals under more favorable circumstances will be achieved. The reasoning in my testimony deals with equilibrium tendencies.

Response of Witness Mitchell to ABM/TW et al.-T1-96

ABM/TW et al.-T1-96. Do publishers have sources of revenue associated with their publications—such as, for example, rental of mailing lists and ancillary products—other than subscription and advertising revenue?

RESPONSE

Yes, including revenue associated with conventions, the provision of training, databases, and library services, in addition to those you cite.

Response of Witness Mitchell to ABM/TW et al.-T1-97

ABM/TW et al.-T1-97. With respect to the formula on page 61, line 19, does inclusion of the "V" term mean that advertising revenue is directly proportional to the number of subscribers?

RESPONSE

On a long-term equilibrium basis, yes. Keep in mind that publishers can make changes in what might fashionably be called their basic business model, which might change the proportionality. But such changes are second-order in nature and would not generally be a response to rate changes. For example, *Forbes* magazine might find it in order to reduce its advertising rates if the average income of its readership declines. In terms of ECSI value and any interest in making the editorial content available to all who desire it, the implications of restricting readership to higher-income individuals are not clear.

Response of Witness Mitchell to ABM/TW et al.-T1-99

ABM/TW et al.-T1-99. What is the source for your statement at page 65, line 11, that the marginal cost of printing "is estimated" to be $0.17 per copy.

RESPONSE

Information of this kind is difficult to obtain, since publishers do not generally supply the details of their contracts with printers and printers do not supply details of their contracts with specific customers.

In order to obtain my estimate, I worked with production people at Time Inc. I asked them to use their general knowledge of how the printing industry works and to prepare an educated guess. They went to a newsstand and a library to obtain copies of the publication. They measured the trim width, the trim length, the paper stock used for the cover, the paper stock used for the body, the number of pages, and evaluated the colors used. The physical information was adjusted to be consistent with a copy weighing 3.3 ounces. They used a print order of 70,000 and 90,000. They built printing costs with estimates of plate preparation costs, running costs, ink costs, paper costs, binding costs, binding operation costs, inkjet supplies, inkjet operating costs, and packaging and handling costs. The fixed costs were separated from the marginal costs. The cost of 17 cents resulted. I agreed not to reveal details of the analytical process, but only to use final estimate as a ballpark figure.

The opportunity to go further exists. Any publication believing that more refined inputs would change my analysis can supply actual costs from its printing contract. If this is done, care should be taken to prepare marginal costs and not to focus on any kind of average. This is important because common bookkeeping practices sometimes do not focus on marginal costs.

Response of Witness Mitchell to ABM/TW et al.-T1-100

ABM/TW et al.-T1-100. (a) Have you asked the publisher of The New Republic whether it earns $49.55 less the cost of account maintenance for each zone 8 subscriber? (b) If so, what was the response?

RESPONSE

No.

Response of Witness Mitchell to ABM/TW et al.-T1-101

ABM/TW et al.-T1-101. What is the source for your marginal cost of printing of 31 cents for Pit & Quarry, cited at page 66, line 10?

RESPONSE

Based primarily on differences in publication weight, I made a rough adjustment to the estimate I had for *TNR*, as explained in my response to ABM/TW et al.-T1-99.

Response of Witness Mitchell to ABM/TW et al.-T1-102

ABM/TW et al.-T1-102. At page 66, line 12, you cite 46.63 cents as the postage cost of a zone 8 copy of Pit & Quarry. What would that postage cost be under your proposal?

RESPONSE

Based on the assumptions made in my response to Question 1 of POIR No. 1, along with the specific information for *Pit & Quarry*, the corresponding postage under the proposed rates would be 43.07 cents.

Response of Witness Mitchell to ABM/TW et al.-T1-103

ABM/TW et al.-T1-103. What is your understanding of the profit level, from the periodicals themselves, in the periodicals industry today?

RESPONSE

I cannot provide expert testimony on profit levels in the publications industry. It is generally true, however, that profit levels vary substantially among competitors and among firms in industries. I doubt if rates of return are correlated with circulation. It is also generally true that competition tends to keep the profit levels from being substantially above or substantially below the normal level. An exception can involve firms that are perpetually innovative and efficient.

Responses of Witness Mitchell to APWU/TW et al.-T1-1

APWU/TW et al.-T1-1. On page 1 of your testimony you state that you are describing the deficiencies in Periodical rates. Is it your contention that the current rates are not valid because they do not meet the requirements of the Postal Reorganization Act? If this is your contention please provide a precise listing of ways in which the rates fail to meet the PRA requirements.

RESPONSE

The legal validity and compliance of the current rates with the requirements of the Postal Reorganization Act are questions of law on which I am unable to provide an expert opinion. The respects in which I believe the rates fail to fulfill the policies of the Act, from the perspective an expert in rate design and regulatory economics, are described in my testimony.

Responses of Witness Mitchell to APWU/TW et al.-T1-2

APWU/TW et al.-T1-2. The PRC's rules for complaints (§3001.83 (c)) require that all complaints include copies of all correspondence or written communications between the complainant or his/her agent and the Postal Service which relate to the subject matter of the complaint. Your description of your background and your response to ABM/TW et al.-T1-1 show that you have experience and knowledge related to periodicals rates and rate increases over several years and have had discussions on these issues with all parties. Please provide copies of all written communications on these matters of which you are aware. Please include written communications between any of the complainants and the Postal Service as well as communications related to these interactions in a group setting, such as presentations during MTAC or other meetings of the periodicals mailers and the Postal Service.

RESPONSE

I am neither a complainant nor a representative of any complainant. Nor am I aware of any written communications between the complainants and the Postal Service that relate to the subject matter of the complaint. I am generally aware that various of the complainants have participated in public discussions regarding Periodicals issues for many years in a variety of forums, including the Commission, MTAC, ad hoc efforts such as the Periodicals Operations Review Team, congressional testimony, and testimony to the President's Commission on the Postal Service. I do not possess copies of these "communications" or specific knowledge by which I could identify them, other than the generally shared knowledge that they are matters of public record. For my own "communications" to the Postal Service or the complainants regarding Periodicals issues generally, see my responses to ABM/TW-T1-1 and 13.

Responses of Witness Mitchell to APWU/TW et al.-T1-3

APWU/TW et al.-T1-3. To better understand the potential impact of this proposed change in rate structure on smaller mailers, it is helpful to look at publications before and after such a rate structure change and see what the differences would be in the postage. The APWU's bimonthly publication *Postal Worker* is mailed out to its membership. A recent mail.dat file for this publication was analyzed using a program that Time-Warner has made available to mailers to estimate the change in postage that might be experienced using the rate structure proposed in this case. Theses are summary statistics generated by that program for the "current rates" calculation,

277, 755 pieces
100% editorial content,
0.25 pounds per piece,
mailed to all eight postal zones (90% to zones 3-8)
100% machinable,
88% 5-digit barcoded,
10% 3-digit barcoded,
no drop shipping,
93% received discounts for palletization.

However, the comparative analysis generated by the program indicates that the *Postal Worker* would pay higher postage under the new structure than under the current structure.

A) What would a publication with similar characteristics have to do to avoid increases in postage under this new structure?

B) What could a publication with similar characteristics do to reduce the number of sacks and increase the number of pallets beyond current levels?

C) APWU is more than pleased with the performance of the current printer/mailer for the *Postal Worke*r, however, the somewhat flexible publishing schedule of the *Postal Worker* and many other publications handled by this printer/mailer offer little opportunity for co-palletizing and this mailer does little dropshipping. Would APWU be forced to change its publishing schedules and long-time printer/mailer to avoid higher postage under the new rate structure?

D) Are there significant numbers of companies that are currently co-palletizing so that there would even be a viable co-palletizing option?

E) While this publication is mailed from the Washington metro area, would mailers in other areas have similar opportunities to take advantage of the service?

F) Please provide a count of all companies that are currently providing the services needed to achieve fewer sacks and more pallets to small mailers and indicate their general geographic distribution.

RESPONSE

Responses of Witness Mitchell to APWU/TW et al.-T1-3

A) I am not able to provide an expert opinion on what changes you should consider or on what effects they might have. I would note that you appear to have an unusually high zone distribution and that you provided no information on the number of bundles per sack or the number of pieces per bundle. These latter measures are very important in determining rate levels under the proposed rates.

B) Again, I have no experience in schemes to reduce the number of sacks or to convert sacks into pallets. It appears that you are heavily palletized already. It might be that further increases would require co-palletizing or co-mailing, options some printers can offer. With respect to either of these alternatives, the proposed rates provide a continuum of options, aligned with costs.

C) I understand that ties with printers are important and that there is often a preference to avoid disruption. Nevertheless, it is a fact that a widely distributed publication will have a lower average haul if mailed from a central location. Perhaps more important, however, is what the printer is able to offer in the way of coordinating with other mailings. No one will be *forced* to change schedules or printers. On the question of schedules, though, I believe technological change has led to many adjustments over the past few decades and I have no doubt that more are possible. It is also the case that many consultants recommend reexamining them occasionally to see if they are optimal and if the reasons behind them are really good.

D) I do not know how many companies are offering this option, although the issue is being widely discussed. I would note, however, that the experimental rates for co-palletization, existing and proposed, require dropshipment to get the discounts, even though a co-pallet will allow savings without dropshipping. Also, the passthroughs of savings for co-palletization in the current rates are small to the point of providing a

cash cow for the Postal Service. The proposed rates are neither biased, skewed, nor warped in these regards.

E) I do not understand the question. The rates proposed would apply nationwide, uniformly.

F) I am not able to provide this information. As for changing the number of sacks, however, it is my understanding that all printers face alternatives, particularly in the sense that parameters of various kinds must be input to the mailing software. In addition, the various software vendors will undoubted make adjustments to the software as experience under the rates is obtained.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-1

MH/TW et al.-T1-1: Under the reasoning presented in your testimony at page 16 lines 3-8, please explain whether, assuming cost-based rates, it would be efficient, as you use that term, for the Postal Service to handle 500 one-piece sacks in lieu of one 500-piece pallet.

RESPONSE

The evidence shows that the Postal Service's cost of handling 500 one-piece sacks is higher, on average, than the Postal Service's cost of handling one 500-piece pallet. The question of efficiency, however, is a little different, and it involves more than just issues of Postal Service handling.

Suppose that the mailer views himself as receiving $50 in value of service from using the sacks instead of the pallet, that the cost to the mailer of preparing the sacks is $500 lower than the cost of preparing the pallet, that handling the 500 sacks costs the Postal Service $550 ($1.10 per sack), that handling the pallet costs the Postal Service $25, and that the rates are cost-based in the sense that the sack charge (from the Postal Service to the mailer) is $1.10 and the pallet charge is $25. If the mailer shifts to the pallet under these conditions, the mailer will lose $25.00 (50+500-550+25), the Postal Service will remain at financial breakeven, and the nation will lose $25.00 (gain $25 in resources released by the Postal Service and the mailer (550-500-25) and lose $50 in value of service). Under these conditions, a change to pallets would not be an efficiency improvement and, in view of the alternatives that we know about, there is nothing inefficient about the mailer using sacks.

The numbers in this example were developed for illustrative purposes. Actual numbers could be different. An outcome suggesting an efficiency improvement for shifting to pallets could easily occur. Such an outcome should not be taken as a

reflection on anything the Postal Service or the mailer had been doing before the rate change, but no shifting will occur unless improved signals are sent in the rates.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-2

MH/TW et al.-T1-2: Based on the reasoning presented in your testimony at page 16 lines 3-8, will the Postal Service be efficient under cost-based rates regardless of whether mailers modify their behavior?

RESPONSE

I hope that the Postal Service is productively efficient whether it handles several sacks with one bundle each or one sack with several bundles. But the reasoning you cite relates to economic efficiency, not productive efficiency, which is a broader concept than just what the Postal Service does. On this point, please see my response to MH/TW et al.-T1-1.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-3

MH/TW et al.-T1-3: Please discuss the extent to which unit costs for Postal Service transportation, and its unit costs of handling sacks, can be expected to increase assuming that mailers engage in increased dropshipping and reduce their use of sacks.

RESPONSE

A unit cost is usually for some operation or group of operations, and is the cost of that operation or group divided by the volume going through it. The operations about which you ask are those of (a) transporting mail and (b) handling sacks. The cost measure receiving prominent attention in virtually all proceedings before the Commission, and which is most relevant to virtually all economic analyses, is the attributable cost or the volume variable cost.

(a) The unit cost of transporting mail will remain the same when mailers engage in dropshipping, because the percentage decrease in the numerator is the same as the percentage decrease in the denominator. If the volume reduction is large, there is a possibility that the marginal cost will decline, due to scale effects. This would come about from a lower volume variability of the Postal Service's transportation systems, and would result in lower unit transportation costs, not higher ones. Such an effect would be second-order in nature. But there is no magic level for volume and there is no justification for attempting to control volume to obtain a specific unit cost outcome.

(b) The unit cost of handling sacks will remain the same when mailers shift to pallets, because the percentage decrease in the numerator is the same as the percentage decrease in the denominator. In this case, economies of scale are not generally believed to exist, so the size of the volume change should not matter.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-4

MH/TW et al.-T1-4: Does your testimony at page 21 line 19 through page 22 line 1 that the "expectation would certainly be for [local and regional publications] to print near their areas of delivery" assume that postage costs are or should be the primary factor in choosing a printing site? Please explain your answer, including the basis for any such assumption.

RESPONSE

No. Although publishers often negotiate with printers over the requirements (or specifications) of the job, with the end result thereby influenced by the capabilities of the printers and what they are able to offer, the common situation often boils down to printers submitting bids and publishers deciding what is best for them. The publisher would be expected to consider any postage differences as well as any differences in printing prices. Note, however, that the postage is often influenced by the way the printer prepares the mail, which in turn influences the printer's costs. Under these conditions, the printing costs cannot really be separated from the postage costs. Also, it would not generally be wise for a publisher to take the lowest-cost printing bid and then say: "Just pass on to me any postage costs that you incur." See also my response to ABM/TW et al.-T1-61 (corrected).

Response of TW et al. Witness Mitchell to MH/TW et al-T1-5

MH/TW et al.-T1-5: Does your testimony at pages 23 and 24 regarding "Camp 2" mailers assume that a local or regional publication that is printed at some distance from its delivery area would not have the same incentives as a national publication, with comparable circulation in that area, to dropship into that area? Please explain your answer, including the basis for any such assumption.

RESPONSE

No. However, local and regional publications that print at a distant location and then dropship could be viewed as Camp-3 mailers. The point of this passage in my testimony does not concern these mailers, because both the printing prices and the transportation prices they pay are market prices that would be expected to reflect all associated costs. They are, in effect, Camp-1 mailers with a market-based adjustment.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-6

MH/TW et al.-T1-6: With reference to your testimony at page 35 lines 14-15 that the current one-cent-per-piece discount for dropshipped pallets "presents an unnatural incentive to remove potentially attractive pallets from the Service's transportation system," (a) please explain what you mean by a "potentially attractive pallet" and (b) please explain whether you are suggesting that it would be more beneficial for the Postal Service to transport that pallet than if it were dropshipped, and explain the basis for any such assumption.

RESPONSE

(a) I mean that if the Postal Service is going to receive the same postage for transporting a pallet as it would receive for transporting an equivalent number of sacks (adjusted for the one-half-cent pallet discount), it should prefer to handle the pallet and should not arrange a discriminatory and unbalanced incentive to get the pallet to dropship. Certainly with the handling costs included (which are not in the dropship discounts), the unit transportation cost for an all-pallet system would be lower than that for an all-sack system, an outcome providing lower rates to mailers for transporting their mail. This would allow a more effective and more competitive postal system, in line with what should be its goals.

(b) Under the current rate, it would not be beneficial for the Postal Service to transport the pallet instead of it being dropshipped, because the extra postage it receives for transporting the pallet is less than its additional costs. This relationship does not hold under the proposed rates, under which the Postal Service should be indifferent.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-7

MH/TW et al.-T1-7: Based on the rate structure proposed at page 43 of your testimony, please confirm that in lieu of a 3-digit origin entered pallet consisting solely of 5-digit bundles totaling 500 copies and weighing 250 pounds, it would be less costly to (a) the mailer and (b) the Postal Service if the same bundles were mailed in ten 50-copy, 3-digit origin sacks. If you do not confirm, please explain and provide your calculations. If you do confirm, please explain whether mailing the sacks in lieu of the pallet would be more efficient, as you use that term.

RESPONSE

Not confirmed, unless the mailer's cost of preparing the pallet is the same as his cost of preparing the sacks and the value of the service received is the same. Until this additional information is known, a conclusion on efficiency cannot be reached. See also my response to MH/TW et al. -T1-1. Your example illustrates an aspect of reality that is rarely acknowledged and seems little understood, that the use of sacks can in some circumstances be a low-cost, efficient way of preparing and handling the mail. There is no reason to be against them *per se.*

Response of TW et al. Witness Mitchell to MH/TW et al-T1-8

MH/TW et al.-T1-8: Referring to your statement on page 45 note 39 that "Periodicals mailings are to a considerable extent repetitive," please confirm that weights of publications can vary widely from issue to issue and that under the current and proposed rate structures, such variation can substantially change the way that the mail is prepared and entered. Please explain your answer fully.

RESPONSE

Confirmed, due in part to the acknowledgment of regulations and in part to decisions made by the printer/publisher. Note, however, that postage variations and the costs of making preparation changes are presumably considered when such changes are made. Also, the rates being proposed will send improved signals to guide decisions on preparation changes.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-9

MH/TW et al.-T1-9: With reference to your testimony at page 47 lines 12-14, consider two Periodicals mailings by different mailers, one mailing consisting of 20,000 pieces and the other consisting of 2,000,000 pieces, with each mailer using the same presort software parameters and identical piece characteristics. Under the current rate structure the larger mailer pays considerably lower rates due to its higher volume, although an identical effort was undertaken to achieve the presort. Please explain whether and how it would be fair and equitable to widen this gap under the proposed rate structure, given that the mailers are taking identical steps to prepare and ship their mail efficiently, and assuming that the smaller mailer is unable to comail or co-palletize.

RESPONSE

Your question seems to presume that the status quo just happens to be fair, even though it too was created by following (an earlier set of) cost-based arguments, but that any improvement in the recognition of costs that might widen any rate differences would be less fair, based on a subjective impression about the amount of effort by the mailers involved. By implication, it would seem, any back-steps in the recognition of costs that might narrow any rate differences would be more fair. Fairness arguments, however, are always in the eye of the beholder and often warrant further review.

The rates being proposed are a step from the present situation to recognize costs in more appropriate ways. A number of reasons for doing this have been explained, including sending appropriate signals, improving efficiency, and making the Periodicals subclass more effective. But the steps are also justified on fairness grounds, because the current recognition of costs is now understood to be misaligned with how costs are actually incurred. It is difficult to argue the fairness of presenting a given rate to all mailers when some of the mailers incur lower costs and some of them incur higher costs.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-10

MH/TW et al.-T1-10: Referring to your testimony at page 49 note 40, please explain the basis for your confidence that but for the mailbox rule, private operators would be delivering a substantial portion of periodicals.

RESPONSE

Over some period of years, a number of private delivery operations have existed, and many still exist. I have talked with the operators of some of them, and the common theme has almost always been: "If only we could use the mailbox." But my confidence at this point is due almost entirely to my understanding of the experience of Publishers Express.

Publishers Express was a delivery operation for magazines begun in Atlanta. It grew from serving 2 ZIP Codes in one city to serving 1,000 ZIP Codes in 32 cities. Its CEO was Jim O'Brien, with whom I now work and with whom I have discussed this issue many times. He has explained that only one difficulty limited the operation's success. It was not the level of its rates relative to those of the Postal Service, or its costs, or a lack of interest and support from publishers. Rather, it was the persistent preference of recipients for receiving their magazines in their mailboxes. I have taken the position many times that I would be happy to put two boxes in front of my house, one postal and one non, but it has not been found possible to bring about such an outcome on a broad basis. It is also suggestive to note that Publishers Express had just scratched the surface on the opportunities of automation. Given time, advances would have been made, costs would have declined, and the effectiveness of operations would have increased.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-11

MH/TW et al.-T1-11: With reference to your testimony on page 40 lines 3-7 that "[t]o build these non-transportation costs into the pound rates, as well as to recover the revenue loss associated with the unzoned editorial pound rate, the usual procedure has been to develop first-cut pound rates based on transportation costs alone, and then to add an additional amount (23.8 cents per pound in PRC LR-8, R2001-1) onto each zoned rate:"

> (a) Please specify what portion of the additional amount of 23 cents is attributable to the revenue leakage associated with the unzoned editorial pound rate, what portion is attributable to pound-oriented non-transportation costs, what portion is attributable to non-distance-related transportation costs, what portion is attributable mark-up for institutional costs, and what portions are attributable to any other factors (please specify any and all such other factors and the portion attributable to each). If necessary, please provide your best estimate. Please specify the precise source for your answers, and for the 23.8 cents per pound figure, and explain any necessary calculations.
>
> (b) Please specify which of such portions, if any, of the referenced additional amount of 23.8 cents is incorporated in the pound charges for DDU, DSCF and DADC, respectively, and the extent to which each is so incorporated. If necessary, please provide your best estimate. Please specify the precise source for you answers and explain any necessary calculations.

RESPONSE

I have discovered that the reference in my testimony on line 7 of page 40 should be to the Outside County Excel workbook in PRC Library Reference *9*, instead of *8*. Unless otherwise noted, cells in that workbook referenced in this answer are on sheet 'Pound Data_Adv', the 23.8-cent figure being in cell F73.

(a) The calculations below are based on the scheme used to develop the settlement rates as contained in the library reference. Since the editorial pound rate in the settlement is 77.8 percent of the zones 1&2 pound rate for advertising, instead of the traditional 75 percent, the proportion developed for it is somewhat lower than normal, but not much. The advertising pound rates are shown in cells D78-D92, and the corresponding volumes are in cells E78-E92. The editorial pound rate in the settlement is $0.19. The pounds of editorial are in cells D28-D37 on sheet 'Pound

Response of TW et al. Witness Mitchell to MH/TW et al-T1-11

Data_Ed'. If the editorial pounds are distributed to the zones on the advertising pounds, and then multiplied by the difference between the advertising rate and the editorial rate, and summed, the result is a leakage of $214.3 million, which is 47.2 percent of the $453.6 million shortage (cell F72) behind the 23.8-cent figure.

It is not entirely clear to me how to go about tracing the non-distance-related transportation costs, shown in cell C43 to be 2.4 cents per pound. They are in the first-cut advertising pound rates, and since the editorial pound rate is 77.8 percent of the zones 1&2 rate, one could argue that 22.2 percent of 2.4 cents (=0.53 cents) times the editorial pounds is a revenue leakage of $13.0 million that is due to the non-distance-related transportation costs and is already part of the $214.3 million.

The markup on Outside County Periodicals is $33.3 million (Appendix G, Opinion, Docket No. R2001-1). If 40 percent of this comes from the pound rates, the markup on the pound rates is $13.3 million, which is 0.31 cents per pound. This is 2.9 percent of the $453.6 million. Applying the 22.2-percent figure suggests a leakage of 0.07 cents per editorial pound due to markup, which is $1.68 million. This too is already part of the $214.3 million.

The per-pound portion of the DADC, DSCF, and DDU discounts for advertising resulted in a leakage of $15.2 million (the discounts in C47-C49 times the volumes in cells C4-C6). This is 3.5 percent of the $453.6 million.

Based on this reasoning, the remaining 46.4 percent (100 – 47.2 – 2.9 – 3.5) of the $453.5 million, and therefore of the 23.8-cent figure, is for non-transportation costs recovered in the pound rates, by virtue of the decision to obtain 40 percent of the revenue from the pound rates.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-11

(b) All of the 23.8 cents is included in all of the pound rates in all of the zones, including DADC, DSCF, and DDU.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-12

MH/TW et al.-T1-12: With reference to your testimony at page 40 lines 3-7 that an additional amount (some undefined portion of 23.8 cents per pound) is incorporated in each of the current zoned advertising pound charges to recover the revenue leakage associated with the unzoned editorial pound charge:

(a) Please confirm that a Periodical comprised of 100% editorial content would not pay any portion of such additional amount, regardless if it were mailed a relatively short distance or a relatively long distance. If you are unable to confirm, please explain fully.

(b) Please confirm that only a Periodical comprised of 100% advertising content would pay such additional amount in full, and would do so regardless of the distance it was mailed. If you are unable to confirm, please explain fully.

(c) Please confirm that under the Domestic Mail Classification Schedule (e.g., sections 412.4 and 413.3), Periodicals are generally required to have no more than 75% advertising content. If you are unable to confirm, please explain fully.

(d) Please confirm that a Periodical mailed from zone 8, and containing 60% advertising content, would pay more – 50% more – of the referenced additional amount than a Periodical mailed from zone 1&2 and containing 60% editorial content, assuming that each Periodical mailed the same number of pounds. If you are unable to confirm, please explain fully.

(e) Please confirm that a Periodical mailed from zone 8 will always pay more of such additional amount for each pound mailed than will a Periodical mailed from zone 1&2 so long as the Periodical mailed from zone 8 contains a higher percentage of advertising content than the Periodical mailed from zone 1&2. If you are unable to confirm, please explain fully.

(f) Please confirm that Periodicals with identical percentages of advertising content will always pay an identical portion of such additional amount for each pound mailed, regardless of whether such a Periodical is mailed from zone 8 or zone 1&2. If you are unable to confirm, please explain fully.

(g) Please confirm that the extent to which a Periodicals mailer pays an additional amount to recover the revenue leakage associated with the unzoned editorial pound charge is determined solely by the number of advertising pounds mailed by the Periodical, and not by the distance mailed (with the possible exception that the advertising pound charge for short hauls such as DDU entry may not contain any such additional amount at all). If you are unable to confirm, please explain fully.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-12

RESPONSE

(a) Not confirmed. The 23.8-cent figure is added to all pound rates before the editorial pound rate is calculated.

(b) Confirmed, but only because you specified "in full." A periodical with 70 percent advertising, for example, would pay it *in full* on 70 percent of its weight and *in part* on 30 percent of its weight.

(c) Not Confirmed. General publications, but not requester publications, may not have advertising in excess of 75 percent in more than one-half of their issues during any 12-month period.

(d) Not Confirmed. Since the editorial rate is 77.8 percent of the zones 1&2 advertising rate, one could argue that the zone-8 piece pays the full 23.8 on 60 percent of its weight and 77.8 percent of 23.8 on 40 percent of its weight, for a total of 21.69 cents per pound. The zones 1&2-piece would pay the full 23.8 on 40 percent of its weight and 77.8 percent of 23.8 on 60 percent of its weight, for a total of 20.63 cents per pound.

(e) Based on the allocation scheme outlined in my answer to part "d" of your question, confirmed, but only because the zone-8 publication is specified to have more advertising that the zones 1&2 publication, not because it goes further.

(f) Confirmed.

(g) Not confirmed. See my response to part "d" of your question. But, however viewed, the exception you suggest for short hauls is not needed.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-14

MH/TW et al.-T1-14: Referring to your testimony at page 23 lines 17-22 that so-called "Camp 1" local and regional publications "have short hauls and relatively high cost coverages" while so-called "Camp 2" local and regional publications "have a substantial haul and relatively low cost coverages," please confirm that a "Camp 1" publication with a high editorial percentage may have a cost coverage that is below 100%, and lower than the cost coverage of a "Camp 2" publication with a high advertising percentage. If you are unable to confirm, please explain fully.

RESPONSE

Not confirmed, based on my assumption in the paragraph beginning on line 4 of the same page of my testimony that all local and regional publications have an average proportion of advertising. I understand that average cost coverages vary with the proportion of advertising, which is a different effect from the one discussed in the section to which you refer. It is important to keep effects separate.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-15

MH/TW et al.-T1-15: Referring to your testimony at page 24 lines 12-14 that "[t]hose who decide to print locally should not be required to pay elevated postal rates to help support publishers who make different decisions or who mail more broadly," (a) please explain whether your reference to publications printed locally was intended to include only so-called "Camp 1" local and regional publications, and not national publications that have the ability to print in multiple locations, and if so please explain the distinction; (b) please confirm publications printed locally pay no more per pound, if they pay anything at all, to support publishers who mail more broadly than do any other publications that have the same percentage of advertising content. If you are unable to confirm, please explain fully.

RESPONSE

(a) My Camp 1 does not include "national publications that have the ability to print in multiple locations." Subject discussion is intended to focus the characteristics and the fairness of a particular situation that really does exist. This does not mean that it does not have spillover implications for other situations. I agree that a national publication printing in more than one location does have some Camp-1 characteristics, partly in the sense that its cost coverage would be high and partly in the sense that it could decide to print some distance from one of its destination areas if the costs were lower. In doing this, however, it might in effect be relinquishing one of its multiple locations.

(b) On a per-pound basis, confirmed, but they see none of this payment returned to themselves by virtue of their having some higher-zone mail.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-16

MH/TW et al.-T1-16: With reference to your testimony at page 25 lines 6-9 that "[p]ublications whose subscribers are concentrated in limited geographic areas .... are not part of some kind of continuum that warrants averaging for rate purposes:"

(a) Please state whether you believe that separate subclass status may be warranted for such publications, and explain your answer;

(b) Please confirm that under established law and practice, the rate design for a single subclass may properly include a range of varying cost coverages, including cost coverages below 100% so long as the subclass as a whole recovers its costs. If you do not confirm, please explain fully.

(c) Please confirm that the current pound-oriented editorial benefit for outside county Periodicals depends upon where a mailer falls on the continuum of editorial percentages and on the continuum of distance mailed. If you do not confirm, please explain fully.

(d) Please confirm that local and regional publications do not constitute a distinct group in this regard inasmuch as "Camp 2" local and regional publications may be printed at some distance from their delivery area, while national publications may have shorter hauls to many delivery areas due to their ability to print in multiple locations and to engage in dropshipping. If you do not confirm, please explain fully.

(e) Please confirm that the extent, if any, to which a mailer helps pay for the revenue leakage associated with the current flat editorial pound charge depends only (or at least primarily) on where the mailer falls on the continuum of advertising percentages. If you do not confirm, please explain fully.

(f) Please confirm that the revenue leakage associated with the current flat editorial pound charge is recovered in a manner that reflects cost averaging for rate purposes, i.e., solely from a uniform component of each of the zoned advertising rates (with the possible exception that the advertising rates for short hauls such as DDU entry may not contain any such component). If you do not confirm, please explain fully.

RESPONSE

(a) In general, no, because important cost differences can be properly recognized within a single subclass, in line with the instant Complaint. It is interesting to think, however, as discussed on page 53 of my testimony, beginning on line 10, about the effect a separate subclass has had on In-County mailers.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-16

(b) Confirmed in the sense that such is sometimes done and has not, to my knowledge, been held to be illegal, but not in the sense that it generally qualifies as good rate setting. Usually, it does not. My testimony discussing why the proposed rates are more appropriate than the current ones is in agreement with the Commission's statement that: "The Commission begins the rate design process assuming equal implicit markups. This is a neutral starting position which seems to be implied by § 3622(b)(1), a fair and equitable schedule." PRC, Opinion, R2000-1, p. 390, ¶5533. However, note that, in line with the recognition of ECSI value and consistent with the rates now in effect and current Commission practice, the proposed rates involve a coverage on editorial matter that is below 100 percent and a coverage on advertising matter that is above 100 percent. See also my response to ABM/TW et al.-T1-15.

(c) Confirmed. The way distance is recognized is one of the deficiencies in the current rates, as explained in my testimony.

(d) Not confirmed. Your question hinges on the words "in this regard," and I do understand the regard to which you refer. The existence of the nationals has nothing to do with the constitution of Camp-2 publishers.

(e) Not confirmed. First, it would appear to depend also on the weight of the publication. Second, it is not clear that your statement allows for the fact that editorial also helps pay for its own editorial benefit, as explained further in my response to MH/TW et al.-T1-12, section d.

(f) Not confirmed. I do not understand cost averaging to have anything to do with placing uniform burdens from non-cost sources on rate payers. It is true that the leakage is recovered with a per-pound charge on advertising, as well as on editorial, though at a lower level, that is uniform across zones, even without the exception you

note. This is also true of the rates being proposed. The instant Complaint does not focus on the way the leakage (which level is not changed) is recovered, but on the skewed way in which the leakage amount is given to mailers, with attendant degrees of unfairness, poor signals, and little encouragement for economic efficiency.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-17

MH/TW et al.-T1-17: Referring to your testimony at page 53 lines 15-20 that "the rate for DSCF-entered In-County publications is an at cost-rate," and that "if Outside County rates were cost based, the rate for DSCF entered Outside County pieces would be near the corresponding In-County rate," but that "the Outside County rate is in the neighborhood of twice the In-County rate:"

(a) Please confirm that the current rate structure for Within County Periodicals contains only two pound charges: a "Delivery Unit" charge of 11.2 cents per pound and an "All Other Zones" charge of 14.6 cents per pound. If you do not confirm, please explain fully.

(b) Please explain what you are referring to when you refer to "the rate for DSCF entered In-County publications."

(c) Please explain what you are referring to when you refer to an In-County rate corresponding to the rate for DSCF entered Outside County pieces (20.3 cents per pound) that is "in the neighborhood of twice the In-County rate."

(d) Please specify and quantify each of the cost components that make up each of the two pound charges for Within County Periodicals, e.g., distance-related transportation costs, non-distance-related transportation costs, distance-related non-transportation costs, non-distance-related non-transportation costs, mark-up for institutional costs, etc. If necessary, please provide your best estimate. Please specify the precise source for you answers, and explain any necessary calculations.

(e) Please address whether the assumed fact that the DSCF pound charge for Outside County Periodicals is substantially higher than the "corresponding In-County rate" could be explained by a combination of such factors as those referred to you at page 13 lines 9-11 and 15-17 of your testimony (various pound-oriented savings or portions thereof reflected in piece discounts for Outside County Periodicals), by the lower mark-up for Within County Periodicals, by the effect of changes in mail volume on the unit costs of transportation, and/or any other potentially relevant factors.

RESPONSE

(a) Confirmed.

(b) If an In-County publication enters qualifying mail in a DSCF, it pays the pound charge for "All Other Zones." It is true, of course, that an SCF could be the delivery unit for some of the mail in its area.

Response of TW et al. Witness Mitchell to MH/TW et al-T1-17

(c) A number of comparisons can be made. I did not develop a weighted average. Suppose one considers a barcoded flat in a 5-digit bundle entered at a facility qualifying as a DSCF. If the piece qualifies only for the Outside County rates, it pays 20.3 cents per advertising pound plus 19.3 cents per editorial pound plus 22.6 cents per piece minus the per-piece DSCF discount of 0.8 cents minus the per-piece editorial discount minus any pallet discount. If the same piece qualifies for the In-County rates, it pays 14.6 cents per pound plus 6.7 cents per piece. The primary pound rates, 20.3 and 19.3 cents for the Outside County piece are clearly much higher than the 14.6 cents paid by the In-County piece. The piece rate before any adjustments for the Outside County piece, 22.6 cents, is substantially higher than the 6.7 cents paid by the In-County piece. My statement merely means that once total per-piece postages are calculated, the charge for Outside County is often in the neighborhood of twice the corresponding In-County charge. The exact proportions are unimportant. The question is: since the Outside County rate schedule has numerous rate elements designed to recognize the costs of the mailing, both schedules have markups approximating zero, and the In-County schedule is even more clearly at cost (having a much greater degree of uniformity), why does the Outside County piece pay so much more? It must be because something is wrong with the Outside County rate schedule.

(d) PRC Library Reference 9, Docket No. R2001-1, contains a workbook that develops the In-County rates. Based more on continuity with the past than on a cost study, it gets 40 percent of the revenue requirement (the CRA cost times the contingency times the cost coverage), adjusted for fees and Ride-Along revenue, from the pound rates. No transportation costs are used, whether distance-related or not. No non-transportation costs are specified to be pound-related. The pound rate is set to obtain the desired revenue, with a difference between the DDU rate and the

Response of TW et al. Witness Mitchell to MH/TW et al-T1-17

all-other of 3.4 cents per pound. Letting R = the all-other pound rate, it simply solves an equation in which R • all-other pounds + (R – 3.4) • DDU pounds = desired revenue. The 3.4-cent figure is the sum of two components. The first is a 35 percent passthrough applied to the per-pound non-transportation savings between the DSCF and the DDU for Outside County Periodicals. The second is an 82 percent passthrough applied to the 2.4 cent per-pound non-distance-related transportation cost of Outside County Periodicals.

(e) The problems that I discuss on page 13 are too small to explain the large differences in question, and they go primarily to relationships between somewhat similar publications instead of to averages. The markups are both so low that they cause almost no effect. The transportation costs that receive so much attention in Outside County Periodicals are long-haul, segment 14 transportation costs that are unimportant in In-County. Also, to the extent that the variability of transportation costs has been measured correctly, the unit costs would not change much with volume.

A well-researched and defensible explanation for the difference referred to in your question does not exist. My guess would be that at least three factors are important. (1) The offices through which In-County periodicals are handled may tend to be smaller offices than for Outside County and these offices may perform simple and quick operations to get the periodicals on their way. (2) Outside County periodicals may be picking up excess costs in the costing systems, different from those that should be associated with tight, streamlined operations. (3) The Outside County rates are still far from cost-based and the markup on destination-entered periodicals is extremely high. The complainants believe that their proposal will take a first step in dealing with factor number three.

MH/TW et al.-T1-18: Referring to your testimony at page 53 lines 22-23 that "higher zone periodicals have rates that are substantially below costs:"

(a) Please confirm that this assertion depends on the percentages of advertising and editorial content of higher zone Periodicals. If you do not confirm, please explain fully.

(b) Please confirm that under your proposed rate structure, as under the current rate structure, a 100% editorial publication could have a cost coverage of approximately 85% -- substantially below costs. If you do not confirm, please explain fully.

RESPONSE

(a) Paraphrased and stylized, the lines you cite say: If In-County is lower-zone and at cost, and if the lower-zone portion of Outside County has rates that are much higher than the corresponding In-County rates, and further if the Outside County rates as a whole are at cost, then the higher-zone portion of Outside County must be well above costs. My statement is more of an implication than an assertion, although I don't see how it cannot be true. Usually, unless the issue being discussed concerns the level and structure of the editorial benefit, I discuss tendencies for pieces with an average degree of advertising content. This allows cost coverages and per-piece markups within the subclass to be compared with those of the subclass itself. You are correct, of course, that the implicit cost coverages of pieces in the higher zones are affected by the advertising content, as is true for all pieces.

(b) Confirmed. The proposed rates do not change the level of the benefit given to editorial content and do not change the average cost coverages of editorial and advertising matter.

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

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

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

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

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.-T1-26

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

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 $n \bullet k \bullet P_{ADV} \bullet Q_{ADV}$. 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.-T1-34

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

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 is 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

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 NNA/TW et al.-T1-1

NNA/TW et al. T-1-1 Have you provided consulting services to any newspapers or newspaper organizations? If so, please list their titles, the dates and nature of your services and explain how they use the mail, particularly periodicals rate mail. You may omit speaking engagements if no individual services were offered pursuant to those engagements.

RESPONSE

No.

Responses of Witness Mitchell to NNA/TW et al.-T1-2

NNA/TW et al. T1-2 With respect to your statement on p. 1, second paragraph, would you agree that the Postal Reorganization Act requires more than just "efficient rates?" If not, please explain how you believe the requirements in Section 3622 should be interpreted.

RESPONSE

Yes. It must be said, however, that I find most if not all of the § 3622 factors to be well aligned with notions of efficient rates. See also my response to ABM/TW et al.-T1-15.

Responses of Witness Mitchell to NNA/TW et al.-T1-3

NNA/TW et al. T1-3 Do you believe the intended purpose of the unzoned editorial rates was to achieve "efficient rates?'

RESPONSE

No.

Responses of Witness Mitchell to NNA/TW et al.-T1-4

NNA/TW et al. T1-4 *Do you believe any aspect of the intent of the unzoned* editorial rate was to recognize a higher degree of value to the recipient from editorial content in periodicals as opposed to the advertising content?

RESPONSE

Not in the way you suggest. Note first that the zoned advertising rate was a creation of 1917, but the flat editorial rate was a continuation of what had been in effect for some time. The inclination of Congress was to zone the full weight of the publications. Given a strong response from those whose rates would have thereby increased, and arguments that publishing zones would evolve, a compromise decision was to leave in place a low, unzoned rate, but for editorial only, and to put into effect a zoned advertising rate. I believe this low rate was left unzoned as a way of continuing the status quo, of avoiding or tempering a large rate increase for many magazines, and in hopes that the specter of publishing zones could be avoided.

Responses of Witness Mitchell to NNA/TW et al.-T1-5

NNA/TW et al. T1-5 Would you agree that a rate structure with an unzoned editorial rate, if taken alone as a decision driver for publishers, would tend to encourage a higher degree of editorial content as opposed to advertising content in comparison to a zoned rate? If not, why not?

RESPONSE

No. The benefit (and encouragement) given to editorial matter is just as high in the proposed rates as in the current rates. In fact, since the proposed rates are more efficiently designed in almost all respects, the proposed rates should provide even more encouragement to editorial matter than the current ones, as the *MOAA* court apparently had in mind when it said, regarding the unzoned editorial rate, that "the divergence from cost principles has the probable tendency of increasing overall costs of distribution, and thereby reducing the market-clearing level of distribution." 2 F.3d 408, 436 (D.C. Cir. 1993).

Responses of Witness Mitchell to NNA/TW et al.-T1-6

NNA/TW et al. T1-6 Please refer to your statement on p. 6 that your proposed rates leave considerable room for improvement in the future. What improvements do you have in mind? Do you believe the charges for any of the mail that you believe to be inefficient should be higher? If so, how much higher?

RESPONSE

By the statement referenced, I meant primarily that the proposed rates would establish an improved platform from which the future could be faced. I have no particular adjustments in mind and see no reason at this point for arguing that any particular rates should be higher. As experience is gained under the new structure, the flow models and the costing could be improved and refined. There might also be associated adjustments in postal regulations relating to Periodicals preparation.

Responses of Witness Mitchell to NNA/TW et al.-T1-7

NNA/TW et al T1-7 Do you believe that the so-called ECSI values are recognized only in cost coverages? Please explain your answer.

RESPONSE

I believe reduced cost coverages may be the best way to recognize ECSI values in a balanced and fair way that does not cause other problems. My belief on this point appears, by my reading, to be consistent with that of the *MOAA* court, which said that the recognition and encouragement of ECSI value is not a justification for advantaging long-haul and disadvantaging short-haul publications, whether dropshipped or not. 2 F.3d 408, 436 (D.C. Cir. 1993).

Responses of Witness Mitchell to NNA/TW et al.-T1-8

NNA/TW et al T1-8 Would a periodical unable to change its mailing makeup or drop shipping practices to take advantage of your proposed rates experience the low cost of periodicals rates that you believe Congress intended in your recitation of the legislative history on p. 8? If not, do you believe Congress intended only periodicals considered "efficient" to benefit from low rates? Please explain your answer.

RESPONSE

It is difficult to see at the present time that anyone is experiencing the "low cost of periodicals rates," whatever that may mean. Except in a general way, I believe it is treacherous to read too much into what Congress may have intended. The better approach is to look at what Congress did. It arranged a separate subclass for periodicals; it emphasized recognizing costs and mail preparation; it required recognition of ECSI value (but said nothing about an unzoned editorial rate); and it said that rates should be fair and equitable. For Nonprofit Periodicals, which have received substantial benefits in the past, it said that there should be a discount of only 5 percent (and even then on only some rate components). It has not authorized a subsidy for any special rates. It created an expert Postal Rate Commission (on this point, see my response to ABM/TW et al.-T1-15). Under these conditions, it may be that the most that mailers can ask for is that their rates reflect little or nothing more than the costs the Postal Service actually experiences. However you might define the term, I certainly don't believe that Congress intended only "efficient" periodicals to benefit from low rates, and there is nothing in the proposed rates or my testimony that so suggests.

Responses of Witness Mitchell to NNA/TW et al.-T1-9

NNA/TW et al T1-9 Please refer to the "small publications" identified by you on p. 6, lines 21-22. Do you have specific publications in mind? If so, please name them. If not, please explain whether this statement is meant to be hypothetical.

RESPONSE

I do not have specific publications in mind, but their existence is far from being hypothetical. It has been common in rate parlance for some years to refer to small publications, even when it may not clear exactly how they should be defined. Many times the options open to mailers and the characteristics of their mailings are determined more by their density than their size. For example, the *Washingtonian* magazine hits a relatively high proportion of the households in many Washington D.C. neighborhoods, and thus has many characteristics of largeness, even though its circulation is small compared to many magazines with broad national distributions. It probably sorts to carrier route.

The paragraph you cite refers to the proposal to create an ADC presort level. Mailers with a good bit of volume for the ADC but not enough volume for 3- and 5-digit bundles might find this option attractive. Unless they are a local or regional publication, these would be publications with relatively low circulations.

Responses of Witness Mitchell to NNA/TW et al.-T1-10

NNA/TW et al. T1-10 Please refer to your commentary on technological advancements and mailer adjustments on p. 11. Do you believe the Postal Service adjusted its operations to the mail, or the mailers to the Postal Service? Please explain your response.

RESPONSE

I believe that the Postal Service and mailers usually work together on these things, in many ways, including MTAC. See also my response to NNA/TW et al. T1-11.

Responses of Witness Mitchell to NNA/TW et al.-T1-11

NNA/TW et al. T1-11 If you responded to NNA's interrogatory 10 that you believe the Postal Service adjusts its operations to the mail, do you believe it attempted to adjust to all of the mail in the periodicals mailstream or only that mail that it deeded "efficient?" Please explain your response, in particular with respect to adjustments for periodicals.

RESPONSE

I don't think that the Postal Service has skewed any developmental role to certain categories of mail to the unfair exclusion of others. I say this based not only on general observation but on the fact that some years ago I interviewed extensively every Branch Manager, every General Manager, and every Director at the Postal Service's development center. There was strong interest in all cases in developing low-cost ways to handle all of the mail. It does not follow, however, that pushing with equal force in all areas will cause all areas to move forward by the same amount. I believe engineers should have the option, indeed have the obligation, of saying: "Here is what we are capable of offering you. It has a low cost. We can offer you a rate based on that cost. We are sorry we were not able to make all costs low."

Responses of Witness Mitchell to NNA/TW et al.-T1-12

NNA/TW et al T1-12 Do you believe that newspapers were part of the mailstream when Congress created the preferences for periodicals mail that you refer to in section III of your testimony? If so, please explain how you think the technological advances you have in mind on p. 6 have benefited them.

RESPONSE

I believe newspapers were an important part of the mailstream in 1917. I haven't attempted to assemble statistics, but I also believe they were often light in weight, sometimes containing only a few pages. I cannot provide expert testimony on the details of newspaper machinability today. I do understand that it has been difficult to design machinery to handle them. This difficulty is not limited to the Postal Service alone, but also to its contractors around the world and to other countries and their postal services.

Responses of Witness Mitchell to NNA/TW et al.-T1-13

NNA/TW et al T1-13 Do you believe that publishers that do not prepare mail on pallets are uniformly indifferent to postal costs as your niece is to her landlord's water bill.

RESPONSE

No. It has been my experience that many publishers go out of their way to work with the Postal Service and to cooperate in organized efforts like MTAC. But in the absence of appropriate signals and incentives, they may stop short of the kinds of changes in ongoing productive operations that are needed, even in cases where it might cost them little or nothing to make the changes.

Responses of Witness Mitchell to NNA/TW et al.-T1-14

NNA/TW et al T1-14 On p. 16, you assert that in some cases some publishers have a choice between preparing one 24-piece bundle and 24 sacks with one piece each, and that appropriate price signals would cause the publishers to value the sack more highly. Assuming that statement means you believe that in some cases, publishers do not have a choice, do you believe that the publishers who do not have a choice should also be found to "value the sack?" If your answer is yes, please explain how the price signal will influence mailer choice if there is no choice?

RESPONSE

I certainly do not believe that the value a publisher puts on using a sack, in an absolute sense or relative to other alternatives, is or will be affected by any price signals received. Also, it is not necessary to "find" what value a particular publisher might place on a sack; given appropriate signals, the mailer will reveal his preference, which will reflect the valuation he places on the alternatives.

Responses of Witness Mitchell to NNA/TW et al.-T1-15

NNA/TW et al T1-15 Assume a 3,000 circulation newspaper in a Midwestern city has 15 pieces going from a midwestern city to residents of its town who have chosen to winter in Florida. Assume that these 15 individuals live in 15 different zip codes, in three different 3 digit zones. Assume further that each of these 15 individuals have chronically complained about slow and irregular delivery to the postmaster, who has advised unless the publisher creates 15 5-digit sacks with one piece each, service will not improve.

a. What price signal would you wish to send to this publisher?

b. Is this the sort of publisher whom you have in mind with the analogy to your niece?

c. If the Postal Service routinely could not achieve regular delivery with a mixed ADC bundle for this mail, will a price signal to the publisher be the appropriate economic sanction to solve an inefficiency problem?

d. Should the publisher be punished for the Postal Service's inability to achieve reasonable service standards?

RESPONSE

a. My role has not been to "wish" to send specific signals to specific mailers. The rates I propose are cost-based and fair, among other attributes. This mailer should pay them. I do not see why this mailer should be able to make a decision that imposes substantial costs on others. I also believe the service issue for sacks should be examined. It is difficult to understand any reason why 1-piece sacks should whip through the system while pieces going through major processing operations should be delayed. In this regard, see the response of witness Schick to ABM/TW et al.-T4-6.

b. To a considerable extent, yes.

c. Paying prices that reflect the resource implications of decisions made is not a sanction, economic or otherwise. There would be an improvement in efficiency, whether or not the mailer decided to change what he is doing.

Responses of Witness Mitchell to NNA/TW et al.-T1-15

d. I do not see that any punishment is involved. It is true that mailers can get low rates and good service only from a postal service whose technical efficiency is high and that succeeds in providing service according to standard.

Responses of Witness Mitchell to NNA/TW et al.-T1-18

NNA/TW et al T1-18 Have you done any analyses of the operational issues and or the cost consequences of the issues surrounding polybags and the use of automated sorting machines? If you have, please provide copies of your work.

RESPONSE

No.

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

NNA/TW et al T1-19 If the Postal Service told you that carriers required a greater amount of time to handle periodicals on 8.5 x 11 sheets than those on 5x7 sheets, would you recommend a price signal that discouraged publishers from using 8.5 x 11 sheets?

RESPONSE

Under current definitions, a 5x7 sheet qualifies as a letter, unless it is over one-quarter of an inch thick. I have long been in favor of a letter/flat rate differential for Periodicals. Currently we have a poorly constructed arrangement that provides only a larger barcode discount for letters than for flats.

If there were a letter/flat differential in Periodicals, or some other similar rate differential, possibly like the one you suggest, I would be emphatically against referring to it as a structure designed to discourage mailers from sending the higher-cost pieces, just as General Motors does not discourage you from buying its higher-priced automobiles and SUVs. Ask yourself the following question: "If the Postal Service, which is a governmental organization owned by the people of the United States, had available an efficient, low-cost mailstream for handling and delivering 'letters' and it did not make that mailstream available to you, a 'letter' mailer or a potential 'letter' mailer, but rather persisted in presenting you with a much higher rate that happens to be designed for higher-cost flats, simply because many of your friends send flats, how would you feel?"

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

NNA/TW et al T1-20 If the Postal Service told you that greater efficiency would be achieved if all magazines dispensed with color or typography on their covers so that optical character readers could better identify and read mailing labels, would you recommend a price signal that discouraged publishers from using attractively designed covers?

RESPONSE

The technical efficiency of the Postal Service is not going to be affected by whether it produces a different proportion of high and low cost products. If it is economic efficiency that has the potential of being increased, the way to achieve it is to give fair signals in rates, based on costs, and to let the mailers choose. It is not to tell mailers to stop doing something that you don't like.

This question, and some others you have asked, goes toward the possibility of developing rates that recognize cost differences that could be large in number, small in size, difficult to quantify, and of questionable existence. Ease of administration and use can become important at some point, and complexity could become an issue. Basically, however, the Postal Service should tell mailers what it can do for them, what it costs, and let them choose. The following question, which you should ask yourself, and which is similar to a question I suggest in my response to NNA/TW et al T1-19, is illuminating: Suppose the Postal Service had (or could easily offer) two efficient, low-cost, sophisticated mailstreams, one that could handle only black-and-white covers and one that could handle color covers. And suppose further that you are a mailer of inherently black-and-white covers (because you send to handicapped people who are color blind) and that a suitable rate for the black-and-white mailstream is 6 cents while a suitable rate for the color mailstream is 12 cents. How would you feel if the Postal Service refused to make the black-and-~~while~~ white mailstream available to you, but instead persisted in charging you 10 cents, which is based on a weighted average of the two lines?

Responses of Witness Mitchell to NNA/TW et al.-T1-21

NNA/TW et al T1-21 Please refer to your footnote 16. Does all cost averaging create a "subsidy" by the units at the lower end of the average to those at the higher end?

RESPONSE

Subject footnote focuses on a particular problem often associated with the provision of welfare. Suppose 4 percent of the miles driven in the United States are driven to and from work by people who make near the minimum wage and are having great difficulty making ends meet. And suppose you believe that the government should help them pay for their gasoline, and that doing so would help the unemployment problem as well because the unemployed would search for jobs over a wider area. Would you achieve this end through a government program that sets all gasoline prices at 50 cents per gallon and funds (in direct payments to the oil companies) the difference between the market price and 50 cents? It is clear that about 96% of the drivers receiving the subsidy would not be the intended recipients. This is a very inefficient way to provide a benefit. Yet that is exactly what would tend to be happening if large groups of mailers were provided lower postal rates when only a few of them were in any kind of needy situation, whatever that might mean. In addition, these low rates would encourage the start-up of new publications whose costs to the nation are higher than their benefits.

Formally, the existence of a subsidy is usually taken to mean that the price is not high enough to cover the incremental costs of the product, for which the attributable (or volume variable) costs are often used as an indicator. Under this definition, averaging will not always imply a subsidy when there is a markup. In the case of Periodicals currently, however, the markups are essentially zero. Therefore, one could argue that almost all averaging produces subsidies. I have not advocated that all averaging be eliminated or that ECSI value not be recognized. I have carefully

selected important cost variables and designed rates accordingly. I do not think I have gone to any extremes in the number of rates or their complexity, and I do not think difficulties of administration and control are a problem.

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

NNA/TW et al T1-22 Please provide the citation to the location on the website, http//:www.citymag.org, mentioned in your footnote 19 that supports your statement that "very few" regional and city magazines use the In-County rates. If the website does not provide support for your statement, please identify the sources that support your statement.

RESPONSE

I did not intend to suggest that the footnote provided support for that particular statement. When I was considering local and regional publications, I called the MTAC representative of the City and Regional Magazine Association. I asked a number of questions, in response to most of which he declined to provide much information. When I asked if he knew how many of his members use In-County rates, his reply was something to the effect: Oh no, almost none of them do.

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

NNA/TW et al T1-23 Have you asked The Baltimore Afro-American whether it uses the in-county rates? If so, please provide the name of the official with that newspaper whom you consulted, and the dates of your conversation. Please also provide any information you collected from that newspaper on its mailing practices.

RESPONSE

No.

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

NNA/TW et al T1-26 Does the city magazine discussed in NNA/TW et al T1-24 and 25 belong in Camp 1 or Camp 2 as described on page 24 of your testimony.

RESPONSE

It belongs in Camp 1. Please see my response to ABM/TW et al.-T1-70.

Responses of Witness Mitchell to NNA/TW et al.-T1-27

NNA/TW et al T1-27 Are you aware of any city or regional periodicals that belong in Camp 2? If so, please specify how far away the printer or printers are and why you believe the periodicals have chosen that printer or those printers?

RESPONSE

When I talked to the MTAC representative of the City and Regional Magazine Association, a call discussed further in my response to NNA/TW et al T1-22, I asked if he knew how many of them had their publications printed in the city where they were distributed. His response was something to the effect: No, I would say most of them are printed kind of far away. I did not ask, and know nothing, about any dropshipping that is done. I would assume that the process of selecting a printer for them focused on the package that the printer offered, including price, and that the postage was considered in some part of the process. No one would expect them to consider the costs to the Postal Service of any decision they might make.

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

NNA/TW et al T1-28 Please refer to your statement on p. 28 that neither In-county nor Ride-Along rates are affected by your proposal. Does that mean that you believe In-County rates would not be affected if the Commission were to adopt your proposal, or that you have not recommended different rates for In-county? Please explain your response.

RESPONSE

It seems abundantly clear that no decision by the Commission would affect In-County rates, if for no other reason than because the situation there is substantially different. The segment-14 transportation costs in FY 2003 were only $79,000, and therefore *de minimis*. The use of containers is probably quite different. The question of the flat editorial pound rate does not arise. There is no difference between the rate for advertising and the rate for editorial. The machinability is different. At least for newspapers, the printing is probably all done locally. The option of exceptional dispatch is used heavily. The service needs are different, at least on average. The proximity of the printer to the stations and branches is probably different. With sufficient study, it may well be that an improved structure for In-County could be developed, but we are a long way from that.

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

NNA/TW et al T1-29 Are Outside County costing data ever used as proxies for In-County costs? If so, please explain how your proposal would affect their future use.

RESPONSE

Yes. Please see my response to MH/TW et al. – T1-17. I see no reason, however, for any difficulty. The differences will still be available. Also, the passthroughs in In-County are rather arbitrary and would in all likelihood be selected to provide continuity. For another, the Postal Service needs to do separate cost studies for In-County if the rates are to be cost based, and especially if the structure is changed.

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

NNA/TW et al T1-30 If the sack charge you propose for 3-digit and 5-digit sacks sent the signal to mailers that the appropriate behavior was to combine the contents of those sacks into mixed ADC sacks and the mailers responded as you wish them to respond, would you expect the service received by those mailers to improve or deteriorate? If you expect the service to improve, please explain your response.

RESPONSE

I do not "wish" mailers to respond in a certain way. The question of sack makeup and service is an important one that needs attention. Please see the response of witness Schick to ABM/TW et al.-T4-6.

Responses of Witness Mitchell to NNA/TW et al.-T1-32

NNA/TW et al T1-32 *If a reduced value of periodicals mail cannot be* recognized in your rate structure because you have already assumed a very low cost coverage, would it be a desirable outcome for that mail to disappear from the mailstream as recipients responded to the declining value by ceasing to subscribe or request those periodicals?

RESPONSE

I have not *assumed* a "very low cost coverage"; the Commission has *recommended* a very low cost coverage. *I do not believe that coverage can be viewed as a* reflection in any well defined way of the value that mailers put on the use of *Periodicals mail.* The value that mailers put on it, however, does influence how much of it they purchase. I think it would be grossly unfortunate if the rates became so high that mailers disappeared, particularly if those rates were higher than should exist under the honest and economical management of a technically advanced, state-of-the art postal system.

Responses of Witness Mitchell to NNA/TW et al.-T1-33

NNA/TW et al T1-33 Do you believe that all periodicals publishers use computers to prepare their mail and that they will welcome rates that "appear complex?"

RESPONSE

It is possible that there are some mailers that do not use computers. I would expect the volumes of these mailers to be limited, but I would not see them as viewing the proposed structure as complex. They would certainly know where they entered their mail, the number of sacks and their makeup, and the number of bundles. Information on presort levels, zones, and pounds already needs to be know.

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

NNA/TW et al T1-34 Do distant subscribers have different values to publishers, depending upon their subscription price structure, the nature of their advertisers or other factors? Please explain your response.

RESPONSE

Except to the inconsequential extent discussed in Appendix A of my testimony, I do not see how the value of a distant subscriber could depend on the subscription price structure.

I would guess that advertisers in local and regional publications might be less interested in the number of distant readers than in the number of local and regional readers.

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

NNA/TW et al T1-35 Please explain how you know that periodicals do not or would not "zone" their subscription rates?

RESPONSE

This is discussed on page 60 of my testimony, beginning specifically on line 10. Over a period of 20 years, I have raised this question many times with many publishers; they usually laugh at the idea.

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

NNA/TW et al T1-36 Have you examined any newspapers to determine whether "zoned" subscription rates, or any other type of charge to reflect increased mailing rates beyond local zones are being used? If so, please identify and describe the newspapers you have examined. If not, please explain why you have apparently included newspapers in your statements on p. 60 without undertaking such an examination.

RESPONSE

I have not examined newspapers. I am generally aware that some newspapers give customers an option of having copies sent First Class or Priority, at an extra charge, instead of sent at Periodicals rates.

Responses of Witness Mitchell to OCA/TW-T1-1

OCA/TW-T1-1. As a general proposition, all other things being equal, is it correct that if a particular amount of Periodicals volume takes advantage of the proposed rate revisions and discounts, and a smaller amount of Periodicals volume does not take advantage of the proposed rate revisions and discounts, then, on average, the Periodical pieces not taking such advantages will necessarily see unit rate changes larger than the unit rate changes for those Periodicals taking advantage of the proposed rate revisions and discounts? Please explain any "no" answer.

RESPONSE

No. I am assuming that by unit rate changes, you mean net unit postage changes. I do not see that the levels of any net unit postage changes would depend on the amount of volume that does or does not make preparation changes. Also, I do not see any reason why the mailers making changes would tend to be those experiencing rate increases of a certain size. It seems entirely possible that many mailers not making changes would be among those experiencing relatively low increases.

Responses of Witness Mitchell to OCA/TW-T1-2

OCA/TW-T1-2. Please give your estimate of the Periodicals volume that will take advantage of proposed discounts.

RESPONSE

I am not able to provide any estimate of the volume you seek. I would offer two observations, however. First, the proposed rate structure is much more than a change in the discounts available. It involves a significantly different set of options and provides the mailers with a great deal of information that has heretofore not been reflected in rates. Second, given the possibility of many different kinds of adjustments in plans and equipment in response to these new set of options and this new information, and the likelihood that the Postal Service will work with mailers to revise regulations in an effective way, I believe that the number of mailers choosing to make no changes at all would be small. The magnitudes of the changes made, of course, would be expected to vary substantially.

Responses of Witness Mitchell to OCA/TW-T1-5

OCA/TW-T1-5. Generally speaking, will provision of "efficient" pricing signals, such as those proposed, tend to give higher volume publications that prepare their mail "efficiently" a competitive edge over publications that cannot or do not prepare their mail "efficiently?" Please explain any "no" answer.

RESPONSE

It would be interesting to have a program that would accept a publication name as an input and then instantly display all of its competitors. It is entirely possible that if the input were *Newsweek*, the display would show large, national news magazines that in fact have per-piece postage bills that are approximately the same. Similarly, if the input were *Pit & Quarry*, the display might show aggregate-oriented publications of similar size. But even the best of us, including the most insightful of industry observers, would not be able to agree on who is a competitor and who is not. Moreover, there might be little correlation between per-piece postage and the rates of growth or the levels of profitability.

The rates in virtually all classes of mail are designed to reflect the costs incurred and to send signals concerning associated resource usage, for a range of good reasons. Consequently, they may contribute to any competitive edges that larger mailers have. But it is not clear to me that the ratesetting process for postal rates should be guided by, or indeed could be guided effectively by, some kind of interest in trying to equalize competitive edges, even if differences in postal rates were the only differences among competitors, which they are not. See also my response to MH/TW et al. – T1-22, part c. On the issue of what it means for mail to be efficiently prepared, see my response to ABM/TW et al.-T1-90.

Responses of Witness Mitchell to OCA/TW-T1-6

OCA/TW-T1-6. Please give a ballpark estimate of the pool of revenues that will be de-averaged based upon the TW et al proposal, i.e., the sum of rate reductions for mailers that can utilize the proposed rate revisions and discounts as compared to the sum of rate increases for mailers that do not utilize the rate revisions and discounts.

RESPONSE

I have no way of addressing this question. If I understand it properly, it would seem to require before-and-after-adjustment billing determinants for every publication using Outside County Periodicals rates, as well as an ability to dichotomize publications into those that adjust and those that do not, when in fact it is more of a continuum. Also, it is not true that all mailers who adjust will receive rate reductions, net or before adjustment, or that all mailers who do not adjust will receive rate increases.

Response of Witness Mitchell to USPS/TW et al.-T1-1

USPS/TW et al.-T1-1. Between the time that you became aware that you would testify in this proceeding and today, did you conduct any field observations of flats mail processing, distribution, and delivery activities at postal facilities? If your response to this question is yes, please list the dates, facility type, facility location, and tasks observed. Please provide any copies of notes that you may have taken during those observations.

RESPONSE

No.

Response of Witness Mitchell to USPS/TW et al.-T1-2

USPS/TW et al.-T1-2. Between the time that you became aware that you would testify in this proceeding and today, did you conduct any field observations of flats printing, binding, mail preparation, and distribution activities at mailer facilities? If your response to this question is yes, please list the dates, mailer names, facility names, facility locations, and tasks observed. Please provide any copies of notes that you may have taken during those observations.

RESPONSE

No.

Response of Witness Mitchell to USPS/TW et al.-T1-3

USPS/TW et al.-T1-3. On page 3, lines 16-18 of your testimony, you state "[i]mprovement in our understanding of costs in recent years has brought the existing deficiencies into clearer focus and has suggested new paths that cost recognition should follow."

(a) Please list the specific "improvements" to which you are referring.

(b) Please list the "suggested new paths" to which you are referring and explain how they correlate to the "improvements" you have listed in your response to (a).

RESPONSE

The section on page 3 of my testimony, to which you refer, is a summary section that relates in large part to Section III. C., beginning on page 14, which contains additional references and discussion.

(a) The improvements I have in mind relate to a clearer understanding of the importance of cost drivers and their rolls in understanding cost incurrence. Such drivers have been discussed in recent years in Postal Service testimony before the Commission, including that of witness Bozzo, who stated that he employed a multi-stage procedure that "breaks down the connection between cost and volume into a two step procedure. The first ('attribution') step requires measurement of the elasticity of an operation's costs with respect to its outputs (or 'cost drivers'); the second ('distribution') step requires estimates of the elasticities of the cost drivers with respect to subclass (RPW) volumes." Docket No. R2000-1, USPS-T-15 at 52.

(b) The new paths relate to the recognition of the cost drivers in the design of the rates, such as the recognition of the costs of handling bundles, the costs of handling sacks, and the costs of handling pallets. These are all recognized in the proposed rates. Points of entry are also recognized in an improved way.

Response of Witness Mitchell to USPS/TW et al.-T1-4

USPS/TW et al.-T1-4. On page 3, lines 18-21 of your testimony, you state that "the makeup of bundles, sacks, and pallets, including their entry points and associated interactions, are now understood to be important cost drivers, but these factors are all but neglected in rates."

(a) Please list the specific cost drivers that you feel affect bundle costs. For each cost driver, please indicate whether you feel it is neglected in the rates.

(b) Please list the specific cost drivers that you feel affect sack costs. For each cost driver, please indicate whether you feel it is neglected in the rates.

(c) Please list the specific cost drivers that you feel affect pallet costs. For each cost driver, please indicate whether you feel it is neglected in the rates.

(d) Please list the specific cost drivers that you feel affect piece distribution costs. For each cost driver, please indicate whether you feel it was neglected in the rates.

RESPONSE

(a) The issue is not that some unidentified cost drivers affect bundle costs. It is rather that the number of bundles is the driver that affects bundle handling costs. Another link in the analysis is between volume and the number of bundles.

(b) The issue is not that some unidentified cost drivers affect sack costs. It is rather that the number of sacks is the driver that affects sack handling costs. Another link in the analysis is between volume and the number of sacks.

(c) The issue is not that some unidentified cost drivers affect pallet costs. It is rather that the number of pallets is the driver that affects pallet handling costs. Another link in the analysis is between volume and the number of pallets.

(d) The issue is not that some unidentified cost driver affects piece handling costs. It is rather that the number of pieces is the driver that affects piece handling costs. Another link in the analysis is between volume and the number of pieces.

Response of Witness Mitchell to USPS/TW et al.-T1-5

USPS/TW et al.-T1-5. On page 4, lines 1-2 of your testimony, you state, "[i]f the factors that drive costs were reflected in rates, mailers would respond accordingly."

(a) Please confirm that the mail preparation activities that are performed at a given mailer plant are not only affected by postal operations and equipment, but are also affected by the operations and equipment at the mailer plant. If not confirmed, please explain.

(b) Please confirm that there may be instances where mailers would not necessarily respond to a revised rate structure (e.g., the ability to respond was deemed to require a cost prohibitive investment, etc.). If not confirmed, please explain.

RESPONSE

(a) Confirmed. It might be more complete to say that mailers make decisions on mail preparation in view of current and anticipated postal rates, postal regulations, postal operations, and the equipment in their plants. Also, plans for equipment are made in view of current and anticipated postal rates and regulations, which emphasizes the importance of rates such as those being proposed.

(b) I agree that "there may be instances where mailers would not necessarily respond to a revised rate structure" in a way that would lead to immediate increases in efficiency. We need to keep in mind, however, that the framework within which this question is faced involves more than just investment, that changes can be small or large, and that the likelihood of zero change is low. I believe most or all mailers go through some kind of reasoning process to decide what is best for them. This could also be referred to as an optimization process, although it is not necessary to allude to advanced calculus to acknowledge that reasoning takes place. When most of the inputs to this optimization process are changed, it is difficult to argue that the decisions will be unaffected.

Response of Witness Mitchell to USPS/TW et al.-T1-6

USPS/TW et al.-T1-6. Please see Graph 1 on page 10 of your testimony. Please provide the underlying data points and indicate the source(s) for those data points.

RESPONSE

The development of the graph is detailed in the spreadsheet Indexes-T1.xls, being filed as Library Reference, TW et al.-LR-4. The variables in it should be self-explanatory. The CPIU is from the Bureau of Labor Statistics. The percentage rate increases, markups, and markup indexes for Periodicals are directly from the Commission's Opinions.

Response of Witness Mitchell to USPS/TW et al.-T1-7

USPS/TW et al.-T1-7. On page 12 lines 14-17 of your testimony you state, "There is little question, for example, that some of the recent growth in the volume of parcel post has been due to cost-based rate innovations, and Standard Mail rates have been moving in the direction of closer alignment with costs."

(a) Please describe the Parcel Post "cost-based rate innovations" to which you refer.

(b) Please describe the basis for your claim that "Standard Mail rates have been moving in the direction of closer alignment with costs."

RESPONSE

(a) The cost-based rate innovations in parcel post, to which I refer, are primarily those of Docket No. R97-1, where the Commission recommended a DSCF rate, a DDU rate, an OBMC rate, a balloon rate, a change in the recognition of oversize pieces, and a prebarcoded rate, much as proposed by the Postal Service.

(b) My basis is the development of the irregular shape surcharge, the extension of barcode discounts to machinable parcels, the recognition of non-machinability for letters, and the deaveraging of basic presort into mixed AADC and AADC. Earlier, a number of changes were made in and soon after Docket No. R90-1, including dropship discounts (based on both transportation and non-transportation costs), letter/flat rate differentials, extensive barcode discounts, and high-density and saturation rates.

Response of Witness Mitchell to USPS/TW et al.-T1-8

USPS/TW et al.-T1-8. On page 12-13 of your testimony, you describe how mailers have become increasingly sophisticated in their ability to respond to rate signals and specifically mention how this circumstance is related to computers.

(a) Based on that statement and the extensive Periodicals experience you describe in your response to ABM/TW et al.-T1-1, please describe the current level of sophistication for the customers of Periodicals mailers. Specifically address how increased internet usage may have resulted in the adoption of on-line Periodicals subscriptions, rather than Periodical subscriptions that have been obtained through the mail.

(b) Based on your experience working with the various members of the Periodicals industry, as described in your response to interrogatory ABM/TW et al.-T1-1, how has the increased usage of the internet affected Periodicals mail volume?

RESPONSE

(a) I have only a layman's knowledge of the practices of the "customers of Periodicals mailers." Since I see ads on the Internet regularly, I am aware that subscriptions are promoted there. For example, the website of *PC World* magazine shows such promotions.

(b) I do not know and I do not believe that anyone else knows.

Response of Witness Mitchell to USPS/TW et al.-T1-9

USPS/TW et al.-T1-9. On page 13, lines 11-13 of your testimony, you state that "many of the costs depend on the quantities and sizes of the bundles, sacks, and pallets in a.mailing, but this fact goes largely unrecognized in rates." Please state which costs depend on those factors and indicate how they are unrecognized in the rates.

RESPONSE

The costs of handling bundles depend on the number of bundles, yet there is no per-bundle rate element. The same could be said for sacks and, to a slightly limited extent, for pallets.

Response of Witness Mitchell to USPS/TW et al.-T1-10

USPS/TW et al.-T1-10. On page 13, lines 13-15 of your testimony, you state that "the costs of handling bundles depend on the makeup (e.g., ADC, SCF, 3-digit, or 5-digit) of their containers and where they are entered, but neither are these factors recognized in rates."

(a) Based on this statement and the statement referenced in USPS/TW et al.-T1-13, please confirm that the occurrence of broken bundles also affects Periodicals costs. If not confirmed, please explain.

(b) Please confirm that the materials which mailers use to secure bundles is one element that affects bundle breakage. If not confirmed, please explain.

(c) Please describe the different materials and methods that Periodicals mailers use to secure bundles.

(d) In general, are there differences as to the materials and methods that large Periodicals mailers use to secure bundles, when compared to small Periodicals mailers? If so, please describe these differences.

(e) Have you conducted any studies that evaluate the appropriateness of various mailer bundling materials, given their impact on bundle breakage in postal facilities? If so, please provide the results of those studies.

(f) Do you believe that the materials used to secure bundles by mailers (in terms of the likelihood those materials would result in broken bundles) should also be incorporated into the rates a given mailing should be assessed? If not, please explain why not.

RESPONSE

(a) Confirmed. The costs of bundle breakage are recognized in the costing systems and in the costing models used to develop the current rates and the rates proposed in this Complaint. Also, I am generally aware that there have been, and may be ongoing, joint Postal Service/mailer efforts to deal with the bundle breakage question.

(b) Confirmed.

(c) I do not have an understanding that would allow me to provide such a description.

Response of Witness Mitchell to USPS/TW et al.-T1-10

(d) I do not know.

(e) No.

(f) Mailers who prepare bundles that do not break would certainly seem justified in being opposed to having their rates elevated by practices of mailers whose bundles do break, even though one of the elements in the breakage question is the way the bundles are handled by the Postal Service. I am not prepared to provide advice on whether this issue is best pursued through Postal Service development, joint Postal Service/mailer efforts, regulations, rates, or a process of recognizing the costs as done now.

Response of Witness Mitchell to USPS/TW et al.-T1-11

USPS/TW-et al.-T1-11. On page 14, lines 11-12 of your testimony, you state that, "[t]he current rates send underdeveloped signals to mailers, thus failing to provide them with a reasonable and valuable avenue for responding to the high costs." Please confirm that it is possible that, even if the Postal Service, the Commission, and the Periodicals mailing industry expended the resources required to develop alternative price signals and/or respond to those price signals, the result might have little to no effect on Periodicals costs and cost coverage. If not confirmed, please explain.

RESPONSE

Not confirmed. Mailers historically have responded to price signals and will continue to do so. When mailers perform functions previously undertaken by the Postal Service, and those functions incur volume variable costs, postal costs will decline unless the Postal Service fails to adapt.

Thus, as publishers make changes, the Postal Service's costs would be expected to change. This is suggested by the cost analysis supporting the rates and is a consequence of the control of the Postal Service of its operations. The cost coverage is a result of the changes in postage and in the Postal Service's costs.

Response of Witness Mitchell to USPS/TW et al.-T1-13

USPS/TW et al.-T1-13. On page 30 of your testimony, you describe the per-sack and per-pallet rates associated with your proposal. Are smaller mailers more likely to enter their mail in sacks when compared to large mailers? Please explain your answer.

RESPONSE

Yes, assuming they both distribute nationally. But the importance of recognizing the costs of sacks in rates goes to more than the question of whether a mailer will switch from sacks to pallets. For example, there is the question of how many sacks are used and how full they are, and there is the question of how supplemental mailings and special or separate editions are mailed. These questions are not faced by large mailers only.

Response of Witness Mitchell to USPS/TW et al.-T1-14

USPS/TW et al.-T1-14. Your proposed rate schedule, on page 43 of your testimony, proposes rates that are expressed in terms of dollars per bundle, dollars per sack, and dollars per pallet. Do you believe that these rates would cause some mailers to submit larger bundles, fuller sacks, and larger pallets? If not, please explain why not. If so, would there be instances where that might not necessarily be a good thing? Please elaborate.

RESPONSE

I agree that the rates would cause some mailers to submit larger bundles, fuller sacks, and/or larger pallets. To the extent that the rates reflect the costs involved, it is not clear to me that there are instances where this might not be viewed as a "good thing."

Response of Witness Mitchell to USPS/TW et al.-T1-15

USPS/TW et al.-T1-15. On page 54, line 9 of your testimony, you discuss how your proposed rates (page 43) meet the criterion specified in U.S.C. 39 § 3622(b)(4), concerning the effect of rate increases on mailers.

(a) Please confirm that some mailers would experience large rate increases were your proposed rates to be adopted and implemented. If not confirmed, please explain.

(b) Did you consider a phased approach to implementing the proposed rate schedule in order to mitigate the impact of rate shock on some mailers? If not, why not?

(c) When compared to the rates you propose on page 43, do you feel that a phased implementation (incrementally increasing rates for those impacted mailers) would better meet the requirements of U.S.C. 39 § 3622(b)(4)? If not, why not?

RESPONSE

(a) If one assumes that they change nothing in response to the new rates, confirmed.

(b) Yes.

(c) Not necessarily. The Commission has already indicated that it will not recommend specific rates in this docket, implying that any effects from the proposed changes are in the neighborhood of two years off. This provides considerable notice to mailers. When the Postal Service does propose rate changes, it will have the option of proposing a phasing scheme. When this is done, it should be noted that the structural deficiencies identified in the Complaint have been accumulating for some time. The changes that need to be made are, in my opinion, overdue. Please see also my response to ABM/TW et al.-T1-30.

Response of Time Warner Inc. et al. Witness Mitchell to POIR No. 1, Question 1

POIR 1, QUESTION 1

TW et al.-T-1, at page 64, shows Zone 8 postage of $0.3416 for The New Republic under current rates with a $0.101 per pound editorial benefit. Please construct the postage for this same publication using the proposed rate schedule. Please show the calculation of each element of the postage and explain any assumptions made.

RESPONSE OF WITNESS MITCHELL

As my testimony indicates (at 64, n. 43), the $0.3416 figure is based on mailing profile data for *The New Republic* provided by witness Dearth (its publisher) in Docket No. R90-1, which indicated that its pieces were all in sacks, its per-piece weight was 3.3 ounces, and its proportion of advertising was 23 percent. *See* Docket No. R90-1, Tr. 27 (part 2), 13361-78. In order to make my estimate consistent with current rates and classifications as they have evolved subsequent to Docket No. R90-1, it was necessary to make an assumption of some kind about the mailing's levels of prebarcoding and presortation. I based my estimate on an assumption that the pieces are barcoded and that they are presorted into 3-digit bundles.

In order to apply the proposed rates to the mailing, it is necessary to make assumptions about some additional characteristics of the mailing that were not included in the Docket No. R90-1 mailing profile data. I assume that the sacks are entered at an origin office, that the pieces are machinable, that the bundles are in 3-D/SCF sacks, that there are 3 bundles per sack, and that there are 16.93 pieces per bundle. The actual makeup for *The New Republic* (*TNR*), of course, is not known to me. The 3-bundle-per-sack assumption is an average for Outside County 3-digit sacks, developed from the 'BT inputs' sheet of my workpaper WP-Mitchell-3F (cell D137 divided by the sum of cells C94 through J94), and the 16.93-pieces-per-

bundle assumption is an average for Outside County 3-digit bundles, developed from the same sheet (the sum of cells E50 to E53 divided by cell D134).

When the proposed rates are applied, the corresponding *TNR* per-piece postage for Zone 8 declines from $0.3416 to $0.3296. If one assumes that the bundle size or the number of bundles per sack is increased, the applicable postage declines rapidly. Publishers need to evaluate these relationships as they consider the proposed rates.

The development of the $0.3296-figure is as follows, all cost figures being in dollars. The pound charge is 0.498 (the zone 8 rate) • 3.3/16 (the per-piece weight in pounds) = 0.1027. The per-pound editorial benefit, which is subtracted from the otherwise rate, is 0.101 (the per-pound editorial benefit rate) • 3.3/16 (the per-piece weight of the publication) • 0.77 (the proportion of editorial content) = 0.0160. The per-piece editorial benefit, which is also subtracted, is 0.074 (the per-piece editorial benefit rate) • 0.77 (the proportion of editorial content) = 0.0570. The per-piece charge is 0.230 (taken directly from the Schedule). The sack charge, on a per-piece basis, is 3.22 (the charge per sack from the Schedule) / (16.93 • 3) (the number of pieces per sack) = 0.0634. The bundle charge, on a per-piece basis, is 0.110 (the charge per bundle from the Schedule) / 16.93 (the number of pieces per bundle) = 0.0065. Using negative signs for the two discounts, these sum to the per-piece postage of $0.3296, as indicated above.

Response of Time Warner Inc. et al. Witness Mitchell to POIR No. 1, Question 3

POIR 1, QUESTION 3

Apart from the impact caused by the exclusion of letter-shaped pieces, would your proposal alter the proportion of Outside County revenue from regular rate, nonprofit and classroom? Please explain fully.

RESPONSE OF WITNESS MITCHELL

The Billing Determinants developed annually by the Postal Service show that there are differences among regular rate, nonprofit, and classroom with respect to things such as their per-piece weight, proportions of advertising, zone distribution, and presort levels. Similarly, there are differences in their use of bundles, of containers, and of associated entry points. Accordingly, one would expect the incidence of rates to vary.

Estimates of the revenues of each of these Outside County qualification categories, which recognize the effect of Science of Agriculture rates and the application of the 5 percent discount for nonprofit and classroom, are shown in my workpaper WP-Mitchell-3F. The before-rates revenues are on sheet 'by.' The after-rates revenues for letters are on sheet 'LtrBD' and, for non-letters, are on sheet 'New.' Rounded, 83.35 percent of the before-rates revenues are from regular, 15.94 percent from nonprofit, and 0.70 percent from classroom. The after-rates revenues are 84.83 percent from regular, 14.47 percent from nonprofit, and 0.71 percent from classroom. Since the rates for letter-shaped pieces would not change, these changes in the proportions are due entirely to the rates for non-letters.

Response of Time Warner Inc. et al. Witness Mitchell to POIR No. 1, Question 4

POIR 1, QUESTION 4

TW et al.-T-1, at page 33, discusses three adjustments to R2001 periodicals analysis. Were you able to calculate the separate financial impact of each of the three adjustments? If so, please provide the results of your calculations and a reference to where the impacts are shown in your workpapers. If not, please explain why not.

RESPONSE OF WITNESS MITCHELL

None of the three adjustments affects the revenue obtained from the Outside County subclass. Also, none of the adjustments affects the piece rates or any of the associated per-piece discounts.

I do not have a spreadsheet that generates the existing rates, which were the result of a settlement agreement. Since the question is directed at the effects on rates of the adjustments, I believe the best approach is to base the analysis on witness Taufique's original spreadsheet (contained in USPS-LR-107). Accordingly, I show the rates originally proposed by the Postal Service and then show the rates that are implied by making the adjustments, *ceteris paribus*. The differences between the adjusted rates and the proposed rates are the effects of the adjustments.

The third adjustment involves changing the 0.75 to 1.0 in the referenced cells of the spreadsheet. No rates are affected, however, since the change is small; its effects are lost in rounding.

The effects of the first and second adjustments are shown in the table on the next page. The rates implied by the first adjustment are developed by changing the proportion 0.5 to 0.4047 in cell C40 of the 'Pound Data_Adv' sheet. The rates implied by the second adjustment are developed by removing the reference to cell E49 from cell E57 on the same sheet.

Response of Time Warner Inc. et al. Witness Mitchell to POIR No. 1, Question 4

Table POIR-1-4: Effects of Making Adjustments to the Development of Outside County Periodicals Rates, as Described in TW et al.-T-1			
Description	**USPS Proposed Rates (cents per pound)**	**With First Adjustment**	**With Second Adjustment**
Regular Rate			
Advertising Pounds			
DDU	16.0	17.8	15.7
DSCF	20.4	21.8	20.2
DADC	22.5	23.6	22.6
Zones 1&2	25.0	25.7	25.1
Zone 3	26.8	27.2	27.0
Zone 4	31.7	31.1	31.8
Zone 5	39.0	37.1	39.2
Zone 6	46.7	43.3	46.9
Zone 7	56.0	50.8	56.2
Zone 8	64.0	57.3	64.2
Editorial Pounds			
DDU	15.8	16.2	15.6
DSCF	18.0	18.2	17.9
DADC	19.1	19.1	19.1
All other	20.3	20.1	20.3
Science of Agriculture			
Advertising Pounds			
DDU	12.0	13.3	11.8
DSCF	15.3	16.3	15.1
DADC	16.8	17.7	17.0
Zones 1&2	18.7	19.3	18.9
Editorial Pounds			
DDU	12.0	12.1	11.8
DSCF	13.6	13.6	13.4
DADC	14.3	14.3	14.3
Zones 1&2	15.2	15.1	15.2

1 CHAIRMAN OMAS: Is there any additional
2 written cross-examination for witness Mitchell?
3 MR. STRAUS: Mr. Chairman, I have a question
4 on the existing --
5 CHAIRMAN OMAS: Mr. Straus.
6 MR. STRAUS: I think we may get a cleaner
7 record. Mr. Mitchell corrected one conversion problem
8 on that -- on I guess from powerpoint to PDS, and
9 where he added the half before ounce. A very strange
10 gap. That would be page 8 of that Exhibit A, and if
11 in fact the witness agrees that those interrogatory
12 responses should be changed, they could in fact be
13 changed on the copy that the reporter has, and the
14 record could reflect the correction.
15 I may be misinterpreting, but it says rates,
16 bracket, space, and summary, space, back slash.
17 CHAIRMAN OMAS: Mr. Mitchell.
18 THE WITNESS: I think I am at the correct
19 location. We are on page 8 of our attachment.
20 MR. STRAUS: And our big number two, and my
21 copy says, "Summary," and then there is a space, and
22 then there is a bracket, and then there is some more
23 spaces, and then there is --
24 THE WITNESS: Okay.
25 MR. STRAUS: Do you have the same thing I

1 do?

2 THE WITNESS: I do not have the original,

3 but it is apparent that there is a problem. My

4 recollection is that I used up and down arrows at that

5 point. This was on a powerpoint screen, and I assumed

6 that the audience would be able to latch very quickly

7 on to an up or down arrow.

8 So I think that it is a summary increase and

9 summary decrease.

10 MR. STRAUS: I don't know if your counsel

11 wants to make that change or not given that you are

12 not sure what was there in the original.

13 CHAIRMAN OMAS: Mr. Keegan.

14 MR. KEEGAN: We have no objection to making

15 that change.

16 CHAIRMAN OMAS: Without objection.

17 THE WITNESS: I wonder if I have the

18 original.

19 MR. KEEGAN: From the context that would

20 make sense, and if you are willing to say that is what

21 you would say today, and we will accept it, I don't

22 think we need to go any further with it.

23 THE WITNESS: Can you give me just a moment

24 here.

25 (Brief Pause.)

1 CHAIRMAN OMAS: Mr. Mitchell.

2 THE WITNESS: I think I am almost there, and
3 if I am not, I will live with the up and down. I'm
4 sorry this is going so slow. My computer keeps
5 telling me that I did not update my anti-virus
6 program.

7 CHAIRMAN OMAS: Why don't we just say the
8 change is made subject to check.

9 THE WITNESS: Certainly. That is very
10 satisfactory, Mr. Chairman.

11 CHAIRMAN OMAS: Is that okay with counsel?
12 Mr. Straus?

13 MR. STRAUS: That's fine. Certainly.

14 MR. KEEGAN: I would also accept the change,
15 not subject to check, but to make the exchange as that
16 is what he intended to say.

17 CHAIRMAN OMAS: Okay. Thank you.

18 THE WITNESS: I don't believe I have it.

19 CHAIRMAN OMAS: This brings us to oral
20 cross-examination. Three parties have request oral
21 cross; the American Business Media, McGraw-Hill, and
22 the National Newspaper Association. Mr. Straus.

23 MR. STRAUS: Yes, I am ready.

24 CHAIRMAN OMAS: Would you please come to the
25 mike, Mr. Bergin.

1 MR. STRAUS: In interrupted your call for
2 additional written designations. I'm sorry.
3 MR. BERGIN: Excuse me. I do have some
4 additional designations and written cross-examination
5 to offer into evidence.
6 CHAIRMAN OMAS: Without objection.
7 MR. BERGIN: Mr. Mitchell, I am going to
8 hand you a copy of your responses to McGraw-Hill's
9 interrogatories to Time-Warner, et al., T1-39 to 44,
10 which were filed on July 9, 2004. And I would like to
11 ask you, Mr. Mitchell, whether those responses were
12 prepared by you under your direction?
13 THE WITNESS: Yes, they were.
14 MR. BERGIN: And if you were responding to
15 those interrogatories today would your answers be the
16 same?
17 THE WITNESS: Yes, they would. However, we
18 have found one typographical omission in Number 39, on
19 line 8 of that response, which is the fourth line from
20 the bottom. The word, "Opinion" with a Capital O,
21 should be put in after the word, "Commission."
22 I am making those changes physically on the
23 copies that you gave me.
24 CHAIRMAN OMAS: That would be fine.
25 MR. KEEGAN: I hate to correct my own

1 witness, Mr. Chairman, but I believe the word
2 "Opinion" should not have a capital O.
3 CHAIRMAN OMAS: Mr. Mitchell.
4 THE WITNESS: In that case, I always defer
5 to counsel on his advice, and so I will attempt to
6 make it a small o.
7 CHAIRMAN OMAS: Thank you. Mr. Bergin.
8 MR. BERGIN: And with that change, Mr.
9 Mitchell, are you satisfied with your response to
10 those interrogatories?
11 THE WITNESS: Yes.
12 MR. BERGIN: And, Mr. Chairman, I would
13 offer those responses into evidence and ask that they
14 be transcribed into the record.
15 CHAIRMAN OMAS: Without objection.
16 (The Exhibit, previously
17 identified as TW et al. - T1-
18 39, was received into
19 evidence.)
20 //
21 //
22 //
23 //
24 //
25 //

Response of Witness Mitchell to MH/TW et al.-T1-39

MH/TW et al. – T1-39: With reference to your response to MH/TW et al. – T1 – 3:

(a) Please explain fully the basis for your statement that "['i]f the volume reduction is large, there is a possibility that the marginal [transportation] cost will decline, due to scale effects," and reconcile your statement with the statement by witness Stralberg in response to MH/TW et al. – T2 – 8 that "when volume declines dramatically the marginal costs might increase for the volume that remains."

(b) Please explain fully the basis for your statement that a large reduction in volume may result in "lower volume variability of the Postal Service's transportation systems."

(c) Please explain fully the basis for your statement that a lower volume variability of the Postal Service's transportation systems "would result in lower unit transportation costs, not higher ones."

(d) Please explain fully the empirical basis for your statement, regarding the unit cost of handling sacks when mailers shift to pallets, that "the percentage decrease in the numerator [cost] is the same as the percentage decrease in the denominator [volume]," and reconcile your answer with the testimony by witness Stralberg in response to MH/TW et al. – T2 – 8 that: "Regarding sack sorting and other sack handling operations, there may be some disagreement over how volume variable those costs are. I do not know the answer to that question."

RESPONSE

(a) The first paragraph of my answer to MH/TW et al. – T1 – 3 defines unit cost. The numerator is the volume variable transportation cost and the denominator is the associated volume. The second paragraph of the same answer suggests that large volume declines might cause the unit cost to decline, because of a proportionate decline in the numerator that is larger than the proportionate decline in the denominator. This possibility is based on my belief that, faced with a large volume decline, the elasticity factors developed in the Commission's transportation analysis might tend to decline. That analysis is discussed in the Commission's ~~opinions~~ opinions and is based in large part on the analysis presented in several cases by Postal Service witness Bradley. See Docket No. R2001-1, USPS-T-18; PRC Op. R2001-1, March 22, 2002, at 167-92; and PRC Op. R97-1, May 11, 1998, at 204-18.

Response of Witness Mitchell to MH/TW et al.-T1-39

The response of witness Stralberg that you cite refers to *dramatic* volume declines and says that the marginal costs *might* increase. I would not argue that some increase in marginal costs could not occur. Speculating about extreme positions, however, may not inform the questions being faced. Other parts of Stralberg's same response provide particularly insightful comments about more realistic issues concerning the transportation of Periodicals. These deserve greater attention.

(b) Until an altered future arrives and the analysis is done, it is not possible to know the outcome for sure. My line of reasoning assumes continuous curves and focuses on likely behavior in the limit. The first limit is a presumption that a large volume *increase* would lead to *increases* in the elasticity factors. One could certainly argue that as there become multiple, full runs every day of the largest transport equipment available, all of the elasticities would be 1.0. The second limit is to reduce the overall volume levels to very low levels. There I see a transportation system where, say, a 10 percent volume increase might cause an increase in cost of only a few percentage points.

(c) The context of my statement is: "If the volume reduction is large, there is a possibility that the marginal costs will decline . . ." I then state, in effect, that if this occurs: "This would come about from a lower volume variability of the Postal Service's transportation systems, and would result in lower unit transportation costs, not higher ones." By definition, the marginal cost at issue equals the total accrued cost of all postal transportation times the variability times the distribution-key proportion divided by the Periodicals volume. The upward effect of variability on marginal cost is obvious.

Response of Witness Mitchell to MH/TW et al.-T1-39

(d) The basis for my statement is in the fourth and fifth lines of my answer to part "b" of subject response, where I say that "economies of scale are not generally believed to exist" in sack handling operations. This is consistent with the Commission's analysis of cost segment 3.

I do not see any conflict with witness Stralberg's response to MH/TW et al.-T2-8. When he says that "there may be some disagreement over how volume variable those [sack sorting or sack handling] costs are," I understand Stralberg to be acknowledging that questions have been raised by the Postal Service in several recent cases about whether the variabilities of some manual operations might be less than 100 percent. The Commission has found, however, that the costs are fully variable.

Response of Witness Mitchell to MH/TW et al.-T1-40

MH/TW et al. – T1 – 40: With reference to your response to MH/TW et al. – T1 – 7, please explain whether you are suggesting that the "value of the service received" may not be the same for the 3-digit pallet and the 3-digit sacks, and explain fully the reasons for your answer, and reconcile it with your response to MH/TW et al. – T1 – 1.

RESPONSE

As you note, I suggested only that the value of service received *may* be different, not that it *would be expected* to be different. Whether it is different in any particular situation is an empirical question. My discussion would not be complete if I did not allow for the possibility that it could be different. There is no conflict with my response to MH/TW et al. – T1 – 1, which is a hypothetical for the purpose of explaining the concept of efficiency. It too allows for the possibility of differences in the value of service.

Response of Witness Mitchell to MH/TW et al.-T1-41

MH/TW et al. – T1 – 41: With reference to your response to MH/TW et al. – T1 – 11(b), please explain fully how "[a]ll of the 23.8 cents" is included in the DADC, DSCF and DDU pound rates when each of those rates is less than 23.8 cents.

RESPONSE

Conceptually, the explanation is reasonably simple. The first-cut pound rates, to which your earlier question (MH/TW et al. – T1 – 11) refers, are per-pound transportation costs, by zone, and are 0 at the DDU level, 0 at the DSCF level, very low at the DADC level, and a little higher at each succeeding zone. Then (a) the non-distance-related transportation costs are *added* to the DSCF and above zones, (b) the 23.8 cents (which includes the editorial benefit and the non-transportation costs to be recovered from the pound rates) is *added* to all zones, and (c) the per-pound portions of the non-transportation cost avoidances are *subtracted* for the DADC level, the DSCF level, and the DDU level. Whenever the per-pound portion of the non-transportation cost avoidances "c" is larger than the sum of the first-cut transportation costs and the non-distance-related transportation costs "a," the resulting rates are less than 23.8 cents. It would be appropriate to view the removal of "c" as removing a portion of the non-transportation costs in "b," but not as removing any of the editorial benefit in "b." You might want to note that the spreadsheet of Docket No. R2001-1 leaves something to be desired, since some of the numbers were hard-wired to obtain the settlement rates.

Response of Witness Mitchell to MH/TW et al.-T1-42

MH/TW et al. – T1 – 42: With reference to your response to MH/TW et al. – T1 – 11(a):

(a) Please confirm that according to your analysis of PRC LR-9 in Docket R2001-1, the full revenue leakage associated with the unzoned editorial pound rate is $214.3 million. If you do not confirm, please explain fully.

(b) Please confirm that the above-referenced $214.3 million represents the difference between revenue generated by the flat editorial pound rate and the revenue that would be generated by editorial pounds if, in lieu of the flat editorial pound rate, editorial pounds were assessed the zoned pound charges that apply to advertising matter. If you do not confirm, please explain fully.

(c) Please confirm that no portion of the above-referenced $214.3 million is recovered from the flat editorial pound charge. If you do not confirm, please explain fully.

(d) Please confirm that a Periodical comprised of 100% editorial content would not pay any portion of the above-referenced $214.3 million, regardless of whether it was mailed a relatively short distance or a relatively long distance. If you do not confirm, please explain fully.

(e) Please confirm that under the current rate structure, the above-referenced $214.3 million is to be recovered fully from the zoned pound charges for advertising content. If you do not confirm, please explain fully.

(f) Please confirm that the extent to which a Periodical mailer pays any portion of the above-referenced $214.3 million depends solely on the advertising percentage of the Periodical, and not at all on the distance that it is mailed. If you do not confirm, please explain fully.

RESPONSE

(a) Confirmed.

(b) Confirmed.

(c) Not confirmed. Since the flat editorial pound is, in Docket No. R2001-1, 77.8 percent of the zones 1&2 advertising pound rate, which has been elevated by the 23.8-cent figure, it follows that the flat editorial pound rate is elevated by 18.5 cents per pound (0.778 * 23.8).

Response of Witness Mitchell to MH/TW et al.-T1-42

Consistent through all rate cases since Reorganization, including Docket No. MC95-1 but excepting Docket No. R2001-1, the flat editorial pound rate has been set at 75 percent of the zones 1&2 advertising pound rate. In Docket No. R2001-1, the Postal Service proposed an alternative way of specifying how much of the overall revenue was to come from the editorial pound rate, and the 75-percent proportion was increased to 81.2 percent. During the settlement discussions, adjustments were made that reduced the 81.2-percent proportion to 77.8 percent. At the same time, many of the cells in the spreadsheet were hard-wired, so that the sheet in the Commission's Library Reference 9 is not really a working spreadsheet.

Using the 77.8-percent figure, however, the effect can be illustrated. Suppose there are only three zones, 1, 2, and 3, with zone 1 taking on the characteristics of zones 1&2, and suppose further that the direct transportation cost for transporting mail is 3 cents (per pound) for zone 1, 5 cents for zone 2, and 9 cents for zone 3. These costs are estimates of actual per-pound marginal costs and are not influenced by whether the material being carried is advertising or editorial. Now add a non-distance-related transportation cost of 1 cent per pound and increase these three figures to 4, 6, and 10 cents. If the editorial pound rate were to be set at this point, it would be set at 0.778 • 4 cents = 3.112 cents per pound (although it would be rounded).

Now find the sum of 4 times the pounds of advertising in zone 1 plus 6 times the pounds of advertising in zone 2 plus 10 times the pounds of advertising in zone 3 plus 3.112 times the pounds of editorial. This sum provides a revenue-so-far figure. Subtracting this revenue-so-far from the revenue desired from the pound rates yields a deficit. Part of the deficit is due to the fact that a lower rate is being given to the editorial pounds.

Response of Witness Mitchell to MH/TW et al.-T1-42

The next step is to increase the pound rates by enough to make up the deficit, accounting for the fact that the editorial pound rate will be increased by only 77.8 percent of any resulting increase for advertising. Suppose it is calculated that the advertising pound rates need to be elevated by 5 cents per pound (a figure which corresponds to the 23.8-cent figure in your question designated MH/TW et al.-T1-12). The new rates for advertising become 9, 11, and 15 cents (5 cents added to each of the above figures of 4, 6, and 10). The zone 1 rate is now known to be 9 cents per pound, so the flat editorial rate will be 0.778 * 9 = 7.002 cents per pound (which will be rounded to 7.0 cents). It is clear that 7.002 cents per pound (for editorial) is much higher than the 3.112-cent figure calculated above, and specifically that the difference between 7.002 and 3.112 (7.002 – 3.112 = 3.890) equals 0.778 • 5 cents. In other words, the editorial pound rate has been elevated by 3.890 cents per pound (before rounding).

The figure of $214.3 million is a measure of the extent to which the editorial pound rate is reduced. (Drawing on the above illustration, it corresponds to (9.0 – 7.0 0) * zone-1 editorial pounds + (11.0 – 7.0) * zone-2 editorial pounds + (15.0 – 7.0) • zone-3 editorial pounds.) The proposed rates do not change this measure; they simply give it in an improved way.

(d) Not confirmed. Please see my response to part "c" above.

(e) Not confirmed. Please see my response to part "c" above.

(f) Not confirmed. Please see my response to part "c" above.

Response of Witness Mitchell to MH/TW et al.-T1-43

MH/TW et al. – T1 – 43: With reference to your response to MH/TW et al. – T1 – 13(b), please explain fully and precisely what "additional amount" – beyond the flat editorial pound charge – is paid by editorial pounds to recover revenue leakage associated with the flat editorial pound charge.

RESPONSE

The total number of pounds of Outside County Periodicals, TYBR, is 4,355,054,865 (see cell B52 of sheet 'Test Year BR' in the Commission's Library Reference 9, Docket No. R2001-1). Since editorial pounds are going to pay only 77.8 percent of any elevation in the pound rates, it is convenient to work with weighted pounds, equal to 77.8 percent of the editorial pounds plus 100 percent of the advertising pounds, which is 3,810,631,220 pounds. The figure of $214.3 million divided by the weighted-pound figure is an elevation of 5.62 cents per pound. The editorial pound rate is elevated 77.8 percent of this amount, which is 4.37 cents per pound. This is the "additional amount" you seek. When this amount is multiplied by the total number of editorial pounds, the result is $109.3 million. In other words, the benefit to editorial matter, in the pound rates, is $214.3 million, $109.3 million of which is paid by editorial itself.

These figures outline a particularly perverse characteristic of the flat editorial pound rate. Suppose there were *no* flat editorial pound rate and *no* pound-rate editorial benefit of any other kind either. The figure of $214.3 million would then be revenue that would be used to lower *all* pound rates. Specifically, $214.3 million is 4.92 cents per total pound (214,300,000/4,355,054,865, expressed in cents). Therefore, the full weight of the publication would pay the current advertising pound rates less 4.92 cents per pound, these rates being, after rounding, 15.4 cents at the DSCF level, 17.4 cents at the DADC level, and 19.9 cents at the zones 1&2 level.

Under the flat editorial pound rate, a 100 percent editorial publication pays 19.3 cents (per pound) at each of the DSCF level, the DADC level, and the zones 1&2

Response of Witness Mitchell to MH/TW et al.-T1-43

level. Under the no-editorial-benefit rates just described, the same 100 percent editorial publication would pay, in the same order, 15.4 cents, 17.4 cents, and 19.9 cents. It is clear, then, that without any per-pound editorial benefit at all, all-editorial publications, compared to their current situation, would be 3.9 cents per pound better off at the DSCF level (accounting for 40.59 percent of Outside County volume), 1.9 cents per pound better off at the DADC level (accounting for 8.5 percent of Outside County volume) and only 0.6 cents per pound worse off at the zones 1&2 level (accounting for 9.36 percent of Outside County volume). In other words, due to the skewed nature of the way the benefit is provided, editorial matter is paying so much of the editorial benefit that much of it would be better off not having the benefit at all. It could be argued that a substantial portion of editorial matter is paying a *penalty* for being editorial. The rates proposed in the Complaint do not have this infirmity.

Response of Witness Mitchell to MH/TW et al.-T1-44

MH/TW et al. – T1 – 44: With reference to your response to MH/TW et al. – T1 – 14, please put aside the assumption adopted in your testimony that all local and regional publications have an average proportion of advertising content, and answer the interrogatory as asked.

RESPONSE

Removed from its context, your question is whether a local or regional publication with a "high" proportion of editorial content, printed and entered near the location of its readership, might have a cost coverage that is below 100 percent and at the same time whether this cost coverage (that is below 100 percent) might be lower than the cost coverage for a local or regional publication with a "high" advertising proportion that is printed and entered a considerable distance from the location of its readership.

As it stands, the question refers, without being specific, to high proportions and considerable distances. For discussion purposes, let's assume the high-editorial publication is 100 percent editorial and the high-advertising publication is 100 percent advertising, and further that the former is entered in the DSCF and the latter in zone 8. And let's recognize that high-editorial publications are considerably lighter in weight-per-piece than the average publication, so that the zone rates play a lesser role in their postage (see my response to MH/TW et al. – T1-24b). As noted on line 12 of page 37 of my testimony, the average cost coverage on editorial matter is 84.7 percent and on advertising matter is 129.5 percent, and these would apply if the billing determinants of both the editorial and the advertising were the same as the billing determinants of the subclass as a whole.

The editorial piece would be expected to have a much higher cost coverage in the DSCF than in zone 8, due to the nature of the flat editorial pound rate and to the fact that the non-transportation cost difference among the zones are not recognized in

Response of Witness Mitchell to MH/TW et al.-T1-44

the rates. Also, I showed in my response to MH/TW et al. – T1 – 43 that the flat editorial pound rate at the DSCF level is higher that would be a more cost-based rate under a structure without a flat editorial pound rate and without any other editorial pound benefit. Particularly for a lightweight piece, however, and due in part to the fact that there is also a per-piece editorial benefit, it seems doubtful that the DSCF coverage would be enough higher than 84.7 percent to cross 100 percent. Therefore, the suggestion in your question is probably correct. The coverage on the advertising piece would not vary as much by zone as the coverage on the editorial piece; since some of the cost differences are recognized in rates, however, it would vary, and it would be lower in zone 8. It seems unlikely that the figure of 129.5 percent would decline by as much as 29.5 percentage points for zone 8, so that, again, the suggestion in your question is probably correct that the coverage on the advertising piece is both higher than the coverage on the editorial piece and greater than 100 percent.

As can be seen from this analysis, the benefit being received by the editorial piece, relative to the cost coverage of the subclass, may be rather small. Also, back to the context of my testimony, the editorial piece is in a position where it could be printed at a distant location, for little or no increase in postage, and thus be carried back by the Postal Service virtually free. On the other hand, the advertising piece is not as likely to print at a distant location, because its rates do increase, although not as much as the Postal Service's costs. Accordingly, it seems more likely that the printing of the pieces in your question would fall the other way, the editorial printed far and the advertising printed close.

1 CHAIRMAN OMAS: Are there any additional
2 written cross-examination?
3 (No response.)
4 CHAIRMAN OMAS: Not hearing any, now this
5 brings us to oral cross-examination. Mr. Straus, you
6 may begin.
7 CROSS-EXAMINATION
8 BY MR. STRAUS:
9 Q Mr. Mitchell, please take a look at page 2
10 of your response to ABM's C1-1.
11 A I have it.
12 Q At the bottom of that page, you refer to
13 some large increases in the basic pre-sort rate in the
14 1980s. Do you see that?
15 A You are on page 2 of -- oops.
16 Q No, page 2 of ABM C1-1.
17 A It refers to docket number R-84-1?
18 Q Yes, that's it.
19 A Yes.
20 Q Those increases were in the basic presort
21 rate for periodicals; is that right?
22 A Yes. In fact, there were other increases in
23 the other rates, but I used that one as an example.
24 Q Because those are so large?
25 A I think they were all pretty large as I

1 recall, because there was some revenue burden shifted
2 to the piece rates, which meant that all the piece
3 rates went up.
4 Q But they did select these two rates because
5 they were -- or this rate because it was the largest
6 increase, and you were giving an example of how large
7 increases sometimes are necessary or appropriate?
8 A I can't say for sure right now whether I
9 selected it for that reason. I think it was also the
10 basic reference point, particularly for small
11 publications that do not have the density required to
12 reach the other levels.
13 So I am sure that that rule, in addition to
14 its size, was also a factor. But I can't specifically
15 recall whether or not it was the largest.
16 Q How many pieces does one need in order to
17 avoid the basic presort rate? How many pieces to a
18 destination?
19 A Well, at the time the proportion of all
20 periodicals, pieces at the basic rate was much higher
21 than it was today, and also at that time the next
22 presort tier down was a 3/5 presort tier, often
23 referred to as a level B.
24 So under some conditions, if you had, I
25 think, maybe 10 pieces or 5 or 10 pieces per the

1 appropriate three digit level, or five digit level, I
2 think you were required to proceed to prepare the mail
3 in those packages.
4 Q So you are saying that a mailer who had,
5 say, six pieces to a three digit zip code had to
6 bundle that way, and therefore the only pieces paying
7 the basic rate were those that had to be pay the basic
8 rate as it were? Nobody could avoid the basic rate
9 basically?
10 A There were a very limited number of three
11 digit zip codes which you could do that in. For the
12 most part, the three digit mail resided in the basic
13 category. They were called three digit cities at the
14 time, and there was a limited number of them which
15 were listed in the DMM.
16 And my recollection is that it was a
17 reasonably small proportion of all three digit areas.
18 Q You addressed in this response your
19 employment at first the Postal Service, and then the
20 Postal Rate Commission. When you were at the Postal
21 Service did you ever testify about the flat editorial
22 pound rate?
23 A Yes, I did.
24 Q And did your testimony at that time support
25 a change to the zone rate?

1 A The change to?
2 Q To a zone editorial rate?
3 A Yes, it did.
4 Q And what case was that in?
5 A It was Docket Number R-87-1, and Docket
6 Number R-90-1 before this Commission.
7 Q And the Commission declined at that time to
8 zone the editorial rate; isn't that right?
9 A Yes, they did.
10 Q And then when you worked at the Postal Rate
11 Commission, and I am not going to ask you what advice
12 you gave them, as I don't think that would be
13 appropriate, but did you change your mind about
14 whether the zone editorial rate should be zone?
15 A No, I didn't.
16 Q When you were at the Rate Commission did you
17 advise the Commissioners in terms of their decisions,
18 and what other agencies would call the Decisional
19 Staff?
20 A I don't know the full legal meaning of the
21 phrase, advised the commission. In formal briefings
22 with the Commission, when I was involved, those
23 briefings focused on issues that were before the
24 Commission, and I don't believe that issue was before
25 the Commission.

1 Now, if you want to know whether or not
2 informally I discussed this issue with colleagues over
3 the 10 years that I was at the Commission, the answer
4 is, yes, I did.
5 Q Well, thank you. You were at the Commission
6 during the reclassification case in 1995 were you not?
7 A Yes, I was.
8 Q And was one of your roles to advise the
9 Commission on the issues in that case?
10 A I think that I discussed with the
11 Commission, and briefed the Commission, on most all
12 issues in that case. It doesn't mean that I was the
13 only person having an input to the Commission, but it
14 does mean that I provided advice on what I thought.
15 Q I guess we are going to have to go back into
16 publications and websites again. Your response to
17 Question Number 4 -- and for the record, when I refer
18 to question numbers, they are all going to be T1
19 question numbers, unless otherwise stated.
20 A Thank you. I get very confused when you put
21 in all these extra letters.
22 Q The et al. makes it even more complicated.
23 You say there that Folio maintains a website of its
24 own, which appears to make its articles available. Do
25 you know whether it includes the entire content of the

1 hard copy publication?

2 A My understanding, and my experience in

3 general, has been that websites often don't include

4 the entire publication, and that they don't include

5 the advertisements from the publication.

6 But I did not take a copy of Folio and

7 compare it with the website for that issue.

8 Q Is the website -- do you have to pay for

9 access to the information on the website?

10 A No, you don't.

11 Q Is Folio a paid circulation, periodical, or

12 request periodical?

13 A I believe it is paid.

14 Q Can you tell me why anyone would pay for the

15 hard copy if all the information is available for free

16 on the website?

17 A Well, let me say two things. Number 1, if

18 you are like me, you really like hard copy. You can

19 take it with you places very easily, and you can mark

20 it up, and you can make copies of it, and you can keep

21 it in an orderly place on a shelf.

22 You can read it in any room in the house,

23 and because I don't have a wifi computer system in my

24 house yet, and so I like hard copy and I am willing to

25 pay for it when it is important.

1 The second thing I would like to say is that
2 I think this business of free websites is in a state
3 of transition right now. There are a very large
4 number of people making information available free on
5 the web, but it is not free to put it there.
6 And it is not free that they can continue
7 that forever, and if we get to the point here someday
8 where people use the web predominantly, they are going
9 to have to pay for it. I don't think it is going to
10 continue to be free, just like television used to be
11 free when you didn't have to buy cable, and you could
12 just pick it up out of the air, and advertisers paid
13 for it entirely.
14 So I think the whole world is going through
15 a transition here, where we figure out how to go about
16 charging for websites. I was on a mini-newspaper
17 website and when I asked for a copy, they wanted my
18 credit card and $5.95 for the first copy.
19 And so I am not sure that we can say as an
20 equilibrium situation, a long term equilibrium
21 situation, that these websites are going to continue
22 to be free. I think people are going to have to pay
23 for them.
24 Q At the end of that answer, you referred to
25 websites of the Association of Postal Commerce and

1 lines of nonprofit mailers, and Postal Rate
2 Commission, DM News, and a couple of others, Postal
3 Insight. Are those the same type of information as
4 Folio?
5 A I would say only that there is some overlap.
6 In other words, Folio is much, much broader than some
7 of these sites. If you look at Pitney-Bowes Postal
8 Insight, they quite often have full copies of
9 presentations and speeches that people make.
10 Those kinds of things obviously aren't
11 available in magazines usually. Sometimes the
12 articles in the magazines are a summary of something
13 that is available on these other sites, but I should
14 not be interpreted to be saying that these other sites
15 suffice for the publications that you asked me about.
16 I am a fan of the publications of maybe all
17 of your members, although I am not familiar with all
18 of them. I think the --
19 Q Do you read Pork?
20 A I will tell you what I have read.
21 Q Or Swine Practitioner?
22 A If you look at my resume, you will see that
23 I worked at a concrete firm once, and at that time I
24 was reading Concrete Magazine. And if you also note,
25 I was an engineer at one time. I was a mechanical

1 engineer, and I worked on a drawing board, and I
2 worked at an R&D Center.
3 I got Machine Design Magazine, which I
4 appreciated. I got Automotive Industries. I got
5 Steel Magazine. I think very highly of those
6 magazines, and I still do. I get Aviation and Space
7 Technology right now. I appreciate it as much now as
8 I did 30 years ago.
9 So I think very highly of the content and
10 the integrity of these magazines, and I also was
11 pleased to see in Mrs. Zuckerman's book on the
12 business press that she seemed to feel like nearly all
13 these business to business publications had done a
14 very effective job separating their advertising people
15 from their editorial people so that their editorial
16 people could be independent.
17 And I think that many of them are very
18 highly thought of for good reason.
19 Q Thank you. I think the American Business
20 media will appreciate reading that. I would like to
21 turn now to the -- I guess what was a powerpoint
22 presentation to which you made the corrections
23 earlier. This will be in response to ABM 13.
24 A Yes.
25 Q And more specifically on page 3.

1 A Yes.
2 Q You say or you list there your biases.
3 Number 4 was that mailers will respond to rate
4 signals, and there is an exclamation point under that,
5 and I don't know if originally you had an exclamation
6 point or some other symbol and PDF converted it.
7 A Actually, PDF converted it from something
8 else, but I can't remember what the original symbol
9 was.
10 Q I don't think it matters much. The words
11 after the first exclamation point are facilitated by
12 high volumes. Can you tell me what you meant there?
13 A What I mean is that as mailers mail in
14 larger volumes, you begin to be able to respond to
15 signals. If you have 10 or 20 copies, a hundred
16 copies, 500 copies, if you have 500 copies and you
17 save a penny, that is $5.
18 Nobody is going to get very excited about
19 saving $5. It just is not going to be on their radar
20 screen. But what we have today is a very large number
21 of highly sophisticated mailers who have a good deal
22 of volume, and 50,000 I think is a good deal of
23 volume.
24 And 25,000 is even a good deal of volume,
25 and you are doing these things repetitively. In other

1 words, you have got a weekly magazine, or a monthly
2 magazine, and that means that you do it every week or
3 every month, or maybe quarterly.
4 And if you set yourself up to make a change
5 in what you are doing, then you can often repeat that
6 change many times. So when you are dealing with
7 sophisticated mailers of a substantial volume, and I
8 am not just talking about the people that are over a
9 million.
10 I am talking about a lot of people way under
11 a million, and even the ones with a circulation of
12 25,000 are using very sophisticated printers. They
13 are using printers with very high technology, and with
14 a good computer system, and as is very often the case,
15 very small differences in rates, and they are able to
16 make a change, which is a very effective change.
17 So my point here in my presentation was that
18 mailers are in fact able to respond today, and that
19 makes it all the more important to give them good
20 signals.
21 Q Please look at page 5 of the same
22 presentation. You have what I think can fairly be
23 characterized as some criticisms of the First-Class
24 Mail structure. I gather, and would I be correct in
25 concluding that you do not believe that the First

1 Class Mail structure is appropriate? The rate
2 structure, that is?
3 A I believe that there are improvements that
4 could be made effectively in the First Class Rate
5 structure. I think the Postal Service in fact is
6 considering some of them for the next case. It is
7 widely understood that they are going -- or are
8 thinking about separating letters from flats.
9 For example, if you take a two ounce letter
10 and a two ounce flat, they both take 60 cents. So a
11 mailer of a letter can easily say, gee, I will convert
12 this into a flat. It is a little easier to me, and I
13 will impose some additional costs on somebody else.
14 It doesn't make any difference.
15 But a person with a flat might say, gee, I
16 can convert this into a letter, but there is no reason
17 to. And if there is a rate difference, and if they
18 have to pay their own way, they might make the change
19 and everybody might be better off.
20 So for that reason, among others, you would
21 not call the First Class rate structure efficient
22 would you?
23 A No, I wouldn't. I think there is some
24 variable changes that could be made. We have been
25 moving in that direction very slowly, I think.

1 Q And you would not call it a standard mail
2 classification, which you criticize on the next page,
3 efficient either would you?
4 A I believe in the standard as well that there
5 are some improvements that we understand now that we
6 are in a position to make, and many of them are the
7 same as the ones that are discussed in the complaint.
8 I think that they imply that similar changes
9 could be made for standard.
10 Q And on page 7, one of your criticisms, or it
11 looks to me like a criticism of standard mail, is that
12 you have two dropped shippers, one with mail from New
13 York, and one with mail to Chicago, and they get the
14 same discount.
15 And your problem there, I guess, is that
16 standard mail isn't zoned; is that right?
17 A That's right. Now, this structure of
18 dropped shipper discount in the standard was just put
19 in the R90 case. So it may be time to take a further
20 step.
21 Q So First Class isn't zoned; that's right,
22 isn't it?
23 A That's right, it's not.
24 Q And standard isn't zoned?
25 A You could argue that standard has a

1 nationwide zone and a DBMC zone and DSCF zone, and a
2 DDU zone. But it does not have a traditional zone
3 structure.
4 Q Is priority mail zoned?
5 A I am trying to distinguish in my mind
6 between priority and express. It seems to me like
7 express started out zoned and became unzoned, and
8 maybe it is zoned again. I am not sure, but I think
9 that priority is zoned.
10 Q And what about express mail?
11 A I think the postal service had a separate
12 classification case back a number of years ago which
13 made it unzoned because of the Hub system. And I
14 think the Hub system, when the competitors have made
15 changes today, which suggest that it might be better
16 to zone it again in order to be competitive and
17 recognize costs. Part of the --
18 Q Mr. Mitchell, the question is whether it is
19 zoned, and not -- we are going to be here a very long
20 time --
21 CHAIRMAN OMAS: Mr. Mitchell, would you just
22 answer the question that is being addressed to you. I
23 think we would all appreciate that. Thank you.
24 THE WITNESS: I don't believe that express
25 mail is zoned at this time.

1 BY MR. STRAUS:
2 Q So you think that priority mail is zoned,
3 and the periodical advertising rate is zoned. What
4 else is zoned today?
5 A Parcel Post.
6 Q And that's it?
7 A Bound printed matter.
8 Q Is there a question mark with that or a
9 period?
10 A I always feel funny trying to give all-
11 inclusive lists extemporaneously.
12 Q Well, you can state, "I don't recall," and
13 is an acceptable answer to me if it is to you.
14 A I think that's it.
15 Q Please look at page 9 of that presentation.
16 A Yes.
17 Q This presentation appears to have been made
18 a little more than a year ago, May 8th, 2003, and that
19 is what appears at the top of that page; is that
20 right?
21 A Yes.
22 Q And your first numbered point there is that
23 UPS must do studies to support changes. Can you tell
24 me what studies the Postal Service has done since then
25 to support changes?

1 A I don't believe I can tell you what studies
2 the Postal Service has done since May 2003.
3 Q You don't know the result of any studies do
4 you? What kind of studies were you talking about here
5 that are necessary to support changes?
6 A You are asking me if I know the results of
7 any of those studies?
8 Q Yes. Do you know the results of any studies
9 the Postal Service has made since 2003, the kinds of
10 studies that you say are necessary?
11 A I have not seen the results of any studies
12 done since then.
13 MR. KEEGAN: Mr. Chairman, I object to the
14 question. It mischaracterizes the witness' testimony.
15 He does not state that these studies are necessary for
16 anything. He says that USPS do them.
17 MR. STRAUS: Part B says that the studies
18 are needed now, and needed to me means necessary, and
19 if it means something else to Mr. Keegan, we will
20 brief the issue, but I don't think I misrepresented
21 when the witness himself used the word needed.
22 MR. KEEGAN: Needed or necessary or not is
23 the same in my view.
24 CHAIRMAN OMAS: I will allow it.
25 BY MR. STRAUS:

1 Q Well, I think the question was answered
2 anyway. In 2C, Mr. Mitchell, you say the changes
3 cannot be made by the Rate Commission. What changes
4 did you mean there?
5 A Okay. You have to understand that this is a
6 general presentation to an audience of envelope
7 manufacturers, and so it is a very general statement.
8 What I mean is that it is very difficult for the Rate
9 Commission to look at a set of rates or a mail
10 classification structure, and initiate changes itself.
11 It does have the right to initiate mail
12 classification changes, but quite often those get
13 rejected by the Postal Service, and quite often we do
14 not have the cost analysis necessary to proceed with
15 them without the help of the Postal Service.
16 So all I mean there is that it is very
17 difficult for the Rate Commission to take the initiate
18 to do these things.
19 Q Please look at page two of Attachment B.
20 A Okay.
21 Q Your Number 9 indicates that in Docket R71-
22 1, piece rates, came into existence. Was the
23 introduction of piece rates a cost-based change to the
24 periodical rates?
25 A I believe it was.

1 Q And when Congress added exe (phonetic) value
2 in 1976, assuming that was a change rather than a
3 codification of an existing policy, was that cost-
4 based?
5 A No, it wasn't. It was never intended to be
6 cost-based.
7 Q And then in Number 11, you talk about the
8 per piece editorial discount came into existence. Was
9 that cost-based?
10 A No, it wasn't.
11 Q Is the carrier rate a cost-based rate?
12 A A carrier route discount?
13 Q Yes.
14 A I think it was.
15 Q Is the bar code discount a cost-based
16 discount?
17 A Yes.
18 Q Is the pallet discount today inadequate as
19 you may think it a cost-based discount?
20 A I think it is stretching matters to refer to
21 it as a cost-based discount. It has strange
22 characteristics. I said in an interrogatory response
23 to you that my definition of cost-based was that the
24 costs were known and recognized, and that a mark-up
25 over costs was selected on a defensible basis.

1 And I don't think that there is a defensible
2 basis for the structure of the current pallet discount
3 even though it does refer to costs in the process.
4 Q Well, pallets are less expensive to handle
5 than sacks, right?
6 A Yes, they are.
7 Q And the pallet discount recognizes some of
8 that cost difference doesn't it?
9 A Yes, it does.
10 Q And in Number 13, little paragraph 13 on
11 pate 3 of that presentation, you refer to the cost
12 coverage in the 2000 case for periodicals, and explain
13 that the coverage for editorial is 82.3 percent, and
14 the coverage in advertising is 125.6, from which you
15 concluded that the editorial content is being handled
16 well below costs. Do you object to that?
17 A No, I don't. There is nothing in our
18 complaint that deviates from that.
19 Q So therefore you don't object, even if the
20 hundred percent editorial publication can be mailed
21 for rates lower than costs?
22 A Congress is the one that said that exe
23 (phonetic) value should be recognized. I think that
24 this is a way of recognizing that exe value, and I
25 believe it is an acceptable way, and I have no

1 personal problem with it.

2 Q Does pricing periodicals that are a hundred

3 percent editorial send proper price signals?

4 A In what respect?

5 Q In the respect that you use --

6 A No, I think it is a very poor placed signal.

7 I think I have many examples of bad characteristics of

8 that price signal in my testimony.

9 Q And therefore would it also be your

10 conclusion that it is inefficient to price a hundred

11 percent editorial products below costs?

12 A I believe that it prevents many changes that

13 would be an improvement in efficiency. Yes, I think

14 it is an inefficient rate structure, and I don't think

15 it is accomplishing anything.

16 Q But you said that you don't object to it?

17 A Are we talking -- I'm sorry if I got lost.

18 Are we talking about whether or not we have a lower

19 market on editorial or whether or not we have a flat

20 editorial rate?

21 Q Whether we have editorial content being

22 handled well below costs, to use your words? I asked

23 if you objected to that.

24 A No, I don't.

25 Q Despite the fact that it sends poor price

1 signals, and it is inefficient?

2 A Okay. As soon as you said sending poor

3 signals, I began to think of the flat editorial rate

4 and I am sorry for that. I guess the signal that it

5 sends is that if you are a publisher and you add

6 editorial pages, the increase in your rate is going to

7 be less than the increase in postal costs.

8 But I don't view that as an unacceptable

9 signal. I think that is implied when you make a

10 decision to give a lower cost coverage on the

11 editorial. So I don't have any problem with that

12 signal.

13 Q So in that case, because Congress has

14 directed editorial -- has directed that that special

15 attention or special rate concession be given for

16 editorial content, because of that policy, you don't

17 disagree with the concept of editorial being carried

18 below costs, not withstanding the price signals and

19 the inefficiencies; is that right?

20 A I think that's right.

21 Q You say in response to Number 14 that you

22 have worked on this case since July of 2003. Pardon

23 me. To be more precise, you say that since that time

24 much of your work has been involved with this case.

25 Did you have a hand in drafting Mr. Gordon's

1 testimony?

2 A No, I didn't.

3 Q Did you review it before it was filed?

4 A I reviewed it once.

5 Q Did you notice Mr. Gordon's statement that

6 multiple printing plant usage by periodicals has led

7 to a significant reduction in the portion of

8 periodical costs that are attributed to

9 transportation?

10 MR. KEEGAN: Objection, Mr. Chairman. That

11 is a mischaracterization of the witness' testimony as

12 he himself testified today.

13 BY MR. STRAUS:

14 Q I will restate it. Did you specifically

15 focus on Mr. Gordon's testimony about the causes for

16 the reduction in the percentage of periodical costs

17 attributable to transportation?

18 A I don't recall commenting on that part of

19 it.

20 Q The question is do you recall focusing on

21 it, and not do you recall commenting on it?

22 A No.

23 Q In response to our Question 16, in your

24 second sentence. You state that some concepts of

25 efficiency would require that consideration be given

1 to the value of the service provided. I must admit
2 that I don't follow that. Could you -- and I hate to
3 do this, but could you expand on that a bit and tell
4 me how value of service enters into an assessment of
5 efficiency?
6 A You are on 15?
7 Q I am on 16.
8 A Sixteen?
9 Q Yes, the second sentence.
10 A The second paragraph?
11 Q The second sentence.
12 A Okay. Some concepts of efficiency would
13 require that consideration be given to the value of
14 the service provided. I mean service to be very
15 general there, and to be associated with the entire
16 publication.
17 When people buy a magazine, or a
18 publication, they get some utility from it. They get
19 some benefit from it. They in effect have a demand
20 code, and based on that utility, and based on that
21 demand, and based on what they gain from it, they make
22 a decision to buy it instead of buying something else.
23 And efficiency concepts and economics focus
24 very much on the utility and benefit that people
25 receive from buying magazines.

1 So that is what I mean when I say efficiency concepts
2 require consideration be given to that value.
3 Q Also in that same paragraph, you refer to
4 the possible improvement in your neighbor's welfare
5 when you receive a periodical and when you receive a
6 catalog, and I must admit that I don't know why you
7 are discussing your neighbor's welfare rather than you
8 own.
9 A I think -- am I missing a word,
10 externalities there, and I think I do.
11 Q Well, this is an example of an externality?
12 A It is an externality. In other words, if my
13 kids talk about good important things, it has an
14 influence on my neighbors' kids, because they go to
15 school together. If I vote intelligently, it has an
16 influence on my neighbor because he has to live under
17 the same laws.
18 There are a large number of things that
19 could happen to me that would have a positive
20 spillover on my neighbor. But the problem is that I
21 don't consider any benefit to my neighbor when I
22 decide whether or not to buy a publication, and that
23 is the justification for -- well, at least one
24 justification in my mind for an exe value is to
25 correct for that situation which is not recognized

1 when people make decisions.

2 Q Is it possible that your neighbors' welfare

3 is improved when you receive certain types of

4 publications, but is actually diminished when you

5 receive other types? Let me give you an example.

6 If you receive Newsweek, and your kids

7 discuss current events, as opposed to receiving

8 Hustler, and your kids take it next door. I am not

9 saying whether that should be reflected and raised,

10 but is it at least possible that those externalities

11 can go in opposite directions, depending upon which

12 type of periodical you receive?

13 A Well, if you are asking for my personal

14 opinion, yes, I do think that the content of some

15 publications is more valuable or more positive than

16 the content of others. However, I am not sure that it

17 is fair to ask me my personal opinion on that issue as

18 though it should guide anything, because that seems to

19 me to be a process of censorship.

20 Q That's fair enough. Do you think as a

21 general proposition that therefore it is better to

22 have more publications than fewer publications, in

23 terms of externalities?

24 A There are implications of having more

25 instead of fewer. If I had to subsidize publications

1 in order to have more, so that when they go into
2 business they understand full well that they are going
3 to be using a lot more resources than they paid for,
4 because they think I am going to be interested in
5 buying it, then I have reservations about doing that.
6 Q But you have no reservations about
7 subsidizing a hundred percent editorial publications
8 no matter what their content; is that right?
9 A Yes.
10 Q In our Question 17, we asked a question
11 about the graph on page 3.
12 CHAIRMAN OMAS: Mr. Mitchell, if you would
13 move the mike a little bit away, maybe we can adjust
14 it so that we don't get the popping noise. Okay. And
15 up a little bit.
16 THE WITNESS: Up?
17 CHAIRMAN OMAS: Yes, that's good. Now,
18 let's see if that is better. I'm sorry to interrupt,
19 Mr. Straus.
20 BY MR. STRAUS:
21 Q That's fine. I made a mistake anyway and
22 that is a good break. Your testimony on page 3, lines
23 10 through 12, where you are discussing periodicals
24 rates compare with the Consumer Price Index, and we
25 asked you about that.

1 And you refer in your answer to page 9 of
2 your testimony, where you say at that latter page that
3 the rate index is a clumsy way to a price index using
4 base period weights. I couldn't find that discussion
5 on page 9, and I still don't know exactly what you
6 used for periodical rates, because I don't understand
7 quantity weighted price index.
8 So could you tell me again what you used as
9 a measure for periodicals rates for those different
10 years?
11 A In each recommended decision, the Commission
12 provides a percentage rate increase for periodicals.
13 That is a quantity weighted price index, in the sense
14 that it takes one set of billing determinates, and
15 evaluates both prices at those same billing
16 determinates.
17 So it is not a revenue for piece. It is a
18 price index. So I took those price indexes out of
19 each recommended decision, and linked them together so
20 that if one went from a hundred up to 105, which is a
21 5 percent increase, and then the next one was a 6
22 percent increase, then you multiply the 1.05 by 1.06
23 in order to get what the rate level is at the end of
24 the second case. So I linked together quantity
25 weighted price indexes.

1 Q So that would be sort of the average
2 increase for the periodicals class?
3 A Yes, it would.
4 MR. STRAUS: Please look at your response to
5 Number 18. I must confess, I don't understand the
6 answer. You said that to the extent that postage
7 reductions were equal to the cost reductions, these
8 steps would not cause rates to decrease. Maybe I
9 should try the question a different way.
10 If the placing of a bar code on a piece
11 reduced the Postal Service's costs by two cents, and
12 the Postal Service reduces its postage charges by two
13 cents, then postal rates will have declined by two
14 cents.
15 MR. MITCHELL: No. That's not a rate
16 decrease. The bar code rate is the same was it
17 before. The nonbar code rate is the same as before.
18 All of the rates are the same as before, but the
19 mailer is using a little different rate than he was
20 before, which means that his postage per piece goes
21 down, but there is no decline in any rate.
22 MR. STRAUS: Unless we're talking about the
23 first time a bar code rate is established. If we're
24 talking about the establishment of a bar code
25 discount, that would reduce the rate. Right? You're

1 saying that changes in billing determinants aren't the
2 same as changes in rates.
3 MR. MITCHELL: Basically, I'm saying that a
4 reduction in the mailer's postage per piece is not the
5 same as a rate decrease. There is a slight question
6 about how to construct proper price indexes at the
7 initial time when a new feature is added to a rate
8 structure when you put in a bar code discount. That's
9 kind of a separate subject but a minor one because it
10 starts our very small.
11 MR. STRAUS: Please look at number 24. What
12 I would like you to do is read Response A and tell if
13 you really meant "less than" rather than "more than"
14 because if you did, then I don't understand the
15 answer.
16 MR. MITCHELL: In context, a mailing
17 practice becomes more economical if the mailer makes a
18 change such that the decrease in postage under cost-
19 based rates, which also equals the decrease in the
20 cost to the Postal Service and in the cost to the
21 nation, including the value of any changes in the
22 level of service received, is less -- the decrease in
23 postage is less than the cost to the mailer of making
24 the change.
25 MR. STRAUS: Don't you mean that it's

1 economical if the decrease in postage is more than the
2 cost to the mailer of making the change?
3 MR. MITCHELL: Becomes more economical if
4 the decrease in postage -- the mailer gets a four cent
5 decrease -- is less than the cost to the mailer -- it
6 costs him two cents to do it --
7 MR. STRAUS: Then the four cents wouldn't be
8 less than the two cents; it would be more than the two
9 cents.
10 MR. MITCHELL: If the mailer makes a change,
11 the Postal Service costs go down four cents, his
12 postage goes down four cents, it costs the mailer two
13 cents to make the change, then the mailer is two cents
14 better off, and that's an increase in efficiency.
15 It's a net gain.
16 MR. STRAUS: But in that case, the decrease
17 in postage is more than the cost to the mailer; it's
18 not less than the cost to the mailer.
19 MR. MITCHELL: The decrease in postage,
20 which is four cents, is less than -- I agree. It
21 should say "more than the cost to the mailer."
22 MR. STRAUS: I'm not going anywhere with it.
23 I'm not trying to trap you into changing. I just
24 thought that that's what you meant.
25 MR. MITCHELL: I think you're right.

1 MR. STRAUS: Now, you say that whatever this
2 phenomenon, that a practice is economical if the
3 decrease in postage under cost-based rates acts in
4 this way. It would also be economical if a decrease
5 in postage under noncost-based rates were to act in
6 this way, wouldn't it?
7 MR. MITCHELL: Well, in that case, I don't
8 know what happened to the Postal Service's costs. I
9 lose that reference point.
10 MR. STRAUS: It would be economical to the
11 mailer.
12 MR. MITCHELL: Oh, yes.
13 MR. STRAUS: In response to Question 25, you
14 decline to use the word "penalty," which we put in the
15 question, because your proposition, you say, is that a
16 rate ought to recognize the costs of the mail
17 involved. You don't mean to say, do you, that the
18 rate for every single piece of mail must recognize the
19 cost for that single piece of mail?
20 MR. MITCHELL: Well, excluding all of the
21 questions that you have raised about ECSI value, not
22 every piece, no. You know, we have some averaging
23 certainly left in the rates that we have proposed in
24 the complaint.
25 MR. STRAUS: A hand-addressed, first-class

1 letter dropped in a collection box where the writing
2 might be a little messy; the Postal Service doesn't
3 try to capture the cost of that mail, does it?
4 MR. MITCHELL: I don't have any difficulty
5 with the way first class is handled in that respect.
6 I don't mean it shouldn't be thought about, and you
7 might even want to ask whether or not there would be a
8 response to a rate structure like that, but I'm not
9 suggesting that that's really what we want right now.
10 MR. STRAUS: In the next paragraph in that
11 response, you say, "It's not irrational to assume that
12 all mailers have made decisions concerning what is
13 best for them under the current rate schedule." Were
14 you in the room when Mr. Schick testified about In
15 Style magazine, a publication of Time Warner?
16 MR. MITCHELL: Yes, I was, but I can't
17 remember the details of that particular query.
18 MR. STRAUS: Do you recall when he was asked
19 why certain changes in the way they prepare the mail
20 weren't made sooner to save money under the present
21 rates?
22 MR. MITCHELL: I don't recall what he said.
23 I think that at some point one has to recognize that
24 there is a long-term, evolutionary process occurring
25 on a number of these fronts. There are things going

1 on all the time, improvements being made all the time.
2 Whenever you're in a process like that, there is
3 always some situation that hasn't quite caught up.
4 MR. STRAUS: And this concept of making
5 changes over time is addressed in your third paragraph
6 where you say, "Even if changes --" I guess you mean
7 changes in the way mailers prepare their mail "-- are
8 not made immediately, the new rate structure will
9 inform future decisions." What happens in the
10 meantime to people who have a 50 or 70 or 80 percent
11 rate increase staring them in the face if the changes
12 aren't made immediately?
13 MR. MITCHELL: The playing that I have done
14 that yielded rate increases of that magnitude in
15 general involved a very, very small number of pieces
16 per bundle and a very small number of pieces per sack,
17 which means that those publications are being very
18 heavily subsidized. Now, when you have an incredibly
19 small number of pieces per sack and pieces per bundle,
20 personally I think you're in a position to make some
21 changes immediately. So I think some of the highest
22 rate increases may be some of the people who are in a
23 position to make some changes immediately as well as
24 plan for the future. So I meant for the planning for
25 the future to be an added dimension to the situation,

1 not necessarily the primary dimension.

2 MR. STRAUS: Let's discuss those kinds of

3 analyses you made. You say, in response to number 26,

4 that you considered the effects of the proposed rates

5 on mailers. Actually, you say that in your testimony,

6 and we asked you some questions about that

7 consideration. You said that Witness Stralberg

8 considered them. Are you suggesting that Witness

9 Stralberg's testimony deals with impact on mailers,

10 are you just saying that he considered them as part of

11 the overall strategy of the case?

12 MR. MITCHELL: I did not mean to suggest

13 that his testimony discussed that consideration.

14 MR. STRAUS: Did he have input into the rate

15 proposals or just into the development of the costs?

16 MR. MITCHELL: I discussed rate issues with

17 him regularly and how the costs were going to be

18 recognized and what the effects were going to look

19 like and asking questions on why those effects

20 existed. I think there were probably literally

21 hundreds of discussions of that type.

22 MR. STRAUS: When you say there that you

23 considered and refined the proportion of revenue to

24 get from the piece rates, was that one of the places

25 you considered impact in determining how much money

1 comes from the piece rates?

2 MR. MITCHELL: Yes, I think it was. His

3 initial work back in nine months ago in the early part

4 did not pull a number of pound-related costs out of

5 the bundle costs, and at the time that we began

6 discussing the level of the bundle charges, he began

7 to look more strongly at whether or not there were

8 pound-related costs in there that could be taken out.

9 So that was a refinement in his work that did not

10 exist early on.

11 MR. STRAUS: You also say that you

12 calculated -- you, plural -- you say, "We calculated

13 rate increases for mailings with various

14 characteristics." Did you make any changes to your

15 rate proposal to reflect the work you did in

16 calculating rate increases for mailings with various

17 characteristics? Is the question unclear, or are you

18 just thinking?

19 MR. MITCHELL: No, but I'm not sure it

20 occurred entirely in that specific way. In other

21 words, I looked at things like piece rates. I

22 compared them to piece rates for in county. I

23 compared them to current piece rates. I compared them

24 to his costs. I asked questions about it. We changed

25 the percentage of revenue from the piece rates, and

1 different piece rates came out. I don't recall
2 saying, you know, a publication with these 14
3 characteristics get this kind of increase; let's lower
4 the piece rate.
5 MR. STRAUS: So your impact analysis didn't
6 lead you to make any significant changes in your rate
7 design. You didn't say, Woa, I'm about to propose
8 these rates, but if I do, then this group of
9 periodicals with this kind of characteristic will
10 either have too big an increase or too big a decrease,
11 and so we'd better propose something a little bit
12 different in order to minimize or ameliorate that
13 impact.
14 MR. MITCHELL: I think we can say that there
15 is no ad hoc adjustments to the recognition of these
16 costs because of some particular rate level outcome.
17 MR. STRAUS: There was a related question,
18 which is ABM Question 93, to which I would like to
19 direct your attention now.
20 MR. MITCHELL: Okay.
21 MR. STRAUS: Part A of that question, which
22 is based in part on your testimony, says: "Please
23 describe in detail and provide the results of any
24 analysis you have made to examine the impact of your
25 proposed rates on individual publications." You

1 didn't do that in the response. You gave an example
2 of a hypothetical periodical in that response.
3 Did you, in fact, examine the impact of the
4 proposed rates on individual publications before you
5 finalized your proposal?
6 MR. MITCHELL: We didn't have sufficient
7 billing determinants to evaluate the impact on
8 specific publications. It was rather late in the
9 process after we had a pretty final set of rates. It
10 was late in the process when we began to use the
11 mail.dot.dat files for Times publications to see what
12 its particular rate increases were? Prior to that, it
13 was exploration on my part. In other words, I had
14 stacks of backs of envelopes -- when I said, Let's
15 assume we've got this many pieces per bundle and this
16 many pieces per sack, and this is where it's entered,
17 or this is how much the pallet weighs, let's see what
18 the percentage increase for the publication would be.
19 MR. STRAUS: So you didn't even have time to
20 run the numbers for the Time Warner publications or
21 the other publications of the Complainants.
22 MR. MITCHELL: I don't know that it was a
23 matter of not having time. I mean, does that mean if
24 we had had a bigger staff, we could have gotten the
25 work done sooner? Maybe. We knew those were

1 interesting questions, but we weren't aiming at
2 particular publications; we were attempting to develop
3 a set of appropriate costs and to develop a rate
4 structure and begin to put it together and see what it
5 looked like. Then the task of trying to decide what
6 effect these rates were going to have came about. So
7 it's not a matter of not having time, but it's a
8 matter of where it occurred in a process.
9 MR. STRAUS: In the middle of that response
10 you state what the effect would be on that
11 hypothetical publication of changing the pieces per
12 bundle from seven to 12. When you calculated the rate
13 increase under that alternative, did you assume the
14 same presort level for the bundle?
15 MR. MITCHELL: I can't tell you for sure
16 right now. My guess is that I did.
17 MR. STRAUS: Why would a publisher put seven
18 pieces in a bundle, say, the three digits or five
19 digits, if they had 12 pieces to that same three
20 digits or five digits?
21 MR. MITCHELL: I think the question is that
22 if you're going to compare three-digit sacks, you
23 could have a small sack of five-digit bundles or a
24 large sack of three-digit pieces. You're getting into
25 details of mail preparation here which I often discuss

1 with others. But it's not always the case that you
2 need to change the presort level in order to make
3 general changes in the way they are prepared and
4 packaged.
5 MR. STRAUS: If you take someone, though,
6 and say, We want you to go from seven pieces per
7 bundle to 12, isn't it likely that they are going to
8 lose presort level by doing that? In other words,
9 instead of having five-digit bundles with seven
10 pieces, they might wind up with three-digit bundles
11 with 12 pieces?
12 MR. MITCHELL: I can't give you a thorough
13 answer at this point.
14 MR. STRAUS: Mr. Chairman, I'm through with
15 this particular subject. If you wanted to break now,
16 this would be a good time.
17 CHAIRMAN OMAS: Thank you, Mr. Straus. I
18 appreciate that. I was just about ready to ask you
19 when would be a good point --
20 MR. STRAUS: This would.
21 CHAIRMAN OMAS: -- in your cross-examining.
22 I think what we'll do is we'll take a lunch break and
23 come back at approximately -- why don't we go for an
24 hour? -- until 2 o'clock, and we'll see you then.
25 //

1 (Whereupon, at 1:00 p.m., a luncheon recess
2 was taken.)
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1 A F T E R N O O N S E S S I O N

2 (2:01 p.m.)

3 CHAIRMAN OMAS: Mr. Straus, would you like

4 to continue your cross-examination?

5 MR. STRAUS: Certainly.

6 CROSS-EXAMINATION (Resumed)

7 BY MR. STRAUS:

8 Q Mr. Mitchell, please look at your response

9 to number 28.

10 A Yes.

11 Q What do you mean in that response on the

12 next-to-the-last-line when you say "well-prepared

13 pieces"? What does "well-prepared" mean?

14 A Well, I said that because I believe that

15 Publishers Express probably would have accepted only

16 pieces that didn't cause severe disruption to an

17 efficient processing system. In other words, if

18 pieces required unusual quantities of annual labor, or

19 they were unusually large and couldn't fit into any

20 kind of package or any kind of system that they had,

21 that they might not agree to deliver those.

22 Q Your forecasts state that but for the

23 mailbox rule that competitors would be delivering a

24 lot of periodicals. Would that be at rates lower than

25 the Postal Service periodical rates today?

1 A I believe they would.
2 Q In Question No. 30, we asked you to explain
3 how your proposed rates moved "at a measured pace."
4 The first paragraph of your answer doesn't seem to me
5 to be responsive. Could you maybe rephrase what's in
6 that paragraph to say how the proposed rates move at
7 measured pace?
8 A The Postal Service also asked an
9 interrogatory on this, to which I responded.
10 Q It seems to me that your first paragraph is
11 explaining why they should not move at a measured
12 pace.
13 A Well, when you start moving to a new
14 position, it's always difficult to know how fast to
15 move. If you move too slowly, you don't provide the
16 information, you don't allow people to plan, and you
17 don't get the desired effect. It becomes very
18 difficult to design a new position that does not
19 reduce some of the signals that are already in effect.
20 In other words, we already have presort discounts. We
21 already have some drop-ship discounts. We already
22 have some pallet discounts. And you have a constraint
23 which says, you know, let's not reduce any of the
24 incentives that people are already depending on, but
25 let's move toward this new position, and it becomes a

1 little bit difficult.

2 So you could argue that we have gone there

3 in one step and that there is the possibility of doing

4 some phasing, but the phasing is not real easy to

5 arrange. You know, one of the things that's clear,

6 Witness Stralberg was a little conservative in a few

7 places where he said, at least for now, I want to take

8 a conservative, defensible first step in order to get

9 there. So, in some sense, I think we've been

10 conservative, but if you want to argue that we've

11 taken a big step, you're right.

12 Q What I want to do is find out what you meant

13 at page 6 when you said that the rates you're

14 proposing do, in fact, move at a measured pace. I

15 don't want to argue whether they should, at least not

16 here.

17 A Well, in addition to the USPS interrogatory,

18 I discuss that on page 9 of my testimony.

19 Q I think it's line 9, page --

20 A Part of the measured pace was that we built

21 in some characteristics relating machinability and to

22 mixed ADC and ADC entry, which, I think, will help

23 some of the small people, and some of the ones that it

24 does not help are pieces that have unusually high

25 costs, and we're proposing that they be recognized.

1 Q Let's look at page 54. I think you misspoke
2 when you said you discussed it at page 9. Your answer
3 says line 9.
4 A Oh, line 9, page 54. I'm sorry.
5 Q One of your statements there is that there
6 is no markup proposed on these charges, --
7 A Yes.
8 Q -- meaning the bundle, sack, and pallet
9 charges. Had you not been measured, and had you
10 proposed a markup on those charges, what would that
11 markup be?
12 A Well, I think it would be pretty small right
13 now. There wouldn't be any justification for going
14 over the markup on a subclass, which is not a
15 permanent fixture. It's under the discretion of the
16 Commission. I'm just pointing out that we did not put
17 a markup on it, and that makes it favorable.
18 Now, if you want to say, gee, a markup at
19 this point wouldn't have had a big effect, you're
20 right, but it's still a favorable way to be treated.
21 Q But it's de minimis, isn't it?
22 A I agree that at this point the effect would
23 not be large.
24 Q Would you agree that it's de minimis?
25 A Well, in a mathematical sense, it's not

1 negligible. It is certainly finite. It's on the
2 order of a cent or so instead of four or five cents.
3 I get told to be careful with the word "de minimis."
4 Q Especially on the spelling. Right?
5 A It isn't in my dictionary, and when I
6 finally found a dictionary that had "de minimis" in
7 it, I was told that I had to underline it and that it
8 was used more by lawyers than by lay people, and I'm
9 always careful about things that are used more by
10 lawyers.
11 Q I guess we've just proven that. But I mean,
12 we're talking about a markup of what, one percent?
13 A Of 1.3, I think presently.
14 Q So if there were a 20 cent charge proposed
15 for something here, had you put the markup on, that
16 charge would have been 20.2 cents.
17 A That's right.
18 Q So when in response to Question No. 31, you
19 say that you left the markups where they are now, thus
20 minimizing the effects of the change, we're talking
21 about that 1.3 percent. Is that right?
22 A Yes. I think one could argue that if you
23 have certain rate cells that have zero markup, and the
24 average is 1.3, that maybe some of the other cells
25 must have 2.6 or something. So, in fact, some of the

1 traditional cells probably have a markup above the
2 1.3.
3 Q But the avoided markup is the 1.3.
4 A Yeah.
5 Q Now, I would like to ask you about your
6 response to number 32. You defend there your
7 statement that recognition of machinability will help,
8 or at least you state that it will help many small
9 mailers that have machinable pieces. Do you have any
10 idea of what percentage of the total periodical pieces
11 today are machinable?
12 A No, I don't.
13 Q If that percentage is very small, then the
14 recognition would have a very small impact on those
15 that are machinable, wouldn't it? If the
16 nonmachinable portion were small, then the impact of
17 making a distinction would be small when it came to
18 the machinable pieces --
19 A It would be small on the machinable pieces,
20 but it would not be small on the nonmachinable pieces.
21 Q Right. Okay. I don't understand the last
22 sentence of that answer, which reads: "Pieces saying
23 an increase due to this recognition are those that are
24 now being provided below-cost rates corrected for ECSI
25 value." What do you mean "corrected"?

1 A In effect, I mean to take -- let's consider
2 pieces with an average proportion of editorial so that
3 we're not down at 80 percent coverage, we're not up at
4 129 or whatever it is; we are, in effect, at 103. So
5 we'll take pieces with an average degree, and for
6 those pieces, the ones that see an increase are now
7 being carried below cost.
8 Q I understand that part of the sentence.
9 What I don't understand is the phrase, "corrected for
10 ECSI value." What's being corrected, and how is it
11 being corrected?
12 A I mean, in effect, that the comparison I
13 wished to make is for pieces with an average
14 proportion of editorial content. I know that 100-
15 percent editorial pieces are being carried below cost,
16 so I don't need to tell you that, and I know that all
17 advertising pieces have a coverage, in effect, that
18 starts at 126, so they might not be below cost, but, I
19 mean, let's just talk about an average piece here.
20 Q Please explain, again, another phrase, if I
21 could explain, your response to number 33 and the
22 penultimate sentence where you say, "when sacks are
23 used effectively." What's an effective use of sacks?
24 A The last sentence?
25 Q The next-to-last sentence.

1 A Well, when a sack is the best way to mail,
2 given appropriate signals concerning the Postal
3 Service's costs, when a mailer decides that that's the
4 best way to mail, then there is nothing wrong with
5 that. It's a perfectly legitimate way to mail as long
6 as the costs of it are recognized.
7 Q But you say when sacks are used effectively,
8 not when they are priced appropriately. I would like
9 you to focus on the use of sacks, not the way they are
10 priced, and how a sack can be used effectively versus
11 ineffectively.
12 A Well, I think I explained basically what I
13 meant. If you want to get into a discussion about
14 whether "effective" is quite the right word, maybe
15 "efficiently" would be just as good.
16 Q Okay. In Question 36, it was a two-part
17 question, even though it didn't have two little
18 letters in it. The first part was whether it's still
19 important that periodicals rates be attractive, and if
20 so, why, and you answer is that "Congress thinks it's
21 important, and so do I," and I don't believe that the
22 rest of the answer ever answers the question why you
23 believe that it's important that periodicals rates be
24 attractive. Could you do that?
25 A There is a slight definitional problem in

1 deciding what it means for rates to be attractive, and
2 I think the position that I've taken, for the most
3 part, is that they ought to be lower than the
4 alternative, and if there is a mail category that
5 would fit for a periodical, and it has a rate, and you
6 give it a special subclass, and the rate comes out a
7 good bit lower, then I view it as an attractive rate.
8 So all I'm saying is that it's not clear to
9 me how this provision that Congress has made would be
10 honored if periodicals rates were to come out higher
11 than others.
12 Q So are you saying that periodicals rates
13 should be attractive because Congress said so? Is
14 that the answer to the "why" part of this question?
15 A I think that's a good enough reason. But
16 I'm also saying, in a very general sort of way, that
17 if you make a special provision for someone, and it
18 makes them worse off, then I don't think that you've
19 done much for them.
20 Q In the analysis that you did that we
21 discussed this morning, the rate comparabilities, the
22 impact estimates you and Mr. Stralberg made, did you
23 see whether the rates you proposed would push the
24 rates for some periodicals higher than the standard
25 rates?

1 A You know, the answer is that I tried on a
2 few occasions, and I didn't get as far with it as I
3 wanted to. The comparisons there become very complex.
4 I've done them over the years for the rates that exist
5 as well as for these, and I didn't succeed in getting
6 a good final answer on that. There are some standard
7 rates right now that are below periodicals rates,
8 depending on the particular pieces involved, and I've
9 been concerned over the years that maybe that
10 shouldn't happen.
11 Q Would you be concerned if a rate proposal
12 expanded that phenomenon so that even more periodicals
13 pieces would be cheaper at standard rates than at
14 periodicals rates?
15 A I would be interested. I don't know that
16 it's quite fair to say that I would be concerned.
17 Part of the problem is that it's not only the
18 periodicals rates that are involved. It's also the
19 standard rates that are involved, and if you have some
20 very unusual standard rates relative to their costs,
21 and you're comparing the periodicals rate with an
22 unusual standard rate, it might be the fault of the
23 standard rate instead of the periodicals rate. So it
24 becomes a question that deserves a little exploration,
25 but it's not clear where it would come out.

1 Q I would like to direct your attention now to
2 Question and Answer No. 40. The question was whether
3 if your proposed rates increase rates for most
4 periodicals, that would make periodicals rates less
5 attractive, and you answer no, a surprising answer.
6 And then you say that the level of attractiveness is a
7 summation over volume of the difference between an
8 applicable alternative rate and the periodicals rate.
9 Is the attractiveness of a rate simply a matter of
10 comparability without regard to the absolute level of
11 the rate?
12 A Absolute levels are terribly difficult to
13 evaluate in isolation. I would like to be able to
14 say, "Gee, you know, it seems like 10 cents would be a
15 really good rate for these things to have," but I have
16 to have a reference point, and one of my reference
17 points is the costs, and one of the reference points
18 is other alternative rates, and then you can look at
19 trends over time and prices and things. So in my
20 responses to you, vis-a-vis the word "attractive,"
21 I've tried to be just a little bit qualified in how
22 I've said it.
23 Q I understand that, but can't we agree that
24 if somebody raises the rate for an activity that
25 you're engaged in, that rate is less attractive than

1 it used to be?

2 A Yeah. I think that's clear.

3 Q You don't need to know what other rates --

4 if the rate for taking the subway to work goes from

5 $1.15 to $2.15, that's a less attractive rate whether

6 it costs you $10 to drive, $2 to drive, or you can

7 drive for free. Isn't that right?

8 A I don't disagree with that at all, but I

9 would add one further thing, and that is that you need

10 to be very careful that you don't imbue the current

11 rate as being somehow meritorious and saying that

12 anything that increases that is bad. It may very well

13 be that the current rate is defective, and if you take

14 a position that anything that changes the current rate

15 or makes it go up is bad, then you maintain the status

16 quo forever, and you never make improvements, so I

17 think you need to be careful with that.

18 Q You've already testified many times, and I'm

19 sure I won't get any disagreement with you, that the

20 periodicals rates today are not cost based. Is that

21 fair?

22 A Basically, it's fair, but I think you can

23 certainly point to elements of periodicals rates.

24 We've paid a lot of attention to costs and periodicals

25 rates over a period of a long time. Starting in 1971

1 when we introduced piece rates, and all we had was
2 pound rates, when we put in the presort discounts,
3 when we built the zones, we've paid an awful lot of
4 attention to rates in an awful lot of places, but I'm
5 just saying we can do an awful lot better.
6 Q In response to Question 41, you say that as
7 you define the term, periodicals rates are not market
8 based. Is there anything that you can say they are
9 based on? Are they simply arbitrary if they are not
10 cost based or market based?
11 A Well, I've certainly not said that they are
12 arbitrary, and I think I just explained. I explained
13 what I meant by market based, I explained what I meant
14 by cost based, and I just got through explaining that
15 over a period of 33 years we have made extensive
16 adjustments to periodicals, and I think all of them
17 have been based on costs. Now, that doesn't mean that
18 the current situation is extremely good, but it
19 certainly means that we worked hard. You know, we've
20 introduced four presort levels. We've shifted the
21 balance between pieces and pounds. We've put in a
22 destination SCF rate. We've put in a DDU rate. We've
23 put in a saturation rate. We've put in bar code
24 discounts. We've put in bar code discounts different
25 for letters than we have for flats.

1 It's certainly true that we have done a lot
2 of things in periodicals, and we've done cost work to
3 support every single one of them.
4 Q So is it accurate to describe your position
5 as that periodicals rates are cost based but not
6 sufficiently cost based?
7 A Yes.
8 Q Is the five-digit presort rate cost based?
9 A If you're talking about difference between
10 the three-digit and the five-digit rate, the way I
11 think of the five-digit discount is that I look at the
12 three-digit rate as a reference, and I find the cost
13 difference between three digit and five digit, and I
14 recognize that cost difference in the rate. And I
15 think the answer, if you look at it in that way, is
16 yes.
17 Q Is the rate difference between three digit
18 and five digit less than or greater than the cost
19 difference?
20 A We could look up the details of the current
21 rates. I would point out that they do present
22 difficulties because they came in as a settlement and,
23 therefore, that they don't necessarily reflect
24 Commission costing decisions. But my recollection is
25 that on a three digit versus five digit that the

1 Postal Service passed through 100 percent of its cost
2 estimate in the case. I could be wrong, but I think
3 that on the basic presort levels, that they were
4 sitting right at 100 percent.
5 Q If it were significantly higher than 100
6 percent, would that be problematic?
7 A We could go through and discuss -- the
8 three-digit presort rate was a new creation just a
9 couple of rate cases ago, and whether or not we have
10 fully adjusted to the new level, I'm really not sure.
11 In other words, we de-averaged the basic rate and the
12 five-digit rate and created the three-digit rate. So
13 there is a possibility that we still have some
14 movement to make to get toward 100 percent, and one
15 would have to be clear about whether we should use
16 Commission costs or Postal Service costs, but I think
17 we have tried, "we" being some kind of a corporate
18 "we," we have tried very hard to honor the costs on
19 those presort differences.
20 Q Mr. Mitchell, I'm going to hand you a copy
21 of the present periodicals rate schedule, which I'll
22 tell you I got from the Domestic Mail Manual on the
23 Internet. It's printed out with a July 6, 2004, date.
24 A Okay.
25 Q Could you look at the piece charges on there

1 --

2 A Okay.

3 Q -- and then look at your answer to American

4 Business Media Interrogatory 54?

5 A Which number?

6 Q 54.

7 A Yes.

8 Q On the rate schedule, do you see different

9 piece rates for flats versus letters?

10 A I see a bar code discount for letters. I

11 don't see a separate piece rate.

12 Q I gave away all of my copies.

13 A There is an automation category which has a

14 separate rate for letters and flats, and that's a bar

15 code discount which comes off of the presort level.

16 The presort level itself has no rates for letters and

17 flats.

18 Q Maybe we're just talking semantics here, but

19 doesn't this say, under Section 1.2, per addressed

20 piece, basic, and then under automation it says letter

21 size, 28.1; flat size, 32.5 cents. Isn't that a

22 letter-size, basic-piece rate for automation and a

23 flat-size, basic-piece rate for automation?

24 A No. That's the result of a bar code

25 discount from the basic rate of 37.3, and the letter

1 bar code discount is a little larger than the flat bar
2 code discount, and those are based, at least for the
3 flat, it's based on bar code savings. On the letter,
4 it's based on something that goes a little bit beyond
5 bar code savings but not fully on the basis of it
6 being a letter instead of a flat.
7 Q What I'm looking at says "per addressed
8 piece," and under automation it says "$0.281." That
9 is not a piece rate?
10 A It's, in effect, a bar code discount from
11 the .373.
12 Q Well, 28.1 cents isn't a discount; 28 cents
13 is a piece rate, isn't it?
14 A That's right.
15 Q And 32.5 cents is a piece rate. It's
16 arrived by applying a discount to something else, but
17 it's a piece rate.
18 A But if you look under nonautomation, which
19 is the reference rate in the rate design, there is no
20 difference between letters and flats.
21 Q So there is a piece rate difference under
22 automation, and there is no piece rate difference
23 under nonautomation.
24 A That's right, and the automation difference
25 is a bar code discount which comes off of the basic

1 rate.

2 Q Every piece rate is a discounted rate from

3 the basic rate. The three-digit rate is a discounted

4 rate, too, isn't it? And the five-digit rate is a

5 discounted rate, and the carrier-route rate is a

6 discounted rate off of a basic rate.

7 Let's look at your answer to number 54. The

8 question was, "Is the periodical-letter-flat

9 differential cost based?" Your answer: "The

10 periodicals rate structure does not have a letter-flat

11 differential." Isn't this a letter-flat differential?

12 A No.

13 Q It's not?

14 A It's a bar code discount. It's a different

15 bar code discount for letters than for flats.

16 Q That doesn't create a differential?

17 A Not a letter-flat differential. It's a

18 differential due to the recognition of bar codes.

19 It's not due to it being a letter instead of a flat;

20 it's due to it having a bar code instead of not having

21 a bar code.

22 Q The difference between 28.1 cents under

23 letter size automation and 32.5 cents under flat size

24 automation; that's the difference between having a bar

25 code and not having a bar code?

1 A Yes. The difference between the .373 and
2 the .281 is a bar code discount. The difference
3 between the .373 and the .325 is a bar code discount.
4 Those bar code discounts are different for letters and
5 flats.
6 Q And do those different discounts create
7 differentials in the postage charges that are applied?
8 A Sure.
9 Q So there are postage differentials based on
10 whether it's a letter or a flat.
11 A It's not based on whether it's a letter or a
12 flat; it's based on whether it has a bar code, and the
13 bar code is different for a letter from what it is for
14 a flat.
15 Q I'm going to try this one more time. The
16 28.1 cents and the 32.5 cents; they both have bar
17 codes. Right?
18 A Yes.
19 Q So we have a 28.1 cent rate for a letter
20 size with bar code, we have 32.5 cents for a flat size
21 with bar code, but you're telling me that difference
22 is based on whether or not they have a bar code.
23 A Yes. It turns out, of course, that --
24 Q Even though they both have bar codes, the
25 difference is based on whether or not they have one.

1 A A letter piece goes through one set of
2 automation. A flat piece goes through another set of
3 automation. The savings for having a bar code on the
4 two is different.
5 Q Maybe it is a semantic difference. I guess
6 we'll have to talk semantics a bit more. Please look
7 at your response to number 56.
8 A Okay.
9 Q There, we asked you whether in your proposal
10 the differential between the editorial pound rate and
11 the advertising pound rate is cost based, and your
12 response is there is no difference between the
13 editorial pound rate and the advertising pound rate.
14 And, therefore, you say, since there is no difference
15 in the cost of handling and advertising, the answer is
16 yes. I don't know why you're answering yes if there
17 is no differential.
18 Is your answer here based upon the fact that
19 you apply a discount to all editorial pounds; and,
20 therefore, you have an editorial pound rate that is
21 discounted to a different rate, and that's why you're
22 saying the rates are the same?
23 A I think if you had referred to a net
24 editorial pound rate, I would have had to agree, but,
25 in effect, then you're talking about the discount for

1 being editorial, and, of course, that's not cost
2 based.
3 Q Do any editorial pounds pay the same charge
4 as advertising pounds?
5 A In the basic rate structure in our proposal,
6 they pay the same, and then the editorial gets a
7 discount in recognition of ECSI value. The discount
8 is not cost based.
9 Q I said "charge," not "rate." All editorial
10 pays a charge that's lower than all advertising.
11 Right?
12 A I hope I'm not lost. If you look at our
13 rate schedule, it has a pound charge which applies to
14 both advertising and to editorial, and then as an
15 adjustment, you take a 10.1 cent-per-pound discount
16 for the editorial pounds.
17 Q Couldn't you just as easily have called the
18 editorial pound rate a rate that's 10.1 cents lower?
19 A Yes, and if you did, it would not be cost
20 based. I think we understand clearly that the benefit
21 given to editorial content is not based on any cost
22 difference.
23 Q Directing your attention to Question and
24 Answer 57, you found yourself unable or unwilling to
25 confirm that the contribution to inefficiency of a

1 flat editorial rate has declined as the percentage of
2 revenues received from the pound rate decline. Does
3 the flat editorial pound rate contribute to the
4 inefficiency of periodicals rates?
5 A I think it does, yes.
6 Q And what percentage of the revenues -- let
7 me rephrase that. Is the percentage of revenues
8 received from the editorial pound rate now lower than
9 it was prior to 1970?
10 A I'm not sure.
11 Q Let me ask a hypothetical question, then.
12 If the periodicals rates had evolved to the point
13 where 95 percent of their revenues were based on the
14 piece rate and 5 percent on the pound rate, would you
15 agree that the contribution to inefficiency of the
16 structure of the pound rate was lower than it had
17 been?
18 A You know, in a general sort of sense, yes,
19 but if we pursued the question very far, I think the
20 efficiency question has a lot to do with whether or
21 not mailers would respond to it because efficiency
22 improvements occur when there is a response. I know
23 the response -- for mailers is a lot higher now than
24 it was then, and I think we would have to look at
25 absolute differences between the zones as well as a

1 portion of total revenue that is received from the
2 piece and pound rate. You know, in some sense, I'm
3 agreeing, but I think you have to be very careful with
4 this.
5 Q Let's look at Question and Answer 60.
6 There, we asked you about your statement that there
7 was an "enormous waste of resources" resulting from
8 the fact that 14.6 percent of standard mail was drop
9 shipped before 1990, but 73.3 percent is now. Then
10 there were a series of questions labeled A, B, C, D,
11 and E. Your answer doesn't provide A, B, C, D, and E
12 answers, and I had trouble finding the answers to
13 those questions in this narrative response, so maybe
14 we could go through them one at a time.
15 The first question is, "What resources were
16 wasted?" What's the answer to that part of the
17 question?
18 A Well, I think in every case where a mailer
19 could do the work for less than the Postal Service,
20 that the extra resources that the Postal Service used
21 were wasted.
22 Q "Extra resources" being what?
23 A Beyond what the mailer would use to do the
24 work.
25 Q So if the Postal Service spent $100, whereas

1 the mailer would have spent $90, then $10 was wasted.
2 A I think so.
3 Q Is it your testimony that Postal Service
4 transportation is inherently less efficient than
5 private transportation? That was Part C.
6 A No. It's not my testimony that their
7 transportation is inherently less efficient. We're
8 talking here about giving mailers control of a
9 situation, and when mailers get control of a
10 situation, they do different things. They alter their
11 operations in order to get full trucks. They control
12 their trucking operations in a different sort of way.
13 They combine mailings in order to get filled trucks.
14 They schedule their production in a way in order to
15 use trucking effectively when it's the right thing to
16 do. They don't do any of these things when the Postal
17 Service has to transport it.
18 So what has happened is that the Postal
19 Service's cost savings were the basis for the
20 discounts that were provided, and mailers made a
21 decision on what to do, and these must have been
22 efficiency improvements. I don't think it points a
23 finger at the Postal Service and says that you're
24 necessarily inefficient. Given the job that they have
25 to do, they may be the most efficient operation in the

1 world or the most efficient operation possible.
2 Q Please look at your answer to Question 64.
3 Let me read it to you. "Do you believe that
4 periodicals rates were established without regard to
5 their ECSI value, and if, as a result, the markup over
6 attributable costs were to increase to the average
7 system markup, there would be any effect on the flow
8 or availability of information in the United States?"
9 And you give a full-page answer there, but I can't
10 tell whether your answer is yes with this explanation,
11 no with this explanation, or maybe with this
12 explanation. Could you tell me what your answer is
13 that goes along with this explanation?
14 A Well, let's assume that we're not talking
15 about the fact that there might be decreases in some
16 other subclasses' rates in order to have the Postal
17 Service break even when you make this change, and
18 let's recognize that we're talking about the overall
19 subclass here and not about any segments of the
20 subclass. I specifically said that the best estimate
21 we have is Tolley's elasticities, which has an
22 elasticity of -0.17. So if we put a 10 percent
23 covering on it, 10 percent markup, then presumably the
24 buying of periodicals would go down 1.7 percent,
25 ceteris paribus. So I think, yes, as far as

1 periodicals go, if that elasticity is right, there
2 would be a lower quantity of information sent.
3 Q That elasticity doesn't tell you, does it,
4 whether there would be 100 percent of one periodical
5 gone and no percent of other periodicals; just an
6 average would be 1.7 percent.
7 A That's right. It's a market elasticity. It
8 means that some people might mail more or less, or it
9 means that different people might mail. You can't
10 always tell what's going to happen; it's just a
11 result.
12 Q Please look at Question and Answer 66.
13 A Okay.
14 Q You disapprove of my attempt to summarize
15 your testimony by use of the word "adverse
16 consequences," and you say that's not what you said.
17 What you said is that it's hard to see how even if
18 zoning the editorial rate caused some areas to be
19 disfavored, that would have any effect on the unity or
20 cohesion of the nation, a significant effect. Is that
21 another way of saying that there might be adverse
22 consequences, but you didn't want to agree with that
23 statement?
24 A Well, that was an "if" statement.
25 Q Yes.

1 A My appendix clearly shows that I don't
2 believe that anyone will disfavor someone in a further
3 zone that wants the magazine, but then I said that if
4 this did occur, and there were some areas that were
5 favored slightly less, that I don't think that the
6 effects on -- what's the word here? -- on the cohesion
7 of the nation would be significant. I think that's
8 what my statement related to. What I immediately
9 think is when I go on a trip to California and buy a
10 Sunday paper, I see the same ads for Wal-Mart and
11 Sears that I do here in Washington. I think we've got
12 a pretty cohesive nation, and I think, you know, if
13 there were a slight effect here, and I'm saying if, if
14 there were a slight effect, I just don't think it
15 would be significant.
16 Q What do you pay for a New York paper on the
17 West Coast, the same as you pay on the East Coast?
18 A I don't know.
19 Q The last word of your answer to Question 66
20 is "subsidized." Could you tell me how you're using
21 that word in that sentence? I know that economists
22 and others sometimes disagree on exactly what the word
23 means.
24 A Well, you have been talking about the
25 possibility that some rate increases could be in the

1 neighborhood of 40, 50 percent or even greater. All
2 of these rates that cause those increases are because
3 we've moved closer to recognizing costs, and within a
4 subclass that has a coverage of 101.3 percent
5 presently, if someone gets a 50 percent rate increase
6 because we moved their rates toward costs, there is an
7 implication there that they have been very heavily
8 subsidized.
9 Q By "subsidized," you mean carried below
10 cost.
11 A Carried substantially below cost, not
12 considering ECSI value, not considering an average
13 proportion of editorial content. So we're not talking
14 about the fact that editorial has a higher or lower
15 markup than advertising. We're talking about an
16 average publication, and I'm saying that they are
17 being held substantially below cost. So by any
18 definition of "cross-subsidy," there is a subsidy
19 there.
20 Q In your answer to Question 67, you said it's
21 not possible to say how is now paying for the
22 institutional costs of the Postal Service that
23 periodicals avoid by virtue of their ECSI recognition.
24 Isn't it likely that those costs are being paid by
25 first- and/or third-class mailers?

1 A Well, maybe you could raise each other
2 subclass by one percentage point to make up for it.
3 If each other subclass went up one percent, then
4 because first class and third class are so big, the
5 bulk of the dollars would be paid by them, but that
6 doesn't mean that there is a tremendous burden on
7 first-class mail anymore than there is a tremendous
8 burden on some mailer of another class when he looks
9 at his rates. I think there is a danger in looking at
10 overall proportions and saying, "Oh, gee, it must be
11 paid by them because they are so big."
12 Q In Question 70, we asked you about a
13 particular periodical that you mention in your
14 testimony at page 23, City Magazine, and we asked
15 where it's printed and whether it's drop shipped.
16 Your answer refuses to provide the information. Is
17 this the only mailing statement that you received?
18 A It is the only mailing statement that I
19 received. It's not the only local and regional
20 publication that's printed close to where it's
21 distributed.
22 Q Did you get this mailing statement from the
23 periodical itself or from a third party?
24 A How did I say it? I got it, I would say,
25 from the periodical itself. I was referred through

1 two different people. I talked to one person who
2 suggested I call somebody else, and when I talked to
3 somebody else, he said, "I'll have someone call you,"
4 and this person, who I didn't know at all, talked to
5 me on the phone for a few minutes, and I asked him a
6 couple of questions, and he said, "Why don't I just
7 fax you a mailing statement?" and I said, "That would
8 be great." So that was the only full mailing
9 statement that I had for such a publication.
10 Q Well, he apparently also told you not to
11 tell anybody who the printer was or --
12 A That was part of our discussion, the two
13 people that I talked to.
14 Q Would giving the location of the printer
15 give away the name of the printer? Is that the
16 problem?
17 A Well, I've found that readers as well as
18 attorneys are very insightful at searching through
19 these things when you start providing information.
20 You never know when to stop when somebody starts
21 asking things, so I think it's just better not to
22 start identifying.
23 Q When an interrogatory asked you to identify
24 somebody you didn't choose to identify yourself,
25 that's one thing, but here you affirmatively chose to

1 use this particular periodical in your testimony. We
2 asked you whether it was drop shipped. You would say
3 it's entered at a point not substantially distant from
4 where it is printed. Is that a yes or a no to "Is it
5 drop shipped?"
6 A If drop shipping means that it's carried
7 some distance over the highway before it's entered,
8 the answer is, no, it was not drop shipped.
9 Q Is it entered at an origin facility?
10 A It was entered at origin?
11 Q Yes.
12 A Whose origin?
13 Q The printer's origin.
14 A I think, yes.
15 Q Please look at your answer to Question 71.
16 The third sentence says: "Within the framework of a
17 fixed cost coverage and fixed billing determinants,
18 the costs are covered by other periodicals' mailers,"
19 and that would be the costs not incurred by the mailer
20 that causes them. By "within the framework of a fixed
21 cost coverage," do you mean that if you assume that
22 the cost coverage is fixed before the rates are
23 designed, that would be the effect?
24 A I think, yes, it means that you select a
25 cost coverage, you set some rates, and then the mailer

1 ships. And then the next time you set rates,
2 everybody's rates are going to have to go up because
3 of it if you keep the same cost coverage and other
4 factors and everything.
5 Q If the rates are established, and then a
6 cost coverage is derived from those rates, or if it's
7 an iterative process, and it's sort of hard to tell
8 which comes first, then it wouldn't be possible, would
9 it, to know which mailers are paying the costs that
10 aren't being covered by the mailers who have below-
11 cost rates?
12 A Well, if you set the rates at 101.3 percent
13 markup, and after you set the rates, some mailer
14 shifted, then your markup would go down.
15 Q The question and answer here don't deal with
16 shifts. The question is, who paid the costs not paid
17 for by those who are getting the free transportation?
18 We're not talking about shifting. Basically, this is
19 about your testimony that basically some people are
20 getting a free ride on the backs of others, and I'm
21 trying to find out who those others are. You say that
22 within the framework of a fixed cost coverage, the
23 costs are covered by other periodicals' mailers. I'm
24 saying, if it weren't for that condition, if the cost
25 coverage were not fixed, but if the rates were set so

1 that the Commission or whoever sets them says, "These
2 look like a fair set of rates to us. Now let's see
3 what the cost coverage is" -- rather than the cost
4 coverage determining the rates, it works in the other
5 direction -- then you wouldn't know, would you, who
6 was paying the costs?
7 A I suppose there wouldn't even be any effects
8 because you've just selected all of the rates
9 arbitrarily and said they are fixed, so how could
10 there be any effects of a change?
11 Q Are you suggesting that when rates are set
12 by this Commission over the years, they always come up
13 with the cost coverage first and then the rates?
14 A Yes. I mean, there's obviously a process.
15 Q So when the Commission decided in the last
16 case 101.3 was the right number, that wasn't, in part,
17 developed from the actual rates as an iterative
18 process?
19 A Well, I think that at some point here we
20 need to read the record and read their opinion and
21 recommended decision on what they did, and I'm not
22 sure that I should be trying to make any personal
23 observations on the process that I saw while I was
24 here, but I can tell you that I worked very hard to
25 help prepare some of these opinions, and I think we

1 did a good job.

2 Q There is clearly an attempt in your

3 proposal, not only the rates but the structure, to

4 impose greater costs on certain periodicals which are

5 now, in your view, not paying costs sufficient to the

6 service they receive, and you're trying to either

7 charge those periodicals more, or if they want to not

8 pay that increase, change the way they mail. But at

9 the present time, it's your view that they are paying

10 too little, and you think they should pay too much if

11 they continue to mail the same way. Isn't it possible

12 that the dollars that they are not paying that you

13 want to shift onto them are now not paid by other

14 periodical mailers at all but are being paid by all

15 other classes of mail?

16 A Well, you're kind of engaging in a little

17 process which finance people often call "sources-and-

18 uses-of-funds controversy." It's like you can take so

19 many dollars here and move them over here and say, "I

20 choose to say that these are paid by somebody else,"

21 or "This is who I choose to say they are paid by."

22 I'm just having a little trouble following what you're

23 constructing. I'm not sure it's a process that we go

24 through in order to set the rates.

25 Q By "we," you mean whom?

1 A The corporate "we." It's the Commission and
2 the Postal Service, mostly the Commission. It's a
3 community. The Commission, of course, sets rates
4 based on a record, so there is an input from a lot of
5 people that's recognized.
6 Q In Question 74, we asked you about the ride-
7 along rate, and you said, one reason you haven't
8 considered proposing a zoning of that is because the
9 revenues are handled as an appendage to the billing
10 determinants. I'm not here proposing that it be
11 zoned, but I would like to know what you mean when you
12 say that because the revenues are handled as an
13 appendage to the billing determinants, you didn't
14 really consider it.
15 A When you asked me that question, it took me
16 slightly by surprise, and I thought, gee, why didn't I
17 think of this? I got to thinking about it, and I
18 thought, you know, if you look at the periodicals
19 billing determinants, we've got an entire page of such
20 small numbers that you can't even read them, and then
21 down in the right-hand corner, you have this little
22 adjustment that says, we're going to add in some
23 revenue from ride along. If you look at the rate-
24 design spreadsheets, you see the same thing. We make
25 a little adjustment for fees and ride along, and then

1 we design all of the rates.

2 So I was so busy looking at all of the rate

3 issues that it never really crossed my mind to

4 consider that we might zone ride along. I think if we

5 did that, I point out in this question that we would

6 have to look and see what data are available. We

7 would also have to look at some costing issues and how

8 it would fit in. I'm not opposed to it being

9 considered.

10 Q In Question 76, we pointed to your statement

11 at page 28 that you're not suggesting that all mailers

12 can make changes and asked you what types of mailers

13 you had in mind, and your answer was that basically

14 you didn't have any particular types of mailers in

15 mind. Let me ask again. You weren't thinking about

16 any type or description of periodical mailers that

17 might not be able to make the kinds of changes you

18 would like to see?

19 A I have two reactions. Number one, I usually

20 attempt to avoid all-inclusive statements, so I don't

21 want to suggest that all mailers, with "all"

22 underlined, I don't want to suggest that all mailers

23 can do this. But basically what I think is that most

24 mailers can make some changes, and I think that it may

25 very well be that some of the smaller mailers are in a

1 position to make more changes than the big ones. It
2 may be that the big ones are maxed out, in some sense,
3 as far as making any changes.
4 Q I'm not asking you about the ones who can;
5 I'm asking about the ones who can't.
6 A You're asking me to categorize them, and you
7 would like for me to say that they fall into a
8 particular, you know, set of cells as far as size or
9 distance or editorial content or zone or being sacked
10 or density or something else, and I'm saying that some
11 of these that are getting large increases may be in a
12 position to respond more than any others. They may be
13 using sacks very inefficiently. They may be preparing
14 bundles very inefficiently. This is not all about
15 pallets.
16 So I'm very reluctant to say, "Gee, my guess
17 is that people who have this characteristic can't
18 change." I don't know how to do it.
19 Q You are willing, like Socrates, to say that
20 all men are mortal, presumably, so there are some
21 absolutes in this world. Your testimony at page 28
22 says that you're not suggesting that all mailers find
23 themselves in situations where changes are feasible or
24 costless. I'm just asking you whether you have any
25 particular kind of mailer in mind when you said "not

1 all mailers."

2 A No. I don't have any one particular in

3 mind.

4 Q In Question 81, we asked you about why DSCF

5 entry pieces would pay not distance-related

6 transportation costs, and your first response is that

7 they pay none now, and you have made no changes in

8 this regard but to follow current practice. There's a

9 lot of current practices you've disturbed in your rate

10 proposal. Why this one did you decide to leave alone?

11 A Well, unless there is something that I don't

12 understand, the costs at issue here are long haul,

13 Segment 14, contract transportation for carrying mail

14 within the confines of a destination SCF. So we could

15 be talking about Gaithersburg, Maryland, here and

16 taking mail to Rockville and Germantown. You know,

17 they are pretty small to begin with because Segment 14

18 transportation isn't used very much for that, and the

19 ones that are, we don't have any information about how

20 far they drive within the DSCF.

21 I don't know whether they drive five miles

22 to Rockville or 15 miles out to Germantown or whether

23 they go out to Frederick, so what I'm saying is that

24 we've just made no attempt to set any rates which

25 recognize how far this stuff travels within an SCF or

1 a destination SCF, and we've continued to do it as we
2 do now by making all mailers pay a little bit of it
3 because all mail destinates [sic] in some kind of an
4 SCF.
5 Q What about DDU-entered mail?
6 A The discount takes that out for them.
7 Q Takes what out?
8 A The nondistance-related transportation cost
9 that's layered in.
10 Q What about the distance-related
11 transportation costs?
12 A Well, it's already out of the DSCF. We just
13 have to take the nondistance out to get the DDU.
14 Q Nobody pays distance-related costs once the
15 mail reaches the destination SCF. Right?
16 A Right. So we have none in it.
17 Q Some mail incurs distance-related costs, the
18 mail that goes from the SCF to the DDU.
19 A No. That incurs some nondistance costs.
20 Q It doesn't incur any distance costs?
21 A No.
22 Q There is no cost to transport the mail from
23 Merrifield to Alexandria?
24 A We don't attempt to identify it over how far
25 the station is from the SCF.

1 Q That's not the same as saying there are no
2 costs. There are distance-related costs, are there
3 not?
4 A And they are put in on a per-pound basis for
5 all mail regardless of distance, so it's a
6 nondistance-related, volume-variable, transportation
7 cost. That's the way nondistance --
8 Q It seems to me it's a distance-related cost
9 that's a nondistance-related charge.
10 A If you look at the development of
11 transportation costs, we have a volume-variable
12 transportation cost for all of periodicals that moves
13 up and down with periodicals volume, and as a part of
14 that volume variable attributable transportation costs
15 for periodicals, we identify a part of it that we view
16 as not distance related, and that not-distance-related
17 portion is overwhelmingly determined by these intra-
18 SCF transportation legs, and we layer those onto all
19 mail on a per-pound basis without differentiating the
20 distance that specific pieces go. Again, it's a
21 corporate "we." For 30 years, I've been accused of
22 using the word "we" without it being clear who "we"
23 is, but that's the way the rates are designed.
24 Q In Question 84, we asked whether all work-
25 share discounts should be equal to avoided costs, and

1 you responded, as you have here this morning, that
2 blanket rules are dangerous, and you prefer not to
3 engage in them. But the question didn't ask you,
4 should all work-share discounts be equal to avoided
5 costs, or should none of them; it was should all of
6 them. Is your answer no, that you're not willing to
7 make that blanket assertion that all should be equal
8 to avoided costs?
9 A No. I'm not willing to make a blanket
10 assertion.
11 Q So the answer to Question A is no.
12 A Okay. It's no.
13 Q Therefore, there may be times when it is
14 appropriate to deviate from avoided costs, may be
15 times.
16 A And I think my answer identifies a range of
17 considerations, many of which could be involved in
18 deviating from avoided costs.
19 Q Please look at Answer No. 86.
20 A Okay.
21 Q Again, I guess I'm having trouble with how
22 you're accounting for a noncost factor such as ECSI
23 value. When you say in the last sentence, "and if
24 account is taken of the benefit given to editorial
25 matter," is that, again, where you're saying let's

1 take the median kind? You're not talking about
2 heavily editorial or heavily advertised but taking out
3 of consideration the fact that there is ECSI value,
4 then there's implicit equal-cost markups.
5 A Yes.
6 Q Question 87 asked you to speculate about
7 what might happen if delivery-point sequencing of
8 flats were to be implemented, and the value of the
9 carrier-route presort were to disappear, and you
10 suggested that the rates for five-digit flats would
11 decline to the point of being lower than the rates for
12 the carrier route. Isn't it more likely that the rate
13 for carrier route would increase to the point where it
14 was greater than the rate for five digit?
15 A I certainly hope not. You say, is it
16 possible?
17 Q Yes.
18 A I mean, we have to depend here, we, the
19 Commission and all of the community, has to depend, to
20 a considerable extent, on some Postal Service costing
21 results in how they present their case. So you can
22 speculate yourself on what's possible, but I think
23 that if there is a return on investment associated
24 with delivery-point sequencing of flats, that that
25 ought to be the lowest-cost way to go, and we ought to

1 have the lowest-cost rate for it. And I certainly
2 hope that we don't have a big, expensive,
3 technological innovation which is designed to produce
4 the lowest-cost-possible mail stream and then, lo and
5 behold, find out that it's a lot more costly than
6 doing it manually.
7 So I understand that this is an issue which
8 is being discussed by the entire postal community here
9 and has been acute for probably a year, but I'm
10 personally optimistic as well as hopeful that it works
11 out in a sensible sort of way.
12 Q In Question 89, we asked you about, again, a
13 hypothetical, that if the Commission should find that
14 publishers of small weekly periodicals have no choice
15 but to mail their product in five-digit sacks in order
16 to obtain reasonable service, should the Commission
17 take that finding into consideration in assessing your
18 proposal, and if so, how? I think that the first
19 question is susceptible to a yes or no answer, and I
20 think your answer is no, that they should not take it
21 into consideration, but could you tell me if I'm
22 correct or incorrect?
23 A If you mean by taking it into consideration
24 to mean that we should neglect that those costs exist
25 and have them all paid by someone else, then I don't

1 believe it should be taken into consideration.

2 Q Well, it's one thing to deny that they exist

3 and another thing to figure out what to do about them.

4 Just on the second part, if the Commission were to

5 say, yes, those costs exist, but we just think, for

6 policy reasons, they ought to be borne by others, you

7 would disagree. You would think that that would be

8 inappropriate.

9 A We have here a national postal service which

10 is owned by the nation. Now, I'm willing to assume

11 that they are doing the best job possible of handling

12 all of the mail technically efficiently, but that

13 Postal Service that we all own has a behavior. It

14 does, in fact, have some costs that it draws in from

15 the rest of the economy. Every time it hires a

16 person, that's a person that can't work somewhere else

17 and do something else. So that Postal Service does

18 have some costs, and I'm saying that those costs need

19 to be recognized in the rates.

20 I don't understand why someone should be

21 able to say, "Gee, I've found out that if I prepare my

22 mail like this, which has an awful a lot of costs

23 associated with it, I've found out that I get a little

24 bit of value from it, and since I don't have to pay

25 for it, let's do it that way." I don't understand why

1 that should exist.

2 Q In Question 91, we asked you about the

3 Alaska air costs. Your counsel objected to the

4 question. The presiding officer decided that it

5 should be answered, and your answer says that you

6 respect the decision, you don't agree with the

7 characterization of the costs as institutional, and

8 you believe it's a policy-based exception by the

9 Commission. I don't think you quite answered the

10 question about whether you agree with it or not,

11 though. Do you have an opinion?

12 A I think that I said here that I cannot agree

13 that volume-variable costs are properly characterized

14 as institutional. Now, it's possible that I would

15 have reached the same decision through a different

16 path.

17 Q Would you have been more comfortable if

18 those costs were considered to be attributable costs

19 for the parcel class and were paid by other parcel

20 mailers rather than being treated as institutional

21 costs and paid by whoever pays institutional costs?

22 A No. I don't think I would have done that.

23 Q The other question is, would you have been

24 more comfortable with that result, if they had called

25 the cow's tail a tail but treated it the way they did?

1 A In terms of outcome, I would not have been
2 more comfortable.
3 Q You say that it was a policy-based
4 exception. Do you know what that policy was?
5 A I think the policy is that we're going to
6 deliver, that we have made a policy decision to
7 deliver parcels to people in Alaska as though they
8 existed on highways with normal transportation
9 available, even though we have no choice but to carry
10 it there by air.
11 Q In Question 94, we asked you about a
12 quotation in footnote 41 of your testimony, a
13 quotation by the Commission that carries over from
14 page 55 to 56. Do I read this answer correctly, that
15 you disagree with the Commission's statement that you
16 quote there?
17 A I'm sorry. Was there a Commission statement
18 -- with respect to the quotation in footnote 41?
19 Q After citing El Cono, et al., you go on to
20 say, "Also the Commission said," and you have a quote
21 about productivity cited to the decision in MC-95-1.
22 I read your answer as disagreeing with that quote.
23 I'm just asking whether that's, in fact, the case.
24 A "The concept of work sharing has been widely
25 applied and is credited with helping the Service to

1 attract expanding volumes of mail." Well, certainly,
2 if you attracted expanded volumes of mail, which a lot
3 of analysis shows has resulted from the advent of work
4 sharing, that should increase your productivity due to
5 scale effects in general, but my answer to this
6 interrogatory was perhaps a little narrower than that.
7 If you have a productivity for handling
8 sacks, a technical productivity, and you have a
9 productivity for handling pallets, and you have a
10 productivity for handling pieces, just because someone
11 buys more sacks and fewer pallets or more pieces and
12 more pallets, just because they change their mix
13 doesn't change your productivity for anything you're
14 doing. You're still just as productive at sacks,
15 maybe fewer of them, maybe more. You're still just as
16 productive at pallets, maybe fewer, maybe more.
17 You're just as productive at handling pieces.
18 So if your productivity in every single
19 operation that you have hasn't changed, you can't
20 change your overall productivity simply because
21 somebody buys a little more of one of those areas and
22 less of another.
23 Q In Question 97, we asked you about a formula
24 on page 61 and whether the V term in that formula
25 meant that advertising revenue is directly

1 proportional to the number of subscribers, and your
2 answer begins: "On a long-term-equilibrium basis,
3 yes." What does "on a long-term-equilibrium basis"
4 mean?
5 A It means that I'm dealing here with general
6 tendencies, and I understand that there are short-term
7 cases where the formulas don't exactly apply. In
8 other words, someone may have a rate base that they
9 have set their advertising rates for, and they obtain
10 a new subscriber. They don't run out the next day and
11 change their advertising rates. It might be a while
12 before they change their advertising rates. If they
13 promised a customer a certain number of recipients,
14 and the number of recipients went a little above that,
15 they can't necessarily go back the next day and say,
16 "Hey, look, we sent your magazine to a few extra
17 people. Give us some more money."
18 So all I'm saying is that I'm dealing here
19 with tendencies over time, and I'm not trying to deal
20 with day-to-day variations. I understand there's a
21 lot of little special situations.
22 Q This is an important formula in your
23 testimony because here is where you conclude that a
24 magazine like Pit and Quarry would not cut a Zone 8
25 subscriber because it makes a lot of money on that

1 Zone 8 subscriber, and the biggest revenue impact of
2 your formula is this V term, which is advertising
3 revenue per subscriber. Do periodical publishers'
4 rates for advertising, are they based on a per-
5 subscriber basis?
6 A They are based on a level of circulation
7 that's promised.
8 Q In all cases, is that a fact, that it's
9 promised?
10 A Well, we're back to these unequivocal
11 statements about whether that's true in all cases.
12 Q In most cases, is there a promised rate
13 base?
14 A Along with a promised circulation, you
15 usually have some information about the demographic
16 characteristics of what that circulation is, but
17 basically I think the rates are based on some factor
18 relating to the circulation, yes.
19 Q "On some factor related to" is getting a
20 little vague. Is there a promised circulation for
21 most periodicals? Do you know?
22 A I think there is an understood circulation
23 base that's associated with the advertising rates that
24 are charged.
25 Q Prior to preparing your testimony, had you

1 examined the ad rates of any periodicals?

2 A Well, I'm thinking long term/short term

3 here. I started preparing my testimony -- I started

4 writing major sections to see what they looked like in

5 July of last year. I think probably before July I had

6 looked at some Web sites and pulled off some

7 advertising rates. I did so more extensively after

8 July, after I started writing it.

9 This was not a short-term process that

10 occurred instantaneously. In years past, I have

11 looked at advertising rates before, not extensively.

12 I've never bought any myself.

13 Q Please take a look at the material you've

14 provided in response to American Business Media

15 Question 98, which asked you specifically about the ad

16 rates for a few of the Complainant's periodicals. Do

17 you have your response there?

18 A I have my response.

19 Q If you look at the ad rates for Time U.S.

20 editions, Time national, it says "rate base 4

21 million." Is that right?

22 A I have my response, but I don't have the

23 library reference.

24 Q You don't have the material you provided --

25 A I don't have the library reference that we

1 submitted.

2 MR. STRAUS: Perhaps counsel can provide it

3 to you.

4 MR. KEEGAN: I do not have it with me.

5 MR. MITCHELL: I would point out that these

6 sheets that we've provided are publicly available if

7 you subscribe to, you know, -- there is some kind of

8 an industry publication which has rates and

9 circulations in it, so these are directly available to

10 anybody in the country who subscribes to that.

11 MR. STRAUS: I'm going to give you a copy.

12 Unfortunately --

13 CHAIRMAN OMAS: Mr. Straus, I think Mr.

14 Keegan just got a copy of that library reference.

15 MR. STRAUS: Can we give it to the witness?

16 (Pause.)

17 BY MR. STRAUS:

18 Q The first page, the first rate card there,

19 says "Time, U.S. editions; Time, national; rate base 4

20 million." Is that right?

21 A Yeah. Time, national; Time business.

22 Q Let's just look at the first one: "Time,

23 national, rate base 4 million." Do you see that?

24 A Yes.

25 Q Does that represent essentially a promise by

1 Time that there will be 4 million copies in
2 circulation?
3 A My understanding is that that's a commitment
4 that there will be at least 4 million, yes.
5 Q And if they fall below 4 million, is it your
6 understanding that Time would owe rebates to its
7 advertisers?
8 A You know, I have read before -- in fact, I
9 think there's been issues in the Wall Street Journal
10 about legal cases involving how magazines behave under
11 those kinds of situations, and I don't know the
12 details of how any one handles it.
13 Q Do you know whether Time tries to keep its
14 circulation above 4 million to have a comfortable
15 cushion so that it always can provide what it
16 guarantees, the 4 million copies?
17 A You know, everyone is willing to tell you
18 that they are honest. When I read about some of these
19 issues in the Wall Street Journal that have been
20 raised in the courts about whether magazines are
21 behaving properly, I asked Jim O'Brien at Time whether
22 or not this affected them, and his response was that
23 they are very honest and straightforward about this,
24 and they aren't a part of it at all, and they don't
25 like some of what's going on in the industry, and I

1 shouldn't worry about them.

2 Q My question, Mr. Mitchell, is whether you

3 think Time keeps its circulation above 4 million so it

4 has a comfortable cushion to make sure it delivers

5 what it promises. I wasn't asking if they do anything

6 bad.

7 A Implicitly, my answer was yes.

8 Q Let's go on. Look at the Time, U.S.

9 editions, geographic editions. It's got a page 8 at

10 the bottom left-hand corner. There seem to be two

11 pages per sheet here. It lists a whole bunch of state

12 editions.

13 A Okay. I see page 8.

14 Q Can you see all of those state editions?

15 A Yes.

16 Q And you see that the rate for Alaska, with a

17 rate base of 10,000 copies, is $16,958. Do you see

18 that?

19 A Yes.

20 Q And for New Jersey, with 150,000 copies,

21 that rate is also $16,958. Do you see that?

22 A Yes.

23 Q So even though one has 10,000 and one has

24 150,000, the rate is the same.

25 Let's look at Connecticut, with 75,000

1 copies. That's also $16,958, isn't it?

2 A Well, you have gone well beyond my level of

3 expertise. As an expert witness, I can't interpret

4 these numbers for you.

5 Q I'm not asking you to interpret. Doesn't

6 this say "Connecticut, rate base 75,000; the cost per

7 page for a black-and-white page, $16,958"?

8 A I don't disagree that you appear to be

9 reading it properly. I don't quite know what it

10 means. I can't answer questions about the

11 interrelationships involved.

12 Q You're the one who is testifying that

13 periodicals losing one subscriber or adding one

14 subscriber will change their revenues by $100 or more.

15 Doesn't this page show you that for a 10,000

16 circulation in Alaska, 75,000 circulation in

17 Connecticut, 150,000 circulation in New Jersey, that

18 the Time, Inc., stated rate is the same for the state

19 editions?

20 A This is an issue that I haven't thought

21 about. I don't know whether the appropriate response

22 is to say that there is a mixture out here, and my

23 model takes an aggregate view or whether I should

24 design models for specific situations. The results of

25 the model were robust enough that there can be

1 substantial differences among territories, and it
2 wouldn't make any difference.
3 Q Let me ask you this question. Do you think
4 that if the New Jersey number fell from 150 to 140 --
5 MR. KEEGAN: Mr. Chairman, I'm going to
6 object at this point. If Mr. Straus wants to ask
7 questions about this subject, we are perfectly welcome
8 to direct him to Time, Inc., which will provide
9 answers, but this witness has already said he is not
10 expert on this subject.
11 MR. STRAUS: I'll move on to a slightly
12 different question.
13 CHAIRMAN OMAS: Thank you, Mr. Straus.
14 MR. STRAUS: I think that if Time, Inc.,
15 wanted to put information into this record about
16 advertising revenues for periodicals, maybe it should
17 have produced an expert on the subject.
18 BY MR. STRAUS:
19 Q Look at Motorcross on the periodicals sheet.
20 A Have you got a page number?
21 Q My came out printed in stripes. I'll show
22 you what I've got.
23 A Okay. Motorcross.
24 Q Is there a rate base listed there?
25 A It has a 2004 circulation projection section

1 which points to newsstand sales, subscriptions and
2 total, but I don't see the word "rate base" beside
3 that, so I'm again in a position where I can't do a
4 good job of interpreting these figures.
5 Q So whereas Time magazine had a rate base,
6 Motorcross has a circulation forecast.
7 MR. KEEGAN: Mr. Chairman, I object again.
8 The witness has already said that he cannot interpret
9 these figures.
10 MR. STRAUS: I asked him not for
11 interpretation, just for the words on the sheets that
12 he provided.
13 MR. KEEGAN: Your last question asked for an
14 interpretation, Mr. Straus.
15 CHAIRMAN OMAS: Rephrase your question.
16 BY MR. STRAUS:
17 Q There is a number identified as rate base
18 for Time magazine, is there not? The ones we went
19 through before, rate base 4 million, state rate bases.
20 A I can tell you that when we discussed this
21 particular interrogatory, we reached the conclusion
22 that we should supply the sheets that were available
23 to the entire country to people that subscribe to the
24 rates and circulation information for magazines and
25 that that would be the appropriate way to respond, so

1 we provided those pages. These pages are subscribed
2 to by practitioners all over the country. I hope they
3 know how to interpret them. I don't.
4 Q But does the word "rate base" appear for
5 Time magazine? I'm not asking you to interpret
6 anything.
7 A Yes, it did.
8 Q And does the word "rate base" appear on the
9 Motorcross circulation, or is it a projection? How is
10 it described? Is it described --
11 MR. KEEGAN: Mr. Chairman, I renew my
12 objection to this line of questioning.
13 MR. STRAUS: I'm asking how --
14 MR. KEEGAN: Mr. Straus is asking what is
15 being substituted --
16 CHAIRMAN OMAS: Mr. Keegan, please.
17 Mr. Straus, proceed but --
18 MR. STRAUS: One more question in this line.
19 BY MR. STRAUS:
20 Q How is the 90,000 circulation described for
21 Motorcross? Is it described as a rate base, or is it
22 described as something else on the rate sheet?
23 A Well, it's true that I see the word
24 "projection," which you pointed out. It's true that I
25 see the word "rate base" on the first page, but when

1 it comes to comparing those two words and saying why
2 one was used instead of the other or how those
3 particular figures should be interpreted on each page,
4 I'm not really sure.
5 Q I didn't ask you that, so let's go on to
6 Question 102.
7 A Okay.
8 Q This was a question about postage costs for
9 Pit and Quarry, a periodical that you referred to in
10 your testimony, and we asked what the postage would be
11 under your proposal, and you said in your answer that
12 you're making assumptions based on your response to
13 Question No. 1 of POIR No. 1. Those assumptions play
14 a pretty important part in determining that postage,
15 don't they?
16 A Yes, they do, consistent with what I've said
17 here a number of times, that sizes of sacks and the
18 bundles and so forth are very important cost
19 determinants.
20 Q So you really don't know what the postage
21 would be under your proposal for a Zone 8 copy of Pit
22 and Quarry without knowing a lot more information
23 about Pit and Quarry.
24 A That's true. I just took industry averages.
25 I thought that was the only reasonable thing that I

1 had.

2 Q Well, do you really believe that 43.07 cents

3 is a reasonable estimate for the postage for a Zone 8

4 copy of Pit and Quarry under your proposed rates?

5 A I don't have a specific figure in mind for

6 them that's reasonable. I've played with my rates

7 enough to know that if you have reasonably full sacks

8 and reasonably good-sized bundles, you can come out

9 pretty well. If someone has very small bundles and

10 very small sacks, they can take a pretty substantial

11 increase. I don't know anything at all about how Pit

12 and Quarry is prepared, so the answer is that I have

13 no other estimate in mind.

14 Q So "I don't know" would have been a truthful

15 answer to this question. I'm not saying this is not

16 truthful; I'm just saying, if you had just said "I

17 don't know," that would have been a perfectly truthful

18 answer to what the postage would be under your

19 proposal.

20 A I don't know.

21 Q Okay. In Question 103, we asked you about

22 your understanding of basically the economic health of

23 the periodicals industry today, and you say you can't

24 provide expert testimony, but earlier, in your

25 interrogatory responses and in your testimony, you

1 described your activities in recent years, and you
2 spent an awful a lot of time with magazine publishers,
3 with printers, with the Postal Service. Do you have a
4 sense for how healthy the periodical industry is today
5 as a result of all of those contacts?
6 A Well, I think there's a few very general
7 things that I can say. I'm, in effect, a lay observer
8 of all of these articles about the pressures that they
9 are under, but I think most people feel like they have
10 been under increasing pressure, just like many other
11 industries have. I believe that the circ. net figure
12 that somebody keeps asking me about may have come down
13 for some magazines. I think, in the recent recession,
14 that the business-to-business took about a drop of
15 about a third in their advertising, whereas consumer
16 publications went down around 12 percent.
17 Nevertheless, people keep saying that all of
18 the money is in business to business and that the mass
19 markets are disappearing, and you have to go for niche
20 markets, that these things are privately held, and
21 some of them are very profitable. I keep hearing
22 people say that they need to put on more trade shows
23 in order to get more revenue. I don't think trade
24 shows have very much to do with geographic
25 distribution.

1 So I know there has been turmoil in the
2 industry. There has been turmoil in a lot of
3 industries, and this is an adjustment process that
4 occurs over time. So I don't know whether that's
5 helpful or not. I agree that these things are going
6 on and that these people are under pressure just like
7 everybody else.
8 Q Do you happen to know what the trend has
9 been with the stock of periodical publishers like
10 Penton and Prime Media, some of the publicly traded
11 companies?
12 A I have no idea what's been happening to
13 their stock. I have read that an inordinately large
14 number of business-to-business publications and niche
15 publications are privately owned, but that doesn't
16 answer your question.
17 Q No. Is there any reason to believe that
18 privately owned publications are doing any better
19 financially than publicly owned publications?
20 A Not necessarily.
21 (Pause.)
22 MR. STRAUS: I'm editing myself. Bear with
23 me. Please look at your response to McGraw Hill
24 Question 26.
25 CHAIRMAN OMAS: Excuse me, Mr. Straus, could

1 you give the Chair an idea of how much longer?
2 MR. STRAUS: About two minutes.
3 CHAIRMAN OMAS: Oh, fine. Then we'll go
4 take our afternoon break. Thank you, sir.
5 MR. MITCHELL: McGraw Hill 26?
6 MR. STRAUS: I'll withdraw that question.
7 Maybe you're talking about the bar code discount for
8 five digit pieces, and I probably already talked to
9 you about the pre-sort discount. I thought they were
10 the same, but let's move on. I'll move on. My two
11 minutes are up. I'll quit now. I actually didn't
12 want to ask any more.
13 CHAIRMAN OMAS: Well, thank you very much,
14 Mr. Straus. I think we will now take a ten-minute
15 break, and we'll come back at a quarter of four.
16 Thank you.
17 (A brief recess was taken.)
18 CHAIRMAN OMAS: If I could have your
19 attention for just a moment. During the break,
20 counsel spoke with Mr. Bergin, and it is our
21 understanding that he has approximately two hours of
22 cross examination. And Ms. Rush said she had about 20
23 minutes to half an hour. So that we can all be fresh
24 and ready to go, if it's okay with Mr. Bergin, I'd
25 like to let Ms. Rush go this afternoon, and we will

1 reconvene at 9:30 in the morning and we'll let you
2 cross examine for as long as you like.
3 MR. BERGIN: That's perfectly fine with me,
4 Mr. Chairman.
5 CHAIRMAN OMAS: Is that all right with you,
6 Ms. Rush?
7 MS. RUSH: Yes.
8 CHAIRMAN OMAS: Counsel?
9 MR. KEEGAN: Yes, that's agreeable, Mr.
10 Chairman.
11 CHAIRMAN OMAS: Thank you.
12 Ms. Rush, would you introduce yourself for
13 the record, please?
14 MS. RUSH: Thank you, Mr. Chairman.
15 BY MS. RUSH:
16 Q Good afternoon, Mr. Mitchell. I'm Tondra
17 Rush with National Newspaper Association.
18 A Good afternoon.
19 Q I'm going to try not to cover -- recover any
20 of the territory Mr. Straus did. And we're not going
21 to go through the complexities of weekly newspapers
22 rate base, so maybe we can get through this quickly.
23 You have at least a decade and a half of
24 experience in looking at periodicals rates. Is that
25 true?

1 A Yes.

2 Q From R-87 -- or '90 with the Postal Service,
3 and then about ten years here with the Commission. Is
4 that correct?

5 A Well, I worked on them before R-87. In R-84
6 they were developed in a branch that I was the manager
7 of, so prior to R-87 I worked on them, too.

8 Q Well, let's take the R-84 rates, then. Were
9 those rates more efficient than the rates we have now?

10 A The biggest thing that I remember that we
11 did in R-84 was to get a substantially larger portion
12 of the revenue for the piece rates instead of the
13 pound rates. So in some sense, that includes signals
14 to mailers who might be interested in sending
15 additional weight, because it said if you increase the
16 weight of your publication, we're not going to
17 increase your postage as much as we used to, and the
18 reason we're not going to is because our costs don't
19 go up as much as the previous rates implied. So for
20 that reason alone I think you would have to argue that
21 the rates in R-84 were more efficient.

22 Q Would you look at your response to NNA's
23 Question Number 8? You begin your answer to that
24 question by quarreling with the way I had phrased it.
25 You said it's difficult to see that anyone was

1 experiencing the low cost in postal rates, whatever
2 that may mean. Are you trying to say that no one
3 really is enjoying a low cost rate now?
4 A Well, you used the phrase low cost of
5 periodicals, and I didn't know exactly what that
6 meant.
7 Q Let me rephrase that, then. I'm talking
8 about the cost to the publisher. Do you believe that
9 the publishers enjoy relatively low rates, or do you
10 believe the rates are higher than they should be?
11 A Well, on average, I'm not here to say
12 whether Postal Service costs should be higher or lower
13 than what they are. For my purposes I'm fully willing
14 to take Postal Service costs as being the result of
15 doing a very good job of running their operation. I
16 think what this complaint is about is that the rates
17 aren't very well aligned with what those costs are,
18 and that some of the signals given by the rates are
19 not very good, and that if things are improved a
20 number of changes could be made which will increase
21 economic efficiency of the nation and mailers as a
22 whole.
23 Q When you were involved in the R-84 case,
24 were publishers complaining that the rates were too
25 high then?

1 A Well, that's kind of a strange question,
2 because people always tend to complain about the rates
3 being too high, whether there's an objective reason to
4 believe that they should be at a different level or
5 not. So I think yes, the Postal Service has faced
6 resistance to every rate increase that it's ever made.
7 Q So that answer probably would be true
8 regardless of which rate case we picked?
9 A I think so.
10 Q Okay. Is it true that the concerns about
11 periodicals rates seems to have intensified in the
12 past, say, two rate cases or three rate cases?
13 A I think that's true.
14 Q Is that associated with increased
15 periodicals mail processing costs, in your view?
16 A Well, something has certainly caused the
17 periodicals rates to go up inordinately, and there's
18 only one thing that can cause that, particularly when
19 there's been no increase in cost coverage, and that's
20 cost.
21 Q Particularly with mail processing?
22 A Well, I think most of the attention has been
23 on mail processing and productivity for flats, and
24 because of that the questions have extended into
25 standard mail as well, and also into first class,

1 although flats are not as big a proportion of first
2 class as they are of standard and periodicals. So a
3 lot of the questions have been on productivity for
4 flats. I don't have a mapping of the various cost
5 components and which ones have contributed the most.
6 Q All right. You have made many mentions, in
7 your testimony, about the magazine industry.
8 Newspapers are also a part of this mail class, are
9 they not?
10 A Yes, they are.
11 Q Have you done any analysis specifically
12 about the effect of your recommendations upon
13 newspapers?
14 A Are you talking about newspapers in general?
15 Q Newspapers in general. Large ones, small
16 ones.
17 A Well, I would say no, I haven't done any
18 specific analysis. I mean, my general reaction to the
19 question is that the large newspapers, by and large,
20 are delivered by paper people to my door early in the
21 morning, and the amount of volume that they send
22 through the mail is pretty small.
23 Q Let me restrict my question then to
24 newspapers that are in the mail stream.
25 A Well, I mean, are you talking about in

1 county? I mean, I understand that in some small towns
2 some of the newspapers are in the mail and some of
3 them are delivered privately, and they can be very
4 heavy users of the mail.
5 Q Well, any size newspaper -- big newspaper,
6 little. Have you analyzed any specific publisher's
7 results if they employed the rates that you might
8 recommend in this case?
9 A No.
10 Q Have you followed the Copalletization cases
11 that have happened here at the Commission in the past
12 couple of years? Copal 1, Copal 2? Is there another?
13 A I have followed them to some degree, yes.
14 Q Are you aware of any newspapers that have
15 expressed an interest in copalletization?
16 A None come to mind, no.
17 Q Would you turn to your response to NNA's
18 Question 33, I believe it was. I was asking you there
19 whether you believe that all periodicals publishers
20 use computers to prepare their mail, and really the
21 percentage of their mailing lists here, I suppose.
22 Have you used any of the mailer software? Have you
23 looked at any of it? Tried to manipulate numbers, or
24 do what ifs on any of the popular mailer software?
25 A Not personally, no.

1 Q Are you familiar with any of the products
2 that are out in the market for this purpose? First
3 Logic or any of those types of products?
4 A Well, now that you mention First Logic, I'm
5 aware that there are two or three large software
6 firms. Pitney Bowes just bought one of them, and
7 maybe after they bought one recently there's one less,
8 because I think Pitney Bowes did some of it
9 themselves. There are a limited number of very large
10 mailers that do all their own programming. They think
11 they come out ahead by it. They may not.
12 But I attribute these software firms as
13 being very, very good computer people. I'm not
14 familiar with their specific products.
15 Q Would you say, by and large, that the
16 periodicals industry -- the parts that you're familiar
17 with -- use off the shelf software to prepare mail, or
18 are these proprietary, specially designed, custom
19 designed software? Can you characterize it in any
20 particular way?
21 A I don't think it's off the shelf in the
22 sense that you go down to Comp USA and pull the one
23 that fits you. But I think that when you buy from
24 these people that some of the products have recently
25 standardized.

1 Q Do you have any idea of the cost of any of
2 them?
3 A No, I don't.
4 Q Would you assume it was three figures? Four
5 figures? Five figures?
6 A I don't know.
7 Q Any idea?
8 A I don't know. I would guess it's coming
9 down, but I don't know.
10 Q Do you have any knowledge of the software
11 development that's necessary when a publisher begins
12 to palletize?
13 A No, I don't. But the time to get to
14 pallets, I think we're talking about reasonably
15 sizable mailings. But your question here that we're
16 still talking about starts off by talking about
17 whether all publishers use computers, and I'm assuming
18 that you're really talking about the software used by
19 small mailers. So I'm kind of struggling here with
20 the difference between large and small mailers.
21 Q I'm not asking you specifically about size.
22 What I'm curious to know is whether you have talked
23 with any of the publishers that you've worked with, or
24 with your clients in this case, about what is involved
25 when a publisher or a printer decides to move from

1 sacks to pallets for mail preparation.
2 A I don't know what's involved.
3 Q Let me ask you to turn, then, to NNA's
4 Question Number 15. Do you have it there?
5 A Yes, I do.
6 Q And is this a great example of the exact
7 sort of problem you're targeting in this complaint, or
8 what? I'm asking you here about a 3,000 circulation
9 newspaper in a Midwestern city that has 15 residents
10 that move to Florida for the winter, and without going
11 through all the details of it, this publisher has had
12 a hard time getting the copies of the newspaper to
13 these residents in a timely manner, and has been
14 advised by the Postmaster to create 15 five-digit
15 sacks with one piece each. That's the kind of
16 inefficient mail preparation that you have discussed
17 in your testimony, is it not?
18 A I think basically yes. The question that
19 you're raising here in this question has been
20 discussed extensively by Witness Schick as well as by
21 Witness Strawburg. Also, there's an inquiry underway
22 to see whether there really are service differences
23 associated with this. My feeling is that when these
24 sacks get to the final three-digit area, that the
25 Postal Service is supposed to open them, process them

1 that night, and take them out for delivery the next
2 morning. If the Postal Service is not doing that, we
3 have a serious problem. And I think that a lot of
4 people think that they're getting a whole lot better
5 service by putting them in sacks -- putting them in a
6 large number of sacks instead of a small number of
7 sacks.
8 Q Let me go back to the nature of my question.
9 If this publisher is creating these 15 one-piece
10 sacks, is this publisher creating something that in
11 the vernacular is known as a skin sack?
12 A Known as a skin sack?
13 Q Exactly.
14 A Yes.
15 Q Okay. It doesn't matter for your economic
16 analysis, does it, whether the publisher's doing this
17 because the Postmaster recommended it or because the
18 publisher created it out of his own head, or was
19 advised by a postal consultant. From an economic
20 point of view, that doesn't make any difference, does
21 it?
22 A No, it doesn't.
23 Q You made the statement in response to this
24 question that said it's difficult to understand any
25 reason why one-piece sacks should whip through the

1 system while pieces going through major processing
2 operations should be delayed. Would you explain what
3 you meant by that? Did you mean that it should not or
4 that it likely was not having better service? What
5 did you mean when you said should whip?
6 A My understanding is that the Postal
7 Operations Manual has some service standards in it
8 that facilities are supposed to honor. And that
9 service standard is that when this large sack, with a
10 lot of bundles in it, gets to a -- or maybe with one
11 big bundle in it -- when it gets to a destination
12 facility, it is priority mail. It stands just behind
13 first class. It's supposed to be opened. It's
14 supposed to be given an incoming secondary if it needs
15 it or an income primary to secondary. That occurs
16 late that night, and it goes out the next morning for
17 the mailer.
18 Now, why it is that a one-piece sack that
19 gets to the same facility should be sorted very
20 quickly and get out the next day and the other mail
21 should not, I don't know. It seems to be misaligned
22 with their processing standards.
23 Q So what you're saying should here, is you
24 don't think it really happens, or you don't think they
25 should handle them that way. That's what I'm trying

1 to find out.

2 A I have serious questions about whether it

3 really happens --

4 Q You don't think it does?

5 A -- and if it does, I think it ought to be

6 fixed. But if it can't be fixed, then that is the

7 behavior of this monstrous national postal system that

8 we all own. It does have this behavior. It does have

9 these costs. Mailers have the option of saying I want

10 it handled a certain way, and if they do that, they

11 should be charged according to the costs involved.

12 Q You mentioned a moment ago the service

13 standards that you believe are in the mail processing

14 manuals. Are you familiar with any published service

15 standards for periodicals?

16 A Well, I know that if you call up Memphis,

17 you can get what used to be a three and a half inch

18 disk, and I think it's now a CD, and you can put in

19 your origin and your destination zip code, and it will

20 tell you the expected service standard for every class

21 of mail in terms of days. So in some sense there is

22 an understood way that the system is supposed to

23 operate.

24 Now, beyond that, I don't know if they have

25 a highly calibrated process of giving you a service

1 standard and saying we're going to live by this.
2 Obviously, too many people are having bad experiences
3 and are reporting that they aren't getting the service
4 that they should have, and we have an ongoing system
5 for looking into that.
6 Q Have you seen any data from the Postal
7 Service in which they measure their performance
8 according to any of those service standards?
9 A No. I know the Reg Tag Association measures
10 it for their members, but I don't think the Postal
11 Service has a system that does it.
12 Q Have you heard testimony from publishers
13 during your tenure at the Postal Service or the Rate
14 Commission here that newspapers have a hard time
15 achieving reasonable delivery, particularly to
16 Florida, or to any long distance where they have a low
17 density of delivery?
18 A I have heard a number of questions raised
19 about small quantities of newspapers going long
20 distances not getting very good service, yes.
21 Q Have you ever heard testimony that
22 publishers say that those newspapers tend to be
23 delivered in clumps of twos and threes instead of in
24 some reasonable orderly fashion, in the order in which
25 they're dropped in the Postal Service?

1 A Yes. In fact, we had a former Commissioner
2 who still got a local community newspaper from out in
3 Kansas, and it came out every week, and sometimes he
4 got two in the mail on one day.
5 Q Were you here last week when Mr. Strawburg
6 testified?
7 A Yes, I was.
8 Q Do you remember a calculator exercise that
9 Mr. Straus created in which they tried to figure out
10 what the appropriate postage costs would be under a
11 cost-based rate system, if you took the piece and the
12 pound and the bundle and the container and the drop
13 ship, and you came out with a number that was rather
14 protracted?
15 A That was a long question.
16 Q It was. Let me save time here. I don't
17 want to send us to the calculator again, because I
18 don't have one with me. I think you do, so you'd be
19 way ahead of me here.
20 Would you accept their conclusion that they
21 came to a number that the price per piece for my one
22 piece in a skin sack would come around somewhere in
23 the $3 range, just for purposes of hypotheticals.
24 A Was that the one where somebody said you
25 could send it first class and not --

1 Q Pay less. It was. So would you accept my
2 hypothetical at $3 for that price?
3 A Okay.
4 Q So if that happened, and you just identified
5 my next question, the price would entice the publisher
6 probably to shift to first class. Would you agree?
7 A Yes.
8 Q Maybe even priority mail at that rate.
9 Priority mail might be in the $3.50 range, it might be
10 cheaper and faster to get it there by priority mail
11 than by periodicals rate.
12 A I understand that a number of newspapers
13 give people the option of having it sent by priority.
14 Q Okay. Then let me go to the alternatives
15 that you've explored for this publisher and this skin
16 sack. You've addressed some of these in your
17 Attachment A. But let me just walk through what the
18 real world experience might be for the publisher in
19 trying to grapple with this potential $3 charge, if
20 that's what he was faced with.
21 The publisher could raise the price for
22 those particular copies to Florida, correct?
23 A Yes.
24 Q And I think in your testimony at page 60 you
25 kind of walked through your idea of how that might be

1 dealt with. You said you had discussed the
2 possibility of a zone-based subscription rate with
3 publishers, and you found that they all told you it
4 was unrealistic. Is that correct?
5 A Yes.
6 Q So you think that that would not be a
7 realistic scenario from the publishers that you've
8 talked with?
9 A Yes, but I agree that most of the ones that
10 I talked with were periodical publications as opposed
11 to newspapers.
12 Q Magazines?
13 A Uh-huh.
14 Q Are you aware of any magazines that charge a
15 different subscription rate for their in market copies
16 than for the ones that are mailed out of town?
17 A I suspect that if there is, it's not
18 graduated by zones, but is rather a process of whether
19 we have to do a special job of sending this out as
20 opposed to delivering it through a normal local
21 channel. And it ma be related to the fact that some
22 of the local advertisers are not too excited about
23 paying for papers that are going to distant locations
24 where people won't buy anything.
25 Q Well, let me just explore the possibility of

1 passing this charge on to the Florida resident for a
2 moment. It could happen, right? It could happen?
3 A Yes.
4 Q It would be a business decision for the
5 publisher to decide if that subscriber wanted to pay
6 $3 per issue for the paper?
7 A Yes.
8 Q Okay. Let's assume the publisher decides
9 that that Florida reader is not willing to do that.
10 Let's assume the publisher has really only two other
11 sources of revenue to recover that $3. And let's
12 assume further, these particular residents are snow
13 birds; people who go away for a period of time and
14 then they come back when the weather is nicer, maybe
15 to a place like Wisconsin, for example. So they have
16 an interest in maintaining those people, those
17 subscribers.
18 So let's assume that they have to find a way
19 to get back the few dollars that they're going to be
20 spending for the skin sack piece. An alternative
21 would be to raise the subscription rates for everyone
22 in town, and basically average out the cost within
23 their own subscriber base, is that correct?
24 A I suppose that would be an option, just like
25 the option to raise everybody else's rates so you

1 could subsidize their postage.

2 Q If you were an economist, would you

3 recommend that they take that option?

4 A No.

5 Q Then let's look at the advertising rates.

6 You just made a reference to the advertisers' interest

7 in these people. Could you raise the advertising

8 rates to absorb this extra cost for these advertisers

9 in a town in Wisconsin to reach the people in Florida?

10 A I don't see how you could.

11 Q Why would you not?

12 A Well, if I were an advertiser, and somebody

13 wanted to increase my rates to pay for sending my

14 advertisement to somebody that's out of town and could

15 never buy anything from me, I don't think I'd be

16 overjoyed.

17 Q Well, what about eliminating the $3. Let's

18 give up the skin sack, and let's put it in a mixed ADC

19 bundle, in a mixed ADC bag, and enter the bag in an

20 origin SCF and just send it through the system however

21 it goes. Is that a reasonably good alternative for

22 the publisher in your view?

23 A Well, at some point you need to tell the

24 recipient that these are the options that we have.

25 We're sorry that the options aren't different, but

1 these are what's involved. And I have -- we're
2 talking about a very low volume thing here. You had
3 five sun birds, I think, 15 sun birds down here. It's
4 not clear to me why someone else should be subsidizing
5 them, just because you don't want --
6 Q Well, that's not what I'm saying. Would you
7 tell that publisher that it's a good alternative to
8 put those pieces in a mixed bundle in a mixed sack and
9 let them go through the system however they will.
10 A Yes, I think I would make specific inquiry
11 into why the Postal Service isn't handling those
12 pieces the way it should.
13 Q Let's assume the publisher has done that.
14 Let's assume the Postal Service has said we have no
15 earthly idea, and we're incapable of fixing it. And
16 if you put it in a mixed bag then that will get there
17 when it gets there. Now, do we have any alternative
18 left for our snow birds if they still want to get the
19 information from Wisconsin while they're in Florida?
20 A I don't think there's any obvious ones.
21 Q What about the internet?
22 A Well, the internet's amazing, but I'm not
23 sure it suffices for everything. I was reared in
24 Dayton, Ohio, and every morning the Dayton Daily News
25 sends me an email with the headlines in it. And I can

1 click on any headline I want, and it goes to the
2 story. But I don't think that solves everything.
3 Q I was interested in your comment a few
4 minutes ago -- I guess it was in response to something
5 Mr. Straus said, that you think that we who read
6 things on the internet are unrealistic to think that
7 it will continue to be free.
8 A Yes.
9 Q I think you said you thought that at some
10 point we'd have to have a model where the subscribers
11 paid for it. Is that true?
12 A I said that, basically, yes.
13 Q Let me just try the New York Times, since we
14 used that one on Mr. Gordon. He referred to it, and I
15 believe you were in the room during that discussion.
16 Do you ever read the New York Times online?
17 A No, I may have done one or two searches on
18 some things, but I can't even remember whether I had
19 to pay.
20 Q Do you read it in print?
21 A Usually not.
22 Q Okay. Let's assume that you're a
23 subscriber, and that you do enjoy receiving the paper
24 in print, and maybe you occasionally read it on the
25 internet. It probably wouldn't be too inaccurate to

1 say that a typical newspaper might hope to recover
2 maybe 20 percent of its costs from subscriptions,
3 which you said as a hypothetical. Would you assume
4 that in your future world where the readers finally
5 realize that there is a cost to the internet, that the
6 reader might be willing to pay 20 percent of the cost
7 of producing a New York Times for an online
8 subscription?
9 A I wasn't quite sure when you got through
10 with the question.
11 Q Let me ask it a different way. Would you
12 assume that an online reader would be willing to pay
13 reasonably the same amount for the online subscription
14 as for the print product?
15 A It seems like the obvious first response is
16 that we didn't have to buy any paper and we didn't
17 have to pay for any printing, and we didn't have to
18 pay for any distribution. I don't understand why it
19 wouldn't be lower.
20 Q Okay, so you would hope for a lower price
21 than you would receive if you purchased the paid
22 paper?
23 A Yes.
24 Q Okay. Were you also here for my discussion
25 with Mr. Gordon about the technology called Tivo?

1 A Yes.
2 Q Do you know what it is?
3 A Yes.
4 Q Are you familiar with the term Ad Zapping?
5 A I guess I would have to give you almost the
6 same answer that Mr. Gordon did. I don't know whether
7 it's automatic. I know you can record -- even if you
8 don't subscribe to Tivo, you can get yourself a VCR
9 with a recorder. You just have to manage it yourself
10 instead of having Tivo provide you with the management
11 software. But you can certainly skip through
12 commercials, yes.
13 Q Would you assume that readers tend to have a
14 bit more resistence to reading the advertising than
15 they do the news online?
16 A A bit more resistance -- well, I'm not sure
17 I can make an expert statement on that. I could say
18 something on a personal note.
19 Q Let me ask you as a consumer. Do you read
20 much advertising online?
21 A No, I neglect it entirely unless there's
22 something I'm looking for.
23 Q Do you have any patience with pop-ups?
24 A I have a pop-up zapper.
25 Q Do you have any patience with banner ads?

1 A I don't pay any attention to them.
2 Q How often do you go to the advertisers'
3 sales sites that are linked to the websites? If you
4 had a Ford dealership, for example, listed on a
5 website that you were visiting, would you be likely to
6 click through to it?
7 A No. Entirely unlikely.
8 Q If you take your future world of website
9 news, and you factor in the assumption that many
10 readers are about as interested in the advertising as
11 you are, is it reasonable to assume that a larger
12 percentage of the cost of gathering that information
13 and producing it is going to be borne by the
14 subscription price?
15 A We live in a very strange world, where all
16 this stuff existed for forty years with all our
17 entertainment on television being paid for by some
18 advertiser that we don't know in hopes that we'll buy
19 something. In some sense, that's a wonderful world if
20 you don't buy anything and feel like you're getting it
21 all free.
22 I don't know that we can count on the world
23 functioning in a certain way in the future. If
24 advertising doesn't pay on average, then people won't
25 advertise. And if material is valued and it's good to

1 have it produced, and someone is doing a good job of
2 it, the costs of preparing it and delivering it are
3 going to have to be paid. There isn't any free lunch.
4 Q So it's all demand-based, is it not?
5 A Demand-based in what sense?
6 Q Readers will accept what they have an
7 interest in receiving, and they are willing to pay for
8 it according to the value that they perceive from the
9 product.
10 A I think that's true for many things.
11 Q All right. So if you're telling me that you
12 think the price that the New York Times might charge
13 you for the print product would be too high for the
14 internet product, is it fair to say that the $23 print
15 subscription would be your ceiling for purchasing an
16 online subscription?
17 A I lost track of where the $23 came from.
18 Q Let's assume the New York Times charges you
19 $23 to receive your print paper. Would you pay that
20 much for the online subscription?
21 A No, I wouldn't.
22 Q So, shouldn't it go without saying that you
23 also wouldn't pay more than that amount if you had to
24 absorb some of the cost that the advertisers formerly
25 would have borne for producing that product?

1 A Well, I can get -- at my house I can get the
2 New York Times delivered every morning if I want. I
3 forget how much it is. But my problem is information
4 overload. It's very easy to finance and get
5 considerably more than I can look at every day. So my
6 problem is to be selective and if I value it highly
7 enough, I'll pay for it.
8 Q Is it fair to say from the tone of your
9 answers and the direction you seem to be going with
10 the internet questions that you don't agree with Mr.
11 Gordon that the internet is going to come in and sort
12 of replace all these print products that may be
13 inefficiently passed through the Postal Service's
14 system?
15 A Well, I am not a think tank that tries to
16 make future projections about things like this. Often
17 future projections on things like this turn out to be
18 absolutely, completely wrong. I can tell you that I
19 personally get eye strain and get dizzy when I have to
20 read too much on the internet. And the prospect of
21 printing it all out isn't very attractive to me,
22 because I feel like I'm paying somebody's salary at
23 Hewlett-Packard for all these little cartridges I have
24 to buy for my printer, and it irritates me. So I'm
25 very willing to let a professional print it for me.

1 They do a very good job and deliver it to me. And if
2 it has value, I'll pay for it.
3 MS. RUSH: I have no further questions.
4 CHAIRMAN OMAS: Thank you. That brings us
5 to the conclusion today. We will reconvene in the
6 morning at 9:30 with Mr. Bergin cross examining the
7 witness.
8 Thank you all, and have a nice evening.
9 (Whereupon, at 4:21 p.m., the hearing was
10 adjourned, to reconvene the following day at 9:30
11 a.m.)
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