

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
DAVID SCHAEFER
ON BEHALF OF
THE MCGRAW-HILL COMPANIES, INC.

September 9, 2004

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3 **DIRECT TESTIMONY OF DAVID SCHAEFER**
4 **ON BEHALF OF THE McGRAW-HILL COMPANIES, INC.**
5

6 **I. Autobiographical Sketch**

7 My name is David W. Schaefer. I am the General Manager, Logistics and Postal
8 Affairs, for The McGraw-Hill Companies, a position that I have held since July 1998. In
9 this position I am responsible for a team of twelve domestic and international employees
10 and oversee the worldwide logistics operations for McGraw-Hill's publications. I
11 negotiate a variety of corporate-wide global transportation contracts for the company,
12 including express couriers and international mail services. I serve as the primary liaison
13 for McGraw-Hill to the United States Postal Service and represent the company on the
14 Periodical Operations Advisory Committee (POAC) and the Periodicals Advisory Group
15 (PAG). I also serve as a member of the Mailers Technical Advisory Committee (MTAC)
16 representing the interests of American Business Media, of which McGraw-Hill is a
17 member. Prior to joining The McGraw-Hill Companies, I was employed by Primedia
18 where I served as Associate Circulation Director, Distribution. During various periods of
19 my five-year tenure at Primedia, I had responsibility for distribution, customer service
20 and fulfillment for Primedia's consumer magazine division. I began my career as a Field
21 Auditor for the Audit Bureau of Circulations in 1991. I received a Bachelor of Arts
22 Degree in Economics from the State University of New York, Stony Brook in 1990.

23
24 **II. Overview of Testimony**

25 Part III of my testimony discusses the impact that the rates proposed by
26 Complainants would have upon Periodicals published by McGraw-Hill, and outlines the

1 company's basic position in this proceeding. Under the proposed rates, McGraw-Hill
2 would likely save some \$300,000 overall on an annual basis, due largely to its high-
3 circulation publication *Business Week*, although all but three of McGraw-Hill's eighty-
4 four Periodicals would incur substantial rate increases. McGraw-Hill is less concerned
5 with its overall savings than with the adverse impact of the proposed rates on smaller
6 publications, and maintenance of a broad, vibrant and diverse Periodicals class as a
7 whole. McGraw-Hill believes that efficient mail practices can and should be fostered in
8 ways that are more balanced and equitable than the rate structure proposed by
9 Complainants.

10 Part IV of my testimony demonstrates that smaller publications have in fact borne
11 the brunt of the inordinate cost increases attributed to Periodicals over the years. It
12 appears that smaller Periodicals have incurred aggregate postage increases nearly
13 double the rate of inflation, while the postage paid by larger Periodicals such as those of
14 Complainants, and *Business Week*, has not generally exceeded the rate of inflation and
15 actually declined between 1995 and 1999. Thus, the remedy that Complainants now
16 propose for the above-inflation cost increases – a radical de-averaging of Periodicals
17 costs and rates – seems fundamentally misdirected. It would provide a relatively few
18 large publications with an enormous windfall (with no change in their mailing practices)
19 while exposing thousands of smaller publication to correspondingly large rate increases
20 – on top of the above-inflation cost increases borne primarily by smaller mailers already.

21 Part V of my testimony focuses in part on the incentives that already exist to
22 prepare Periodicals mail on pallets rather than in sacks, including reduced production
23 and distribution costs and expanding co-palletization and co-mailing opportunities,

1 among others. However, I also focus in part V on the practical constraints that limit or
2 preclude the ability of many publications to reduce their dependence on sacks, whether
3 through co-palletization or co-mailing or otherwise. I further demonstrate that in view of
4 the fees charged to publishers by printers to participate in co-palletization or co-mailing
5 programs, those programs would not likely enable many participating publications to
6 avoid substantial cost increases under Complainants proposed rates. I also explain
7 why the proposed rate structure would be unmanageably complex for most Periodicals
8 mailers.

9 Part VI of my testimony urges the Commission to adhere to its longstanding
10 basic policies that are seemingly at odds with the precipitous de-averaging of
11 Periodicals costs and rates advocated by Complainants. McGraw-Hill believes that
12 providing appropriate discounts from rates that are based on averaged costs is a far
13 wiser approach that balances efficiency considerations with the fundamental purpose of
14 the Periodicals class – to promote the widespread dissemination of diverse editorial
15 content through preferential postal rates in view of its “educational, cultural, scientific
16 and informational” (“ECIS”) value and its role in binding the nation together. Cost
17 averaging is further justified in my view by our experience that higher-cost Periodicals
18 mail in sacks tends to receive less expeditious service than lower-cost Periodicals mail
19 on pallets.

20 McGraw-Hill likewise sees no reason for the Commission to abandon its
21 venerable policy of promoting widespread dissemination of diverse editorial content
22 through a low unzoned pound charge for editorial content. In our view, the vital role of
23 hard-copy Periodicals in binding the nation together is undiminished by the internet.

1 Both witness Gordon and witness Mitchell fail to appreciate the economics of the
2 magazine publishing industry, or the purpose and role of the flat editorial pound charge
3 to help bind the nation together by lowering the cost of mailing editorial content to
4 distant subscribers.

5
6 **III. McGraw-Hill's Interest in This Proceeding**
7

8 McGraw-Hill publishes a wide range of Periodicals that in many ways mirror the
9 characteristics of the Periodicals class as a whole. Its publications include magazines,
10 newsletters, newspapers, and loose leaf periodicals in the fields of business, finance,
11 healthcare, and construction.¹ McGraw-Hill publishes a total of 84 Periodicals, including
12 19 monthlies, 10 weeklies, 2 bi-weeklies and 53 daily bulletins.² These publications
13 vary widely in terms of mailed circulation, and thus in their ability to use pallets and
14 drop-ship highly presorted mail pieces.

15 McGraw-Hill's publications range from the nearly one million subscribers to
16 *Business Week*, which is more than 98% palletized and mostly sorted to the carrier-
17 route level and drop-shipped to the destination-SCF, to the three loyal subscribers to
18 *Dodge Daily Bulletin Western Missouri*. McGraw-Hill's Periodicals likewise vary widely
19 in terms of editorial percentage and weight, ranging from a 1-ounce, 100% editorial
20 publication (*The Outlook*) to a 7-ounce, 40% editorial publication (*Healthcare*
21 *Informatics*) to a 25-ounce, 50% editorial publication (*Architectural Record*). In view of
22 the diversity of its publications, McGraw-Hill is a member of both American Business

¹ McGraw-Hill is also a major publisher of educational and professional books, and owns and operates four TV stations, among other information and media products and services that it provides.

² McGraw-Hill's total Periodicals postage in 2003 was approximately \$17.5 million. We estimate that postage amounts to about 26% of the cost of manufacturing and distributing our Periodicals as a whole.

1 Media and the Magazine Publishers of America, and has representatives on the boards
2 and key committees of both organizations.

3 McGraw-Hill is also using the new methods of electronic publishing to satisfy its
4 customers' desires for information as they wish to receive it. Many of McGraw-Hill's
5 publications provide editorial content on publically available websites, as well as on
6 websites accessible only to subscribers, or through electronic publications in formats
7 such as Adobe PDF and Zinio.

8 Shortly after the Complaint was filed in this case, McGraw-Hill undertook an
9 analysis of the potential impact on its publications of the rates proposed by
10 Complainants. Much of the analysis was prepared through application of a Microsoft
11 Access tool provided by Time Warner to our database of mail.dat files, which contain
12 detailed information about mailings of our larger publications. Once the analysis was
13 completed for a typical issue of each such publication, the percentage rate increase or
14 decrease was applied to each publication's 2004 budget for Periodicals postage to
15 gauge the financial impact.

16 As McGraw-Hill publishes a diverse range of publications, the impact analysis
17 yielded a wide range of results. Our largest title, *Business Week*, would realize savings
18 of approximately 11%, or \$1.175 million on an annual basis. On the other hand, *Platt's*
19 *Energy Business and Technology*, which has since ceased operation, would have
20 experienced a 28.2% rate increase. The largest increase from a dollar perspective
21 would fall on *Engineering News Record*, amounting to approximately \$140,000, or 13%,
22 on an annual basis.

1 Our *Dodge* and *Standard & Poor's* publications are small in circulation, and do
2 not generate mail.dat files. We initially assumed that these publications would incur rate
3 increases on the order of 15%, as this would be in line with the average increases for
4 our other relatively small publications. We have more recently determined, however,
5 that the impact on our *Dodge* and *Standard & Poor's* publications would likely be
6 significantly more adverse due to their lower circulation. We now estimate that they
7 would incur rate increases on the order of 50%.

8 When we first performed the impact analysis, we estimated that on a corporate-
9 wide basis, McGraw-Hill could realize savings under the proposed rates amounting to
10 close to \$800,000 annually – primarily due to *Business Week*. However, that number is
11 reduced to about \$300,000 under our current analysis of the impact of the proposed
12 rates on our *Dodge* and *Standard & Poor's* publications. Notwithstanding any such
13 savings, all but three of McGraw-Hill's publications would incur substantial rate
14 increases under the proposed rates, with most of the increases well into double digits.

15 From the start of this proceeding, as in the MC95-1 reclassification case,
16 McGraw-Hill has been less concerned with the savings that it might realize overall under
17 the proposed rates than with the adverse impact of such rates on smaller publications.
18 Due largely to their lower circulation, smaller publications already bear a substantially
19 higher cost burden than larger-circulation publications, and would not likely be able to
20 avoid onerous rate increases by changing their mailing practices. Beyond the adverse
21 impact on most of McGraw-Hill's own publications (which must stand on their own
22 financially), we are concerned that the extensive de-averaging of costs and rates
23 proposed by Complainants would undermine maintenance of a broad, vibrant and

1 diverse Periodicals class, and could bring into question its long-term viability. We
2 further believe that more efficient mailing practices can be fostered and rewarded as
3 appropriate through rate design changes that are more balanced and equitable than
4 those proposed by Complainants.

5
6 **IV. Complainants' Proposal Is Fundamentally Misdirected Because**
7 **Smaller-Circulation Publications Have in Fact Borne the Brunt of the**
8 **Cost Increases Upon Which Complainants Focus.**
9

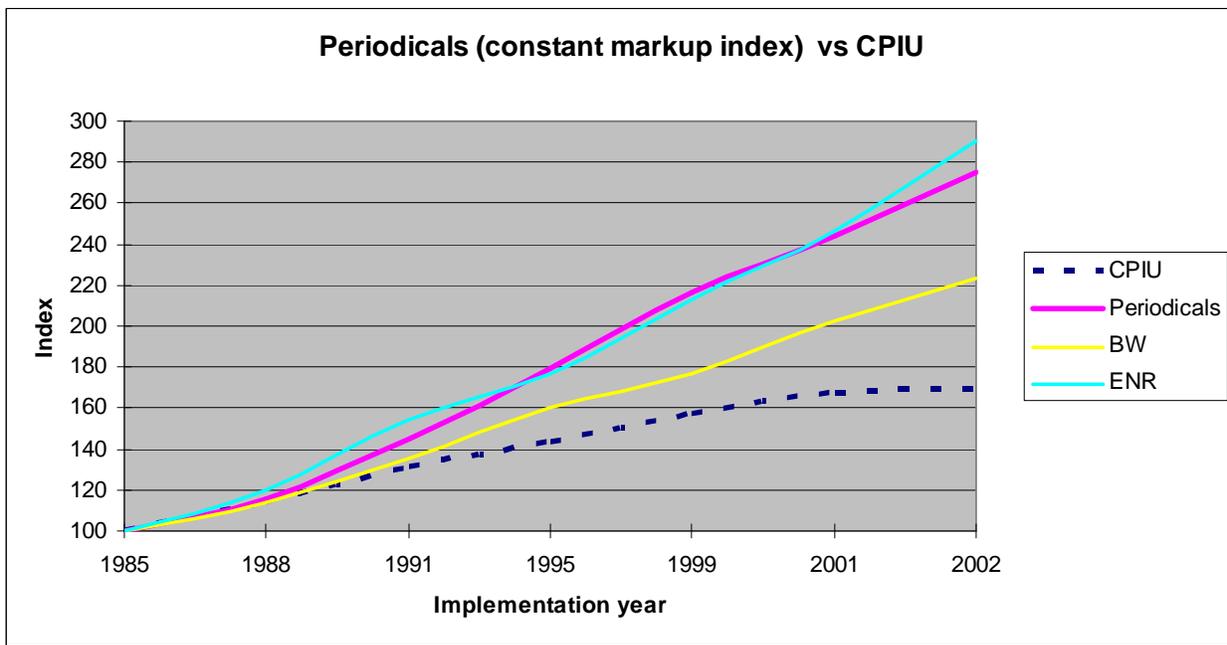
10 Testimony presented by witness Mitchell focuses on the inordinate rise in mail
11 processing costs attributed to Periodicals since the late 1980's (Tr. 3/805-08) as the
12 point of departure for Complainants' proposal in this proceeding to de-average
13 Periodicals costs and rates, which would result in enormous savings to Complainants
14 (without any change in their mailing practices, or any cost savings to the Postal Service)
15 while exposing most smaller Periodicals to corresponding rate increases. Witness
16 Mitchell illustrates in a chart that outside-county Periodicals rates, at a constant markup
17 index (which isolates the growth of attributed costs), have grown at rate considerably in
18 excess of inflation as measured by the CPI-U. He also notes that this took place over a
19 time when technological advances occurred, so in effect we have experienced *negative*
20 *technological productivity change*. While, as witness Mitchell states, "[b]y any measure,
21 the situation is troubling" (*id.* at 808), I suggest that the situation has been much more
22 "troubling" for smaller-circulation publications that lack presort density than it has for
23 large titles.

24 Chart A below was taken from the testimony of witness Mitchell and modified to
25 include some additional information. McGraw-Hill modeled postage increases for the
26 same period of time for several of its publications, including *Business Week*, a relatively

1 high-circulation magazine (with nearly a million domestic mailed copies per issue) that is
2 highly presorted, heavily palletized and extensively dropshipped, and *Engineering News*
3 *Record*, a smaller-circulation magazine (approximately 74,000 domestic mailed copies
4 per issue) that is less finely presorted, less extensively palletized, and origin-entered.
5 Using their current mailing profiles, I estimated their increased postage for the period in
6 question (holding constant a 24% markup, as did witness Mitchell, to highlight growth of
7 attributable costs), with adjustments being made for changes in the rate structure over
8 the period.

9

Chart A



10
11

12 Chart A makes clear that the constant-markup rates for *Engineering News*
13 *Record* exceed the CPI-U by approximately twice as much as do the corresponding
14 rates for *Business Week*. This indicates that smaller-circulation publications like *ENR*,
15 rather than large-circulation publications like those of Complainants, have borne the
16 brunt of the costs attributed to Periodicals since 1985. Moreover, the rate differential

1 continues to grow at an alarming rate. Even more troubling, borrowing a phrase from
2 witness Mitchell, the actual situation could become worse than the picture. The rate
3 differential would widen significantly under the proposed rate structure, with *Business*
4 *Week* experiencing an 11% decrease in rates and *Engineering News Record* a 13%
5 increase. Even if *ENR* were able to take steps to mitigate some of the increase, as the
6 Complainants suggest, the rate disparity would still grow considerably.

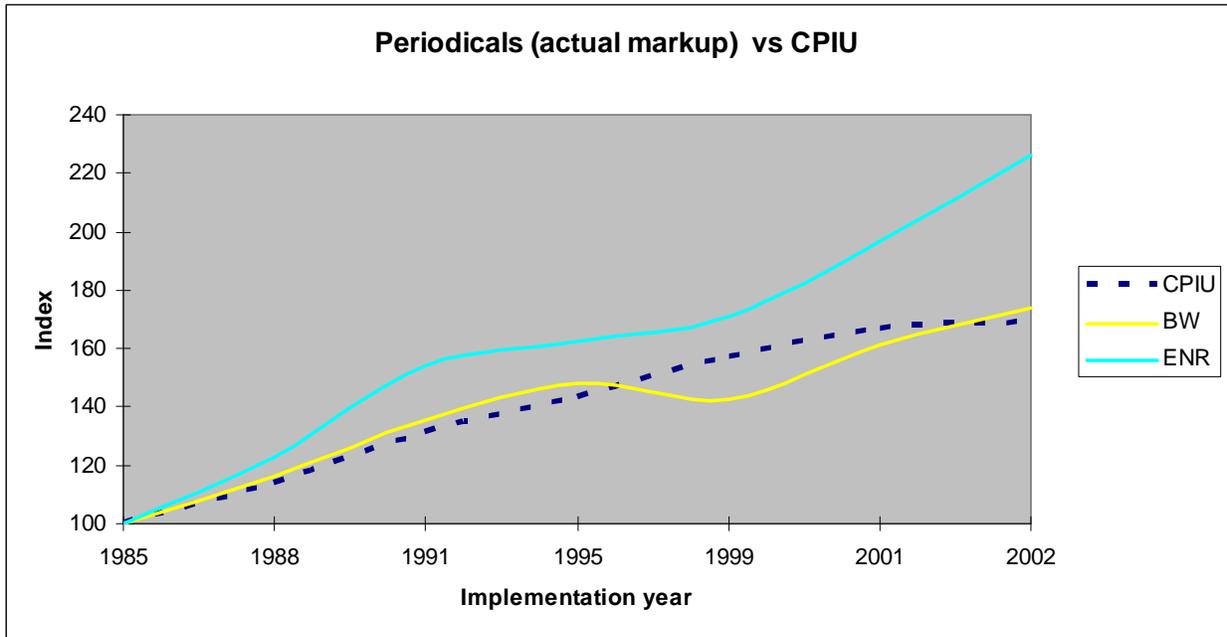
7 It is hard to believe in this light that, as stated by witness Mitchell, the current
8 rates provide signals that are “hidden by excessive tempering.” (Tr. 3/852). During the
9 time period analyzed, numerous rate design changes have been introduced that
10 primarily benefit high-volume/high-density mailers rather than relatively low-volume/low-
11 density mailers. These changes have included the introduction of destination-entry
12 pound rates, destination-entry discounts from the piece rates, a slower rate of increase
13 in low-zone pound rates, enlarged carrier route discounts, and the introduction of pallet
14 discounts, to name a few. Large-circulation Periodicals mailers, including
15 Complainants, have benefited from such rate design elements in minimizing the share
16 of Periodicals costs borne by them.

17 It is also instructive to compare the actual postage paid by relatively large and
18 small Periodicals mailers over the years. Chart B below is similar to Chart A except that
19 it reflects actual markups and postage paid. Chart C below is similar to Chart B except
20 that it includes all McGraw-Hill publications except its *Dodge* publications and *Standard*
21 *& Poor’s* publications.

22
23

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Chart B

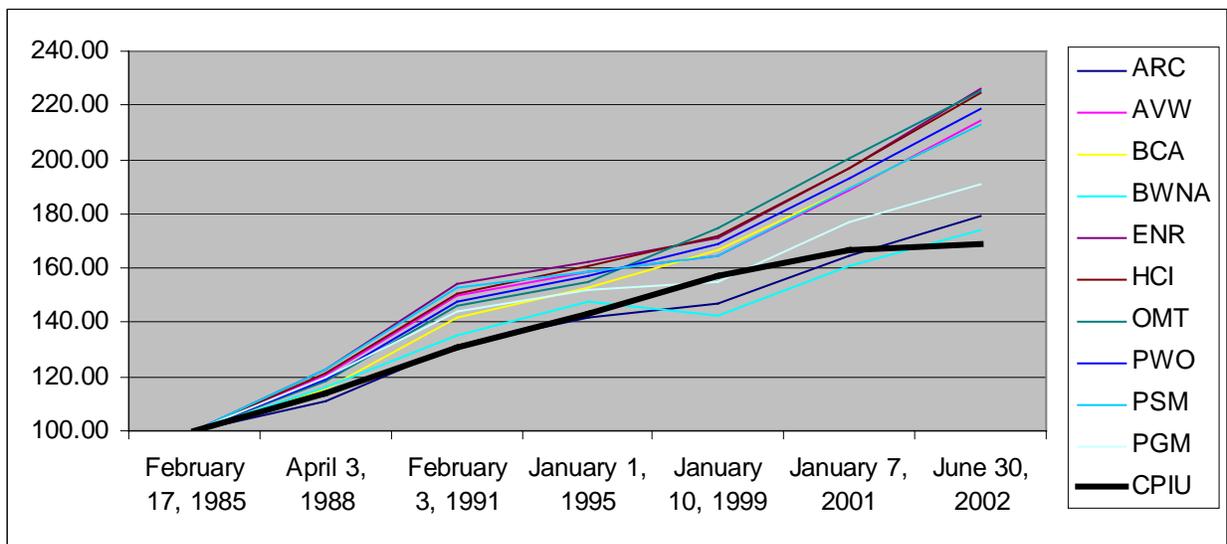


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Chart C



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8

Notably, while the average increase for regular-rate Periodicals during the period between January 1995 and January 1999 was 5%, many large publications apparently saw a decrease in postage during this period, as was the case with *Business Week*.

1 Further, by putting aside the artificial “constant 24% markup” adopted in witness
2 Mitchell’s chart, Chart B above makes clear that the actual aggregate postage increases
3 incurred since 1985 by *Business Week* – and presumably other high-circulation
4 publications like those of Complainants – have *not* generally exceeded the CPI-U, while
5 smaller-circulation publications like *ENR* have incurred aggregate postage increases
6 nearly *double* the CPI-U. Indeed, the increase for at least some of Complainants’
7 publications appears to be well *below* the rate of inflation, and under the proposed
8 rates, their postage will have *decreased* over the past decade.³

9 In this light, the remedy advocated by Complainants – a radical de-averaging of
10 Periodicals rates that would provide an enormous windfall to a relatively few large-
11 circulation publications such as those of Complainants,⁴ even with no change in their
12 mailing practices, while exposing most smaller-circulation publications to corresponding
13 rate increases – seems wholly misaligned with the chronic problem of above-inflation
14 cost increases attributed to Periodicals mail that Complainants purport to address. It is
15 the smaller-circulation publications, not the large-circulation publications, that have
16 borne the brunt of those cost allocations. It therefore seems misplaced for
17 Complainants to seize upon those cost allocations as a reason to further increase the
18 cost burden borne by smaller-circulation publications.

³ For example, Time Warner publications *Time* and *Sports Illustrated* respectively paid postage per piece of 15.6 cents and 16.8 cents in 1995 (MC95-1, Tr. 29/13508), and currently pay 17.67 cents and 18.73 cents per piece, respectively. (Tr. 1/116). These increases, 13.3% and 11.5% respectively, are well below the aggregate rate of inflation for the period, which has amounted to approximately 23%. Moreover, under the proposed rates, *Time* and *Sports Illustrated* would respectively pay 15.3 cents and 15.4 cents per piece (*id.*) – lower postage than they paid in 1995.

⁴ Based on data in the record (Tr. 1/72-75, 112-126), it appears that under the proposed rates, aggregate annual postage savings would amount to approximately \$16.8 million for Time Warner publications, \$13.6 million for *TV Guide*, \$10.7 million for Conde Nast publications, \$6.7 million for *Reader’s Digest* publications, and \$4.4 million for *News Week*.

1 To the contrary, it would seem in this light that the inordinate cost increases
2 attributed to Periodicals over the years is a reason *not* to de-average Periodicals rates,
3 or at least to proceed cautiously and incrementally in that regard. This is particularly so
4 to the extent that those cost increases may have been to a significant degree
5 *misallocated* to the Periodicals class – a possibility that has been acknowledged by
6 witness Mitchell in this proceeding (Tr. 3/1027, 1029-1031) and, I am informed, has
7 most strenuously been urged in the past by Time Warner.

8 Considering that possibility, as well as all of the rate design changes that have
9 occurred over the years, fostering increased worksharing (presortation, barcoding, and
10 drop-shipping) and palletization, I question whether the high cost increases attributed to
11 Periodicals as a whole are due primarily to inadequate price signals to Periodicals
12 mailers to modify their behavior. It seems at least as plausible that many smaller
13 publications simply lacked the circulation density (or practical opportunities to combine
14 their mail with that of other publications) in order to increase significantly their
15 worksharing and palletization.

16 At the very least, however, the sharp cost increases attributed to Periodicals mail
17 over the last twenty years despite a range of new rate incentives does indicate that
18 considerable caution is warranted before undertaking the radical rate design changes
19 proposed by Complainants. Prudence would seem to dictate a more incremental
20 approach.

21 The Postal Service, in its Answer to the Complaint filed in this proceeding, has
22 stated (at 21-23) that it is taking measured steps to foster a more efficient mail stream in
23 a manner designed to achieve consensus among the Periodicals class as a whole.

1 These steps include, for example, establishing experimental co-palletization discounts
2 in order to determine whether smaller Periodicals are in fact able to change their mailing
3 practices in meaningful ways. Proceeding cautiously in this regard will have at least two
4 major benefits. An incremental approach would lessen the otherwise harsh impact of
5 precipitous rate increases on many mailers that may not presently have the ability to
6 change their mailing practices significantly, and will allow those that can change, along
7 with their printers, the time to do so. Further, it will allow the Postal Service to evaluate
8 the feasibility of such changes and their effect on the efficiency of its operations.

9 It is critical to understand fully how rate design changes impact both mailers and
10 the efficiency of the mailstream. The rate de-averaging proposed by Complainants
11 could well lead to *inefficient* mail preparation practices, such as the movement of small
12 pallet volume to large sacks, with larger bundles prone to breakage. While witness
13 Mitchell states that “the use of sacks can in some circumstances be a low-cost, efficient
14 way of preparing and handling the mail” (Tr. 3/1011), this seems at odds with the
15 current thinking of the Postal Service. As recently as May of this year, Anita Bizzotto,
16 Chief Marketing Officer for the Postal Service, stated that a MTAC workgroup was being
17 considered to eliminate the use of sacks altogether.

18 The Commission should look to the Postal Service to take the lead if any major
19 rate design changes for Periodicals mail are to be considered fully. If some of
20 Complainants’ assumptions in this proceeding were not borne out, the unintended and
21 counter-productive consequences of adopting their proposal could be considerable.
22 Too many publishers have too much at stake to take such a gamble.

23

1 **V. A Precipitous De-Averaging of Rates Is Unnecessary for Large Periodicals**
2 **and Would Be Unmanageable and Harmful for Many Smaller Periodicals.**

3
4 McGraw-Hill publishes a wide range of Periodicals, as discussed at the outset of
5 this testimony, and we know first hand the issues facing many types of publications.
6 McGraw-Hill actively pursues worksharing and palletization for each of its publications
7 to the extent feasible. Some publications, however, face considerable practical
8 obstacles in this regard. Simply raising the cost of postage for those titles that cannot
9 palletize and dropship will not cause the activity to take place.

10
11 **A. Periodicals Mailers Already Have an Array of**
12 **Effective Efficiency Incentives.**

13
14 Mailers already have significant incentives to prepare Periodicals mail on pallets,
15 rather than in sacks, to the extent feasible. These incentives extend well beyond the
16 many pallet and drop-ship discounts under the current Periodicals rate structure. Sacks
17 are expensive not only for the Postal Service but also for everyone else involved in the
18 process. In a printing plant it is much more labor intensive to sack Periodicals mail than
19 to palletize it. Sacks are also less efficient and more expensive than pallets for
20 transporting (drop-shipping) Periodicals mail in non-postal trailer trucks. If *Business*
21 *Week* were to direct its printers to prepare its print run largely in sacks, it would incur
22 significant additional printing and drop-shipping expenses.

23 Accordingly, McGraw-Hill and its printers have increased significantly their use of
24 pallets and reduced significantly their use of sacks for most of its publications. *Business*
25 *Week* and *Aviation Week* alone have eliminated over 1,000,000 sacks on an annual
26 basis over the course of the last four years. Complainants have likewise heeded the
27 existing incentives to palletize rather than sack their Periodicals mail to the extent

1 feasible. (See Tr. 1/116-120, 122-23, 125-26). Many McGraw-Hill publications have
2 sack minimums set high at 24 pieces and pallet minimums set low at 250 pounds, which
3 tends to minimize the number of sacks and maximize the number of pallets used. Apart
4 from reducing our postage bill, these practices have also helped us to avoid incremental
5 expenses from the printer and to lower non-postal transportation costs.

6 In undertaking to reduce sack usage in favor of pallets, McGraw-Hill engages in
7 co-palletization and co-mailing to the extent feasible. A number of our *Dodge* regional
8 publications are produced at Publishers Press and participate in its co-palletization
9 program. As a result, the vast majority of these short-run publications are nearly
10 completely palletized. We have also co-mailed publications though the use of selective
11 binding technology, resulting in both larger bundles and finer presortation.⁵

12 Late last August both Brown Printing and Fairrington Transportation announced
13 plans to commence co-palletization programs and associated drop-ship pools by early
14 next year. Further, Quebecor World announced in early August that it would invest in
15 co-mailing technology to be housed in a new facility in Chicago.⁶ While full details are
16 not yet available to us, we view these announcements as positive steps in creating
17 additional opportunities for Periodicals mailers to save postage through greater presort
18 density, palletization and drop-shipping. I note that these developments are occurring
19 under current postal rate incentives, and thus further call into question the need for the
20 type of rate structure proposed by Complainants.⁷

⁵ McGraw-Hill also makes use of drop-ship pools, most notably for *Architectural Record*. It is noteworthy that *Architectural Record* is drop-shipped by a different printer than the one that prints the publication – a situation that we have been unable to duplicate for co-mailing or co-palletization.

⁶ The respective press releases of Brown, Fairrington and Quebecor in this regard are compiled in attachment A to this testimony.

1 I further note that these developments in and of themselves will not make co-
2 palletization or co-mailing available in the near future to all or most Periodicals that
3 could benefit from such programs, or to all or most Periodicals that would need to do so
4 in order to mitigate large postal rate increases under Complainants' proposed rate
5 structure. That may not occur until nearly all printers offer co-mailing or co-palletization
6 to their Periodicals customers. Moreover, in the case of many publications there are a
7 number of practical constraints that limit or preclude the publication's ability to reduce its
8 dependence on sacks, whether through co-mailing or co-palletization or otherwise.

9

10 **B. There Are Many Reasons Why Many Publications**
11 **May Not Be Able to Respond Effectively to the**
12 **Price Signals Advocated by Complainants.**

13

14 **1. *Co-Mailing and Co-Palletization Costs Absorb***
15 ***Much of the Postage Saved by Co-Mailing.***

16

17 To the extent that co-mailing or co-palletization may be an option for some
18 publications (although for many publications they are not, as discussed in parts 2 – 4
19 below), the Commission should consider the added costs incurred by publications as an
20 integral part of the potential impact of the proposed rate structure on smaller
21 publications. In McGraw-Hill's experience, those printers that do offer such services
22 typically charge as their co-mailing or co-palletization fee at least one-half of the
23 postage saved by each participating publication. Witness Schick confirmed that this
24 would be a reasonable approximation. (Tr. 2/560).⁸ When the cost to publishers of co-

⁷ Witness Schick testified that co-mailing enabled even those Periodicals with editorial percentages as high as 85% or more to drop-ship economically under current postal rates. (Tr. 435-36, 531-35). The charge for cross-country transportation in a drop-ship pool is about 6.5 cents per pound.

⁸ The printers' practice of charging co-mailing and co-palletization fees based on the amount of postage saved seems rather unique in that the fees can vary widely based on factors that have little to do with the actual co-mailing costs. This may explain why a printer would favor a rate structure that de-averages

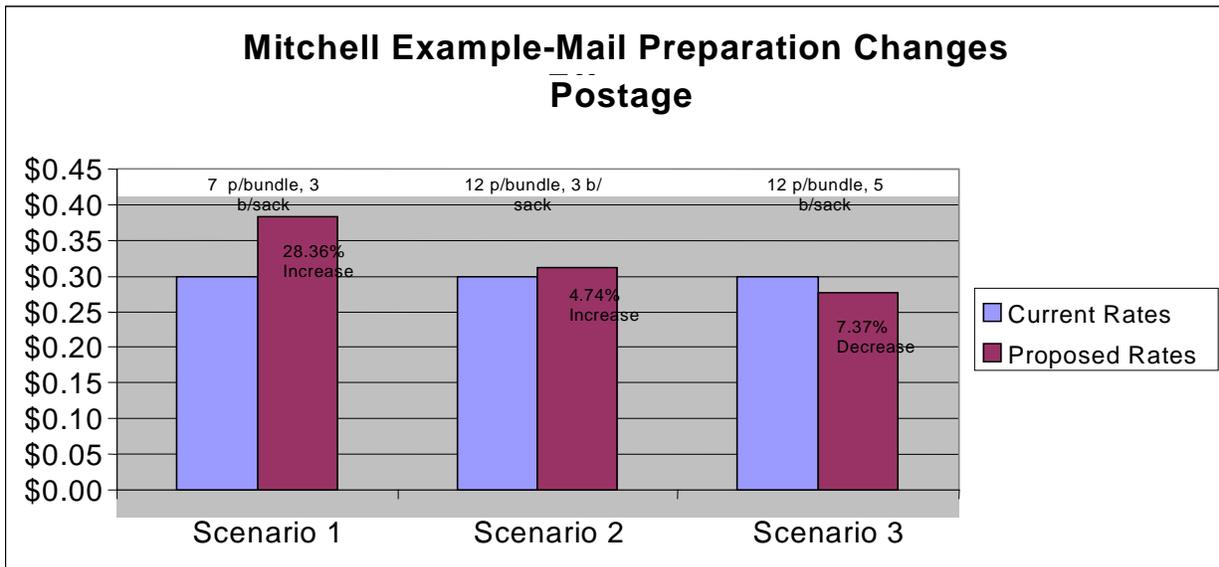
1 mailing or co-palletization is considered, it becomes clear that substantial rate increases
2 for many smaller publications could not likely be avoided under the proposed rate
3 structure.

4 Consider the response of witness Mitchell to ABM/TW et al.-T1-93, which in part
5 asked him to explain his claim that the adverse impact of the proposed rate structure
6 would be "limited." Witness Mitchell presented the following example:

7 [S]elect zone 5 as being representative of non-dropshipped publications.
8 Further, assume 10 percent advertising, in sacks, machinable, barcoded, ADC
9 presort, in an ADC container, origin-office entry, 3 ounces, 7 pieces per bundle,
10 and 3 bundles per sack. The pieces in this situation receive an increase of 28.36
11 percent. If the number of pieces per bundle is changed to 12, the increase
12 becomes 4.74 percent, and if a further change is made to 5 bundles per sack, the
13 increase becomes negative, the postage declining 7.37 percent. I found the
14 number of pieces per bundle and the number of bundles per sack to be quite
15 important.

16 Chart D below represents the information as originally presented by witness Mitchell:

17 **Chart D**



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19

costs and widens rate differentials. The wider the rate differentials are, the greater the potential postage savings from co-mailing, and the greater the potential profits to the printer from co-mailing.

1 The problem with the example is that witness Mitchell fails to explain how this
2 hypothetical publication could achieve greater bundle and sack size. Given the
3 relatively light weight (3 ounces), high editorial percentage (90%) and lack of
4 worksharing (ADC presort, origin-entered) specified for the publication, it seems likely
5 that it would have a relatively low circulation density, which would account for its
6 relatively few pieces per bundle and few bundles per sack.⁹ Assuming that co-mailing
7 would therefore be necessary to achieve the savings, the picture becomes far less
8 encouraging.

9 Chart E below is based on the same data used by witness Mitchell, but assumes
10 that half the postage savings achieved would revert to a printer as a co-mailing fee. As
11 in witness Mitchell's example, the initial scenario is that current postage of \$0.2983 per
12 piece would increase by 28.36% under the proposed rates to \$0.3828 per piece.
13 However, while changing the mail parameters under scenario 2 in witness Mitchell's
14 example supposedly leads to a rate increase of only 4.74% (\$0.3124 per piece), it
15 actually leads to a rate increase of 16.5% (\$0.3476 per piece) when the cost of co-
16 mailing is considered.¹⁰ Similarly, while further changing the mail parameters under
17 scenario 3 in witness Mitchell's example supposedly leads to a 7.37% rate *decrease*
18 (\$0.2763 per piece), it actually leads to a rate *increase* of 10.5% (\$0.3296 per piece)
19 when the cost of co-mailing is considered.

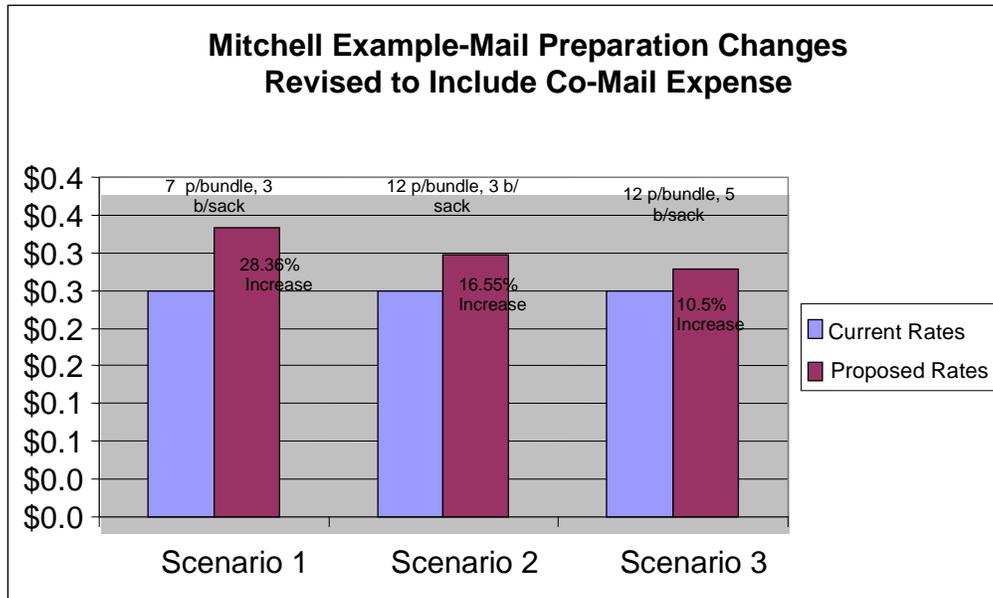
20

⁹ Witness Mitchell presented data that Periodicals with 90-100% editorial content have an average weight of 4.64 ounces and an average circulation of 80,553. (Tr. 3/1041).

¹⁰ The difference between \$0.3828 and \$0.3124 is \$0.074, half of which is \$0.0352. Adding this amount to the reduced postage yields a per piece cost of \$0.3476, an increase of 16.5% over the current rates – nearly 12% more than was stated by witness Mitchell.

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Chart E



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I note that even under witness Mitchell's most optimistic scenario, the proposed rates would increase the total cost per piece for his hypothetical publication to a level 10% above the postage that would be charged for such publication under *Standard* rates (\$0.30 per piece) when the cost of co-mailing is considered. Thus, even to the extent that smaller mailers might be able to participate in co-mailing or co-palletization, they would not apparently be able to avoid a substantial rate increase under Complainants' proposed rate structure.

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2. **Limited Opportunity for Co-mailing Or Co-Palletization Generally**

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McGraw-Hill typically enters into printing contracts for its magazines that run from three to five years. If a printer we use today does not offer co-mailing or co-palletization programs, we cannot simply shift our publications to an alternative printer. McGraw-Hill has engaged a number of printers for its magazines, including R.R. Donnelley, Quad

1 Graphics, Brown Printing, Perry-Judds and Publishers Press. Unfortunately, many of
2 McGraw-Hill's titles that could benefit from co-mailing or co-palletization are printed at
3 plants that do not currently offer such services, Publishers Press being a notable
4 exception.

5 In an attempt to circumvent this constraint, McGraw-Hill has approached a
6 number of our print vendors that do offer co-mailing or co-palletization programs to
7 explore whether the printers would accept into such programs McGraw-Hill publications
8 printed elsewhere. This effort has been unsuccessful to date due to technical issues
9 that arise when a printer lacks control over the entire production process, as well as the
10 unwillingness of printers to unbundle a service that may give them a competitive edge in
11 seeking printing contracts. Thus, an operation that thrives on volume and the ability to
12 build density is segmented in a way that hinders growth in co-mailing and co-
13 palletization. A greater willingness on the part of printers to accept into such programs
14 titles manufactured by another printer would clearly help to build a critical mass. To
15 date, we have not seen that type of commitment on any significant scale.

16 Putting aside the unavailability of dedicated co-mailing equipment and programs
17 at printing plants used by McGraw-Hill, we have found that our opportunity to co-mail
18 publications through the use of selective binding technology is often severely limited by
19 manufacturing constraints. Although we have the benefit of controlling the schedule for
20 both publications, the composition of each title plays a role as well. There are a limited
21 number of pockets on the binder, and running more than one publication at a time
22 requires additional use of these pockets. The publications must also be of a similar

1 size, as more than a 20% variation in page count creates technical problems and is
2 therefore avoided.

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**3. Production Constraints for
Time-Sensitive Publications**

6 McGraw-Hill publishes a number of time-sensitive weeklies. One example is
7 *Aviation Week*, a highly regarded source for in-depth coverage of the aerospace
8 industry. Timely delivery of *Aviation Week* is critical to its approximately 110,000
9 subscribers worldwide. In order to reach subscribers in key markets in a timely manner,
10 *Aviation Week* is shipped via airfreight to a number of domestic and international
11 locations. It is generally difficult to send palletized mail via airfreight, as there are very
12 few commercial wide-body aircraft operating outside of the trans-continental routes.
13 Smaller planes cannot accommodate pallets in their cargo holds. Therefore, while
14 McGraw-Hill seeks to enter *Aviation Week* on pallets, and does so to the extent possible
15 at some entry points, it has little choice but to use sacks for some entries (and sets 24
16 piece minimums for the sacks).

17 Rates such as those proposed by Complainants could not apparently affect this
18 situation. The cost of printing the copies at multiple plants in order to avoid airfreight
19 would be prohibitive and far outweigh the additional cost imposed on the sacks. While
20 the need for timely delivery of news-oriented publications may justify use of multiple
21 printing plants for very-large-circulation publications, the fixed costs of printing
22 operations make it economically impractical to print a smaller-circulation magazine like
23 *Aviation Week* at more than one plant.

1 *Business Week* is a large-circulation, time-sensitive news weekly. It is printed at
2 four plants domestically, located in California, Wisconsin, Virginia and Pennsylvania,
3 and two plants overseas. Although more than 90% of its volume is palletized and more
4 than half is presorted to the carrier-route level and drop-shipped to destination-SCFs,
5 we have looked for opportunities to co-palletize or co-mail *Business Week*. However,
6 the delay that such processes would impose on the production schedule for *Business*
7 *Week* generally prevents us from choosing such an option.

8 Manufacturing and shipping *Business Week* in the shortest possible time frame is
9 essential in order to deliver the magazine to its readership in a timely manner, and
10 allows us to implement alternate plans in the event of an uncontrollable situation, such
11 as weather. Typically, the last pages of *Business Week* are transmitted to the printer at
12 11:15 p.m. on a Wednesday evening. Forms are delivered off the press ninety minutes
13 later and copies of the magazine are being bound by 2:00 a.m. Most weeks, depending
14 on the characteristics of the publication, the manufacturing process is complete and all
15 copies are shipped by 12:00 p.m. on Thursday, in order to achieve timely delivery to
16 most subscribers by Saturday.

17 While on the surface a 24 to 48 hour delay to accommodate co-palletization may
18 not sound significant, it would completely disrupt our distribution plan geared toward
19 achieving delivery by Saturday. Nor would it be feasible to print *Business Week* earlier
20 in the week because news magazines must keep the editorial window open as long as
21 possible for late-breaking news stories. It is very difficult to accommodate the time
22 required for co-palletization or co-mailing in such an environment, as witness Schick
23 acknowledged. (Tr. 2/388, 414, 425, 543-44).

1 **4. Production Constraints for Small-Circulation**
2 **Publications and Loosely Bound Publications**

3
4 Periodicals published by McGraw-Hill encompass a range of circulation levels
5 and binding methods as well as publication frequencies and weights. Each of these
6 factors may present a unique set of challenges when considering palletization or co-
7 mailing. For example, *The Outlook* is a sixteen-page financial newsletter published on a
8 weekly basis by the Standard and Poor's division of McGraw-Hill, sometimes in a loose
9 leaf format. It has a subscription base of approximately 12,500 and weighs about one
10 ounce per issue. Given the relatively small volume and low weight involved, it would not
11 be practical or cost-effective to enter the mail on pallets. Out of necessity, therefore,
12 *The Outlook* is prepared in sacks with six-piece minimums. Even apart from other
13 factors that would preclude co-mailing or co-palletization of *The Outlook*, including its
14 time-sensitivity, printing contract, and relatively small circulation, co-mailing of loosely
15 bound publications would be problematic.

16 The *Dodge Daily Bulletins* present even greater constraints in this regard. These
17 publications provide the latest construction project information. The contents of the
18 publication are transmitted electronically to small print centers in four locations. Each
19 publication print run is quite small; some of these publications have as few as three
20 subscribers. They are printed on Xerox Docu-Tech machines, which in simplistic terms
21 are very sophisticated copiers. The 8 ½ by 11 inch sheets are staple-bound, and
22 generally mailed at Periodicals rates. The size of these files leaves no room for varying
23 bundle size or sack quantities (much less palletization). It would not help to mail these
24 publications together because they each serve a different geographic region. Co-
25 mailing is not provided in these small print shops. The service delay that would be

1 necessary in order to accommodate an outsourced co-mailing operation would be
2 unacceptable for a daily publication – even if a printing vendor were willing to deal with
3 such small volumes that were printed elsewhere.

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C. The Price Signals Advocated by Complainants Would Be Unmanageably Complex for Most Periodicals Mailers.

8 I have long experience with the practical aspects of optimizing mail streams of
9 Periodicals publications in terms of postage and delivery-speed as well as
10 manufacturing and distribution costs. Witness Stralberg's supposition that any
11 individual with a tenth grade math education could optimize a mail stream under the
12 proposed rates (Tr. 1/280) is an oversimplification that fails to recognize the complex
13 interrelationships that would be created by such a rate structure. The permutations
14 involved in such a structure would introduce an entirely new level of complexity. The
15 rates proposed by the Complainants would require significant modeling; files would
16 need to be presorted with various parameters numerous times to determine the optimal
17 balance of service and cost. Changing one set of parameters will inevitably have an
18 effect on others, both from postage and delivery-speed perspectives and from
19 manufacturing and distribution cost perspectives.

20 Software tools to perform this analysis do not exist today. Mail.dat software,
21 which is extensively used for mail planning today, would be of little value for this type of
22 optimization. A mail.dat file consists of a number of files organized in a manner similar
23 to a relational database. Each file contains information about a presorted mailing, some
24 detailing bundle characteristics, others detailing container characteristics and so forth.
25 The files are linked through common database elements, which allows for a variety of

1 analyses to be performed. The real strength, however, lies in the ability to modify the
2 various parameters within the mail.dat file (for example, modifying entries for drop-
3 shipment). It is not possible, however, to use a mail.dat file to vary the number of
4 copies in a bundle – a key cost driver under the proposed rate structure. As stated on
5 the web site of Idealliance, the developer of mail.dat software: “Any analysis of a mailing
6 can be fully satisfied, except analysis unique to an address”. This inability to perform an
7 analysis at the individual address level means that mail.dat software lacks the ability to
8 optimize mail under the Complainant’s proposal.

9 Absent a significant amount of software development work, subscriber files would
10 need to be analyzed under the proposed rate structure through repeated presorting
11 under various parameters. The permutations could be endless because they are
12 interdependent. For example, if a minimum bundle size of ten is set, it may affect how
13 the mail is containerized, which may lead to variations in containers, which ultimately
14 could lead to changes in entry plans. Large mailers may be able to marshal the
15 resources and expertise needed to undertake optimization of their Periodicals mailings
16 in this regard, but I question whether small mailers would be able to do so.

17
18 **VI. The Current Policies of the Commission and the Postal Service Should Be**
19 **Followed.**

20
21 **A. Any Valid Concerns of Complainants Should Be**
22 **Addressed Through Appropriate Discounts**
23 **Rather Than De-Averaging of Rates.**
24

25 The radical de-averaging of Periodicals costs and rates that is proposed by
26 Complainants in this proceeding seems akin to the proposal in MC95-1 to divide the
27 outside-county Periodicals subclass in two. That proposal would have created a new

1 subclass for “efficient” (larger-circulation) publications that would thereby have received
2 large rate decreases, while the majority of other (smaller-circulation) periodicals would
3 have received corresponding large rate increases, unless they were able to co-mail.
4 While, as here, McGraw-Hill as a whole could have benefited financially under that
5 proposal, we nevertheless opposed it because of its impact on smaller-circulation
6 publications, given the practical obstacles to co-mailing, and because we believed that
7 efficient mailing practices could more appropriately be encouraged through new and/or
8 enhanced discounts that rewarded such practices.

9 The Commission agreed with McGraw-Hill’s position in MC95-1 and rejected the
10 de-averaging of Periodicals costs and rates proposed in that proceeding. Since then,
11 the Commission has approved Postal Service initiatives to create and test several new
12 discounts designed to encourage efficient Periodicals mailing practices. These include
13 (among others) pallet and pallet/drop-ship discounts introduced in R2001-1,
14 experimental co-palletization/drop-ship discounts per piece implemented in MC2002-3,
15 and experimental co-palletization/dropship discounts per pound adopted recently in
16 MC2004-1. None of these changes were opposed by McGraw-Hill. I note that the
17 experimental discounts have the virtue of testing assumptions regarding the feasibility
18 co-palletization, as opposed to Complainants’ “ready, fire, aim” approach (Tr. 2/442)
19 that simply assumes that all Periodicals mailers will somehow find a way to adapt if their
20 rates are precipitously de-averaged.

21 These various pallet and drop-ship discounts could be expanded if warranted.
22 An experimental co-mailing discount might also be considered – to test the extent to
23 which co-mailing is presently a viable option for small-circulation publications, and

1 whether the larger bundles generated by co-mailing would impose additional bundle-
2 breakage costs upon the Postal Service. I am not presently in a position to evaluate the
3 merits of any new, expanded or enhanced discounts that might be considered along
4 these lines, much less to offer any concrete proposals. I do believe, however, that for
5 Periodicals mail in particular, providing appropriate discounts from rates that are based
6 on averaged costs is a far better approach than the radical de-averaging of costs and
7 rates proposed by Complainants, as I elaborate below.

8
9 **1. *The Potential Adverse Impact of De-Averaging***
10 ***on Most Periodicals Would Undermine the***
11 ***Fundamental Purpose of the Periodicals Class.***
12

13 As I understand it, the traditional approach to Periodicals rate design is a
14 combination of rate averaging (grouping higher-cost and lower cost mailers in
15 developing base rates) and rate discounts that balances cost and efficiency
16 considerations with the fundamental purpose of the Periodicals class – to promote the
17 widespread dissemination of diverse editorial content through preferential postal rates,
18 in view of the “educational, cultural, scientific and informational [‘ECSI’] value to the
19 recipient of the mail matter” (39 U.S.C. § 3622(b)(8)) and its role in binding the nation
20 together. The radical de-averaging proposed by Complainants seems antithetical to the
21 maintenance of a broad, vibrant and diverse Periodicals class in accord with its
22 fundamental purpose.

23 Complainants’ proposal would in all likelihood expose thousands of smaller
24 publications to large rate increases that may approach or exceed Standard rates in
25 some cases or otherwise threaten the viability of financially vulnerable publications.
26 This seems all the more anomalous considering that smaller publications have already

1 borne the brunt of the inordinate cost increases attributed to Periodicals over the years,
2 as I discussed in part IV above. To the extent that a significant portion of those costs
3 may have been *misallocated* to Periodicals mail rather than caused by any Periodicals
4 mailers, as Time Warner has long asserted, it seems especially appropriate that the
5 cost burden be shared on an equitable basis through rate averaging.

6 Why does McGraw-Hill care, considering that the savings that could be realized
7 by *Business Week* under Complainants' proposal would substantially outweigh the
8 exposure of most of McGraw-Hill's smaller publications to a range of rate increases?
9 Beyond the fact that each of McGraw-Hill's publications must stand on its own
10 financially, the answer lies in a broader perspective that recognizes the considerable
11 benefits inuring to *all* Periodicals -- large and small, low-cost and high-cost -- as
12 members of a mail class receiving preferential rates due to the ECSI value of
13 Periodicals generally.

14 Consider *Business Week* for example. Each week over 30,000 copies are
15 entered on Thursday at the Morgan facility in Manhattan. The vast majority of these
16 copies are delivered either the next day or Saturday. All of this happens at a cost of
17 approximately 18 cents per copy. In my role at McGraw-Hill I am responsible for
18 logistics on a worldwide basis and negotiate contracts with a wide variety of carriers.
19 Rest assured that no alternative avenue available to me provides the combination of
20 price and service that is afforded by Periodicals rates.

21 While we would certainly be happy to see *Business Week* pay only 16 or 17
22 cents per copy, as might be expected under the Complainants' proposal, it seems hard
23 to bemoan our plight without considering the needs of the Periodicals class as a

1 whole.¹¹ All Periodicals, regardless of the size of their distribution, contribute to the
2 purpose of the class and the reasons for its preferential treatment. The Periodicals rate
3 structure should therefore continue to accommodate a broad range of publications, not
4 simply high-circulation/low cost publications. A rate structure that marginalized small
5 publications could ultimately marginalize the Periodicals class itself and call into
6 question its long-term viability. Generally speaking, therefore, it seems that rate
7 averaging is to a considerable degree the glue that holds the class together, and the
8 price for the preferential rates afforded the class as a whole – including both *Business*
9 *Week* and Complainants’ publications.

10
11 **2. Higher-Cost Periodicals Mail Tends**
12 **to Receive Below-Standard Service.**
13

14 Complainants assert that the generally higher costs of processing sacked
15 Periodicals mail should be more precisely reflected in the rate structure. A
16 countervailing consideration, however, is McGraw-Hill’s experience that all other things
17 being equal, palletized mail generally receives better service than sacked mail. For
18 example, a 3-digit pallet entered at an ADC will generally be processed quicker than a
19 3-digit sack entered at the same facility. In our experience, the Postal Service fails
20 more often to meet delivery service standards for Periodicals mailed in sacks than for
21 Periodicals mailed on pallets.¹²

¹¹ In apt words attributed to Albert Einstein: “Not everything that counts can be counted, and not everything that can be counted counts.”

¹² The Red Tag News Association delivery reports for July 2004, while not distinguishing between sacks and pallets, indicate that nearly 40% of the copies monitored were delivered later than the Postal Service standard.

1 Consider *Aviation Week*, a time-sensitive publication printed in Strasburg,
2 Virginia that origin-enters a significant portion of its mailed copies. Over the course of
3 four weeks spanning its July 12 through August 2 issues this summer, we monitored
4 the days it took from origin-entry to final delivery of pre-selected copies of *Aviation*
5 *Week*, and kept track of whether they were mailed in sacks or on pallets, and at what
6 presort level. We found that service for sacked mail was generally slower than for
7 palletized mail on the same route, sometimes markedly so. In one Buffalo, New York
8 zip code, for example, an ADC pallet was delivered in three days while three 3-digit
9 sacks were delivered in seven, six, and three days, respectively. A number of other
10 such examples could be cited. The Postal Service's standard for delivery of this mail,
11 whether entered in sacks or on pallets, is three days.¹³

12 According to the direct testimony of witness Mitchell, the statutory policies
13 governing the Commission's recommendations include maintaining a "fair and equitable
14 [rate] schedule." (39 U.S.C. § 3622(b)(1)). It does not seem "fair and equitable" to de-
15 average Periodicals costs and rates in order to charge more for sacked mail if it
16 receives generally slower service than palletized mail. Moreover, sacked mail already
17 pays a higher rate of postage due to the existing pallet discounts. It therefore seems
18 fair and equitable to continue averaging the rates (and applying appropriate pallet and
19 drop-ship discounts) because even if palletized mail generally costs the Postal Service
20 less, pallets pay less and generally receive better service.

¹³ While we would of course strongly prefer that service variances of this type happened with less frequency, we are also cognizant of the myriad factors that can affect mail delivery. We work with the Postal Service through a number of avenues to address these factors, including dialogue with its Business Service Network and use of its e-PubWatch.

1 As pointed out in witness Mitchell’s testimony, an express ratemaking factor
2 under the Postal Reorganization Act is the “value of the mail service actually provided
3 each class or type of mail service to both the sender and the recipient....” (*Id.*
4 § 3622(b)(2)).¹⁴ Therefore, in considering whether to recommend de-averaged rates in
5 this proceeding, the Commission should consider the level of service actually provided
6 to the mail in question. In my view, below-standard service amounts to a regressive tax
7 on the affected mail. To the extent mailers of sacks receive less service than they paid
8 for, they are already in effect paying higher rates than the Commission intended.

9 It is often said that the Postal Service should behave more like private industry.
10 It is difficult to believe, however, that FedEx would substantially raise the price for a
11 service that it marketed as three-day package delivery if it in fact often delivered the
12 package in more than three days. Rather, I believe that FedEx would likely provide
13 refunds and reduce the price unless and until its service improved. I am simply
14 suggesting here that the Postal Service should continue with averaged rates for
15 Periodicals mail, whether sacked or palletized, at least unless and until equivalent
16 service is provided for sacked and palletized mail.¹⁵

17
18

¹⁴ Another statutory ratemaking policy noted by witness Mitchell is “simplicity of structure for the entire rate schedule....” (*Id.* § 3622(b)(7)). Witness Mitchell acknowledged in his direct testimony (at page 45) that “Periodicals has long been recognized as the class with the most complex rate structure.” Contrary to the statutory policy, Complainants’ proposed new rate structure for Periodicals is even more complex and, indeed, would be unmanageable for most Periodicals mailers, as I explained in part IV.C above.

¹⁵In the view of many mailers, so-called “skin” sacks – typically consisting of only six or fewer pieces, all going to the same 5-digit zip code – generally receive better mail service than sacks with more pieces that are not as finely presorted. My understanding is that the Postal Service is considering distinct rate treatment for skin sacks to the extent that they may be deemed more costly for it to handle. I express no view on this discrete issue. McGraw-Hill makes only limited use of skin sacks for service reasons.

1 **B. The Commission Should Not Abandon Its Longstanding Policy to**
2 **Promote the Widespread Dissemination of Editorial Content Through**
3 **a Low Pound Charge for Editorial Content.**
4

5 As recently as 1998, the Commission rejected a rate design proposal that would
6 have substantially increased the flat editorial pound charge on grounds that, as
7 expressed by McGraw-Hill witness Hehir, it could “undermine the historical commitment
8 (embodied in the Postal Reorganization Act) to promote the widespread dissemination
9 of editorial content through the mail.” (R97-1, Op. & Rec. Dec. ¶¶ 5783-5788).
10 Complainants nevertheless propose in this proceeding to reverse the Commission’s
11 longstanding policy in favor of the flat editorial pound charge, which has traditionally
12 been set at about 75% of the lowest zone charge for advertising content, and to impose
13 on editorial content the same zoned pound charges that apply to advertising content.¹⁶
14 McGraw-Hill does not believe that Complainants have presented any valid justification
15 in this proceeding for abandoning the “historical commitment (embodied in the Postal
16 Reorganization Act) to promote the widespread dissemination of editorial content
17 through the mail.”

18 **1. Witness Gordon**

19 The testimony by witness Gordon presents no reason for the Commission to
20 retreat from that mandate. Indeed, witness Gordon acknowledged that notwithstanding
21 the rise of the internet, the “educational, cultural, scientific and informational value that
22 periodical publications provide today is no less than ... in 1976” (Tr. 3/700) and that
23 Periodicals thus continue to play a role in binding the nation together. (Tr. 3/656-57,

¹⁶ Complainants propose a 10.1 cents per pound discount for editorial content. I note that this approach would provide high-circulation/low cost Periodicals like Complainants’ with a greater percentage reduction in their postage than would be received by low-circulation/high-cost Periodicals with the same weight and editorial percentage.

1 714). It is likewise McGraw-Hill's view that the vital role of hard-copy Periodicals is
2 undiminished, particularly for business, professional and technical publications such as
3 those published by McGraw-Hill.

4 The internet has complemented rather than displaced the role of McGraw-Hill's
5 hard-copy Periodicals. Those publications remain in strong demand because they
6 provide timely, reliable, comprehensive and cutting-edge news and analysis.¹⁷ They are
7 perceived by many as more convenient and portable than computer screens, which may
8 not even be readily available to many subscribers. Our experience is consistent with a
9 recent survey report entitled "The Internet and Daily Life", released last month by the
10 PEW Internet and American Life Project (available at www.pewinternet.org). According
11 to the report (at iii, vi), only 18% of internet users who read for pleasure do so online,
12 and only 5% do so exclusively online while 82% do so exclusively *offline*. Only 22% of
13 internet users who obtain news both online and offline do so more often online; 71% do
14 so more often *offline*. The report concluded (at v): "The integration of the Internet into
15 everyday life doesn't match its popular appeal. Most Internet users still default to the
16 traditional offline ways of communicating, transacting affairs, getting information, and
17 entertaining themselves."¹⁸

¹⁷ As reported on its website (<http://mediakit.businessweek.com/mkh-edall.html>), *Business Week's* mission statement is to "sort[] through the complexity of today's issues for business professionals" and to "separate the inconsequential from the essential. We ask tough questions in approaching any topic across our franchise: Are we being original? Are we breaking a story? Are we adding to the sum of knowledge in a way that is meaningful and important to people? If the answer is no, we don't waste their time."

¹⁸ The survey report also concluded (at v) that younger people were more likely to be comfortable with the internet than older people, and that men were more likely than women to use the internet for information gathering and entertainment.

1 While nearly all of McGraw-Hill's Periodicals feature websites (putting aside our
2 *Dodge* publications), they are a complement to the subscriber-demanded print copy.
3 The websites provide editorial content of the publications as well as ancillary material.

4 Although witness Gordon did not appreciate the continuing significance of
5 preferential Periodicals postal rates in binding the nation together, he admittedly lacked
6 knowledge of the role played by such rates in the viability of start-up magazines and the
7 economics of small-circulation magazines that are mailed long distances. (Tr. 3/739).
8 The voices of such magazines clearly play an important role in binding the nation
9 together by meeting diverse informational needs that may not otherwise be served, and
10 forming and sustaining distinct communities defined by common interests rather than
11 geographic proximity.

12
13 **2. *Witness Mitchell***
14

15 Witness Mitchell likewise failed to appreciate the role played by the flat editorial
16 pound charge in the economics of such magazines. He suggested that under
17 Complainants' proposal to apply the zoned pound charges for advertising content to
18 editorial content as well, the potentially dramatic increase in the cost of mailing a
19 publication across the country would likely be offset by the publication's marginal
20 subscription revenue (unless it is a requester publication that has no subscription
21 revenue) and/or its marginal advertising revenue (unless it is a high-editorial publication
22 that has no significant advertising revenue). (Tr. 3/860, 862-63).

23 However, contrary to witness Mitchell's explicit assumptions, (1) a publisher's net
24 subscription revenue ("circ net") may be a low percentage of the subscription price to
25 the extent subscriptions are sold through independent sales agents, as is common for

1 many publications; and (2) advertising revenue does not commonly vary directly with
2 circulation, and would not necessarily be affected by dropping or avoiding subscribers in
3 high postal zones. The common practice of publications that offer guaranteed rate
4 bases, including *Business Week*, is to base advertising rates on a circulation level
5 comfortably short of actual circulation so that rebates to advertisers will not become
6 necessary as actual circulation fluctuates. Other publications simply provide advertisers
7 with forecast circulation, without any guarantees, as in the case of many McGraw-Hill
8 publications.

9 While witness Mitchell also presents other arguments in seeking overturn the
10 Commission's longstanding policy in favor of the flat editorial pound charge, I
11 understand that the Commission rejected very similar arguments by witness Mitchell in
12 the R90-1 rate case, and I see no reason why it should reverse course now. In my
13 view, the uniform editorial pound charge is no more "discriminatory" than any "rate
14 averaging," which necessarily benefits above-average-cost mailers more than other
15 mailers. Further, in my understanding, the low editorial pound charge is set well below
16 the average (weight-related) costs of mailing editorial content (which are largely
17 absorbed in the advertising pound charges), and benefits Periodicals to the extent that
18 they mail editorial content to distant subscribers.

19 Witness Mitchell focuses on local and regional (outside-county) Periodicals, and
20 assumes that a substantial portion of them are printed and mailed in close proximity to
21 their delivery area.¹⁹ Even if he is correct that some such publications might save some
22 money if the editorial pound charge were zoned, this seems analogous to cross-town

¹⁹ I note that Complainants do not apparently publish any local or regional Periodicals about which witness Mitchell professes concern. Rather, Complainants publish a number of high-circulation/low-cost Periodicals that engage in extensive drop-shipping to their delivery areas.

1 single-letter mailers complaining that they would save money if the flat First-Class
2 stamp rate was de-averaged and zoned. The policy that nevertheless justifies the low
3 uniform pound charge for editorial content, as I understand it, is to help bind the nation
4 together by lowering the cost of mailing editorial content to distant subscribers, and
5 thereby fostering its widespread distribution throughout the nation. It therefore does not
6 seem surprising or troubling that the flat editorial pound charge may provide more
7 benefit to those Periodicals that mail editorial content to more distant subscribers.

8 In R2001-1, the Postal Service proposed to establish drop-ship discounts from
9 the otherwise flat editorial pound charge, asserting that this would address concerns
10 with Periodicals costs in a balanced way and provide further incentive for smaller
11 publications to co-mail or co-palletize and drop-ship the combined mailing. McGraw-Hill
12 and other parties expressed reservations about the proposal, noting that as structured it
13 would require increasing the flat editorial pound charge somewhat above its traditional
14 level, and that it might eventually lead to full zoning of editorial pound charges. While
15 the proposal was not included in the settlement of R2001-1, McGraw-Hill is informed
16 that the Postal Service may consider a similar proposal in the next rate case.

17 We must of course fully reserve judgment on any such proposal. However, I can
18 state that in principle, a proposal to establish drop-ship discounts from the flat editorial
19 pound charge may at least be a more balanced approach to the issues underlying this
20 proceeding than the rather drastic proposals advanced by Complainants. With such
21 discounts, those Periodicals that can drop-ship or otherwise enter their mail close to its
22 destination would see a rate reduction, while those that cannot do so would not incur

1 zoned editorial pound rates that would make it much more costly to reach distant
2 subscribers.

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Conclusion

9 McGraw-Hill has little doubt that the outside-county Periodicals rate design might
10 be improved in some respects. However, McGraw-Hill cannot agree with Complainants
11 that there is any need or justification for radically transforming the current rate structure,
12 and the Commission's longstanding policies that underlie it, in order to provide windfall
13 savings to a relatively few large publications while imposing substantial additional cost
14 increases on thousands of smaller publications that have already borne the brunt of
15 exceptional cost increases over the years.

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BROWN

LOGISTICS SERVICES

Distribution

Directions

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Special Issue

Brown Logistics Services Announces Copalletization Service for Periodicals

“Pallets provide better dropshipping opportunities, which in turn improve delivery and reduces postage.”

*Robert Williams
Manager, Postal Affairs &
Delivery Services
PennWell Corporation*

WASECA, MN August 30, 2004 – Brown Logistics Services (BLS), a division of Brown Printing Company, announced plans to provide copalletization services to its customers by January 2005. This is an initial phase of BLS’ current strategy to achieve greater distribution savings and to enhance services.

The introduction of copalletization will help offset the trend in rising paper, transportation and postal costs for customers whose copies travel in mail sacks. Benefits for participants include copalletization postage workshare discounts, expanded dropship workshare discounts and improved handling and service. Copies can now be placed on pallets for transport and delivery to the USPS. The elimination of sacks will allow bundles to move further into the postal system, thus reducing handling and speeding delivery. Where delivery time for sacked mail could take 7-14 days to reach the desired destination, copalletized mail will be entered closer to the delivery point and can average 3-9 days delivery.

Although magazines that now have a larger percentage of mail that is sacked may realize greater benefits, every customer can participate and receive the benefits without requiring additional process changes or restrictions. BLS’ copalletization service will be part of its everyday mailing and distribution operations, providing seamless mail delivery.

Robert Williams, Manager of Postal Affairs and Delivery Services, PennWell Corporation, agrees. “Copalletizing is the wave of the future for small volume periodical publications. It will help create more pallets while significantly reducing the number of costly mail sacks. Furthermore, pallets provide better dropshipping opportunities, which in turn improve delivery and reduces postage. PennWell is thrilled that Brown is going to be offering this copalletization service.”

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Bernie Schraml, Director of Distribution Services/Postal Affairs at G+J Publishing USA, says, "This is great news for the industry! The benefits of moving publications from sacks to pallets are now within reach for all publications. No matter how many magazines a publisher mails, copalletization will enable publishers to reduce their distribution costs by qualifying for copalletization and drop shipping discounts. This also gives a big boost to the Postal Service in its campaign to replace mail sacks with more efficient containerization."

In conjunction with ongoing USPS changes in rates, processes and technologies, Brown Logistics Services continues to actively work with the USPS and industry leaders to shape the future of mailing and distribution. BLS continues to evaluate and develop enhancements and service offerings as an overall strategy to better serve our customers.

Time Inc.'s Scott Lorenz, Director of Postal Operations and Systems, says, "Time Inc. views co-pal as an opportunity to drive costs out of the U.S. Postal Service for mailings that were originally in sacks. This new program represents one of the positive steps that can be realized by working closely with the USPS in an effective effort to reduce costs while continuing to meet the needs of mailers."

Brown Printing Company is a nationally recognized, high quality and high volume printer serving America's premier magazine, catalog and insert publishers. Brown is the 4th largest printer of consumer, trade and business publications in the country. Founded in 1957, Brown is a long-term industry leader printing more than 500 magazine titles for nearly 400 clients with annual sales of \$375 million and 2,600 employees. A Bertelsmann & Gruner + Jahr AG Company, Brown operates 3 state-of-the-art manufacturing facilities in the United States.

For further information, visit Brown Printing Company's web site at: **www.bpc.com**

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August 20, 2004

Fairrington Transportation announced today that it has completed contractual negotiations with several major clients to begin providing copalletization services for their client's Periodical sacked mail.

Early projections estimate an annual copalletization volume in excess of 60,000,000 pieces and an elimination of over 2,000,000 sacks.

Copal pools will be run daily and the automated process has the capability to process double the estimated annual volume.

Start up is estimated to be in December 2004 or January 2005.



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What's new?

Find out what's in the headlines at Quebecor World Inc.

August 2, 2004

Quebecor World Logistics Expands U.S. Short-Run Co-Mail Platform to Cut Costs and Improve Service for Magazine Publishers

Montréal, Canada – Quebecor World (NYSE, TSX: IQW) Logistics (QWL) is investing in the latest co-mail technology to reduce costs for short- and medium-run magazine publishers. With this investment, QWL will offer its enhanced co-mail process, the Express Collation Mailing System, which will reduce gross postage by up to 30 percent and improve overall postal distribution service.

This initial co-mail enhancement is the first phase of QWL's three-year strategy targeted at creating a multiple-pool platform that will ultimately offer three co-mail machines with at least 30 pockets each. QWL plans to invest in a new Chicago facility in early 2005 to house these enhanced co-mail capabilities in addition to its distribution operations.

"Rising paper and transportation costs – combined with the threat of postal increases – have created an ominous cloud over which we have little control," explains Karen Dauck, Director of Purchasing and Fulfillment for the Cricket Magazine Group of Carus Publishing Company. "But there's light at the end of the tunnel, after all! We are excited about this opportunity for our smaller-run publications to participate in QWL's co-mailing environment and benefit from maximum postal discounts."

Co-mail is a process that merges multiple mail files into a single larger list in order to maximize presort discounts and optimize packaging to get mail deeper into the postal system. QWL's Express Collation Mailing System is unique to the industry in that it offers simultaneous, dynamic multi-origin co-mailing and nationwide distribution. Unlike other networks, publishers need not adjust their scheduling just to enter a QWL co-mail pool.

"We view co-mailing as a great opportunity for short-run publishers and as being absolutely essential if we are to protect our titles from the pending rate increase," said Christy Martin, Distribution Director for Primedia Business Information. "The idea of a dynamic pooling tool as proposed by QWL is certainly very attractive to us and it will make it much easier for us to maximize the amount of mail eligible for co-mailing."

Postal rates are expected to increase by 7 to 13 percent by 2006. Short-run publishers will be hit the hardest in the next rate increase because they don't always have the volume to achieve worksharing discounts like long-run publishers; but QWL's Express Collation Mailing System will help to minimize the overall impact to these publishers. Since postage accounts for approximately 30 percent of publishers' total production costs, mailers are urging the USPS to increase worksharing opportunities such as drop shipping and co-mailing, to reduce the impact of rising rates.

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"These upgrades to our co-mail platform have been well planned, and will result in a seamless process to serve our many valued customers," said QWL's President, Brad Nathan. "Our Express Collation Mailing System will help the USPS streamline operations and increase worksharing initiatives; help publishers save postage dollars; and help QWL maintain superior service in distribution overall."

QWL provides logistics and mail list services for all Quebecor World and various third party customers, handling multiple commodities including catalogs, direct mail pieces, magazines (subscriber copies and newsstand), newspaper inserts, books and bulk printed product.

Quebecor World Inc. (NYSE; TSX: IQW) is one of the largest commercial printers in the world. It is a market leader in most of its major product categories which include magazines, inserts and circulars, books, catalogs, specialty printing and direct mail, directories, digital pre-media, logistics, mail list technologies and other value added services. Quebecor World Inc. has approximately 37,000 employees working in more than 160 printing and related facilities in the United States, Canada, Brazil, France, the United Kingdom, Belgium, Spain, Austria, Sweden, Switzerland, Finland, Chile, Argentina, Peru, Colombia, Mexico and India.

Web address: www.quebecorworld.com

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