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Before The
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

Postal Rate and Fee Changes, 2005) Docket No. R2005-1

INITIAL BRIEF OF THE AMERICAN POSTAL WORKERS UNION, AFL-CIO

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The American Postal Workers Union, AFL-CIO ("APWU") submits this Brief to the Commission to make three points:

1. The Commission should recommend to the Board of Governors an across-the-board increase of rates in an amount necessary to replace funds that must be escrowed in fiscal year 2006 and beyond under the terms of Public Law 108-18. As we discuss below in Part I of this Brief, this should be done because (a) it is justified by the unique circumstances of the statutorily imposed escrow requirement; (b) it is supported by sufficient data in the record in this case to demonstrate that it meets the requirements of Section 3622(b)(3) of Title 39, U.S.C., and it otherwise satisfies the criteria of the Act; and (c) it is the only viable recommendation for the Commission to make.

2. The data in the record in this case are insufficient to provide a basis for rate design changes. Any attempt by the Commission to redesign rates based on these data, which have been disavowed as a basis of rate design by the USPS witnesses who provided them, would result in a Recommendation that could not meet the criteria of the Act.

3. We have not signed the settlement in this case because across-the-board increases in rates exacerbate excessive workshare discounts. For the same reasons that we do not consider the record evidence sufficient to justify any significant rate redesign by

the Commission, we do not consider the record sufficient to justify recommendations for specific corrections in excessive discounts, even though the evidence is clear that some discounts exceed costs avoided. While we are cognizant of the difficulty of redressing rate imbalances in future cases, we have concluded that this consideration is outweighed in this case by the Postal Service's unique need to provide a base of rates that satisfies its obligation to escrow funds as required by P.L. 108-18, and the concomitant need to avoid a larger rate increase in 2007.

I. THE ACROSS THE BOARD INCREASE REQUESTED BY THE POSTAL SERVICE IS JUSTIFIED BY THE UNIQUE CIRCUMSTANCES OF THIS CASE; IT IS SUPPORTED BY SUFFICIENT EVIDENCE THAT IT MEETS THE CRITERIA OF THE ACT; AND IT IS THE ONLY VIABLE OPTION BEFORE THE COMMISSION

A. An Across-The-Board Increase Is Justified By The Unique Circumstance That An Escrow Requirement Has Been Imposed By Law; But The Law Does Not Provide A Basis For Attribution Of The Escrowed Funds

Under Public Law 108-18, postal revenues totaling more than $3 billion per year must be escrowed and not expended. Just as the law does not permit the escrowed funds to be spent, it provides no basis for allocating or attributing them. The Commission may take official notice of the fact that particular uses have been proposed for the escrowed funds in pending legislation. But until legislation passes, it would be speculation to say that any particular use will be directed by Congress or carried out by the Postal Service. This means that, by act of Congress, more than $3 billion per year in postal revenues must be set aside for no particular use. The amount required to be placed in escrow each year will grow inexorably under present law, exceeding $3.3 billion in 2007 and reaching more than $4 billion annually by 2010. (Tayman Testimony USPS-T-6, at 11.) This is an

extraordinary circumstance, and one the Postal Service should not be required to ignore or treat as ordinary. It is necessary and appropriate for the Postal Service to make provision for the escrow fund by adjusting its rates.

The appropriateness of treating the increase needed to make provision for the escrow fund as an across-the-board expense is illustrated by another provision of P.L. 108-18. Under the law, the annual reductions in CSRDF contributions by the Postal Service were used in 2003 and 2004 to reduce postal debt. In 2005, these savings are being used to hold postal rates unchanged and to reduce postal debt. Id. This effect on postal rates is the reverse side of the escrow coin. Just as the savings from the reduction in CSRDF contributions are avoiding postal rate increases, when the same amounts are held in escrow, they will have an across-the-board upward effect on postal rates.

Just as the funds cannot be expended, they cannot be allocated or attributed to any particular class or type of mail. P.L. 108-18 requires the escrowed amounts to be treated as "operating expenses." This requirement is a virtual mandate to adjust rates as a means of compliance with the escrow requirement. As in the case of overhead or institutional costs of other kinds, there is no basis for attributing these funds. But unlike overhead costs or institutional costs of other kinds, the escrowed funds make no contribution to the operations of the Postal Service; neither are they available to pay or reserve against the financial obligations of the Service. In contrast to other unexpected cost increases, such as spikes in energy prices, that amplify costs already present in the system, the escrow requirement is wholly external and provides no basis for attribution. These costs are truly a unique external financial imposition on the Service.

It is also useful to contrast these circumstances with the circumstances that led the Postal Service to propose an across-the-board increase in 1994. In R94-1, the Postal Service contended that it faced unique circumstances because it had many needs:

- It needed to satisfy is revenue requirement.
- It needed to improve service.
- It needed to minimize disruption to mailers.
- It needed to respond to and meet changing market conditions. And
- It needed to prepare for impending classification reform.

R94-1 Opinion and Recommended Decision ¶¶ 1000-1001.

With all due respect to the difficulties faced by the Postal Service in 1994, we observe that history has shown that the circumstances relied on by the Postal Service in its attempt to justify its proposal for an across-the-board increase in that case were not unique. At most, they were a matter of degree. This is in sharp contrast to the imposition of a requirement that the Postal Service place more than $3 billion per year into an escrow fund with no stated purpose.

The present circumstance are also different in kind from the circumstances that led the Commission to approve a settlement proposed by the Postal Service in R2001-1. In that case, the Commission decided that the extraordinary circumstances of the recent terrorist attacks against the World Trade Center and by sending anthrax through the mail, made that settlement "an appropriate alternative to the traditional approach to omnibus rate cases... ." Opinion and Recommended Decision in R2001-1, at 108.

As we see R2001-1, the Commission responded to circumstances that were so extreme that they created extraordinary cost and revenue pressures on the Postal Service that, in the Commission's judgment, justified a non-traditional approach to rate setting. In this case, the escrow requirement, while it lacks emotional impact and drama, also is

unique and demands a similarly unique response. It is a very large, recurring externally imposed cost that must be built into rates.

It is useful to observe, as Postal officials have, that this case serves only the narrow purpose of making provision for the escrow fund.

B. Record Data Are Sufficient To Show That The Across-The-Board Increase Meets The Criteria Of The Act But They Cannot Support Rate Re-Design

Postal Service Witness Maura Robinson (USPS-T-27) testified at length concerning the way in which the proposed across-the-board increase meets the criteria of the Act. She confirmed, in part by reference to the testimony of Witness Kay (USPS-T-18), that the evidence presented by the Postal Service demonstrate that the proposed rates will result in revenues that cover incremental costs for each class of mail or type of mail service. Robinson Testimony at USPS-T-27, pp. 4-5, 16-17; see also Exhibit USPS-27E. This evidence that the objective standard of Section 3622(b)(3) is met in this case has not been seriously challenged by any intervener.

In our view, the across-the-board approach proposed by the Postal Service also sufficiently satisfies the other criteria of the Act to warrant the Recommendation of the Commission. As we see it, the proposition that the Postal Service needs a rate increase now, in the face of nearly $6.5 billion in costs during the next two fiscal years, is self-evident. It would not be fiscally prudent or sound to plan on borrowing to meet these costs, because they are readily predictable and ascertainable now and can be provided for through the proposed rate increase. If legislation to change the escrow requirement does not pass, the Postal Service will face a very large deficit by the end of 2007 and be facing

the need at that time for such a large increase that it could cause real damage to the Postal Service. If legislation is passed that modifies the financial impact of the escrow requirement, a possibility that is becoming ever less likely given White House opposition, then either the Commission or the Governors can take appropriate action in response.[1]

It is also significant that the Postal Service has made a strong commitment to file another omnibus rate case of the traditional sort in the near future. In the September 13, 2005, letter from the Board of Governors, a copy of which congressional leaders have forwarded to the Commission for comment, the Governors state:

> As we consider proposed changes to the ratemaking process, it is also our belief that the Postal Service should initiate a final omnibus rate case under the current rules of the Postal Rate Commission, with metrics similar to the case now pending. If the Postal Service is unable to recover certain increases in costs experienced since the last omnibus case, it would be at a significant deficit when moving into a price-cap regime.

Thus, the interests of those, like the APWU, who believe that there are distortions and unfairness in the present rate design, will be addressed in a forthcoming case. If that were not the so, the APWU would be opposed to the proposed across-the-board increase, because we are of the view that the Postal Service must address rate design issues, particularly workshare discount issues, on the basis of accurate updated financial and operations data, in the near future As we explain in more detail below, however, the data submitted by the Postal Service in this case do not provide a basis for that re-examination and redesign.

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[1]Postmaster General Potter has made a commitment to reevaluate the Service's financial needs in the event legislation is enacted relieving the Service of the escrow requirement. Potter Testimony USPS-T-1, p. 7.

II. THE DATA IN THIS CASE ARE INSUFFICIENT TO PROVIDE A BASIS FOR RATE REDESIGN

It is readily apparent from the presentations made by Postal Service witnesses in this case that the Postal Service data submissions are intended to demonstrate that the proposed rates for each class and type of mail will bear its attributable costs, in compliance with 39 U.S.C. § 3622(b)(3); the data were not intended to support new or modified rate designs, and that it would be impossible to base redesigned rates on the data in the record. As Postal Service witness Abdirahman states in response to POIR No. 1a:

> The Postal Service's across-the-board rate increase proposals do not rely on the results of the special cost studies presented in this case; those results have only been used to estimate final adjustments to the rollforward model. Under these circumstances, the Postal Service used the cost methodology from the R2001-1 case, the BY 1999 nonautomation/automation cost methodology, to develop the cost studies found in USPS-LR-110. However, the Postal Service expects to continue consideration of alternative cost study approaches prior to the filing of the next omnibus case.

A specific example of the problems caused by this approach is also discussed by Mr. Abdirahman's response to POIR No. 1a. Asked to explain apparent anomalies in the cost data supplied by the Postal Service for presorted and nonpresorted letters, Mr. Adirahman explained that a:

> ... change in the treatment of the tallies resulted in costs being moved from the high volume automation presort letters category to the lower volume nonautomation presort letters category. Due to the large volume differences between the two categories, the nonautomation presort letters unit costs increased dramatically, while the automation presort letters unit costs decreased slightly. Consequently, the worksharing related savings estimates for the nonautomation presort letters rate category decreased, while those for the automation presort letters rate categories increased. ...

In oral testimony (Tr. Vol. 4, at 1143) Mr. Abdirahman confirmed that the same problem caused by the misallocation of costs between automated and non-automated workshared mail is also a problem with the allocation of costs of Standard A letters.

Mr. Abdirahman also confirmed that this problem makes it impossible to use the cost data to produce reliable results, regardless of the methodologies applied. He testified that changing from Postal Service methodology to PRC methodology as shown in Table 3 on page 19 of his testimony, which compares results using Postal Service methodology as compared to results using PRC methodology, does not resolve the problems with his data. (Tr. Vol. 4 at 1146).

Mr. Abdirahman also confirmed that a change in the methodology would be likely to result in different results and the alternative methodology "may be more appropriate." Answer to POIR 1a, p. 4.

Another significant anomaly unexplained in this record is the apparent increase in manual costs associated with the outgoing secondary processing of flats since R2001-1, despite an ongoing flats automation effort. Asked to explain this apparent inconsistency, USPS witness McCreary stated "I do not know of any reason why we would have additional manual processing in that." (Tr. Vol. 5, at 1744.) Nor could he say for sure why there should be an increase in manual processing costs in incoming MMP and incoming FCP. Id. at 1745.

Similarly, when Postal Service witnesses Kelley and Cutting were asked to defend the methodologies underlying their testimony, they explained that they were simply updating earlier studies. Mr. Kelley explained that, with regard to the choice of a proxy "the task I had was to update the previous methodologies for the same rate categories .... I was

just trying to update the previous methodology, the rate categories in there." (Tr. Vol. 7, at 2947-51). Asked to justify combining high density and saturation mail, USPS witness Cutting explained "I did that because that was the methodology that I was replicating." (Tr. Vol. 4, at 862) And asked to explain why he chose to use a particular definition based on DMM, Mr. Cutting explained (id. At 864):

> My testimony doesn't deal with rates so I actually don't have an answer as to why it was designed in this way.

III. DESPITE APWU'S CONCERN ABOUT EXCESSIVE WORKSHARE DISCOUNTS, AN ACROSS-THE-BOARD RATE INCREASE IS NECESSARY; NO VALID RATE REDESIGN WOULD BE POSSIBLE BASED ON THE RECORD IN THIS CASE

The APWU will not sign the settlement in this case, but we are not seeking to prevent the Commission from recommending an across-the-board increase in rates commensurate with the amount sought by the settlement agreement. We are not signing the settlement agreement because an across-the-board increase will exacerbate the problem of excessive workshare discounts that led to our objections to the settlement in R2001-1. As USPS witness Taufique testified (USPS T-28, at 4):

> Unlike in more traditional approaches to rate cases, I did not use special cost studies data that would ordinarily provide a basis for the design of rates. Instead, the policy directive described in the testimony of witness Potter (USPS-T-1) served as the guiding principal for rate development in this across-the-board proposal. Subject to the constraints and exceptions described below, our general objective is to increase all rates and fees, including workshare rates, by the same percentage. The result of this approach is that workshare rates and discounts, will tend to increase by roughly the same amount.

As we noted above, the data in this case are flawed in ways that cause anomalous results. This occurs, for example, because of misallocation of costs between automation

presort and nonautomation presort – a problem that affects costing of both First Class and Standard A mail. Another example is provided by the unexplained increase in manual costs for flats processing – an operation that has undergone substantial additional automation since R2001-1. In each of these examples, the problem is apparent, but the record in this case does not provide the data necessary to correct the problem.

The APWU is depending upon the representations of the Board of Governors and other postal officials that the Postal Service will, as promptly as possible, submit a traditional omnibus rate case to the Commission that will provide an opportunity to examine and redesign rates based upon sufficient and appropriate data. It will be important, for example, to re-examine the method by which the Postal Service calculates the cost of Bulk Metered Mail letters (BMM) for purposes of determining the costs avoided by worksharing of First Class mail. USPS witness Abdirahman confirmed that BMM is the appropriate benchmark for First Class workshared mail. He also confirmed that the cost of processing all metered letter mail is used as a proxy for the cost of processing BMM, despite the fact that single piece metered mail is more expensive to process than BMM. (APWU/USPS-T-21-6):[2]

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[2]He stated (APWU/USPS-T-21-6):

"BMM letters are machinable mail pieces that are entered in full trays and weighed into the entry facility as "meter bypass," meaning that they bypass the 020 meter belt operation. They are then routed to the MLOCR-ISS operation. Other metered letters are typically entered as bundles. Those mail pieces arrive at the entry facility mixed with other collection mail pieces. They incur costs related to dock operations and would also incur the costs required to cull them from the residual collection mail. The mail could be culled manually by mail handlers or by postal equipment such as the Dual Pass Rough Cull system. Once culled, the bundles are routed to the 020 operation where they are unbundled, faced, and trayed. If the mail is machinable, it would be routed to the MLOCR-

In these and other areas, we urge the Commission to recognize the limited nature of the data in the record in this case. Other interveners may have sought to recommend alternative rates to the Commission, as did the APWU, but they have been unable to do so based on the available data. Thus, a ValPak witness testified (Tr. Vol. 9, at 5692-5693):

> A. I am not cognizant enough of Witness Kelly's library reference to change the volume of DALs and work through it to what the cost implications would be. I'm not able to manipulate that library reference to that end.
>
> Q. So how does anybody use the volume forecast that you've presented, then, if it hasn't been converted into new cost allocations?
>
> A. I would hope that the Commission would have that capability, and I would hope that Mr. Kelly would have that capability.

We find disquieting the notion that the Commission might undertake to perform extra-record rate calculations, not urged by any party in this case, and to issue a Recommendation based on such calculations. We seriously doubt that any party would truly want the Commission to proceed in such a manner. The rate-making process, with its elaborate written examination and cross-examination plus oral cross-examination would be thwarted by a process that would permit the Commission to issue Recommendations based on calculations that have never been subjected to the exacting scrutiny of the rate proceeding. An example of the difficulties that could arise is provided by an exhibit that was entered into the record during cross-examination of USPS witness Abdirahmin. With regard to the validity of the table, Mr. Abdirahmin testified (Tr. Vol. 4, at 1168-69):

ISS operation."
See also Tr. Vol. 4, at 1151-52.

Q ... . So that if ... as I would see it, the data that you submitted in Table 1 and Table 3 are a leaky boat, this is the deck furniture that you changed in response ... to the MMA, is that correct?

A That's correct.

No party is more determined than the APWU to revisit the issue of costs avoided and the appropriateness of workshare discounts. Unfortunately, the data available at this time are not sufficient for that task; so we will await the forthcoming omnibus rate case for that reexamination.

IV. CONCLUSION

The Commission should promptly recommend to the Board of Governors an across-the-board rate increase commensurate with the rates sought by the Postal Service in this case, in reliance on the commitment of the Postal Service to submit a traditional omnibus rate case to the Commission in the near future.

Respectfully submitted,

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