

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

---

POSTAL RATE AND FEE CHANGES  
PURSUANT TO PUBLIC LAW 108-18

---

:  
:  
:  
:

Docket No. R2005-1

REPLY BRIEF OF THE UNITED STATES POSTAL SERVICE

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.  
Chief Counsel

Kenneth N. Hollies  
Eric P. Koetting  
Nan K. McKenzie  
Sheela A. Portonovo  
Brian M. Reimer  
Scott L. Reiter  
David H. Rubin  
Michael T. Tidwell  
Keith E. Weidner

475 L'Enfant Plaza West, S.W.  
Washington, D.C. 20260-1137  
202/268-2989

October 3, 2005

Table of Contents

- I. INTRODUCTION.....1
  
- II. NEITHER THE “BREAK EVEN” REQUIREMENT OF THE POSTAL REORGANIZATION ACT NOR PUBLIC LAW 108-18 MANDATE THAT CUMULATIVE NET INCOME BE SUBTRACTED FROM THE REVENUE REQUIREMENT .....2
  - A. The Postal Reorganization Act Gives the Board of Governors the Authority and Flexibility to Provide the Nation with a Sound and Effective Postal System.....3
  - B. The Statutory Scheme Supports the Postal Service’s Revenue Requirement.....7
    - 1. The Postal Service’s revenue requirement does not conflict with the plain meaning of section 3621.....7
    - 2. Section 3621 must be read together with the Postal Service’s authority under section 3622 to determine the timing and amount of rate and fee changes.....12
    - 3. Other provisions of the Act provide guidance in interpreting section 3621.....14
      - a. Section 2003(c).....15
      - b. Section 2009.....15
      - c. Section 2005.....15
    - 4. Nothing in the Act’s legislative history conflicts with the Postal Service’s interpretation.....16
    - 5. Judicial and Commission precedent support the Board’s financial policy judgment in this case.....17
      - a. To the extent the Act requires “break even,” it requires “break even over time”.....17
      - b. The Commission has recognized that sound financial management may require the Postal Service to maintain some kind of reserve in order to operate efficiently.....19
      - c. The cumulative net income affords the Board flexibility over the exact timing of the next rate case.....19
      - d. Judicial precedent demonstrates that the Commission should not intrude upon the Board’s financial policy decisions.....20
    - 6. The pending reform legislation’s explicit authorization of “retained earnings” has no bearing on whether the Act currently authorizes the Postal Service to maintain a cumulative net income.....23
  - C. The OCA’s and Valpak’s Flawed Interpretation Misrepresents the Statute and Would Interfere with the Board’s Sound Financial Policy Determinations.....25

1.	The OCA’s and Valpak’s interpretations conflict with the statutory scheme.....	25
2.	The Postal Service’s revenue requirement reflects its policy choices to reserve net income and fund the escrow through a rate and fee increase.....	27
3.	The Commission should not reduce the revenue requirement on this record.....	28
D.	Valpak and OCA Misrepresent Public Law 108-18 When They Assert That it Restricts the Postal Service’s Revenue Requirement in this Case.....	29
III.	ARGUMENTS REGARDING COSTING ISSUES PRESENTED BY THE PARTIES IN THEIR INITIAL BRIEFS IDENTIFY NO ADEQUATE BASIS TO DEPART FROM THE SETTLEMENT RATES.....	32
A.	The Consequences of an Appropriate Modification to the DAL Adjustment are Not as Significant as Valpak Would Suggest.....	34
B.	The Established Costing Systems and the Settlement Rates Are Both Consistent with the Range of Ways in Which the Postal Service Actually Handles ECR Saturation Mail in the Real World.....	39
C.	The Commission Should Disregard the OCA’s Blatant Attempt in its Initial Brief to Attack the Postal Service’s Costing Proposals with Non-Record Materials.....	46
IV.	INTERVENOR ARGUMENTS IN OPPOSITION TO THE ACROSS-THE-BOARD PROPOSAL SHOULD NOT INFLUENCE THE OUTCOME IN THIS PROCEEDING.....	51
A.	The Valpak Trifecta: Wrong On The Law, Wrong On The Facts And Wrong On Commission Precedent.....	51
1.	There is no basis for Valpak’s legislative interpolation.....	52
2.	The evidentiary record is at odds with Valpak’s insinuations.....	53
3.	Valpak mischaracterizes and misapplies Commission Precedent.....	59
B.	Alternative Pricing And Rate Designs Should Be Rejected.....	61
1.	Valpak’s flawed analysis of the pricing criteria does not support a deviation from the Stipulation and Agreement.....	61
a.	Valpak mistakenly seeks to convert custom into law.....	62
b.	Valpak’s conclusions rest upon an unstable foundation.....	62
c.	Valpak’s Brief belatedly singles out a victim.....	65
2.	Valpak’s desire to avoid any escrow burden for Standard ECR blurs its reading of § 3626(a)(6)(A).....	65
3.	Valpak’s carping about the procedural resolution of Docket No. R2005-1 is unfounded.....	69
4.	The OCA presents no real alternative to the rates and fees referenced in the Stipulation and Agreement.....	70
5.	The proposed fee for the electronic option for return receipt	

service is fully supported on the record.....72

6. The Internet/Phone Change-of-Address charge is a result of  
third-party requirements.....74

CONCLUSION

## I. INTRODUCTION

In its Initial Brief, the United States Postal Service summarized the evidence of record in this proceeding and explained why, in light of that record, the Commission should recommend the rates and fees proposed in the Stipulation and Agreement. Most of the other parties that filed initial briefs, given their support for the Stipulation and Agreement, advocated the same conclusion. Because all of the major facets of the case were discussed in the earlier brief, the Postal Service will not attempt to readdress every matter touched upon in that document. Instead, in general, appropriate views are expressed in this brief in the context of responding to the specific arguments in the initial briefs of the few parties that oppose the settlement rates.

Especially in light of the relatively short interval between initial and reply briefs, however, the mere fact that the Postal Service has not chosen to respond to every argument presented in every initial brief should not be interpreted as agreement by the Postal Service with points it has not addressed. In particular, parties vary in terms of the reasons and rationales by which they reach the conclusion that the settlement rates are appropriate under the totality of circumstances facing the Postal Service and the mailers. It is not necessary for the Postal Service to agree with each of those reasons and rationales in order to join with the large majority of parties who have embraced the settlement proposal as the best means of achieving the financial objectives necessary to respond to the unique challenges posed by Public Law 108-18. In this brief, the Postal Service demonstrates why the few parties advocating that the Commission set forth on a different path have failed to undermine either the factual or the legal bases for recommendation of the proposed settlement rates and fees.

II. NEITHER THE “BREAK EVEN” REQUIREMENT OF THE POSTAL REORGANIZATION ACT NOR PUBLIC LAW 108-18 MANDATE THAT CUMULATIVE NET INCOME BE SUBTRACTED FROM THE REVENUE REQUIREMENT

The OCA and Valpak propose to reduce the Postal Service’s revenue requirement by approximately \$ 2.578 billion. Each would offset estimated FY 2006 test year costs with the Postal Service’s cumulative net income at the end of FY 2005.<sup>1</sup>

The OCA concludes that test year costs remaining after the offset (\$ 303 million) should limit the overall rate increase to no more than 0.8 percent. Alternatively, the OCA proposes that the Commission could recommend the settlement proposal’s 5.4 percent increases, but require that rate changes be implemented no sooner than August 15, 2006.<sup>2</sup>

Valpak also proposes reducing the revenue requirement by the “full amount” of the cumulative net income. Valpak Brief at I-19. “Pending consideration of the issue in the next docket,” however, Valpak states that, “at a bare minimum,” the revenue requirement should be reduced by one-ninth of the cumulative net income. Valpak also argues that the revenue requirement should be reduced by the full amount of the net income estimated for FY 2006 under the Postal Service’s proposed rates (\$ 281.473 million). Combined, the two reductions would amount to \$567.824 million. *Id.* at I-20.

Both the OCA and Valpak argue that the Postal Reorganization Act (Act) and P.L. 108-18 require the proposed reductions. They contend that the Act does not permit the Postal Service to maintain cumulative net income and simultaneously raise rates

---

<sup>1</sup> Initial Brief of the Office of the Consumer Advocate (Revised) at 5-7; Initial Brief of Valpak Direct Marketing Systems, Inc. and Valpak Dealers’ Association Inc., at I-13-20.

<sup>2</sup> The OCA prefers this approach, since it would cause rates to “better reflect the escrow payment in FY 2007,” if the escrow requirement extends beyond FY 2006. OCA Brief at 5, n. 1.

and fees by an amount sufficient to cover test year costs. They claim that net income combined with the revenue from proposed increases would violate the “break-even” requirement embodied in 39 U.S.C. § 3621. They further argue that P.L. 108-18 dictates that any net income resulting from that legislation must be used to postpone new rate increases. OCA Brief at 22-26; Valpak Brief at II-13-16. Their arguments are tantamount to a claim that the broad discretion afforded the Board by section 3622(a), to determine when a proposed rate change is in accord with the public interest and the policies of the Act, cannot be exercised in the presence of cumulative net income.

The Commission should reject the OCA’s and Valpak’s unwarranted proposals. Neither the Act nor P.L. 108-18 restrict the Postal Service’s financial policy options by requiring it to deplete accumulated net income prior to seeking rate increases based on costs estimated for a test year under the Commission’s rules. On the contrary, the Act, as it has been construed for many years by the Commission, the Postal Service, and the courts, was intended to give the Postal Service considerable flexibility to manage its finances and operations. Such flexibility in current circumstances would include the option of funding the escrow requirement through the settlement rates. Nor do the Act and P.L. 108-18 restrict the timing of rate increases that the Board of Governors determines under section 3622 to be in accord with the public interest and the policies of the Act.

A. The Postal Reorganization Act Gives the Board of Governors the Authority and Flexibility to Provide the Nation with a Sound and Effective Postal System

Postal reorganization arose out of conditions reflecting the inability of the former Post Office Department to deal effectively with the demands of operating a massive

public business enterprise in a complex economy. As noted by the influential Kappel Commission Report,<sup>3</sup> which helped launch legislative change in 1970, the postal system was in crisis, particularly financially. The Report stated:

The Postal financial picture is bleak. Because revenues from postal users do not cover postal costs, the Post Office is financed jointly by the mail user and the taxpayer, the taxpayer covering what the mail user does not.... The deficit is a growing and unnecessary drain on tax funds, postal costs are far higher than they should be, and postal rates are irrational and often inequitable.

*Id.* at 22. Furthermore, the system was dominated and debilitated by the phenomenon of "no control," which deprived responsible officials and managers of the tools necessary to operate efficiently and effectively. *Id.* at 33-34. In particular, financing by the Treasury proved to be a major structural impediment to efficient operations, planning, and improvement through capital investment. *See Id.* at 34-37.

In reorganizing the postal system, Congress intended to create the Postal Service as an effective businesslike organization.<sup>4</sup> To accomplish this objective, it wanted to provide the Postal Service with greater bureaucratic independence, thereby seeking to free postal operations from the partisan delays that had accompanied direct political supervision. S. Rep. No. 912, 91st Cong., 2d Sess. 2-4 (1970); H.R. Rep. No. 1104, 91st Cong., 2d Sess. 5-6, 11-21 (1970). Pertinent legislative history emphasizes the conclusion that "the Postal Service is a public service but there is no reason why it

---

<sup>3</sup> *Towards Postal Excellence: The Report of the President's Commission on Postal Organization* (June 1968) (hereinafter "Kappel Commission Report").

<sup>4</sup> In *Franchise Tax Board of California v. United States Postal Service*, 467 U.S. 512, 520 (1984), the Supreme Court concluded that Congress "launched [the Postal Service] into the commercial world," giving it "the status of a private commercial enterprise" through a "general design that the Postal Service 'be run more like a business than had its predecessor, the Post Office Department.'" *Loeffler v. Frank*, 486 U.S. 549, 556 (1988) (*quoting Library of Congress v. Shaw*, 478 U.S. 310, 317 n.5 (1986)); *Franchise Tax Board*, 467 U.S. at 530).

cannot be conducted in a businesslike way." *Id.* at 11. Congress sought to achieve that objective by providing for a tenure system, political independence, and managerial authority over labor relations, postal rates, and financing. *Id.* at 12-19.

The Kappel Commission recommended several measures to meet the problems of the old system. Regarding the limitations presented by the prior system of funding, it discussed unrestricted access by management to the postal fund and establishment of separate accounts to finance capital investment among possible solutions. *Id.* Capability to initiate ratemaking and a flexible and varied borrowing authority were also considered important. *Id.*<sup>5</sup>

The Postal Reorganization Act established a new system for ratemaking as a principal element of the statutory scheme. Within that system, section 3621 was enacted as a guide to setting the level of rates and fees. It was intended primarily to ensure that rates and fees would be sufficient to meet the operational needs and other uses of postal revenues. It also required a reasonable provision for contingencies to cover unanticipated expenses in the future.

---

<sup>5</sup> The Kappel Commission was informed by several reports by independent contractors, including a report on financial management. Price Waterhouse & Co., *Financial Management in the Postal Service: A Report to the President's Commission on Postal Organization* (Feb. 9, 1968), in *Id.*, Annex, Contractors' Reports, Vol. I. Among its recommendations for financing the Postal Service, the Price Waterhouse Report stated:

Rate-making initiative, subject to appropriate safeguards and statutory policy guidance, should be delegated to postal management; rate-making principles and mechanisms should be established which will assure the recovery of all operating costs, costs of capital, *and possibly provide for retention of additional funds.*

Price Waterhouse Report at 2, 39 (emphasis added). The report also recommended that "postal management should be empowered to make its own operational and financial decisions." *Id.* at 44.

The OCA and Valpak incorrectly infer that section 3621 fundamentally represents a restriction on the exercise of management's authority to set and carry out financial policy. Their interpretations suggest that it was intended to function primarily as a constraint preventing the establishment of rates and fees that would over-compensate the Postal Service. The Postal Service agrees with the proposition that, as a public enterprise, it was not created to make a "profit."<sup>6</sup> In interpreting section 3621, however, it is important to understand that the break-even guidance in that provision did not principally arise out of circumstances in which abuse of ratemaking authority through rates that were too high was regarded as a major problem. Rather, as demonstrated by the extensive discussion of the Post Office Department's financial condition in the Kappel Commission Report and the Price Waterhouse Report, the main problems were perceived to be the chronic deficit status that was perpetuated by the existing system of funding, as well as the lack of authority by postal management to set policy and manage finances and operations effectively.<sup>7</sup> In this regard, the goal of self-sufficiency, rather than excessively high rates, dominated the creation of the so-called "break-even" requirement.

As we explain below, it is important to read the provisions of the Act as an integrated scheme that creates authority and flexibility, as well as limitations on the Postal Service's conduct. In particular, when focusing on the ratemaking provisions of

---

<sup>6</sup> As the Supreme Court recently summarized, "the PRA gives the Postal Service a high degree of independence from other offices of the Government, but it remains part of the Government." *United States Postal Service v. Flamingo Industries (USA) Ltd.*, 540 U.S. 736, 746 (2004). "Its goals are not those of private enterprise. The most important difference is that it does not seek profits, but only to break even, 39 U.S.C. § 3621, which is consistent with its public character." *Id.* at 747.

<sup>7</sup> See Kappel Commission Report at 22-23, 35.

the Act, section 3621 must be read in its entirety as establishing requirements to ensure that rates and fees are “sufficient” to enable the Postal Service to continue the development of needed postal services. This provision, furthermore, must be read together with the Board of Governors’ authority under section 3622(a) to initiate rate proceedings and propose rates and fees when the Board determines that they are in the public interest and in accordance with the policies of the Act. These policies include ensuring that the Postal Service will have the discretion and flexibility to manage its finances and operations effectively.

B. The Statutory Scheme Supports the Postal Service’s Revenue Requirement

The OCA’s and Valpak’s proposals to reduce the revenue requirement rest on their conclusions that section 3621 of the Act prevents the Postal Service from reserving accumulated net income and simultaneously seeking rate and fee increases to cover costs incurred in the test year. Neither the statutory scheme, nor the plain meaning of section 3621, however, prohibit retention of cumulative net income as a reasonable tool for financial and operational management. Nor do they make cumulative net income and the generation of new revenue from rate and fee increases mutually exclusive.

1. The Postal Service’s revenue requirement does not conflict with the plain meaning of section 3621

There are four basic elements in section 3621. First, it creates the Governors’ authority to establish rates and fees:

Except as otherwise provided, the Governors are authorized to establish reasonable and equitable classes of mail and reasonable and equitable rates of postage and fees for postal services in accordance with the provisions of this chapter.

Second, it describes the basic goals that guide the exercise of the Governors’ authority:

Postal rates and fees shall be reasonable and equitable and sufficient to enable the Postal Service under honest, efficient, and economical management to maintain and continue the development of postal services of the kind and quality adapted to the needs of the United States.

Third, it describes one purpose of, and standards governing, the levels of rates and fees:

Postal rates and fees shall provide sufficient revenues so that the total estimated income and appropriations to the Postal Service will equal as nearly as practicable total estimated costs of the Postal Service.

Fourth, it defines “total estimated costs”:

For purposes of this section, “total estimated costs” shall include (without limitation) operating expenses, depreciation on capital facilities and equipment, debt service (including interest, amortization of debt discount and expense, and provision for sinking funds or other retirements of obligations to the extent that such provision exceeds applicable depreciation charges), and a reasonable provision for contingencies.

It is also useful to note what section 3621 does not say. It does not use the terms “break-even,” “revenue requirement,” “profits,” “net income,” or “retained earnings.”<sup>8</sup> It does not refer to any time period (e.g., “test year”). Nor does its language explicitly impinge on the exercise of the functions and authorities of the Board of Governors or the Postal Service under other provisions of the Act, so as to specifically prohibit particular practices or policies.<sup>9</sup> In fact, its terms are limited to the

---

<sup>8</sup> The term “retained earnings” was used in recent postal financial statements based on generally accepted accounting principals and is used by the OCA and Valpak in their briefs. It was not, however, used by witness Tayman in his testimony, USPS-T-6, and is not used in this discussion. It is more normally applied to profit-making, shareholder-owned corporations to mean “profits that were not paid to a company's shareholders as dividends.” In the context of the Postal Service under current law, therefore, it means nothing other than “cumulative net income.” See also the discussion regarding pending legislation below.

<sup>9</sup> We do not here suggest that the considerations mentioned in section 3621 cannot be read as constituting policies of the Act under other provisions of the statute.

authority of the “Governors,” rather than the Board of Governors or the Postal Service. By contrast, other provisions of the Chapter and the Act explicitly refer to actions by the Board (e.g., 39 U.S.C. §§ 202, 3625(f)) and the Postal Service (e.g., 39 U.S.C. §§ 401, 404, 3622(a), 3623(a)).<sup>10</sup>

The provisions of section 3621 do not stand alone. The Governors are authorized to establish rates and fees “[e]xcept as otherwise provided,” and “in accordance with the provisions of this chapter.” The section thus indirectly incorporates procedures<sup>11</sup>, standards and policies<sup>12</sup>, and limitations on rates and fees<sup>13</sup> found in other parts of the Act. These general references make clear that section 3621 cannot be construed in isolation; reliable interpretation demands observance of the entire statutory scheme and the overall structure and purpose of the Act.<sup>14</sup>

Furthermore, section 3621 must be read in its entirety. Both the OCA and Valpak focus only on the provision that requires that revenues equal as nearly as practicable total costs. That guidance, however, is the second requirement in the section. Section 3621 first requires that rates enable the Postal Service to maintain appropriate postal services. Both requirements, moreover, are expressed more as guarantees than restrictions. They require that the rates and fees be “sufficient,” first to ensure appropriate types and levels of service, and second to ensure that revenues will

---

<sup>10</sup> The Governors acting alone are mentioned only in connection with their authorities to appoint the Postmaster General and Deputy Postmaster General (39 U.S.C. §§ 202(c),(d)) and establish rates (39 U.S.C. §§ 3621, 3625).

<sup>11</sup> See e.g., 39 U.S.C. §§ 3622, 3623, 3625, 3627.

<sup>12</sup> See, e.g., 39 U.S.C. §§ 101(d), 403(c), 3622(b), 3623(c).

<sup>13</sup> See, e.g., 39 U.S.C. §§ 3626, 3682-3686.

<sup>14</sup> “A statute is passed as a whole and not in parts or sections and is animated by one general purpose and intent. Consequently, each part or section should be construed in connection with every other part or section so as to produce a harmonious whole.” 2A NORMAN J. SINGER, STATUTES AND STATUTORY CONSTRUCTION § 46:05 (6th ed. 2000).

cover costs. As noted above, this emphasis is consistent with the history of postal reorganization, in which chronic deficits and service deficiencies were regarded as the main problems. Both requirements in section 3621, moreover, invoke the duties and responsibilities of the Postal Service established under other provisions of the Act that give it discretion to formulate and carry out financial and operational policy in managing the postal system. Two remaining points deserve mention. First, the so called “break-even” requirement in section 3621 does not establish a time frame for analysis. The Commission’s rules of procedure require a single, prospective fiscal year as the basis for evaluating whether the Postal Service’s rate and fee proposals meet the requirements of section 3621. 39 C.F.R. § 3001.54(f)(2). This “test year” standard, however, is only a regulatory convention. Neither the time frame, nor the information required, are specified in section 3621. Furthermore, the rules do not answer the questions raised by the OCA’s and Valpak’s proposals. They merely specify the information to be provided; they do not dictate how that information should be analyzed.

Strictly speaking, the demonstration contemplated by the rules – matching revenues from proposed rates estimated for a single fiscal year with expenses plus contingency estimated for that same year – need not involve consideration of net income (or losses) accumulated in prior years. Nevertheless, in practice the Commission, as well as the Postal Service and the courts, have looked beyond a single prospective year in determining the appropriate levels of rates and fees. Rather than leading to the conclusion that OCA and Valpak reach, however, these considerations have led the agencies and the courts to conclude that it is appropriate to evaluate compliance with the break even requirement over time, in connection with the Postal

Service's adoption of financial policy, as opposed to insisting that proposed rates and fees raise no more revenue than required to cover the specific expenses listed in section 3621 during a single fiscal year.

In this regard, it is no more justifiable to interpret section 3621 as requiring that accumulated net income must be exhausted before test year expenses can be fully recovered than it was, prior to adoption of a prior years losses component, to insist that past losses could not be recovered in future rates, or that, if they could, all losses would need to be recovered in a single rate increase. In practice, section 3621 has been interpreted to permit gradual recovery of prior years losses over time through future rate increases, in accordance with the Postal Service's financial policy choice to recover past losses. Evaluation of the revenue requirement in the current situation should grant similar deference to the Postal Service's policy choices of reserving net income and funding the escrow requirement through moderate rate and fee increases.

Second, in one respect, the structure of the break even requirement in section 3621 creates an expectation that the Postal Service will experience net income at some point. Specifically, the requirement in section 3621 that total expenses be defined to include a contingency provision leads ineluctably to the conclusion that cumulative net income is not only permissible, but contemplated by the Act. In practice, this is because the contingency, in effect, represents an insurance policy against future adversity and mistakes in estimating. The situations the contingency was intended to meet, however, will not always arise, and the revenues generated by the contingency will not always be needed in a particular year. Furthermore, there is no requirement in section 3621 that

net incomes as a result of unused contingency must be used to prolong the time between rate changes.

How much cumulative net income would be appropriate to maintain would be a matter of financial management, which is left to the Postal Service and its Board of Governors to determine.<sup>15</sup> This determination, however, would be made with the understanding that it is not the Postal Service's purpose to "accumulate a substantial amount ... for extended periods to increase our capital."<sup>16</sup> Rather, the decision to retain a level of cumulative net income could reflect a decision by the Governors to fund capital projects out of cash rather than borrowing; to acquire land;<sup>17</sup> to moderate rate increases by maintaining a "rainy day fund" instead of burdening ratepayers with a traditional contingency provision; to provide funding for the development of new services; or any number of considerations bearing on sound financial management.

2. Section 3621 must be read together with the Postal Service's authority under section 3622 to determine the timing and amount of rate and fee changes

Section 3621 creates standards for evaluating rates established by the Governors under the ratemaking provisions embodied in the Act. The exercise of authority to change rates, however, is controlled by section 3622. This provision authorizes the Postal Service to request changes in rates and fees "[f]rom time to time,"

---

<sup>15</sup> For example, in 1995, the Board of Governors issued a resolution stating that the Postal Service would "plan for cumulative net income ... *to equal or exceed the cumulative prior years' loss recovery target* ...." Resolution of the Board of Governors of the United States Postal Service, Resolution No. 95-9, Restoration of Equity and Recovery of Prior Years' Losses (July 10, 1995).

<sup>16</sup> United States Postal Service Annual Report 2004, at 30. Thus, Valpak's claim at page I-19 of its Brief that the Postal Service is asserting to accumulate "unlimited retained earnings" is a red herring.

<sup>17</sup> As witness Tayman testified, the Postal Service has acquired \$2.6 billion in land that has not been included in the revenue requirements. Tr. 2/131.

if it “determines that such changes would be in the public interest and in accordance with the policies of this title.”

These policies include those set forth in section 3621 to ensure that the Postal Service will have sufficient revenues to meet expenses and contingencies and to maintain an adequate postal system. They also include the Postal Service’s general and specific duties, such as its authority to “operate as a basic and fundamental service to the people,” to provide postal services in all areas and communities in order “to bind the Nation together,”<sup>18</sup> to “plan, develop, promote, and provide” postal services by “maintain[ing] an efficient system of collection, sorting, and delivery of the mail nationwide.”<sup>19</sup> As noted above, the amount of cumulative net income that is prudently maintained by a \$73 billion organization charged with such extensive duties is a matter of financial policy, which is left to postal management and the Governors to determine.

As we discuss below, the courts have been quite clear that the Commission cannot infringe upon the Postal Service’s financial and operational policy judgment by restricting the revenue sought through proposed rate and fee increases. In particular, the Commission may not reduce the Postal Service’s revenue requirement to influence the timing of rate changes. The logical and practical consequences of the OCA’s and Valpak’s interpretations of section 3621, however, would have that effect. This result cannot be more clearly demonstrated than in the OCA’s proposals. If the Postal Service were required to offset its cumulative income at the end of FY 2005 against estimated expenses in the test year, it would be left with an impractically small rate increase in

---

<sup>18</sup> 39 U.S.C. § 101.

<sup>19</sup> 39 U.S.C. § 403(a) & (b).

2006 that would be hard to administer through equitable increases for all classes and services. Alternatively, the Postal Service would be required to carry over the deficit experienced as the result of not changing rates in 2006. To the extent that the cumulative net income did not represent cash, furthermore, it would be required to borrow to meet the escrow requirement. Even if it did apply all of the cash represented by the cumulative net income to the escrow, it would be left without a cash reserve. In an emergency, it might be required to borrow for operations. If it decided to maintain some reserve of cash, it might be forced to meet most or all of the escrow requirement through borrowing. Overall, it would be prevented from carrying out the Board's policy judgment to meet the escrow requirement through moderate rate increase in 2006, and to maintain a reasonable reserve for other purposes. The OCA's alternative proposal to delay implementing rate increases until August 15, 2006, would have similar effects. It would deprive the Postal Service of revenue in 2006, and would force unwanted choices on it to meet the escrow requirement and other operational or financial needs.

Section 3622 authorizes the Postal Service to seek rate changes when it determines that they would be in the public interest and in furtherance of the policies of the Act, including the Postal Service's other duties and responsibilities in operating the nation's postal system. Section 3621 should not be interpreted to impair that authority, or deprive the Postal Service of the ability to set financial and operational policy.

3. Other provisions of the Act provide guidance in interpreting section 3621

A careful reading of other provisions of the Act provides support for an interpretation of section 3621 that would not require offsetting cumulative net income

against estimated expenses in the test year. This is evidenced by the following specific provisions.

a. Section 2003(c)

Further support for the accumulation of net income is found in section 2003(c), which states: "If the Postal Service determines that the moneys of the [Postal Service] Fund are in excess of current needs, it may request the investment of such amounts as it deems advisable by the Secretary of the Treasury...." The Act clearly contemplates the possibility of maintaining a favorable balance of revenues to expenses, at least on a cash basis. There is, moreover, no limit on the length time that such investments may be held.

b. Section 2009

Section 2009 requires the Postal Service to prepare and submit to the Administration an annual "business-type budget or plan of operations, with due allowance given to the need for flexibility, including provision for emergencies and contingencies." This budget program shall contain, *inter alia*, "an analysis of surplus or deficit." Thus, Congress clearly contemplated that the Postal Service could have net incomes; indeed, it seems clear that by requiring that the "business-type" plan account for "the need for flexibility" in addition to providing for "emergencies and contingencies," the statute intends that result. Without net income, flexibility is not possible and emergencies and contingencies cannot be handled.

c. Section 2005

Section 2005 authorizes the Postal Service to borrow three billion dollars a year, up to an overall limit of 15 billion dollars, to meet operational expenses and capital

investment needs. The OCA's and Valpak's argument that the revenue requirement must "zero out" cumulative net income is tantamount to a claim that the Act "biases" financial management in favor of debt. That is, rather than recognize the Postal Service's ability to retain a reasonable cumulative net income for any of the reasons noted above, OCA and Valpak would apparently rather force the Postal Service to borrow. OCA and Valpak would therefore limit the financial tools available to the Postal Service, contrary to the Congressional mandate that the Postal Service be managed in a "business-like manner."

4. Nothing in the Act's legislative history conflicts with the Postal Service's interpretation

There is nothing in the legislative history of the Postal Reorganization Act that suggests that Congress intended to prohibit the Postal Service from maintaining cumulative net income. Indeed, the very opposite is true. The Kappel Commission, in its study on organizing and financing the Postal Service, recommended that the Postal Service fix its rates in order to build a "reserve" of "about three to five percent."<sup>20</sup>

The OCA's argument that Congress did not give the Postal Service the power to possess cumulative net income is logically flawed. OCA begins by noting a recommendation within a Kappel Commission annex report that the Postal Service retain earnings for contingencies, and "for minor capital investment in excess of depreciation." OCA Initial Brief at 17. OCA then notes that the phrase "minor capital investment in excess of depreciation" was not in the final version of 39 U.S.C. § 3621.<sup>21</sup> *Id.* From that, OCA leaps to the conclusion that "the power to retain earnings was not

---

<sup>20</sup> Kappel Commission Report at 82 (1968).

<sup>21</sup> Note, however, that "a reasonable provision for contingencies" is within the statute.

delegated to the Postal Service by Congress.” *Id.* This conclusion does not logically follow. The most one can deduce is that Congress intended for the Postal Service to retain earnings for contingencies, but did not feel it necessary to explicitly allow the Postal Service to retain earnings for minor capital investment in excess of depreciation. In no way can this be interpreted to mean that Congress did not intend for the Postal Service to retain earnings at all.

5. Judicial and Commission precedent support the Board’s financial policy judgment in this case

Judicial and administrative precedent supports the Postal Service’s revenue requirement in this proceeding. First, the Postal Service, the Commission, and the courts have interpreted § 3621 as requiring that the Postal Service “break even over time.” Second, the Commission has recognized that operating flexibility is essential to the businesslike operation of the Postal Service. Third, the courts have repeatedly emphasized that it is the Board that has the authority to make financial policy for the Postal Service, and that its financial policy decisions must therefore be deferred to. The Commission must not accept Valpak’s and OCA’s suggestion that it contravene the Board’s reasonable judgment to maintain a modest cumulative net income while raising rates to pay for the P.L. 108-18 escrow expense.

a. To the extent the Act requires “break even,” it requires “break even over time”

The “break even” mandate of § 3621 constitutes a requirement that the Postal Service “break even over time,” rather than a requirement that the Postal Service must achieve “zero” on the balance sheet every time it requests a rate increase. This proper

reading of the Act has been recognized by the Postal Service, the Commission, and the courts, as indicated by the treatment of prior year losses.

The purpose of the recovery of prior years' losses (RPYL) allowance in the revenue requirement was to restore Postal Service equity, thereby leading to long-term financial stability, self-sufficiency, and the attainment of "break even over time."<sup>22</sup> By approving the RPYL allowance in Docket No. R76-1, the Commission recognized that the statutory guarantee of § 3621 is one that "could be achieved over time."<sup>23</sup> This interpretation was approved by the court in *National Association of Greeting Card Publishers v. United States Postal Service*, 607 F.2d 392 (D.C. Cir. 1979), which held that "break even over (a reasonable period of time)" is "a proper reading of the Act's financial policy."<sup>24</sup> In Docket No. R87-1, the Commission further described the "theoretical justification" for the RPYL allowance as being the promotion of "a break-even result retrospectively."<sup>25</sup> Because "break even" is thus a concept that is to be evaluated over time, there is no merit to OCA's and Valpak's suggestions that § 3621 must be read as requiring the Postal Service to offset its cumulative net income against estimated expenses in the test year.

---

<sup>22</sup> See PRC Op. R90-1, Vol.1, at II-31 (January 4, 1991) (noting that the goals of RPYL were equity restoration and "breakeven over time"); PRC Op. R87-1, Vol.1, at 20 (March 4, 1988) (the PYL mechanism designed to restore financial self-sufficiency); PRC Op. R77-1, Vol.1, at 46-47 (May 12, 1978) (the RPYL serves two purposes: 1) to ensure financial stability and 2) to fulfill the statutory requirement of "breakeven").

<sup>23</sup> See PRC Op. R90-1, Vol.1, at II-49, II-50 n.52 (statutory guarantee is one of "(eventual) breakeven operation"). See also PRC Op. R94-1, Vol.1, at II-31 (November 30, 1994) (noting that "it is clear that Congress expected the Service to breakeven over time").

<sup>24</sup> See PRC Op. R90-1, Vol.1, at II-28 (citing *National Association of Greeting Card Publishers v. United States Postal Service*, 607 F.2d 392, 431-432 (D.C. Cir. 1979) (Hereinafter *NACGP III*)).

<sup>25</sup> See PRC Op. R87-1, Vol.1, at 34. The Commission further described the contingency provision as "intended to promote a break-even result prospectively."

- b. The Commission has recognized that sound financial management may require the Postal Service to maintain some kind of reserve in order to operate efficiently

As noted earlier, the maintenance of the cumulative net income at issue here provides the Postal Service with operating flexibility. The Commission has long recognized that such flexibility is essential to operational efficiency, and thus to the Act's goal that the Postal Service operate in a businesslike manner.<sup>26</sup> In Docket No. R76-1, the Commission stated its belief that "Congress intended the Postal Service to have a reasonable supply of operating funds, or 'working capital,' for the execution of its functions."<sup>27</sup>

- c. The cumulative net income affords the Board flexibility over the exact timing of the next rate case

One important by-product of the flexibility that the cumulative net income affords the Postal Service is that it allows the Board to control the timing of the next omnibus case. The Commission cannot adjust the revenue requirement presented by the Postal Service if such an adjustment has the "effect of undermining the Board's exclusive authority in timing changes in postal rates and fees."<sup>28</sup> While the Postal Service has indicated that a subsequent omnibus rate case is currently being worked on,<sup>29</sup> the Board has yet to determine the date for the filing of that case. Reducing the revenue requirement based on the OCA's and Valpak's interpretations of § 3621, so that the

---

<sup>26</sup> See PRC Op. R77-1, Vol.1, at 44 (one of the "major policy determinations" of the PRA was that "the Postal Service would have management flexibility in order to achieve maximum operating efficiency"). See also PRC Op. R94-1, Vol.1, at II-33 (a "well-run business" must have "operating flexibility").

<sup>27</sup> PRC Op. R76-1, Vol.1, at 45 (June 30, 1976).

<sup>28</sup> *Newsweek, Inc. v. United States Postal Service*, 663 F.2d 1186, 1204 (2<sup>nd</sup> Cir. 1981).

<sup>29</sup> Tr. 11/6230.

cumulative net income is eliminated, would constrain the Board's discretion in this regard, in contravention of *Newsweek*.

- d. Judicial precedent demonstrates that the Commission should not intrude upon the Board's financial policy decisions

As noted above, the Board has made a financial policy judgment to maintain the Postal Service's modest cumulative net income while seeking a rate increase solely to fund the escrow expense required by P.L. 108-18. This was a sound business judgment, well within the Board's discretion and the strictures of the Act, and should not be intruded upon by the Commission.

The courts have held that the Board has the "exclusive authority to manage the Postal Service,"<sup>30</sup> and have made it clear that this authority includes financial policy decisions. In *Newsweek*, the 2<sup>nd</sup> Circuit noted that it is "the Board, and not the PRC, [that is] responsible for making policy decisions for the Postal Service," and that the "Board is free to fashion the policies of the Postal Service without interference ... from the PRC."<sup>31</sup> Based on this understanding of the proper role of the Commission, the court held that the Commission had impermissibly intruded upon the "policy-making domain of the Board" when it disallowed RPYL and drastically reduced the contingency

---

<sup>30</sup> *Newsweek*, 663 F.2d at 1204 (citing *Governors of the United States Postal Service v. Postal Rate Commission*, 654 F.2d 108, 114 (D.C. Cir. 1981)). The *Governors* decision states:

The responsibilities of the Postal Rate Commission are strictly confined to relatively passive review of rate, classification, and major service changes, unadorned by the overlay of broad FCC-esque responsibility for industry guidance and of wide discretion in choosing the appropriate manner and means of pursuing its statutory objective.

*Governors*, 654 F.2d at 117 (quoting *United Parcel Service, Inc. v. United States Postal Service*, 455 F. Supp. 857, 873 (E.D. Pa. 1978)).

<sup>31</sup> *Newsweek*, 663 F.2d at 1204-05.

in the Docket No. R80-1 revenue requirement.<sup>32</sup> In a subsequent case, the 2<sup>nd</sup> Circuit interpreted its *Newsweek* ruling as “stat[ing] quite firmly ... that the PRC must accede to the Board’s estimates of the Service’s revenue needs.”<sup>33</sup> Consistent with this precedent, the Commission must not infringe upon the Postal Service’s financial and operational policy judgment by restricting the revenue sought through proposed rate and fee increases.

The *NACGP III* decision is also instructive with regard to the Board’s discretion in determining the financial policy of the Postal Service. There, the court found that the Act allowed the Postal Service, “in the exercise of its sound economic judgment,” to recover accumulated operating deficits through the revenue requirement (the RPYL provision discussed *supra* in section 4.a), rather than through borrowing or appropriations.<sup>34</sup> In response to arguments by appellants that RPYL was impermissible because it would provide a disincentive to efficient and economical management, and would permit rates to be set at levels resulting in a profit, the court stated that “[t]he various economic stratagems and their effects are matters entrusted to the wise discretion and expertise of the Postal Service.”<sup>35</sup> The court went on to state that it would “not substitute [its] judgment concerning the economic wisdom of [the Postal Service’s] decision to recoup these past operating losses through [the revenue requirement rather than through some other mechanism], because its decision [was] consistent with the statutory purposes of the Act – the Postal Service should be

---

<sup>32</sup> *Id.*

<sup>33</sup> *Time, Inc. v. United States Postal Service*, 685 F.2d 760, 775, (2<sup>nd</sup> Cir. 1982).

<sup>34</sup> *NACGP III* at 425.

<sup>35</sup> *Id.* at 431-32.

financially self-sufficient and should 'break even.'"<sup>36</sup> Since the Board's current financial policy to seek to fund the escrow requirement through a moderate rate increase while maintaining a modest cumulative net income is equally consistent with the statute, it is equally entitled to deference.

While the Postal Service and the Commission have often differed over the Commission's proper role concerning the revenue requirement, the Commission has recognized that it must not intervene in the financial management of the Postal Service.<sup>37</sup> For example, the Commission has rejected proposed reductions to the Postal Service's revenue requirement that were justified on the grounds that the Postal Service could issue debt to make up any short-fall by noting that "the decision between borrowing and initiating rate adjustments [falls] within the financial policy responsibilities delegated to the Board of Governors."<sup>38</sup> Instead, the Commission has interpreted its role as being "to translate the consequences of the Postal Service's financial management into rate recommendations, and to do so in a manner that is in accordance with the policies and ratemaking factors of the Act."<sup>39</sup> Consistent with that role, the Commission must not substitute its judgment concerning the proper financial management of the Postal Service for that of the Board.

---

<sup>36</sup> *Id.*

<sup>37</sup> In Docket No. R94-1, the Commission noted: "As some Federal courts have had occasion to state, this Commission's mandate does not include direct intervention in the financial management of the Postal Service." PRC Op. R94-1, Vol.1, at II-21.

<sup>38</sup> PRC Op. R90-1, Vol.1, at II-53.

<sup>39</sup> *Id.*

6. The pending reform legislation's explicit authorization of "retained earnings" has no bearing on whether the Act currently authorizes the Postal Service to maintain a cumulative net income

Valpak argues that because the reform bills currently pending in Congress (HR 22 and S 662) explicitly authorize the Postal Service to have "retained earnings," the Postal Service does not have the authority under current law to maintain cumulative net income. VP Brief at I-12-13. This argument is without merit, for several reasons.

Most fundamentally, Valpak ignores the fact that "retained earnings" as used in section 201 of the reform bills has a definite meaning that is entirely different from the "cumulative net income" at issue here.<sup>40</sup> As the committee report describing H.R. 22 explains, section 201 of the reform bills authorizes the Postal Service to "generate earnings that would be maintained, and which could be distributed as incentives to management as well as employees through collective bargaining."<sup>41</sup> Thus, through their authorization of "retained earnings," the reform bills allow the Postal Service to endeavor to earn a profit, and to use that profit in any manner that it sees fit (including distribution to managers and employees), as one aspect of encouraging efficiency. This is, however, completely different from the "cumulative net income" at issue here, which is not a profit but a pool of funds that allows the Postal Service the flexibility to meet

---

<sup>40</sup> As the Postal Service notes above, the term "retained earnings" as used in recent Postal Service financial statements, and in Valpak's and OCA's briefs, means nothing more than "cumulative net income."

<sup>41</sup> See H.R. REP. NO. 109-66, pt. 1, at 43 (2005). See *also* Testimony of The Honorable Edward J. Gleiman, Chairman, on Behalf of the Postal Rate Commission Before the House Committee on Government Reform Subcommittee on the Postal Service (February 11, 1999), at 4 ("Private utilities operating under a price cap regulation are motivated to operate efficiently because they are allowed to retain any profits they earn while providing service under capped rates. The Postal Service does not have residual claimants who demand a reasonable return for their equity investment. To motivate the Postal Service to operate efficiently, H.R. 22 establishes the opportunity for postal services to earn substantial bonuses if profits are realized while providing promised services under capped rates.").

unexpected expenses and to fulfill its statutory obligations under current law. Thus, the fact that the reform bills explicitly include a provision allowing “retained earnings” has nothing whatsoever to do with the cumulative net income at issue here.

This fact highlights the general inappropriateness of interpreting the Act by reference to the contents of the reform bills. The reform bills would create a ratemaking paradigm that is fundamentally different from the one that currently operates: the Postal Service would be allowed to make a profit in the context of a price-cap ratemaking regime, and § 3621 as currently written would be repealed. It makes no sense to interpret what is allowable under the “break even over time” mandate of § 3621 by reference to the contents of bills that would repeal that very aspect of the Act. The fact that the reform bills specifically authorize “retained earnings” as one part of a completely revamped ratemaking structure simply has no bearing on whether the Postal Service is authorized, under the current statutory scheme, to maintain a cumulative net income.<sup>42</sup>

---

<sup>42</sup> In *Associated Third Class Mail Users v. United States Postal Service*, 405 F.Supp. 1109 (D.D.C 1975), the Postal Service argued that it had the authority to change the fees for certain special services without first going to the Commission partly by pointing to the fact that, prior to the Postal Reorganization Act (PRA), the Postmaster General had the unilateral authority to change the fees for those services without first receiving authorization from Congress. *Id.* at 1116. From this, the Postal Service argued that the fees were not important enough to be part of the chapter 36 administrative process. *Id.* The court rejected this rationale, finding that it “totally ignores the significance of the changes produced by the Act.” *Id.* On appeal, the D.C. Circuit also found this argument unconvincing, for the same reason. *National Association of Greeting Card Publishers v. United States Postal Service*, 569 F.2d 570, 598 (D.C. Cir. 1976). While Valpak’s argument is not identical to the Postal Service’s argument in *ATCMU* (Valpak seeks to interpret current law based on subsequent, and still unenacted, legislative developments, while the Postal Service sought to interpret the PRA by reference to pre-PRA postal law), like the Postal Service in *ATCMU*, Valpak ignores the fact that it is seeking to interpret one postal regulatory regime based on the contents of a fundamentally different postal regulatory regime.

Finally, the courts have often expressed the “warning that the views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one.”<sup>43</sup> Thus, even if the reform bills bore some relation to the current “break even over time” regulatory regime under which the Postal Service currently operates (which, as noted above, they do not), their usefulness in determining whether the Postal Service is authorized to maintain a cumulative net income under current law would still be highly questionable.

- C. The OCA’s and Valpak’s Flawed Interpretation Misrepresents the Statute and Would Interfere with the Board’s Sound Financial Policy Determinations
  - 1. The OCA’s and Valpak’s interpretations conflict with the statutory scheme

The OCA and Valpak rest their proposals to reduce the Postal Service’s revenue requirement principally on their conclusions that accumulated net income, or “retained earnings,” are not permitted under the “break-even” requirement in section 3621. According to Valpak, the Act simply does not authorize the Postal Service to have “substantial retained earnings.”<sup>44</sup> The OCA concludes that, if the Postal Service were to raise rates by the requested 5.4 percent, revenues would exceed expenses by an amount close to the Postal Service’s accumulated net income. In the OCA’s view, this surplus would violate the provision in section 3621 that requires income from rates plus appropriations to equal as nearly as practicable total estimated costs.<sup>45</sup>

---

<sup>43</sup> See *Consumer Product Safety Commission v. GTE Sylvania*, 447 U.S. 102, 117 (1980); *NAGCP III* at 431 n.97 (noting that courts have recognized that “legislative events subsequent to the Act ‘form a hazardous basis for inferring the intent of an earlier [Congress].’”) (quoting *United States v. Prince*, 361 U.S. 304, 313 (1960)).

<sup>44</sup> Valpak Initial Brief at I-7 to I-12.

<sup>45</sup> OCA Brief at 6-9.

As we discuss above, nothing in the plain language of section 3621 or the Commission's rules would prohibit the Postal Service from accumulating net income from prior years. On the contrary, the Act authorizes the Postal Service to set financial policy, including determination of the appropriate uses for revenues. Furthermore, for purposes of demonstrating section 3621's equation of income and expenses in rate cases, the Commission's rules contemplate estimating revenues and costs for a single, prospective fiscal year. Nothing in the Act or the rules would require offsetting costs estimated for this test year with accumulated income.

While Valpak does not define what it means by "substantial retained earnings," its argument is based in the first instance on the failure of the Act to mention "retained earnings" explicitly. Valpak, however, cites the Commission and other sources that use the term "break even" to support its view that cumulative net income is inappropriate. But, just as the Act does not explicitly say "retained earnings," neither does it use the term "break even."<sup>46</sup>

"Break even" is simply shorthand for the provision in section 3621 requiring that rates be sufficient to cover total estimated costs. As noted above, section 3621 defines total costs to include a reasonable provision for contingencies. Theoretically and in practice, if uses for this contingency provision do not materialize, income will accumulate over expenses. The Postal Service would then have the option to reserve this net income for future uses, such as investment, or to use it to operate and thus postpone the next rate increase. Nothing in the Act, however, would require the Postal

---

<sup>46</sup> As noted above, the Act clearly uses the term "surplus" in regard to postal budgets and refers to the possibility of the Postal Service's having "excess moneys."

Service to subordinate its range of financial policy choices to the revenue-cost equation in section 3621. Under the terms of section 3622(a), that determination would be a judgmental decision by the Postal Service, in accordance with its assessment of the public interest and the policies of the Act, including its prerogatives to manage postal operations and finances.

2. The Postal Service's revenue requirement reflects its policy choices to reserve net income and fund the escrow through a rate and fee increase

Valpak argues that cumulative net income was not taken into account in developing the revenue requirement in this case. It concludes that "it is clear from its Request to raise postal rates and fees in the docket that the Postal Service did not take its retained earnings (*i.e.*, cumulative net income) into consideration *in any way* that is reflected in the proposed rates and fees."

It is clear from the very sources Valpak cites, and by virtue of the fact that this docket exists, that the Postal Service was well aware that it has cumulative net income and that postal management, at the highest levels, made a determination to file the Request in order to raise funds to meet its escrow payment obligation, while maintaining for the future the modest amount of cumulative net income that it has (minus the amount of revenue forgone by implementing rates after the beginning of the test year). Part of this determination involved the decision to propose a provision for contingencies of zero percent.

While it is true that there has been no official policy directive regarding cumulative net income, similar to that which evolved over time with respect to recovery of cumulative net losses, Valpak cannot conclude that there is a policy void. In the

context of the unique circumstances that currently prevail, the operative policy was set by the Board when it authorized the Postal Service to file its Request in this docket.

Valpak further states that: “The Commission cannot wait for the Board of Governors to devise a policy for the future.”<sup>47</sup> In this regard, it is noteworthy that the policy on recovery of prior years’ losses evolved over a number of years, in light of the circumstances then prevailing, with the mutual participation of the Postal Service, the Commission, and interested participants. Similarly here, it makes sense to see how the Postal Service’s situation evolves, especially in light of the uncertainty concerning the escrow requirement, among other things.

3. The Commission should not reduce the revenue requirement on this record

It would not be particularly prudent for the Commission to take the kind of precipitous action called for by Valpak and the OCA in this case. No record has been developed in this proceeding concerning the appropriateness of a mechanism for including cumulative net income in the revenue requirement, whether it be the one-ninth PYL-type approach urged by Valpak and the OCA, or some other mechanism fashioned specifically to the circumstances that now prevail. In fact, what the record in this case actually does contain in this regard is witness Tayman’s expert opinion that it is *not* appropriate to invert the treatment of prior years’ losses and apply it to cumulative net incomes. Tr. 2/131. The Commission would certainly be well advised to defer a determination on this subject until it had the opportunity to establish a full record, based on expert analyses and testimony by the Postal Service and interested parties.

---

<sup>47</sup> Valpak Initial Brief at I-19.

The OCA's principal proposal to subtract all of cumulative net income from the revenue requirement cannot be adopted on this record. This proposal would leave the Postal Service with zero cumulative net income at the end of FY 2006 and rates that contain no provision for contingencies; the Postal Service would be forced to suffer losses at the first reversal of fortune. This is not businesslike management. It is not consistent with the Act, as discussed above.

OCA seems to be under the mistaken impression that the cumulative net income is sitting in an "account," waiting for the Postal Service to make withdrawals.<sup>48</sup> Valpak, at least, acknowledges that there is a difference between income statement net income and cash in the bank, noting that the current level is about \$2 billion. Valpak Brief at I-5-6. This is approximately the amount of one payroll, which is postal management's target for cash to be kept on hand. Tr. 2/249-50.

The OCA's argument that "there is no record evidence that mailers are in favor of, or are even neutral, about paying in advance for future cost increases"<sup>49</sup> is flawed. With respect to business mailers, the vast majority of intervenors signed the very stipulation and agreement that the OCA decries as unappealing to mailers.

D. Valpak and the OCA Misrepresent Public Law 108-18 When They Assert That it Restricts the Postal Service's Revenue Requirement in this Case

Public Law 108-18 (PL 108-18) does not restrict the Postal Service's revenue requirement in this case. PL 108-18 directs the Postal Service to use savings resulting from the passage of the law in two ways: 1) to reduce postal debt, and 2) to keep postal rates unchanged through 2005. Once these goals were met, PL 108-18 places no

---

<sup>48</sup> OCA Brief at 7.

<sup>49</sup> OCA Brief at 9.

further restrictions on any savings that result from the law. Both the text of the law, and the legislative history of the law, support these assertions.

PL 108-18 directed the Postal Service to use savings attributable to fiscal year (FY) 2003 and 2004 to reduce postal debt. The Postal Service accomplished this goal in 2004. Tr. 2/133. PL 108-18 then directed the Postal Service to use savings attributable to FY 2005 to hold the postage rates unchanged through 2005.

Congress intended for the Postal Service to use the savings resulting from passage of PL 108-18 to hold postage rates unchanged through 2005. The Senate Report for Senate Bill 380 (which eventually became PL 108-18) states, under the section entitled “Delayed Postal Rate Increase” the following:

The Reform Act expresses the “Sense of Congress” that the savings accruing to the USPS will be sufficient to allow the USPS to fulfill its commitment to hold postage rates stable until at least 2006...Upon introduction of S. 380, Postmaster General Jack Potter announced that enactment of the bill would allow the Postal Service to hold off raising rates until 2006, rather than 2004, as it had planned. S. REP. NO. 108-35, 108<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2003).

Postmaster General Potter, in his testimony before the Postal Rate Commission on June 27, 2005, stated that he helped with the construction of the bill, and affirmed that “the law never addressed what would happen in 2006.” He emphasized that “there is no way that this law can be interpreted to refer to anything in 2006” because he knew “what commitments were made.” Tr. 2/89 – 90.

Beyond the goals of reducing postal debt and keeping postal rates unchanged through 2005, PL 108-18 places no further express or implied restrictions on the use of any excess savings resulting from the law. Therefore Valpak’s argument that “the balance of any savings must be used to continue holding down postal rates until the funds are exhausted” is without foundation. Valpak Initial Brief at I-15. PL 108-18 made

a provisional reform and set in place a mechanism that was expected and intended to be supplanted by more permanent legislation once Congress was able to act on the proposal submitted by the Postal Service under section 3(e). Congress hoped to finish that process before FY 2006. Other than the escrow requirement as a means of further reserving the issues in case that hope was not fulfilled, PL 108-18 provided no restrictions to years after FY 2005.

The OCA's arguments are similarly without merit. The OCA begins by stating that "Congress intended to have the savings...used (among other things) to keep postal rates unchanged for years 2003-2005 and beyond". OCA Initial Brief at 22. However, "and beyond" is not the law or the legislative history. Congress did explicitly intend the savings to be used to keep the postal rates unchanged through 2005. There is no basis, however, for the OCA's claim that PL 108-18 addresses the issue of rate stability beyond 2005. OCA's next argument is that "[t]he Postal Service's decision to file a...rate case flouts one of the chief purposes of the law – to use the savings to hold down the rates paid by mailers." *Id.* This accusation is as undeserved as it is baseless. One of the chief purposes of PL 108-18 was to keep the rates steady through 2005. Therefore, the filing of a request for the purpose of raising rates in 2006 does not "flout" PL 108-18.

III. ARGUMENTS REGARDING COSTING ISSUES PRESENTED BY THE PARTIES IN THEIR INITIAL BRIEFS IDENTIFY NO ADEQUATE BASIS TO DEPART FROM THE SETTLEMENT RATES

As the vast majority of the parties in this case have signed the settlement agreement, it is unsurprising that the majority of initial briefs discuss costing and cost study issues (if at all) as only secondary considerations. The settlement parties, explicitly or implicitly, have concluded that costing disputes should not prevent the Commission from recommending the settlement rates.<sup>50</sup> To the extent that certain of the settlement parties nonetheless address costing and cost study issues, the Commission needs to carefully distinguish between arguments based on existing record evidence, versus arguments based on expert opinions that the parties' witnesses might have offered had they testified, but which currently do not appear on the record. Ultimately, however, since these parties are supporting settlement, there seems little to be gained by addressing in any great detail the pros and cons of each of their arguments.<sup>51</sup>

---

<sup>50</sup> Even APWU, a party that has not signed the settlement agreement, shares this conclusion. See APWU Brief at 9-12.

<sup>51</sup> One exception is a view presented by MMA which, rather than being limited in effect to this case, is intended instead to control in other cases. MMA suggests that the Postal Service be impeded in the future from proposing what MMA refers to as the Postal Service's "theory" of mail processing costs that vary less than 100 percent with changes in mail volume. See MMA Brief at 24-25. In reality, however, the Postal Service's proposed mail processing variabilities are based not on a "theory," but on empirical estimation. In contrast, the approach favored by MMA relies entirely on pure assumption, and is thus much more properly characterized as a "theory." Sound ratemaking practice should actively encourage reasonable empirical efforts to reexamine levels of attribution based entirely on assumption, and should not attempt to shield such assumptions from testing merely because empirical refutation would lead to results inconvenient to one set of adversaries. Moreover, the "theory" favored by MMA assumes that there are no economies of scale in mail processing, whereas MMA in another portion of its brief (MMA Brief at 20) laments that high volume workshare mailers get no credit "from the additional cost savings that result from economies of

For example, despite their strong support for the settlement rates, MMA and ABA&NAPM, and, to a lesser extent, PBI invite the Commission to opine on the “problems” with the cost methodology that they believe leads to an understatement of the First-Class Mail workshare cost savings. Thus, MMA would have the Commission find the use of the nonautomation machinable mixed AADC benchmark for delivery costs to be without merit. MMA Brief at 24. ABA&NAPM challenges the use of Bulk Metered Mail as the benchmark for mail processing costs in calculating the workshare cost savings for FCM. Joint Brief of ABA and NAPM at 13. Not surprising, APWU takes an opposing view. It believes that First-Class Mail workshare cost savings are *overstated*, citing “problems” with the cost methodology in support of their position. See, e.g., APWU Brief at 7-9.

The Commission should decline the invitation to opine on the issues raised by these intervenors because the record in this docket is limited. *Accord*, PRC Op. R2001-1, Vol.1, at 74 (March 22, 2002). See *also* APWU Brief at 1, 11. MMA admits that it is not inviting the Commission to make any change in its workshare cost savings methodology in this case because the issues did not receive a full airing on the record. MMA Brief at 21. As witness Taufique states, at Tr. 3/607, the issues of cost study methodologies and the alignment of discounts will be reviewed prior to the filing of the next omnibus rate filing. See *also* MMA Brief at 21. As a result, the next case will provide the appropriate forum for the full exploration of the Postal Service’s cost study methodology. See APWU Brief at 12. Any comments on the cost study methodology

---

scale.” It is difficult to discern, therefore, why MMA would be so eager to embrace an unsupported assumption that there are no economies of scale in mail processing operations.

underlying the calculation of the First-Class Mail workshare discounts should be deferred until then.<sup>52</sup>

Valpak stands apart as a party that both opposes the settlement, and filed its own testimony presenting its views. For reasons discussed next, however, the costing arguments presented in the Valpak brief do not withstand critical scrutiny. Lastly, the OCA did not present testimony, which fatally undermines the new materials and views presented for the very first time in its brief.

A. The Consequences of an Appropriate Modification to the DAL Adjustment are Not as Significant as Valpak Would Suggest

Valpak spends much of the first portion of Section III of its initial brief arguing that a DAL adjustment is necessary and appropriate. Valpak Brief at III-1 - 5. The Postal Service, of course, proposed a DAL adjustment as part of its filing, and there does not seem to be disagreement from any party that methodologies from previous cases which did not make such an adjustment were deficient. Valpak is in error, though, to insist that the appropriate estimate of DAL volume to use for such an adjustment is still that proposed by Dr. Haldi in his revised testimony. See *id.* at III-8 -11. In fact, as discussed below, the appropriate volume estimate is nearly 200 million pieces lower. Moreover, the rebuttal testimony of Advo witness Crowder demonstrates that amending Postal Service witness Kelley's USPS-LR-K-67 analysis to reflect an appropriately

---

<sup>52</sup> MMA also urges the Commission not to place any reliance on the Postal Service's new CCSTS for city carrier costing. MMA Brief at 36-37. One reason MMA cites is that study's increase in estimated collection costs, which MMA claims was revealed only late in the discovery process, and of which MMA suggests that "not even the Postal Service was aware." *Id.* at 36. In reality, however, the Postal Service was well aware of the collection cost result, and found that result to be reasonable for the reasons explained at Tr. 13/6461-62, 6520-21. Perhaps the reason that MMA did not become aware of this increase earlier is that MMA did not pose *any* discovery to Prof. Bradley, the sponsor of the CCSTS study results.

higher level of DALs (relative to that of witness Kelley) does not generate costs that conflict with the proposed settlement rates. Tr. 10/5736-45.

With respect to Dr. Haldi's DAL estimate, the revisions to his testimony made the day before his hearing incorporated two entirely separate changes. The first change related to his estimate of DALs mailed by Advo and by others with whom Advo has some type of affiliate relationship. This change related directly to new information received from Advo the day before in response to a Valpak discovery request. The effect of this change was to reduce his original estimate from 5.4 billion to 4.323 billion. See Tr. 9/5555. The second change related to "Others, Independent" DAL mailers. It relied in no way on the new information from Advo, and relied instead on information that was just as available to Valpak in July (when Dr. Haldi's testimony was first being prepared in accordance with the procedural schedule) as it was the day before he testified in August. See Tr. 9/5467-71, 5634. The second change was linked to the first change only to the extent that it was a rather blatant attempt to offset some of the reduction generated by incorporation of the new Advo numbers. By revising his "Others, Independent" figure from 168 million to 345 million, Dr. Haldi was able to boost his total DAL estimate back up to 4.5 billion. Tr. 9/5555.

The only justification Dr. Haldi offered for his new estimate of 345 million was that it was a "conservative estimate" that was "amply" supported by new information (which he inserted as Tables A-9 and 10). Tr. 9/5554. His problem, now shared by Valpak, is that most of the data in those tables were torn to shreds during cross-examination, such that the 159-160 million left (Tr. 9/5678, 5710) could by no stretch of imagination be proffered as corroborating any upward adjustment to Dr. Haldi's original estimate of 168

million, much less as ample support for a “conservative” estimate of 345 million. With absolutely nothing left to justify his new estimate of 345 million, it stands to reason that Dr. Haldi should be held to his original “Others, Independent” estimate of 168 million. In other words, of the two last-minute changes he proposed in his revised testimony, the second change must be rejected as unsupported (in addition to being untimely), maintaining the revised DAL total at 4.323 billion.

Valpak now tries to highlight the fact that the Postal Service did not file rebuttal testimony challenging Dr. Haldi’s revised estimate of 4.5 billion. Valpak Brief at III-10. For those who sat through Dr. Haldi’s cross-examination, however, there was no basis to suspect that any reasonable person would maintain at the conclusion of the hearing that Dr. Haldi’s estimate was, in fact, still holding at exactly the 4.500 billion level at which the hearing began. Advo witness Crowder, moreover, did file rebuttal testimony, and she apparently drew a conclusion very similar to that reached by the Postal Service. She employed a total estimate of 4.315 billion, likewise based on the fact that cross-examination had robbed the 345 million figure of all credibility. Tr. 10/5781-82. In any event, the record now speaks for itself, and that record rather loudly and clearly contradicts Valpak’s surprising assertion (Brief at III-11) that “there should be no serious question that Dr. Haldi’s conservative estimate of 4.5 billion should be adopted as a reasonable estimate of annual DAL volume.” An estimate of 4.323 billion DALs is, in fact, the most the record will support.

Valpak also addressed how the total DAL volume should be distributed. Valpak Brief at III-11 - 13. For purposes of deriving the DAL adjustment in this case, the Postal Service does not challenge the distribution applied by Advo witness Crowder, which

both she (Tr. 10/5737) and Valpak (Brief at III-13) indicate used Dr. Haldi's response to Advo/VP-T2-2 as its basis. Thus, there seems to be no material dispute regarding what distribution numbers to use based on this record.

Nonetheless, the Postal Service is compelled to correct certain egregious mischaracterizations in the Valpak brief regarding sources of the numbers used by witness Kelley. Valpak states:

Witness Kelley attempts to shoehorn his estimated volume of DALs delivered by city and rural carriers into an estimate of the annual volumes of saturation letters delivered by city and rural carriers, which estimate was extrapolated from the data contained in the two-week carrier survey. There is no evidence, however, that the two-week period selected for the carrier survey is representative of the entire year, hence no basis exists for relying on such an extrapolation. Consequently, Dr. Haldi did not feel constrained to use these extrapolated annual volumes.

Valpak Brief at III-12 (footnotes omitted). In footnote 12 on that page, Valpak further cites a discussion on sample selection during hearings on witness Kelley's testimony that makes clear its additional belief that the "two-week carrier survey" referred to in the above quote is actually the data collection effort underlying the new CCSTS variability study sponsored by witnesses Bradley, Stevens, and Kelley.

It is difficult to imagine how Valpak's brief could possibly be more in error on these points. To try to unravel how things got so muddled, it is probably necessary to go back to misstatements originally made by Dr. Haldi. In his response to Advo/VP-T2-2, Dr. Haldi indicated that certain numbers are derived "from the few weeks of sample data in the CCS and RCS that have been extrapolated (or 'blown up') to an annual basis." Tr. 9/5627. In fact, CCS and RCS are year-round sampling systems, just like IOCS and TRACS. See USPS-LR-K-11 (CCS), and USPS-LR-K-12 (RCS). Dr. Haldi evidently was confusing CCS and RCS with the Rural Mail Count, which is based on a

few weeks of data, but is used primarily for variability analysis, not for distribution to subclasses and services. See USPS-LR-K-1, Cost Segment 10. Moreover, as its name would imply, the Rural Mail Count relates exclusively to mail delivered by rural carriers. The new CCSTS study, on the other hand, relates exclusively to city carriers, but like the Rural Mail Count, is based on data from a limited time sample. Yet neither CCSTS nor the Rural Mail Count have anything to do with the CCS and RCS data collected year round and used by witness Kelley to attempt to distribute his total DAL estimate into its constituent components. The claims made in the Valpak brief about the “two-week” sample period are totally inapplicable. If Dr. Haldi truly relied upon the chain of alleged facts advanced in the Valpak brief to support his reasoning, his testimony on these matters cannot be afforded any weight whatsoever.

Lastly with respect to DALs, it may be useful to respond to a discussion in the initial brief of Advo on the effect of a DAL adjustment on PRC versions. Advo Brief at 43-46. Advo believes that, while the LR-K-67 methodology is strongly preferred to either, the PRC-version presented by witness Crowder in Advo-LR-1 is more appropriate than the PRC-version provided by the Postal Service as a Category 5 library reference, USPS-LR-K-151, in response to POIR No. 14. On pages 44-45 of its brief, Advo identifies some alleged flaws in the LR-K-151 approach. The Postal Service believes that there is substantial merit to much of what is stated on those pages of that brief.<sup>53</sup> Regardless of the intuitive appeal of the logic proffered by Advo with respect to why coverage-related costs should not be increased simply because DALs and

---

<sup>53</sup> One exception is with respect to the assertion on page 44 that "city route costs are distributed on the basis of weight." As the Postal Service understands the PRC version, that statement is true with respect to letter route loop/dismount costs, but not true with respect to letter route deviation delivery costs, which are distributed on pieces.

associated host pieces are counted as two separate mailings, however, it is the Postal Service's understanding that such is the methodology by which the PRC-version CRA is developed. In responding to POIR No. 14, the Postal Service strove to stay within the bounds of the PRC-version CRA methodologies. The Commission may wish to revisit the issue in light of the appeal of how witness Crowder conducted her analysis (as described in the Advo brief). But until the Commission does so, it is, at best, ambiguous whether the PRC methodology can be viewed as elastic enough to accommodate the approach espoused by witness Crowder, regardless of its merits.

B. The Established Costing Systems and the Settlement Rates Are Both Consistent with the Range of Ways in Which the Postal Service Actually Handles ECR Saturation Mail in the Real World

Valpak's arguments regarding the alleged extra-bundle constraint are presented in Section IV of its brief. Right off the bat, the title of that section exemplifies Valpak's apparent disdain for the facts:

IV. POSTAL SERVICE COSTING SYSTEMS ARE NOT WELL SUITED TO THE THIRD BUNDLE DELIVERY METHOD, ERRONEOUSLY INDICATING THAT THE ECR SATURATION FLATS ARE LESS COSTLY TO DELIVER THAN ECR SATURATION LETTERS.

Even cursory examination of the record, however, reveals the latter claim to be unambiguously false. Table 1 of the direct testimony of Postal Service witness Kelley (USPS-T-16 at 6), with the DAL adjustment he employed, shows the estimated unit delivery costs of ECR Saturation Flats to be greater than that for ECR Saturation Letters. Later, applying a larger number of DALs (as subsequently developed on the record) for her DAL adjustment, Advo witness Crowder generates ECR Flat unit delivery cost estimates that likewise exceed those for ECR Letters, albeit in her case by an even larger margin. Tr. 10/5738-39. The elaborate argument which Valpak attempts to

construct on this issue, therefore, is not only a house of cards from the ground up, but is even more fundamentally lacking any factual foundation on which to build, because the postal costing systems produce exactly the relative cost relationship which Valpak misleadingly claims to be absent.

The cornerstone of the house of cards is Valpak's repeated and emphatic claims that it would be irrational for the Postal Service to handle saturation letters other than as a third bundle for any reason except the occurrence of capacity constraints preventing it from doing so. See Valpak Brief at IV-3, 14, 15, 16, 18, 23, 24, 26. The real world immediately begins to conflict with this claim, however, in the guise of a postal operating policy that requires all automation compatible letter mail to be sorted in the plants to the DPS level to the extent possible. Tr. 12/6237. Valpak's response, to attempt to prop up its house of cards, is to characterize such a policy as "totally dysfunctional and irrational" unless the capacity constraints it envisions are rampant. Valpak Brief at IV-20. Valpak suggests that this policy needs to be reconciled with (1) the assumption that the Postal Service acts to minimize costs, and (2) "the fact that so many saturation pieces are either cased, collated, or DPS'd." *Id.* at IV-20 - 21. This suggestion, however, is manifestly nonsensical, because the fact that so many saturation pieces are DPS'd would be expected to be (at least partially) a *result* of this policy, not something with which the policy would otherwise need to be reconciled. Valpak's challenge to the rationality of the policy, as presented in its initial brief, is thus utterly unavailing.<sup>54</sup>

---

<sup>54</sup> On page IV-20, Valpak purports to find "clear and unequivocal" support in the Postal Service's response to Advo/USPS-9 for a claim that bypass treatment of saturation letters is more efficient than either casing *or* *DPSing*. Even in the portion quoted on page IV-20 of the Valpak brief, however, that response states only that bypass treatment is more efficient than *casing*. Tr. 12/6245. The response, therefore, cannot

Nonetheless, contrary to the insinuations in Valpak's brief, the Postal Service operating policy on DPS and letters is, in fact, perfectly reasonable. The initial brief of Advo offers a comprehensive and commendable summary of the record in this regard (Advo Brief at pages 15-22), and there is nothing to be gained by reiterating each and every detail spelled out there. To underscore the salient points, however, the physical characteristics of letter bundles render them much less attractive candidates than flats for third bundle handling. And while the substantial majority of saturation letters already pass through plants (i.e., are not entered at the DDU)<sup>55</sup>, plants have no feasible means of segregating pieces potentially subject to the third-bundle constraint from pieces in the same mailing that would not be subject to the constraint. When DPS is an option, therefore, as witness Lewis testified, it makes sense just to DPS them all. Tr. 11/5992, 6009. Consistent with its review of the record, Advo concludes that, even in the absence of saturation flats, the Postal Service would still prefer to DPS saturation letters, and thus removing saturation flats from the system would not likely change in any appreciable way the processing or the costs of saturation letters. Advo Brief at 23, 28. The Postal Service shares this assessment, which, as Advo documents, is amply supported by the record in this proceeding.

Valpak, therefore, is wrong to insist that, theoretically, a substantial number of instances of a binding capacity constraint *must* exist because any other conclusion would suggest irrational behavior by the Postal Service. Equally tellingly, however, Valpak's arguments likewise cannot be reconciled with the available empirical evidence

---

justify Valpak's claim that ergonomic issues do not support a preference for DPS over bypass handling for saturation letters.

<sup>55</sup> Valpak mail, in particular, is overwhelmingly (i.e., 99 percent) entered at plants. Tr. 9/5485.

regarding actual instances of a binding capacity constraint. That evidence comes both from the CCSTS conducted by the Postal Service's carrier cost team, and a survey conducted by postal witness Lewis. Both sources show that capacity constraints are the exception, not the rule. The CCSTS information is noted by Prof. Bradley (USPS-RT-3 at 3), and summarized in greater detail by Advo witness Crowder (Tr. 10/5759-35). Valpak apparently has no response to this source of empirical refutation of its hypothesis, as those portions of the rebuttal testimonies of Prof. Bradley and witness Crowder do not appear to be addressed in the Valpak brief at all.

The results of the survey conducted by witness Lewis are summarized in his rebuttal testimony (USPS-RT-2 at 6-8), and presented in detail in the library reference he sponsored, USPS-LR-K-150. His primary conclusion is that, given less than 44 percent of delivery points potentially subject to the constraint, and with survey results suggesting delivery units being required to deliver more than one full-coverage mailing (defined by him even to include every instance of simultaneous delivery of a DAL and a host piece) on only about 23 percent of days, instances in which the third bundle constraint actually creates a capacity issue appear to represent about 10 percent of the total possible occurrences. *Id.* at 8. His ultimate conclusion, based on his personal experience as well as the survey, is that that alleged capacity constraint problem is "much less of an issue than Dr. Haldi's testimony would have someone believe." Tr. 11/6010, 6012.

Valpak takes issue with the LR-K-150 survey in several respects. For example, Valpak questions the representativeness of a three-week survey. Valpak Brief at IV-18. While acknowledging that his sample was not intended to be representative in a

statistical sense (Tr. 11/6012), Mr. Lewis was able to confirm that, given the nature of saturation mail and its inherent regularity, even a three-week period in August should allow the capture of many examples of mailings that appear with a given frequency (Tr. 11/6020-21). Moreover, even if a three-week period precludes the certainty of catching all saturations mailings entered on a monthly basis, which Valpak at IV-18 mentions as a particular concern, there is no reason to believe that the three-week period should not capture a fair proportion of such monthly mailings.

Valpak also criticizes the wording of the message sent by witness Lewis to the field requesting cooperation with the survey effort. *Id.* at IV-18 - 19. Valpak asserts that Mr. Lewis “told them what response he was seeking (that few conflicts exist)” and explained to them “exactly what response he wanted.” *Id.* The plain wording of the message, however, does not support these claims. As quoted at Tr. 11/6014, the two sentences of the email in question read:

In our current rate case proceeding, Val-Pak witness Haldi provides testimony that asserts that in city delivery operations we often must case sequenced, full-coverage mailings because of the third bundle constraint. For a number of reasons, the Postal Service wants to challenge Haldi’s testimony.

Mr. Lewis explained that his intent with this language was to provide background and context, and to reassure the field that he was not trying to evaluate their performance. Tr. 11/6015. The claims made in Valpak’s brief, in contrast, are presented through the lens of litigants to whom every subtle nuance resonates sharply, because of their intimate familiarity with the relatively few matters that have crystallized over time into the fulcra of the most hotly-contested debates. There is no reason to expect, however, that the operative field personnel would focus on any such subtleties. They were simply

being asked to fulfill an entirely objective request to forward basic information about mailings received by their delivery unit. More to the point, without any basis to speculate how “often” Dr. Haldi was asserting that the constraint caused casing, and without any knowledge of how witness Lewis was going to aggregate the information they provided to identify conflicts, recipients of this message would not know “exactly” what response witness Lewis was seeking. They had no reason to do other than accurately provide him the simple information he was requesting. The concerns expressed by Valpak’s brief on this point are unwarranted.

On the record in this proceeding, therefore, are two credible sources of empirical information regarding the limited occurrences of conflicts in delivery units between saturation letter mailings and saturation flat mailings. Since Valpak has no real response to such data, however, it resorts to a feeble makeweight with the appearance of empirical content, but which is actually devoid of anything tangible. This effort appears on pages IV-21 through IV-23 of the Valpak brief. On those pages, Valpak posits three scenarios: saturation volume up to 4 billion pieces, saturation volume between 4 and 8 billion pieces, and saturation volume between 8 billion pieces and the current volume level of 13.8 billion pieces. Supposedly, as we hypothetically move volume upward through the progression of the three scenarios, something happens to increase the marginal cost of saturation mail. But if we look carefully in order to determine exactly what it is that purportedly occurs at the volume points of 4 billion and 8 billion pieces, we find nothing.<sup>56</sup> All that appears is hollow pontification that, as

---

<sup>56</sup> One might have expected, for example, some type of calculation attempting to convert annual volume to pieces per delivery point per week, or something of that nature. Taking the highest volume, however, the FY04 volume of 13.8 billion cited by

volume increases, the opportunity for conflicts increase. But what if most of the increase is in automatable saturation letters which, according to policy, should be DPS'd? Or how do we know that the progression of actual conflicts across the three scenarios would not be increasing, but still trivial (e.g., something on the order of 0.3 percent to 0.7 percent to 1.0 percent)? The ability to absorb additional mailings is an empirical issue, about which Valpak's ramblings on IV-21 to 23 tell us nothing.

In summary, the Postal Service does not disagree with Valpak that saturation mail can be handled in a number of ways – cased, DPS'd, collated, or as a third bundle. But as Prof. Bradley testified (e.g., USPS-RT-3 at 4, 27), the costing systems jointly relied upon by the Postal Service and the Commission appropriately measure the marginal costs of saturation mail across the wide variety of operating environments and under the wide variety of circumstances in which saturation mail is actually handled. The estimated costs reflect the relative proportions of the various handling methods actually employed. Although Valpak's Brief at IV-1 erroneously states otherwise, the costing systems in this case estimate unit delivery costs for Saturation ECR flats that are higher than those for Saturation ECR letters. Valpak's insistence (Brief at IV-25) that the Commission should not accept those marginal cost estimates is grossly disproportional to any real world basis for concern with respect to the theoretical issues that Valpak has raised. But for Valpak (Brief at IV-30 -31) to support Dr. Haldi's

---

Valpak, and dividing by total residential delivery points (129.582 million, 2004 Annual Report, pg. 49), yields 106 average saturation pieces per residential delivery point per year, or almost exactly 2 per week. Since delivery offices generally have up to 2 days to deliver saturation mail (i.e., 2 days over which to juggle 2 mailings), such a calculation would corroborate the other empirical evidence of conflicts occurring only relatively infrequently at current volume levels, which might explain why Valpak eschewed the opportunity to proceed along those lines.

proposal that higher marginal cost for saturation mail be employed *solely* for the purposes of estimating the letter-flat differential, rather than for all ratemaking purposes, demonstrates conclusively how far afield Valpak is willing to stray from sound ratemaking methodology. Certainly nothing offered by Valpak with respect to the third bundle constraint provides the least amount of support for deviation from the settlement rates.

C. The Commission Should Disregard the OCA's Blatant Attempt in its Initial Brief to Attack the Postal Service's Costing Proposals with Non-Record Materials

On pages 36 through 90, across several sections addressing several specific and general costing topics, the OCA has presented testimony masquerading as a brief. Apparently, the OCA would prefer to put forward "expert opinion" without the annoying necessity of having to have a competent expert testify to the opinion, or withstand written or oral cross-examination, or face rebuttal by other experts. Various pronouncements are made on economic theory, econometric practice, and Postal Service operations, usually without a shred of evidence or citation to authority. It is as if the writers of the OCA's brief have anointed themselves, simultaneously, as experts in many different fields. Of course, in reality, they are not experts in the fields of economic theory, econometrics, or operational practice, and this is shown in the number and nature of the errors that are strewn throughout the "testimony."

While a reply brief is not the place to provide rebuttal testimony, illustration of just a few of the errors in the OCA's brief reveals its complete and total inadequacy:

- In discussing Sequenced Mail with the CCSTS, the OCA states "in certain circumstances Sequenced Mail was cased, put into the DPS mail stream or collated, thereby altering the sample size of Sequenced Mail from the way it started out." OCA Brief at 70 (footnotes omitted). This assertion is untrue. As

was made very clear during the case (e.g., Tr. 6/2031, 2245, 2247-48), the Postal Service defines “Sequenced Mail” as mail that is taken directly to the street without in-office handling. By its very definition “Sequenced Mail” cannot be cased or DPSed. If it is, it ceases to be Sequenced Mail and becomes cased mail or DPS mail. Tr. 6/2029-31. Thus, the OCA’s prattling about the fact that saturation mail is handled in different ways, thereby “altering the sample size” for Sequenced Mail, is completely without content and reveals the cavalier fashion in which the OCA’s arguments are made.

- The OCA (e.g., Brief at 66, 78, 86) complains that Prof. Bradley’s equations are necessarily inadequate because some of the estimated coefficients have the “wrong signs.” That is, it complains that some of the estimated coefficients on the volume terms are negative. However, anyone with passing familiarity with economic theory and econometrics knows that this false claim does not reveal a problem with the recommended equation, but rather is a demonstration of the OCA’s inability to interpret econometric results properly. A review of the recommended econometric equation on page 38 of Professor Bradley’s testimony (USPS-T-14) shows that the negative signs occur only on the coefficients on squared volume terms and the density variable. But it is well known that the existence of economies of scale implies that the squared volume terms in a quadratic equation should be negative, revealing that costs are increasing, but at a decreasing rate. Thus, it is not a weakness of the recommended equation that these terms are negative, but a strength! This result is entirely consistent with previous Commission analysis of delivery. Similarly, the sign on the density variable should be negative, indicating that the cost of delivering a given volume of mail falls as the delivery points are closer together. Tr. 6/2092.

These mistakes are whoppers, not just small miscues, and they are symptomatic of the OCA’s feeble attempt at criticizing the new City Carrier Street Time study; an attempt chock full of speculation and error. Similar points of equal significance could be made with respect to the OCA’s presentation on mail processing costs:

- The OCA incorrectly contends that the Postal Service’s mail processing “testimony never relates the cost driver to the form of the underlying production function.” OCA Brief at 45. In fact, in addition to Dr. Bozzo’s discussion of the underlying economic theory in direct testimony (USPS-T-12 at 8-9) and description of how piece handlings relate to workhours related to runtime in automated operations (*id.* at 14), Dr. Bozzo discusses the form of the production function in responding to an OCA interrogatory (Tr. 5/1453-4). In that response, Dr. Bozzo notes that the Postal Service’s “operating plan” governs the relationship between mail volumes and mail processing “outputs,” provides an interpretation of the separability of cost pools, and defines cost pool “output” as

the “aggregate sorting improvements performed within the cost pool,” which is consistent with the OCA’s assertion that “what matters” for mail processing output measurement “is sortation” (OCA Brief at 48).

- The OCA’s critique of MODS piece handlings as output measures for sorting operations (OCA Brief at 48-54) is replete with basic misunderstandings of the piece handling measures. The OCA asserts that the “true output of a plant is depth of sort” which “cannot be measured as or related to—directly or indirectly—an accumulation of piece handlings.” OCA Brief at 48. This is flatly contradicted by the definition of total piece handlings as “the number of pieces processed [i.e., sorted] successfully” (USPS-T-12 at 12), as well as Dr. Bozzo’s exposition of the relationship between piece handlings and depth of sortation (*id.* at 13). The OCA purports to demonstrate hypothetical “contradictions” related to the use of piece handlings, for instance one plant somehow using twice the piece handlings to sort the same pieces to the same depth of sort as another (OCA Brief at 51), that are simply not possible given the Postal Service’s sorting mailflows (see, e.g., USPS-T-21 at 4). This culminates in a “demonstration” that TPF is a measure of “capital input” (OCA Brief at 53) using an equation that relates TPF to machine runtime in Dr. Bozzo’s testimony (USPS-T-12 at 14, line 6). But by the same logic, the very next equation (*id.* at line 8), describing the relationship of TPF to workhours, would identify TPF with labor input. OCA’s contradiction is obvious, as is its failure to recognize that it is completely normal for output to appear on the right hand side of factor demand equations. (USPS-T-12 at 8; Hal R. Varian, *Microeconomic Analysis* [Second Edition] at 54).

Moreover, the issues raised by the OCA relative to the new carrier study (CCSTS) do not at all suggest that the new study is not preferred to the old, outdated, previous carrier studies. The OCA argues as if perfection is the only acceptable improvement over flawed studies now approaching 20 years in age. The OCA apparently does not realize that its criticisms of the new study (e.g., cross sectional data, negative coefficient estimates, lack of demographic data) apply with much greater force to the old studies. Without a doubt, these criticisms cannot provide a basis to prefer the old studies over the new.

Indeed, the OCA reveals its actual agenda when it shockingly argues that perhaps the Commission “should assume that these [carrier street time] costs are 100 percent volume variable.” OCA Brief at 87. Anyone even mildly familiar with the work

done by intervenors in all previous rate cases, by the Commission staff, by experts in other posts, and by academic researchers, would note that this assertion is foolish and completely at odds with the reality of postal delivery.

In large measure, the tone of the costing sections of the OCA's brief is quixotically unrealistic. The OCA speaks as if the Postal Service has an infinite amount of time to apply infinite analytical resources (staff and consultant) to an endless supply of data that can be collected and made available for immediate analysis without cost and without any disruption of operations. It is as if the OCA thinks the Postal Service should get out of the business of delivering mail in order to be able to focus on doing a better job of measuring costs. Ironies in the brief are abundant. For example, the OCA insists that the Postal Service should be required to "*demonstrate empirically that the assumptions needed to generate marginal costs are true.*" OCA Brief at 88 (emphasis in original). The OCA apparently fails to recognize that if empirical information were available to unequivocally confirm or refute all assumptions, then they no longer would be assumptions, they would be fact. More fundamentally, this statement appears in the same brief in which the OCA is urging the Commission to retreat to assumptions that mail processing costs and delivery costs vary in exact proportion to mail volume, with no empirical support for either proposition. The logical inconsistency of these views is manifest.

The Postal Service shares the OCA's aspiration for constant improvement in cost attribution and distribution procedures across dynamic operating environments, but the OCA's brief transcends constructive criticism and ventures into the realm of a fantasy

wish list. In any event, based as it is on non-record materials, the Commission is precluded from placing any reliance upon it.

IV. INTERVENOR ARGUMENTS IN OPPOSITION TO THE ACROSS-THE-BOARD PROPOSAL SHOULD NOT INFLUENCE THE OUTCOME IN THIS PROCEEDING

In determining how to respond to the arguments regarding pricing and rate design made by the several Docket No. R2005-1 intervenors who oppose the July 22, 2005 Stipulation and Agreement, the United States Postal Service invites the Postal Rate Commission to carefully review the record in this proceeding. Then, as Valpak so eloquently put it several years ago, the Postal Service:

urges the Commission to honor the collective judgment of mailers, who, in good faith, participated in the settlement process, and to adopt the totality of the settlement rates without change in its Opinion and Recommended Decision.

See Docket No. R2001-1, Initial Brief of Valpak at 3. (March 4, 2002). Returning to Docket No. R2005-1, the Postal Service observes that the principal arguments in the September 26, 2005, Initial Brief of Valpak opposing the current across-the-board proposal were anticipated and have been refuted by the Initial Brief of the Postal Service, as well as the contemporaneously filed Initial Briefs of such parties as Advo, the Direct Marketing Association, and the Greeting Card Association. In their Initial Briefs, the Office of the Consumer Advocate and Douglas Carlson present additional arguments against or alternatives to the Postal Service's across-the-board proposal. The Postal Service responds to the arguments in the Initial Briefs of Valpak, the OCA, Douglas Carlson, and David Popkin below.

A. The Valpak Trifecta: Wrong On The Law, Wrong On The Facts And Wrong On Commission Precedent

Valpak's Initial Brief is so laden with unfounded, inaccurate and inconsistent assertions that its arguments against the Postal Service's across-the board rates and fees should be dismissed.

1. There is no basis for Valpak's legislative interpolation

At pages 7-8 of Section II of its Initial Brief, Valpak asserts that the identification of the Public Law 108-18 escrow obligation as an "operating expense" -- in combination with the reference to "operating expenses" at § 3621 of the Postal Reorganization Act -- prevents the Postal Service from proposing that the escrow-driven Docket No. R2005-1 test year revenue requirement be recovered through across-the-board rate and fee increases. However, as the Commission will observe, neither PL 108-18 nor § 3621 places any restriction on the broad discretion granted to the Commission and the Governors under § 3622(b) in determining how to distribute the burden of any non-attributable "operating expenses." This applies whether or not the expenses have any relation to the existence of any mail class or service, or to any function or policy of the Postal Service or the Post Office Department. The designation of the escrow obligation as an operating expenses in § 3(a)(3) of PL 108-18<sup>57</sup> merely creates a duty to incorporate that expense into the budget and set it aside in FY 2006. As demonstrated by Postal Service witness Tayman at Exhibit USPS-6A, the Postal Service is acting accordingly.<sup>58</sup>

Section 3621 of the Act identifies "operating expenses" as one of the elements that comprise "total operating costs," which serve as one side of the breakeven equation. However, there is no directive in § 3621 that any particular expense be regarded as attributable or institutional, or that institutional costs be distributed in any particular manner among the subclasses and special services. Thus, there is no basis

---

<sup>57</sup> 117 Stat 624, 627.

<sup>58</sup> Witness Tayman makes clear that under generally accepted accounting standards, the escrow obligation expense is not regarded as an operating expense. Tr. 2/237-38.

for Valpak's assertion that either PL 108-18 or § 3621 dictates "the proper method to address a pending deficit . . . ." <sup>59</sup> Section 205(a) of the Act, which dictates that "[t]he Board shall direct and control the expenditures of the Postal Service," grants the Board of Governors of the Postal Service sole authority to determine how to address pending deficits. In this instance, in lieu of other options, the Board has authorized the Postal Service to address its pending FY 2006 deficit through rate and fee changes. Section 3662(b) governs *how* the burden of that deficit can be distributed among the mail classes and special services.

2. The evidentiary record is at odds with Valpak's insinuations

In comparing the evidentiary record to various characterizations of it by Valpak, the Commission will observe some divergence. The following examples are illustrative.

At II-5 of its Brief, Valpak chastises Postal Service witness Tayman (USPS-T-6) for failing, in its view, to sufficiently provide any basis for the Postal Service treating the FY 2006 escrow obligation differently from other obligations that Valpak describes as "not dissimilar in type or amount from the escrow payment." As the record makes clear, Postal Service witness Robinson (USPS-T-27) testifies on this subject, clearly distinguishing PL 108-18 from earlier Acts of Congress that shifted the burden of personnel-related costs clearly associated with the Postal Service <sup>60</sup> from taxpayers to ratepayers. As she explains, the *nature* of these earlier personnel expenses cannot be analogized to the escrow expense. The various Omnibus Budget Reconciliation Act obligations were directly tied to personnel policies applicable to postal employees. In

---

<sup>59</sup> Valpak Brief at II-4.

<sup>60</sup> Or its predecessor, the Post Office Department.

contrast, the pending FY 2006 deficit is driven by legislatively-defined *postal expenses that are explicitly barred from being expended*,<sup>61</sup> and that explicitly have *no purpose* – postal or otherwise -- assigned to them at all.<sup>62</sup> See Tr. 3/440-44.

Similarly, Valpak seeks to distort the Commission's perception of the record by misrepresenting the testimony of witness Robinson. At pages 15-16 of Section II of its Brief, Valpak references witness Robinson's response to Question 3(b) of Presiding Officer's Information Request No. 4. At Tr. 3/471, in support of the across-the-board approach, witness Robinson explains why the Postal Service regards it as unfair to distribute the escrow burden – which has no nexus to the provision of postal services – to mail classes on the basis of such characteristics as their cube/weight relationships or volume. From that, Valpak fabricates an assertion that witness Robinson subscribes to the notion that “if parcel post costs have no relation to an exogenous [escrow] fund, they should have no relation to parcel post rates either.” There is no basis for ascribing any such belief to witness Robinson. In fact, her discussion elaborates on how changes in Parcel Post costs, the revenue requirement, and other factors are all usually considered in the process of rate design. She reaches the conclusion, however, that the escrow burden should not be allocated on other than a *pro rata* basis, even in the face of a change in the Parcel Post cube-weight relationship. She does not assert that such a change should not ordinarily be considered in rate design.

In a further effort to muddy the waters, Valpak's Brief at II-9 perpetuates the canard in witness Mitchell's testimony (VP-T-1 at 12; Tr. 11/5278) that the Postal

---

<sup>61</sup> Public Law 108-18, § 3(A)(3), 117 Stat 624, 627.

<sup>62</sup> Notwithstanding all steps to-date taken in compliance with §§ 3(e) and (f) of Public Law 108-18. See, Tr. 2/232-33.

Service proposed an across-the-board approach in this docket simply because it considers equal percentage rate increases to be fair. The record in this case makes abundantly clear that the Postal Service elected the across-the-board approach for several integrated reasons: it is a fair method of distributing an extraordinary expense that has no postal purpose and that is being imposed at a time when the Postal Service otherwise would not be raising rates; the obligation is imminent; an across the-board proposal would enhance the prospect for inducing parties to shorten the litigation and create an opportunity for an expedited recommended decision; this, in turn, would permit the Postal Service to recover as much of the expense in FY 2006 as possible under the circumstances. USPS-T-1 at 2-6. Despite Valpak's claims, the testimony of Postmaster General Potter (USPS-T-1) clearly articulates the nuanced policy basis underlying the instant request. Accordingly, there is no basis for Valpak's assertion at II-9 of its Brief that the Postal Service has embraced some unspoken corollary that "across-the-board ratesetting is more equitable than cost driven-ratesetting."

Likewise, at page II-15, Valpak claims that Postal Service pricing witness Robinson did not look at costs *ex post* or study trends in cost over time or assess the costing results in any other way. In doing so, Valpak ignores witness Robinson's discussion of the need to propose deviations from the across-the-board approach out of consideration for the cost floor requirement in § 3622(b)(3) for Registered Mail and the Periodicals Application Fees. USPS-T-27 at 16-17. Such determinations could not have been made without analyzing costs *ex post*.<sup>63</sup> Moreover, one does not calculate and evaluate markup indices – as witness Robinson does (USPS-T-27 at 24) – except

---

<sup>63</sup> See also, *e.g.*, Tr. 3/344-46.

for the purpose of determining whether cost trends (as subsumed in markups and cost coverage relationships from one case to the next) suggest taking particular subclass markups away from the results implied by an across-the-board approach. Without such an evaluation of the cost data, witness Robinson could not have concluded that there was no compelling basis to propose other cost coverages that varied from the result implied by across-the-board rate increases.

At pages V-17-18 of its Brief, Valpak compares unit costs and contribution for the Standard ECR and Standard Regular subclasses and sounds the alarm that the rates proposed by the Postal Service reveal a commitment “to spending more to obtain less net revenue, using an above average percentage rate increase to ECR to further shift volumes to [Standard] Regular.” Valpak continues by asserting that:

The failure to raise Regular rates adequately to cover increases in Regular unit costs causes the burden of institutional contributions to be shifted to other subclasses, such as ECR . . . .

Valpak Brief at V-18. However, when the Commission compares projected Standard ECR and Regular revenues and contribution in Postal Service witness Robinson's Exhibit USPS-27A on a Before Rates Test Year basis to revenues and contribution in Exhibit USPS-27B on an After Rates Test Year basis, the Commission will observe an *increase* in aggregate net revenue, not a decrease, for each subclass. See also, Tr. 3/453-458.

At page V-3, n.4 of its Brief, Valpak chastises Postal Service witness Taufique (USPS-T-28) for not properly crediting *the Postal Rate Commission* with determining that the rates and fees for each subclass or special service generate sufficient revenues to cover its attributable costs. But then, consider Valpak's argument later that:

[A]fter ECR was established as a subclass, the markup imposed on it has jumped from below average (as part of BRR) to the highest of any mail subclass. It has been demonstrated at length that this excessive markup is not the result of an objective application of the non-cost criteria. Rather, it appears to be a consequence of a certain lethargy, or lack of effort on the Postal Service. With every omnibus rate case, the [Postal Service] rate design witness acknowledges that the markup on ECR is too high, and proposes a tempered rate increase to mitigate the damage inflicted. Ten years after MC95-1, ECR and First-Class letters are the only subclasses with markup indexes above 1.000. [footnote omitted]

Valpak Brief at V-19. As for the successive Postal Service omnibus rate case witnesses who have proposed Standard ECR cost coverages that Valpak describes above<sup>64</sup> in its Brief as being *too high*, the Postal Service invites the Commission's attention to the record in each case. In each instance, the Commission will observe that the Postal Service testimony (to which Valpak's Brief refers and to which Valpak witness Mitchell cites at Tr. 9/5308-09) stands for the proposition that the proposed Standard ECR cost coverages are relatively high in relation to other cost coverages, not that the proposed or previously recommended Standard ECR cost coverages are "too high" or higher than the criteria of the Act suggest.<sup>65</sup>

At page II-3, fn. 1, of its Brief, Valpak trumpets the discovery of a description of Postmaster General Potter's testimony (USPS-T-1) that Postal Service witness Robinson inadvertently states in the form of a quotation instead of a paraphrase.

---

<sup>64</sup> And at pages V-12-13 of its Brief.

<sup>65</sup> And, unless Valpak has stumbled upon some heretofore unknown division of responsibilities in chapter 36 of the Postal Reorganization Act, the Postal Service submits that Valpak cannot have it both ways in the above quoted passages from its Brief. It seems that whichever agency -- the Postal Service or the Commission -- gets the credit/blame for determining whether § 3622(b)(3) is satisfied from case-to-case also gets the credit/blame for how the other § 3622(b) pricing criteria are applied as part of the ratemaking process. The historically "excessive" Standard ECR markups about which Valpak wails reflect the successive recommendations of the Commission that have been approved or, in the case of Docket No. R2000-1, modified by the Governors.

Valpak is correct that witness Potter's testimony does not use the *exact* words inadvertently attributed to him in the form of a quotation. However, it would be misleading for Valpak to imply, as it does, that he did not utter words to the same effect. See, USPS-T-1 at 7.<sup>66</sup>

Further, Valpak tries to cloud the issues by juxtaposing witness Robinson's deference to the policy determination (ratified by the Board of Governors<sup>67</sup> in the form of the request in this proceeding) that the Postal Service propose across-the-board rate and fee increases with the Postmaster General's "candid admission that he is 'not an expert in postal costing and pricing . . .'" Valpak Brief at II-6. Valpak questions why witness Robinson would defer to the Postmaster General's policy determination, under such circumstances. At this point, Valpak has reduced itself to sniping at the Postmaster General for being modest. By education, the Postmaster General is an economist. USPS-T-1 at ii. By occupation, he is the chief executive officer of a large Federal agency employing 700,000 people at thousands of facilities around the nation. He directs and consults with Postal Service economists who are responsible, on a day-to-day basis, for working out the complicated details of postal financial and marketing policy options and for providing him advice. Valpak criticizes one of these economists for testifying that she deferred to and implemented a policy determination made by a Postmaster General who (1) routinely consults with and defers to the judgment of his in-

---

<sup>66</sup> See *also*, Tr. 2/89.

<sup>67</sup> Lest Valpak forget, the Postmaster General is a member of the Board.

house experts and (2) modestly asserts that he does not consider himself to be as expert as *they* are.<sup>68</sup> This is not fodder for attack.

3. Valpak mischaracterizes and misapplies Commission precedent. Valpak does not stop at mischaracterizing the testimony of the Postmaster General, but victimizes the Chairman of the Postal Rate Commission as well. In summarizing Docket No. R2001-1, Valpak argues *now* that the proceeding was “not fully litigated, as the case was settled due to (i) ‘the events of September 11,’ and (ii) ‘the use of the mail system for spreading disease.’” As a basis for its summary of the resolution of Docket No. R2001-1, Valpak quotes a statement of Chairman George Omas at the Docket No. R2001-1 pre-hearing conference out of context.<sup>69</sup> There, the Chairman was identifying reasons why the parties might want to explore the prospect of narrowing the scope and duration of that litigation through settlement. However, the Chairman was not, as Valpak implies, declaring at the pre-hearing conference what the basis would be for any rates and fees that the Commission might later recommend.

There probably would never have been so energized an effort by the parties to minimize the contested issues in Docket No. R2001-1, had it not been for the Chairman’s leadership at the October 25, 2001, pre-hearing conference. However, that case was not decided simply because tragic events occurred in September and October of 2001. The case was decided on the basis of the Commission’s finding that the record evidence, which was filed with the request and enhanced through discovery and

---

<sup>68</sup> See also, Valpak Brief at VI-5, where the Postmaster General is chastised for delegating to Postal Service economist and rate design expert Altaf Taufique (USPS-T-28) the responsibility for working out the intricate details of nonprofit Standard Mail rate design in the context of this across-the-board case.

<sup>69</sup> Docket No. R2001-1, Tr. 1/39.

litigation, supported the recommendation of rates, fees, and classifications reflected in a Second Revised Stipulation and Agreement. See PRC Op. R2001-1 (March 22, 2002).

At page II-14 of its Docket No. R2005-1 Initial Brief, Valpak argues that the current rates were “untested” in Docket No. R2001-1. One gets at least a slightly different impression reading the discussion of the Docket No. R2001-1 evidentiary record in the Docket No. R2001-1 Initial Brief of Valpak, filed on March 4, 2002.

At pages 10 and 11 of its Brief, Valpak also misreads the Commission’s Docket No. R90-1 opinion as providing a basis for rejecting the Postal Service’s current across-the-board proposal. At the bottom of page II-10 of its Brief, Valpak focuses on a passage from that opinion in which the Commission explained the basis for its recommendation to increase third-class bulk mail rates 24.7 percent over the rates adopted only several years earlier as a result of Docket No. R87-1. See PRC. Op. R90-1, Vol.1, at ¶¶4099-4118. At ¶4108, the Commission explained that, in contrast to third-class bulk mail, its recommendation of relatively moderate rate increases for First-Class Mail was based on the expectation that the ramping-up of letter automation would significantly moderate First-Class Mail test year cost increases, as compared to costs for mail (such as third-class bulk) consisting largely of flats and parcels. In that context, the Commission rejected entreaties to moderate third-class bulk mail rate increases in lock-step with First-Class Mail increases when it opined at ¶4109 that “[a]ttempting to keep the rate increases for all subclasses equal would make the exacting determination of cost causality meaningless.”

The Commission’s reference to cost causality in ¶4109 was clearly at the aggregate subclass level and, consequently, served to emphasize the importance of the

attributable cost floor requirement in § 3622(b)(3). This passage in the Commission's Docket No. R90-1 opinion cannot fairly be interpreted as implying that, even if subsection (b)(3) is otherwise satisfied, across-the-board rate increases cannot be justified by an application of the remaining § 3622(b) pricing criteria.

In contrast, over an even longer time span than the interval between Docket Nos. R87-1 and R90-1, Valpak is now faced with – not a 25 percent rate increase but – a 5.5 percent rate increase. Exhibit USPS-27D. There is no record basis for concluding that the relative projected test year cost increases between the First-Class Mail and Standard ECR subclasses in the instant proceeding compare to the projected First-Class Mail/third-class bulk test year cost increase differences that informed the Commission's Docket No. R90-1 analysis. Second, there is no basis for concluding that the currently proposed 5.3 percent and 5.5 percent rate increases proposed, respectively, for First-Class Mail Letters and Standard ECR over and above the current Docket No. R2001-1 rates are so out of line out with their relative projected test year subclass cost increases as to warrant deviations from the across-the-board approach, given the rationale for the current request.

**B. Alternative Pricing And Rate Designs Should Be Rejected**

1. Valpak's flawed analysis of the pricing criteria does not support a deviation from the Stipulation and Agreement

Section V of the Valpak Brief discusses and embellishes Valpak witness Mitchell's proposal that the Commission apply the §3622(b) pricing factors to deviate from the across-the-board proposal of the Postal Service for the benefit of Standard ECR mail and at the expense of other mailers. As explained below, Valpak's arguments and other assertions provide an insufficient basis for recommending some alternative to

the rates designed by Postal Service witness Taufique (USPS-T-28) or Postal Service witness Robinson's (USPS-T-27) comprehensive evaluation of the § 3622(b) pricing criteria.

a. Valpak mistakenly seeks to convert custom into law

Valpak's attempts to disparage Postal Service witness Robinson's cost coverage analysis in its Brief (describing it at page V-4 as "perfunctory" and at page V-2 as something that witness Robinson "backs into") fail to tarnish witness Robinson's careful and considered evaluation of the criteria, as discussed at USPS-T-27, pages 4-24A. Thus, the record evidence thoroughly disproves the assertion (Valpak Brief at V-4) that all witness Robinson did was to determine that the across-the-board rates designed by witness Taufique satisfied the § 3622(b)(3) attributable cost floor requirement. Valpak criticizes witness Robinson because her testimony "did not address how each of the non-cost criteria of the Act applies to Standard ECR or Standard Regular mail." Valpak Brief at V-4. However, the courts have affirmed that, with the exception of § 3622(b)(3), the Commission – and by implication, the Postal Service – need not demonstrate the specific effect of every § 3622(b) criterion on each subclass or service. *See Mail Order Association of America v. United States Postal Service*, 2 F.3d 403, 425-27 (D.C. Cir. 1993); *Direct Marketing Association v. United States Postal Service*, 778 F.2d at 102 (2d Cir. 1985). Thus, while a subclass-by-subclass analysis of the application of each pricing criterion may be traditional, it is not mandatory.

b. Valpak's conclusions rest upon an unstable foundation

In its quest to return the Commission to yesteryear and the days when the long-gone third-class mail bulk rate regular subclass enjoyed a 146.2 percent cost coverage

and a below-average markup index of 0.927,<sup>70</sup> Valpak makes arguments that rest upon several fatally flawed assumptions.

First is the assumption that the implied cost coverages and markups for both elements of the former third-class mail bulk rate regular subclass (one of which is now Standard Regular and the other of which is now Standard ECR) were both below the systemwide average before Docket No. MC95-1. It defies reason for one to nostalgically assume that to have been the case.<sup>71</sup> Docket No. MC95-1 established that the two general elements of third-class bulk rate regular had significantly different costs, with the cost for what became Standard ECR being lower. By definition, the implied ECR cost coverage and markup before reclassification would have been higher than those for the former subclass as a whole. This would imply that, prior to Docket No. MC95-1, the different components of the former subclass had significantly different implied markups. Only as long as disparate components were part of the former subclass could each component claim the honor of the relatively low subclass cost coverage and markup that Valpak so fondly remembers.<sup>72</sup>

At page V-5 of its Brief, Valpak argues that the only thing that has changed about Standard ECR since Docket No. MC95-1 is that it has become more price-sensitive. Accordingly, Valpak argues that it would be unfair and inequitable to impose a *dramatically higher* cost coverage on ECR than existed at the conclusion of Docket No. R90-1.

---

<sup>70</sup> Valpak Brief at V-5.

<sup>71</sup> Perhaps only in the fictional and idyllic Lake Wobegon Postal Service might one find all of the subclass cost coverages and markups to be below average.

<sup>72</sup> The same faulty assumption infects Valpak's argument at V-19 that "after ECR was established as a subclass, the markup imposed on it has jumped from below average (as part of BRR) to the highest of any mail class."

Valpak's argument is fatally flawed in two ways. First, as just discussed, it defies common sense to assume, as Valpak does, that mail currently classified as Standard ECR implicitly had the same cost coverage as the third-class bulk rate regular subclass as a whole when it was a component of that subclass. It is only on this basis that Valpak complains that ECR's cost coverage is "dramatically higher" than it was after Docket No. R90-1.

Second, Valpak points to the changes in Standard ECR's own-price elasticity as the additional support for its assertion that its cost coverage is too high. However, the Commission cannot determine cost coverages based on this isolated observation.<sup>73</sup> Notwithstanding changes in the price elasticity for Standard ECR over the last decade, the postal universe has not been frozen in some cryogenic state. Current Standard ECR rates reflect the work of the Postal Service and the Commission from one omnibus rate case to the next balancing all relevant costing and pricing considerations. Despite Valpak's nostalgic yearning, the Commission has declined each opportunity since Docket No. MC95-1 to recommend cost coverages for Standard ECR that more or less match Valpak's Docket No. R90-1 ideal.

At V-6 of its Brief, Valpak inadvertently backs into the critical point that the objective of ratemaking is "reasonable rates." After all, it is rates that mailers pay, not cost coverages or markups. Not unexpectedly, Valpak is shy about mentioning that the rates for what is now Standard ECR declined as a result of Docket No. MC95-1 and remain among the lowest in the Domestic Mail Classification Schedule. See USPS

---

<sup>73</sup> And, in any event, the Commission is encouraged to take into account the concerns expressed by Postal Service witness Thress (USPS-T-7) regarding the evaluation of changes in demand elasticity estimates from one rate case to the next. Tr. 3/282-83.

Library Reference K-73. Nor will Valpak step forward to highlight the reality that, if the rates in the Stipulation and Agreement are implemented in January of 2006, Standard ECR rates will have risen at a pace lower than the rate of inflation since when current rates were implemented in June of 2002. This would hardly seem an unfair and inequitable result, within the meaning of § 3622(b)(1), or one that was insensitive to the impact of rate increases on mailers, within the meaning of § 3622(b)(4).

c. Valpak's Brief belatedly singles out a victim

As observed in the Postal Service's Initial Brief at V-38-39, Valpak witness Mitchell avoided providing the evidentiary record with any explanation of the impact that his proposed Standard ECR cost coverage reduction proposal would have on other subclasses and special services in the zero-sum game of institutional cost distribution, if the Commission were inclined to consider his proposal. Valpak counsel valiantly steps into the breach by condemning the Standard Regular subclass to receive a higher cost coverage and higher rate increases than are reflected in the Stipulation and Agreement. Valpak Brief at V-20. The Postal Service will not be hyper-critical of the Valpak Brief for not offering an explanation of what the resulting Standard Regular cost coverage or rates might be because, if such testimony had been contained in Valpak's Brief, the Commission would be proscribed from relying upon it.

2. Valpak's desire to avoid any escrow burden for Standard ECR blurs its reading of § 3626(a)(6)(A)

In section VI of its Brief, Valpak discusses the Postal Service's application of § 3626(a)(6)(A) in proposing rates for Standard Mail. This provision directs that rates be set so that the average revenue per piece generated for each nonprofit Standard Mail subclass is, as nearly as practicable, 60 percent of the revenue generated by its

corresponding commercial subclass. Balancing this statutory target with the objective of proposing rate increases as close to 5.4 percent as practicable for each subclass, the Postal Service proposes Standard ECR and Standard Nonprofit ECR rate increases of 5.5 and 6.0 percent, respectively.<sup>74</sup> As a consequence, under the Postal Service's proposal, Standard NECR revenue per piece is 56.4 percent of ECR per-piece revenue. Valpak argues that such a result is contrary to the intent of § 3626(a)(6)(A).

Valpak's claim rests on the simple proposition that the clause *as nearly as practicable* in that subsection imposes a rule of absolutely strict adherence to the 60 percent target, except when the application of rate design rounding conventions at the rate cell level make it impossible to hit the 60 percent target with absolute perfection. Although Valpak's speculation about the intent of the statute is not unreasonable, it is unfounded. Valpak points to no legislative history or past interpretations of the statute by either the Postal Service or the Postal Rate Commission to support the conclusion that rounding conventions are the *only* policy considerations that justify deviations from the 60 percent target.<sup>75</sup>

---

<sup>74</sup> At Tr. 3/411-12, witness Robinson explains why the percentage rate increase for each subclass deviates from 5.4 percent.

<sup>75</sup> At VI-9-11 of its Brief, Valpak points to other instances where the Postal Service and the Commission have been subject to an *as nearly as practicable* standard in either calculating cost coverages or designing rates. However, in no instance does Valpak demonstrate the existence of any explicit or implicit statutory mandate that *practicable* deviations from the target markup or rate relationship be limited exclusively to those resulting from rounding conventions. Nor is there any basis for Valpak's assertion at VI-10 that the *as nearly as practicable* standard can be read into statutes where it does not appear. The Comments Of Alliance Of Nonprofit Mailers In Support Of Stipulation And Agreement (September 23, 2005) also are not persuasive. The Postal Service agrees with ANM that § 3626(a)(6)(A) establishes a binding, nondiscretionary 60 percent *target*. However, the Postal Service considers that limited flexibility around that target is permitted by the clause *as nearly as practicable*. Nevertheless, as reflected in the September 19, 2005, letter from the Postmaster General, appended to ANM's

As explained by Postal Service witness Taufique, the Postal Service approached the application of § 3626(a)(6)(A) in a manner that sought to harmonize the statute's inherent, if narrow flexibility with the unusual objective of the request in this proceeding – the implementation of across-the-board rate changes for all subclasses to fund the escrow obligation. Tr. 3/625.

At pages VI-2-3 of its Brief, Valpak correctly recalls that, in the relatively short span between the enactment of Public Law 106-384<sup>76</sup> and the filing of the Postal Service's Docket No. R2005-1 request, the Postal Service and the Commission have had few opportunities to apply the statute, in Docket Nos. R2001-1 and R2000-1. In both cases, neither the Postal Service nor the Commission utilized the limited flexibility inherent in § 3626(a)(6)(A) to deviate from perfect adherence to the 60 percent target on any basis other than their mutual preference for the employment of certain rounding conventions in rate design. In doing so, neither agency expressly addressed or ruled out other possible bases for deviations consistent with that narrow flexibility.

The Postal Service considers that employment of the limited flexibility inherent in § 3626(a)(6)(A) to accommodate one particular policy consideration – rounding -- does not preclude consideration of other compelling policy considerations, as long as the resulting rates are consistent with the spirit and intent of § 3626(a)(6)(A); e.g., the results are – in the particular context – as near to 60 percent as practicable.

Accordingly, Postal Service witness Taufique has applied § 3626(a)(6)(A) in light of the very narrow policy directive to increase existing rates and fees on an across-the-board

---

Comments, in the interest of comity and to simplify future rate litigation, the Postal Service intends to very conservatively limit the exercise of its discretion to considerations of rounding at the rate cell level.

<sup>76</sup> 114 Stat. 1460 (October 27, 2000).

basis to distribute the escrow burden, recognizing that the proposed rates might be different if rounding conventions – and only rounding conventions – were used to justify results varying from 60 percent.

As witness Taufique explains, absolutely inflexible adherence to the 60 percent target, which is not required, would result in the imposition of 13 percent rate increases for nonprofit Standard ECR. USPS-T-28 at 12. This is not necessary to meet the cost floor requirement in § 3622(b)(3), and it is far out of line with the goal of distributing the escrow burden on a relatively equitable basis.<sup>77</sup>

Not surprisingly, since Valpak wants all roads to lead either to no change or, better yet, a decrease in current Standard ECR rates, Valpak argues that witness Taufique should have elected several other options to hit the 60 percent nail on the head. Valpak Brief at VI-8, 11. However, witness Robinson explains that:

granting ECR preferential treatment – a lower [than the target 5.4 percent] rate increase – would effectively penalize non ECR subclasses through a higher percentage rate increase. Given the lack of association of the escrow requirement with the provision of postal services, I do not believe that it would be fair and equitable to exempt any subclass – either partially or totally – from an equal share in this Congressionally-mandated burden.

Tr. 3/413. Contrary to the mangled characterization of this quotation at VI-6 of the Valpak Brief, witness Robinson does not testify that compliance with § 3622(a)(6)(A) would be unfair. She testifies that, under circumstances where the law does not compel such a result, it would be unfair to the other mailers shouldering the burden of the escrow through relatively even percentage rate increases to have their burdens further increased so that Standard ECR can dodge escrow responsibility.

---

<sup>77</sup> This is in contrast to the situations with Registered Mail or Within County Periodicals, where, respectively, §§ 3622(b)(3) and 3626(a)(3), inflexibly mandate significant deviations from the Postal Service's across-the-board approach.

3. Valpak's carping about the procedural resolution of Docket No. R2005-1 is unfounded

Valpak asserts that, in the current docket, the Postal Service has sought a "circumscribed" review in order to "forego a proper and thorough testing on the record of its case-in-chief." *Id.* at 14-15. To the contrary, the parties have been accorded the full panoply of procedural rights in this docket. Valpak cannot credibly claim that it has been denied a full opportunity to conduct full written discovery against the Postal Service and its witnesses and to cross-examine those witnesses. The evidentiary record proves otherwise. Valpak has had at its disposal both the USPS and PRC versions of the intra-subclass cost studies that are usually utilized in rate design for use in attacking the Postal Service's request and putting together its alternative case. Valpak put on a case-in-chief proposing an alternative to the Postal Service's across-the-board rate design and pricing approach.

The Postal Service will not apologize for the fact that there has been very limited opposition to its request in this case. The Postal Service has provided a substantial record basis to support its request in this proceeding. That request induced an overwhelming majority of parties to minimize their usual litigiousness and to seek to resolve numerous issues through settlement. Enhanced by adversarial discovery and examination, the Docket No. R2005-1 record supports the proposed Stipulation and Agreement. Moreover, recommendation of the rates and fees in that Agreement would satisfy the principles enunciated by the Commission in PRC Order No. 1443 (August 23, 2005), as discussed at page II-4 of the Docket No. R2005-1 Initial Brief of the United States Postal Service.

4. The OCA presents no real alternative to the rates and fees referenced in the Stipulation and Agreement.

At pages 28-32 of its Brief, the Office of the Consumer Advocate assumes alternative outcomes on the revenue requirement dispute addressed in Section I of this Brief and proposes alternative across-the-board solutions.

First, assuming that the Commission will embrace its proposal to slash the Postal Service's FY 2006 revenue requirement deficiency from \$3.1 billion to \$303 million, the OCA demonstrates its unwavering commitment to the across-the-board concept by proposing that the Commission recommend 0.8 percent across-the-board rate and fee increases. After all, as the OCA reminds us at page 30 of its Brief, "some slight rate increase . . . is better for the Postal Service than no increase at all . . . ."

In contrast to Postal Service witness Taufique's detailed explanation (USPS-T-28) and carefully documented implementation (USPS LR-K-115) of the Postal Service's across-the-board approach, showing what changes would need to be made rate cell by rate cell, the OCA presented no rate design testimony. Accordingly, there is no explanation on the record regarding which rounding constraints to employ, what their impacts might be, or where exceptions may be necessary to preserve inter- or intra-subclass rate relationships in the OCA's 0.8 percent across-the-board rate increase scenario.

The absence of a record explanation of how the OCA's proposal could be translated into a coherent rate schedule is a fundamental matter that should not be overlooked by the Commission. Any modification of the revenue requirement resulting in a material deviation of the 5.4 percent across-the-board objective would alter the underlying rate relationships that form the glue that binds the parties to the Stipulation

and Agreement to one another. The relatively moderate level of the Postal Service's proposed rate increases and the relatively even distribution of the burden among all ratepayers are critical factors in the willingness of First-Class Mail, Periodicals, Standard Mail, Package Services, and Special Services users to embrace the Stipulation and Agreement. However, of equal importance within and between different mail classes is the manner in which the Stipulation Agreement reflects rate and fee relationships that the settlement parties deem to be fair. The Stipulation and Agreement has as many signatories as it does, not because mailers who have signed are eager to see their rates raised or because they do not harbor their own ideas for changing the rate and classification schedule. They have signed because they agree (1) that the Postal Service's request is necessary to meet the unique financial obligations imposed by the escrow obligation and (2) the rate and fee relationships proposed by witness Taufique under the circumstances are fundamentally fair.

In First-Class Mail, for example, where the integer constraint on the basic First-Class Mail rate and rounding conventions can shift significant revenue burdens among rate cells, underlying rate relationships could fluctuate meaningfully based on the whether a 0.8 percent, 2.8 percent , or 4.8 percent across-the-board proposal were being considered. There is no basis on the record for assessing how parties might view the fairness of some alternative rate and fee structure under some radically different across-the-board proposal that produced different rate relationships. Accordingly, the Commission should give great weight to the broad support for Stipulation and Agreement.

In the alternative, the OCA proposes that, if the Commission should see fit not to radically slash the Postal Service's revenue requirement to \$303 million and, instead, recommend the rates and fees in the Stipulation and Agreement, the Board if Governors of the Postal Service should delay implementing any such changes until August 15, 2006. The selection of an implementation date is a matter reserved to the sole discretion of the Board by § 3625(f). The Postal Service sees no need to address that matter of an implementation date here, other than to recommend that parties seeking to influence any such Board determination take such action as is permitted by 39 C.F.R. § 9.2(b) after the issuance of the Commission's recommended decision.

5. The proposed fee for the electronic option for return receipt service is fully supported on the record

Douglas Carlson argues that the Postal Service's proposal to increase the electronic return receipt fee from \$1.30 to \$1.35 is unsupported by any record evidence. Carlson Brief at 1. However, this fee increase is simply part of the across-the-board 5.4 percent increase explained by witnesses Potter (USPS-T-1), Robinson (USPS-T-27), and Taufique (USPS-T-28). Witness Taufique discusses return receipt service specifically (USPS-T-28 at 29-30), and shows that, because of rounding constraints, the actual proposed increase for electronic return receipt is 3.8 percent. Exhibit USPS-28A, page 57. The proposed increase thus is fully supported on the record.

As explained by witness Taufique, the across-the-board rate and fee increase is applied without regard to special cost study results. The "general objective is to increase all rates and fees, including workshare rates, by the same percentage." USPS-T-28 at 4. Thus, costs have caused rate and fee proposals to diverge from the 5.4 percent increase, for instance, to comply with statutory requirements (such as §

3622(b)(3)'s requirement that revenues for a subclass or special service cover costs, and § 3626(a)(3)'s requirement that the markup for within County Periodicals be one-half the markup for the Outside County Periodicals subclass). USPS-T-27 at 10; USPS-T-28 at 3. Mr. Carlson does not cite any statutory requirement that the electronic return receipt fee not be subject to an across-the-board increase. Nor does he demonstrate that the fee for electronic return receipt should be treated differently from all other rates and fees that are increasing by 5.4 percent to cover the statutory escrow requirement.

Mr. Carlson questions the special cost study for electronic return receipt presented by Postal Service witness Wesner (USPS-T-24).<sup>78</sup> Carlson Brief at 2-5. In his cost study, witness Wesner presents about 33 cents as the window acceptance costs when a customer purchases an electronic return receipt. Library Reference K-60, Worksheet W-8, line 1.1. That cost reflects about 25 seconds of window time, certainly a reasonable estimate for the time it would take for a clerk to listen and respond to a customer request for a return receipt, explain the distinction between the traditional and electronic return receipt options, and advise the customer about how to request the return receipt later over the Internet.

Mr. Carlson notes that the window time does not include obtaining an e-mail address from the customer. Carlson Brief at 3. But the need for the window clerk to explain that the customer must provide the e-mail address over the Internet,

---

<sup>78</sup> Mr. Wesner's cost study would ordinarily be directly considered in determining the proposed fee for electronic return receipt. But in this across-the-board case, the costs, while presented as record evidence, did not affect the 5.4 percent increase applied to determine the proposed fee.

along with other window acceptance requirements for electronic return receipt, fully support the window cost estimate used by witness Wesner.

Witness Wesner also presents 50 cents as an estimate of the computer-related costs associated with storing and transmitting an electronic copy of the return receipt signature. USPS-T-24 at 12; Tr. 8B/3899. While this cost is a proxy estimate, it is reasonable to expect significant costs for developing and maintaining the computer system needed to securely store and transmit signature information. These functions go well beyond the e-mail transmission that Mr. Carlson focuses on in his brief. Carlson Brief at 3-5.

Thus, Mr. Carlson can cite no record support for his comment that a 25-cent fee would cover costs. Carlson Brief at 5. Instead, the \$1.35 fee proposed by the Postal Service as part of its across-the-board proposal is fully supported by evidence, and should be recommended.<sup>79</sup>

6. The Internet/Phone Change-of-Address charge is a result of third-party requirements.

David Popkin argued that the one-dollar charge applied to changes of address completed at [www.usps.com](http://www.usps.com), or over the telephone should appear in the Domestic Mail Classification Schedule, and should be subject to the across-the-board rate increase proposed for postal services in the request that initiated this docket. Popkin Initial Brief at 1-2. Mr. Popkin also noted that the charge was suspended for those affected by

---

<sup>79</sup> Mr. Carlson also recommends that electronic return receipt be combined with Certified Mail in a future proceeding. Carlson Brief at 5-6. While the Postal Service is interested in meeting customer needs in the best ways possible, the cost and revenue impacts of Mr. Carlson's concept need to be investigated further before such a proposal could be justified. Moreover, the many Certified Mail customers who choose Certified Mail without an electronic return receipt may not want or benefit from a bundled service.

Hurricane Katrina, and argued that, if the charge were an approved rate, such a suspension would not be possible. *Id.*

When completing a change of address online or over the telephone, customers are asked to provide a credit card number. To enhance security and prevent fraudulent changes of address, this credit card number is checked against the credit card company's database to provide identity validation. The credit card companies do not perform this validation for free. They require a minimum charge on the credit card. The dollar charge is a result of this third-party requirement. It is not a charge for a postal service, within the meaning of chapter 36 of the Act. Accordingly, it is a matter outside the scope of this proceeding.

If a customer does not want to pay the charge, the customer may mail the Change-of-Address form to the Postal Service, or complete a form at a Postal Service retail outlet. Either of these options entails no charge.

The charge does not apply for those affected by Hurricane Katrina. Changes of address for those affected by Hurricane Katrina are being handled in a separate database, and are being specially monitored and tracked. The enormity of the problem caused by Hurricane Katrina has required that different procedures be put into place.

CONCLUSION

For the reasons stated above, the rates for postal services and the fees for special services contained in the Stipulation and Agreement are supported by the evidentiary record and are in accord with the applicable provisions of the Postal Reorganization Act.

WHEREFORE, the Postal Service requests that the Postal Rate Commission recommend under 39 U.S.C. § 3624(d) the rates and fees contained in the Stipulation and Agreement.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

\_\_\_\_\_  
Daniel J. Foucheaux, Jr.  
Chief Counsel, Ratemaking

\_\_\_\_\_  
Kenneth N. Hollies

\_\_\_\_\_  
Eric P. Koetting

\_\_\_\_\_  
Nan K. McKenzie

\_\_\_\_\_  
Sheela A. Portonovo

\_\_\_\_\_  
Brian M. Reimer

\_\_\_\_\_  
Scott L. Reiter

\_\_\_\_\_  
David H. Rubin

\_\_\_\_\_  
Michael T. Tidwell

\_\_\_\_\_  
Keith E. Weidner

475 L'Enfant Plaza West, S.W  
Washington, D.C. 20260-1137  
October 3, 2005

## **CERTIFICATE OF SERVICE**

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

---

Daniel J. Foucheaux, Jr.

475 L'Enfant Plaza West, S.W.  
Washington, D.C. 20260-1137  
October 3, 2005