

OFFICIAL TRANSCRIPT OF PROCEEDINGS BEFORE THE POSTAL RATE COMMISSION

In the Matter of:)
POSTAL RATE AND FEE CHANGES) Docket No.: R2006-1

VOLUME #29

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OFFICE OF THE SECRETARY

Date: November 6, 2006
Place: Washington, D.C.
Pages: 9575 through 10058

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POSTAL RATE COMMISSION

In the Matter of:)
) Docket No.: R2006-1
POSTAL RATE AND FEE CHANGES)

Suite 200
Postal Rate Commission
901 New York Avenue, N.W.
Washington, D.C.

Volume 29
Monday, November 6, 2006

The above-entitled matter came on for hearing
pursuant to notice, at 9:43 a.m

BEFORE:

HON. GEORGE A. **OMAS**, CHAIRMAN
HON. DAWN A. TISDALE, VICE-CHAIRMAN
HON. RUTH Y. GOLDWAY, COMMISSIONER
HON. TONY HAMMOND, COMMISSIONER
HON. MARK ACTON. COMMISSIONER

APPEARANCES:

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C O N T E N T S

WITNESSES APPEARING:

MARY PAT RESCH (Did Not Appear)

MAX HEATH

STEPHEN E. SIWEK

JAMES A. CLIFTON

<u>WITNESSES :</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>	<u>VOIR DIRE</u>
Max Heath	9586	--	--	--	--
By Mr. Weidner	--	9630	--	--	--
Stephen E. Siwek	9662	--	--	--	--
By Mr. Hollies	--	9714	--	--	--
James A. Clifton	977s	--	--	--	--
By Mr. Ackerly	9933	--	--	--	--
	--	10049	--	--	--
By Mr. Koetting	9941	--	--	--	--
	--	9999	--	--	--
	--	10054	--	--	--
By Mr. Levy	--	9947	--	--	--

C O N T E N T S

<u>DOCUMENTS TRANSCRIBED INTO THE RECORD</u>	<u>PAGE</u>
Corrected designated written cross-examination of Max Heath, NNA-T-1	9589
Responses of Witness Heath to interrogatories of United States Postal Service, USPS/NNA-T1-5, USPS/NNA-T1-20 and USPS/NNA-T1-24	9627
Corrected designated written cross-examination of Stephen E. Siwek, NNA-T-3	9666
Responses of Witness Siwek to interrogatories of United States Postal Service, USPS/NNA-T3-15 and USPS/NNA-T3-23	9712
Corrected designated written cross-examination of James A. Clifton, GCA-T-1	9780
Responses of Witness Clifton to interrogatories of Direct Marketing Association, DMA/GCA-T1-10, DMA/GCA-T1-11 and DMA/GCA-T1-12	9935
Responses of Witness Clifton to interrogatories of United States Postal Service, USPS/GCA-T1-66 and USPS/GCA-T1-71	9943
Cross examination exhibits of Alliance of Nonprofit Mailers, ANM-X-1 through 3	9991

E X H I B I T S

<u>EXHIBITS AND/OR TESTIMONY</u>	<u>IDENTIFIED</u>	<u>RECEIVED</u>
Corrected direct testimony of Mary Pat Resch on behalf of Discover Financial Services and Morgan Stanley, Inc., DFS & MSI-T-1	9584	9584
Corrected direct testimony of Max Heath on behalf of National Newspaper Association, NNA-T-1	9586	9587
Corrected designated written cross-examination of Max Heath, NNA-T-1	9588	9588
Responses of Witness Heath to interrogatories of United States Postal Service, USPS/NNA-T1-5, USPS/NNA-T1-20 and USPS/NNA-T1-24	9626	9626
Corrected direct testimony of Stephen E. Siwek on behalf of National Newspaper Association, NNA-T-3	9662	9663
Appendix E to direct testimony of Stephen E. Siwek on behalf of National Newspaper Association, NNA-T-3, Appendix E (Under Seal)	9663	9664
Corrected designated written cross-examination of Stephen E. Siwek, NNA-T-3	9665	9665
Responses of Witness Siwek to interrogatories of United States Postal Service, USPS/NNA-T3-15 and USPS/NNA-T3-23	9711	9711
Corrected direct testimony of James A. Clifton on behalf of Greeting Card Association, GCA-T-1	9775	9778

E X H I B I T S

<u>EXHIBITS AND/OR TESTIMONY</u>	<u>IDENTIFIED</u>	<u>RECEIVED</u>
Corrected designated written cross-examination of James A. Clifton, GCA-T-1	9779	9779
Responses of Witness Clifton to interrogatories of Direct Marketing Association, DMA/GCA-T1-10, DMA/GCA-T1-11 and DMA/GCA-T1-12	9933	9934
Responses of Witness Clifton to interrogatories of United States Postal Service, USPS/GCA-T1-66 and USPS/GCA-T1-71	9941	9942
Cross examination exhibits of Alliance of Nonprofit Mailers, ANM-X-1 through 3	9951 9979 9987	9990 9990 9990

P R O C E E D I N G S

(9:43 a.m.)

1
2
3 CHAIRMAN OMAS: I want to apologize for
4 being late this morning. **As** it always happens on
5 Monday morning, we had a computer glitch so I just got
6 my script here. You wouldn't want me to conduct this
7 without a script.

8 Good morning. Today we continue hearings to
9 receive the direct case of participants other than the
10 Postal Service in Docket No. R2006-1 considering the
11 Postal Service requests for rate and fee changes.

12 I have one procedural matter before we
13 begin. It concerns the scope of cross-examination of
14 Greeting Card Association Witness Clifton. First, I
15 would like to compliment counsel. Pleadings were
16 reasoned, concise and helpful.

17 I believe that by committing these issues to
18 writing it has become clear that there is little, if
19 any, disagreement between the parties. I am limiting
20 cross-examination as requested by Greeting Card
21 Association and as supported by the Alliance of
22 Nonprofit Mailers.

23 **A** written ruling will I hope be available in
24 the hearing room before Witness Clifton testifies
25 today. Unfortunately, as I mentioned, our computers

1 are not working properly. We're working, and we'll
2 try to get it out as soon as we can.

3 Scheduled to appear today are Witnesses
4 Resch, Heath, Siwek and Clifton.

5 For the convenience of witnesses and
6 counsel, we will first enter the testimony of
7 witnesses for whom there is no cross-examination into
8 evidence.

9 Mr. Brinkmann, would you please assist us in
10 receiving the corrected version of Mr. Resch's
11 testimony into evidence, please?

12 MR. BRINKMANN: Yes, sir. Can you hear me?

13 CHAIRMAN OMAS: No. Put your speaker on.

14 MR. BRINKMANN: Can you hear me now?

15 CHAIRMAN OMAS: Yes.

16 MR. BRINKMANN: Yes, sir. I have two copies
17 of the direct testimony of Mary Resch on behalf of
18 Discover Financial Services and Morgan Stanley, Inc.,
19 and I have two copies of the appropriate declaration,
20 and with your permission I'd like to move this into
21 evidence.

22 CHAIRMAN OMAS: Is there objection?

23 {No response.}

24 CHAIRMAN OMAS: Hearing none, Mr. Brinkmann,
25 please provide the reporter with two copies of the

1 corrected direct testimony of Mary Pat Resch.

2 That testimony is received into evidence.

3 However, as is our practice, it will not be

4 transcribed.

5 (The document referred to was
6 marked for identification as
7 Exhibit No. DFS & MSI-T-1 and
8 was received in evidence.)

9 MR. BRINKMA " : Thank you very much, Mr.
10 Chairman.

11 CHAIRMAN OMAS: Before that, is there any
12 additional written cross-examination for Witness
13 Resch?

14 (No response.)

15 CHAIRMAN OMAS: Thank you, Mr. Brinkmann.

16 MR. BRINKMA " : Thank you, sir.

17 CHAIRMAN OMAS: Ms. Rush, would you identify
18 the next witness so I can swear him in, please?

19 MS. RUSH: Yes, Mr. Chairman. NNA calls Max
20 Heath to the stand.

21 CHAIRMAN OMAS: would you raise your right
22 hand, please?

23 //

24 //

25 //

1 Whereupon,

2 MAX HEATH

3 having been duly sworn, was called as a
4 witness and was examined and testified as follows:

5 CHAIRMAN OMAS: You may be seated.

6 Ms. Rush?

7 MS. RUSH: Mr. Chairman, with your
8 permission, we have one procedural matter we want to
9 note for the record.

10 We noticed an erratum on the docket this
11 morning, a correction on a workpaper that was filed in
12 conjunction with USPS/NNA-T1-29

13 We discovered over the weekend that an
14 outdated document was inadvertently uploaded to the
15 website. We have now corrected that. It's also
16 corrected in the packets.

17 We also discovered one error in a rate cell
18 which unfortunately cascaded into requiring
19 corrections on two interrogatories and one page in the
20 testimony, which have all been now reviewed by the
21 Postal Service, and we'll have the corrections in the
22 materials presented to the witness.

23 CHAIRMAN OMAS: Very good.

24 //

25 //

1 DIRECT EXAMINATION

2 (The document referred to was
3 marked for identification as
4 Exhibit No. NNA-T-1.)

5 BY MS. RUSH:

6 Q Mr. Heath, I'm presenting to you the Direct
7 Testimony of Max Heath, NNA-T-1, on Behalf of the
8 National Newspaper Association and asking you if this
9 testimony was prepared by you or under your direction?

10 A Yes, it was.

11 Q And have there been a -- to this testimony?

12 A Yes.

13 Q Would you explain those --?

14 A Yes. I went through the errata this weekend
15 and found calculations that inadvertently needed to be
16 fixed --.

17 Q --

18 A --

19 MS. RUSH: Mr. Chairman, I'd like to present
20 these to the reporter and request that they be entered
21 into evidence.

22 CHAIRMAN OMAS: Is there any objection?

23 (No response.)

24 CHAIRMAN OMAS: Mr. Heath, would you turn
25 your mic on, please?

1 THE WITNESS: Excuse me.

2 CHAIRMAN OMAS: Is there any objection?

3 (No response.)

4 CHAIRMAN OMAS: Hearing none, I will direct
5 counsel to provide the reporter with two copies of the
6 corrected direct testimony of Max Heath.

7 That testimony is received into evidence.
8 However, as is our practice, it will not be
9 transcribed.

10 (The document referred to,
11 previously identified as
12 Exhibit No. NNA-T-1, was
13 received in evidence.)

14 CHAIRMAN OMAS: Mr. Heath, have you had an
15 opportunity to examine the packet of designated
16 written cross-examination presented to you this
17 morning?

18 THE WITNESS: Yes, I have.

19 CHAIRMAN OMAS: If those questions contained
20 in that packet were posed to you orally today would
21 they be the same as those you provided previously in
22 writing?

23 THE WITNESS: Yes, sir. Yes, they would.

24 CHAIRMAN OMAS: Are there any additions or
25 corrections you would like to make to these answers?

1 THE **WITNESS**: Other than the ones I
2 mentioned this morning that I think are on page 19 of
3 my testimony.

4 CHAIRMAN OMAS: Fine. **Ms.** Rush, would you
5 please provide two copies of the corrected designated
6 written cross-examination of Witness Heath to the
7 reporter?

8 That material is received into evidence and
9 is to be transcribed into the record.

10 (The document referred to was
11 marked for identification as
12 Exhibit **No.** NNA-T-1 and was
13 received in evidence.)

14 //
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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Postal Rate and Fee Changes, 2006

Docket No. R2006-1

DESIGNATION OF WRITTEN CROSS-EXAMINATION
OF NATIONAL NEWSPAPER ASSOCIATION
WITNESS MAX HEATH
(NNA-T-1)

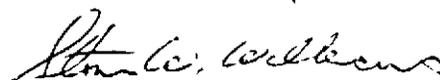
Party

Interrogatories

United States Postal Service

USPS/NNA-T1-1-14, 16-19, 21- 25-3

Respectfully submitted.



Steven W. Williams
Secretary

INTERROGATORY RESPONSES OF
NATIONAL NEWSPAPER ASSOCIATION
WITNESS MAX HEATH (T-1)
DESIGNATED AS WRITTEN CROSS-EXAMINATION

Interrogatory

Designating Parties

USPSINNA-TI-1	USPS
USPSINNA-TI-2	USPS
USPSINNA-T1-3	USPS
USPSINNA-T1-4	USPS
USPS/NNA-T1-5	USPS
USPS/NNA-T1-6	USPS
USPSINNA-TI-7	USPS
USPSINNA-TI-8	USPS
USPSINNA-TI-9	USPS
USPSINNA-T1-10	USPS
USPS/NNA-T1-11	USPS
USPS/NNA-T1-12	USPS
USPSINNA-TI-13	USPS
USPSINNA-T1-14	USPS
USPSINNA-T1-16	USPS
USPSINNA-TI-17	USPS
USPSINNA-T1-18	USPS
USPS/NNA-T1-19	USPS
USPS/NNA-T1-21	USPS
USPS/NNA-T1-22	USPS
USPS/NNA-T1-23	USPS
USPS/NNA-T1-25	USPS
USPSINNA-TI-26	USPS
USPSINNA-TI-27	USPS
USPS/NNA-T1-28	USPS
USPSINNA-T1-29	USPS
USPSINNA-TI-30	USPS
USPS/NNA-T1-31	USPS
USPS/NNA-T1-32	USPS

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-1. Please refer to section III(A) of your testimony. Please provide the underlying calculations, along with specific cites to supporting materials, for all of the percentage rate increases you report in that section. Also, please provide the underlying calculations, along with specific cites to supporting materials, for Tables 1 and 2 on page 20 of your testimony.

RESPONSE:

My worksheet is attached as NNA Appendix B. An erratum to correct a percentage error in the tables has been filed.

Periodicals In-County Rates
E2006-1 USPS Proposed mid-2007
03-Oct-06
USPS2007

NOTE: High Density WBS rate based on 25% of active possible deliveries.

Piece Rate	0.142	0.060	0.060	0.044	0.044	0.033
DU Discount	0.142	0.060	0.060	0.044	0.044	0.033
Round Rate	0.179	0.179	0.142	0.179	0.142	0.142

NNA Appendix B

Discounts:	Carrier Route					
	None	None	None	None	None	None
	Del. Oic					
1 oz.	0.1532	0.0712	0.0609	0.0552	0.0449	0.0339
2 oz.	0.1644	0.0824	0.0688	0.0664	0.0538	0.0428
3 oz.	0.1756	0.0936	0.0768	0.0776	0.0626	0.0516
4 oz.	0.1868	0.1048	0.0875	0.0888	0.0715	0.0605
5 oz.	0.1979	0.1158	0.0964	0.0989	0.0804	0.0694
6 oz.	0.2091	0.1271	0.1053	0.1111	0.0893	0.0783
7 oz.	0.2203	0.1383	0.1141	0.1223	0.0981	0.0871
8 oz.	0.2315	0.1495	0.1230	0.1335	0.1070	0.0960
9 oz.	0.2427	0.1607	0.1319	0.1447	0.1159	0.1049
10 oz.	0.2539	0.1719	0.1408	0.1559	0.1248	0.1138
11 oz.	0.2651	0.1831	0.1496	0.1671	0.1336	0.1226
12 oz.	0.2763	0.1943	0.1585	0.1783	0.1425	0.1315
13 oz.	0.2874	0.2054	0.1674	0.1894	0.1514	0.1404
14 oz.	0.2985	0.2166	0.1763	0.2006	0.1603	0.1493
15 oz.	0.3096	0.2278	0.1851	0.2118	0.1691	0.1581
16 oz.	0.3210	0.2390	0.1940	0.2230	0.1780	0.1670

PERCENTAGE CHANGES - New Rates over Old Rates
E2006-1 USPS Proposed mid-2007
03-Oct-06

Discounts:	Carrier Route					
	None	None	None	None	None	None
	Del. Oic					
1 oz.	38.53%	23.00%	22.21%	31.75%	32.72%	21.80%
2 oz.	36.13%	23.41%	23.18%	30.78%	32.31%	23.47%
3 oz.	35.44%	23.72%	23.94%	30.08%	32.02%	24.59%
4 oz.	34.84%	24.03%	24.55%	29.56%	31.63%	25.38%
5 oz.	34.31%	24.33%	25.09%	28.16%	31.63%	25.99%
6 oz.	33.84%	24.63%	25.45%	26.94%	31.49%	26.46%
7 oz.	33.42%	24.94%	25.84%	25.89%	31.38%	26.84%
8 oz.	33.05%	25.24%	26.15%	25.37%	31.29%	27.15%
9 oz.	32.71%	25.59%	26.42%	24.18%	31.21%	27.41%
10 oz.	32.40%	25.89%	26.68%	23.03%	31.14%	27.63%
11 oz.	32.12%	26.19%	26.95%	21.89%	31.09%	27.82%
12 oz.	31.85%	26.49%	27.05%	20.78%	31.03%	27.98%
13 oz.	31.63%	26.79%	27.22%	19.67%	30.99%	28.12%
14 oz.	31.41%	27.04%	27.37%	18.59%	30.95%	28.25%
15 oz.	31.21%	27.29%	27.51%	17.50%	30.91%	28.36%
16 oz.	31.02%	27.53%	27.63%	16.43%	30.88%	28.46%

Examples of rate increases for Table 1 & 2
Delivery Unit Entered, CR High Density
2005 rates prop 2007 rates % inc.

Delivery Unit Entered, CR High Density	0.02725	0.0335	
2005 rates	0.027	0.036	
Proposed rates	0.027	0.036	
Price rate	0.05425	0.0710	\$0.017 31.80%
Delivery Unit Entered, CR Basic	0.0355		
2005 rates	0.043	0.052	
Proposed rates	0.043	0.052	
Price rate	0.07025	0.0875	\$0.017 24.56%

Final 03-Oct-06
(rate-0)

COPY RESULTS FROM COLUMNS A-H BY / R V

Discounts:	Carrier Route					
	None	None	None	None	None	None
	Del. Oic					
1 oz.	0.1119	0.0579	0.0488	0.0419	0.0338	0.0278
2 oz.	0.1208	0.0668	0.0566	0.0508	0.0406	0.0346
3 oz.	0.1296	0.0756	0.0634	0.0596	0.0474	0.0414
4 oz.	0.1385	0.0845	0.0703	0.0665	0.0543	0.0483
5 oz.	0.1474	0.0934	0.0771	0.0774	0.0611	0.0551
6 oz.	0.1563	0.1023	0.0839	0.0863	0.0679	0.0619
7 oz.	0.1653	0.1111	0.0907	0.0951	0.0747	0.0687
8 oz.	0.1740	0.1200	0.0975	0.1040	0.0815	0.0755
9 oz.	0.1829	0.1288	0.1043	0.1129	0.0883	0.0823
10 oz.	0.1916	0.1378	0.1111	0.1218	0.0951	0.0891
11 oz.	0.2006	0.1466	0.1179	0.1306	0.1019	0.0959
12 oz.	0.2095	0.1555	0.1246	0.1395	0.1084	0.1028
13 oz.	0.2184	0.1644	0.1316	0.1484	0.1155	0.1096
14 oz.	0.2273	0.1733	0.1384	0.1573	0.1224	0.1164
15 oz.	0.2361	0.1821	0.1452	0.1661	0.1292	0.1232
16 oz.	0.2450	0.1910	0.1520	0.1750	0.1360	0.1300

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-2. Please refer to your testimony, section I(B), and to the Domestic Mail Manual (DMM), sections **707.7** and **707.11.3**.

- a. Please confirm that according to DMM **707.11.3.3**, a publisher may mail non-subscriber copies at Within-County rates up to 10 percent of the number of subscriber copies mailed annually at Within-County rates. If you do not confirm, please explain fully.
- b. Please confirm that according to DMM **707.7.3** advertising copies can be mailed at Within-County rates, subject to the limitation identified in part (a). If you do not confirm, please explain fully.
- c. Please confirm according to DMM **707.7.6** that copies mailed to subscribers whose subscription expired within the past six months are still considered subscriber copies that pay Within-County rates provided the publisher makes a good-faith attempt to obtain payment for a renewal during the six-month period. If you do not confirm, please explain fully.
- d. Please confirm that according to DMM **707.7.6** copies mailed to subscribers whose subscription expired more than six months previous are non-subscriber copies that may be mailed at Within-County rates, subject to the limitation identified in part (a). If you do not confirm, please explain fully.
- e. Please confirm that according to DMM **707.7.7** complimentary copies are non-subscriber copies that can be mailed at Within-County rates, subject to the limitation identified in part (a). If you do not confirm, please explain fully.
- f. Please confirm that according to **DMM 707.7.8** one proof copy may be mailed to each advertiser (or representative agent) at Within-County rates. If you do not confirm, please explain fully.
- g. Please confirm that according to DMM **707.7.8** additional proof copies may be mailed to each advertiser (or representative agent) at Within-County rates, subject to the limitation identified in part (a). If you do not confirm, please explain fully.

RESPONSE:

- a. Confirmed
- b. Not confirmed. I do not understand what is meant by "advertising copies" other than the meaning I presume is referenced in subsections f and g. Please see my response to that subsection.
- c. Confirmed.
- d. Confirmed.
- e. Confirmed.
- f. Confirmed.
- g. Confirmed.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-3. Please refer to the testimony of witness Siwek. p. 7, lines 14-18, where he states, "A Periodical's paid circulation may vary based on a number of considerations including changes in subscription discounts. Such changes may render certain Periodicals unable to qualify for Within-County discounts or may even affect the overall eligibility of the publication."

- a. Please list each Landmark Community Newspaper that has lost its eligibility to mail at Within-County rates in the past three years. Please explain the circumstances surrounding each change in status.
- b. Please list each former Landmark Community Newspaper that has lost the eligibility to mail at Outside-County rates in the past three years. Please explain the circumstances surrounding each change in status.
- c. Please list each Landmark Community Newspaper that **lost** its eligibility to mail at Within-County rates in the past three years and then regained it. Please explain the circumstances surrounding each change in status, including the timing of respective changes.

RESPONSE:

- a. None, to my knowledge.
- b. None, to my knowledge.
- c. None, to my knowledge.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-T1-4.

- a. Please confirm that the proposed Within-County per piece rates are reduced from the Outside-County per piece rates by percentages ranging from 64 percent to 83 percent, and that Outside-County rates are higher than Within-County by factors of 2.74 to 5.80. If you do not confirm, please provide the correct ranges of differences.
- a. Do you agree that publishers are strongly motivated to mail eligible pieces at the lower Within-County rates rather than higher Outside-County rates? If you do not agree, please explain fully.

RESPONSE:

- a. confirmed
- b. I agree

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-5. Please refer to your testimony, page 9, lines 16-17, where you state, "All of these circumstances could combine, in an environment where small errors loom large, to cause a tally to be wrongly marked." Please also refer to the response to the interrogatory NNA/USPS-T1-16.

- a. Do you agree that there were 193 direct Within-County tallies in FY2005? If not, please explain.
- b. Do you agree that an error in one tally would affect the estimated costs of Within-County Periodicals on average by less than 1 percent—i.e., approximately 1/193? If not, please explain.

RESPONSE:

- a. I have not examined the tally total. I understand from NNA Witness Siwek that there were 193 direct tallies relating specifically to Clerks and Mail Handlers Mail Processing costs and to City Carrier In-Office costs for Within County.
- b. I neither agree nor disagree. I have not examined the full scope of IOCS tallies for Within County.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-TI-6. Please refer to your testimony, section I(A)(1)(b), and your response to USPS/NNA-T1-2.

- a. You identify situations in which a Periodicals mailpiece may appear to qualify for Within-County rates yet actually pays Outside-County rates. Please confirm that such situations can arise only when the number of nonsubscriber mailpieces exceeds ten percent of Within-County subscriber pieces. If you do not confirm, please explain.
- b. Please confirm that the quantitative significance of the situations you identify for classifying tallies as Within-County or Outside County depends on how many ineligible nonsubscriber pieces there are, relative to pieces claiming Within-County rates. That is, the fewer pieces there are fitting the situations you identify, the smaller is the potential tally classification problem. If you do not confirm, please explain.
- c. Please also refer to Dr. Bozzo's response to NNA/USPS-T46-9 (Tr. 9/2336), listing the titles for publications classified as Within-County Periodicals in the Postal Service's analysis. Based on your experience, please estimate the size of the group of nonsubscriber pieces ineligible for Within-County rates relative to the actual Within-County (subscriber and nonsubscriber) volumes -- i.e., please provide an estimated ratio or percentage of ineligible pieces to Within-County pieces.

RESPONSES:

- a. Not confirmed. An Outside County mailpiece so qualified because of one of the conditions I explain in my testimony is not likely to be considered by the publisher to be a "sample copy" within the 10 percent allowance and therefore would not be mailed at Within County rates. I believe most publishers carefully plan for the use of the sampling allowance.
- b. I believe that the USPS would not know how many such pieces there are in the Postal mail stream at any given time. As a result, I cannot confirm your interrogatory as it is currently phrased.
- c. I have not measured the size of the group and do not believe either I or the Postal Service have the ability to do so at present.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-TI-7 In your testimony on page 14, lines 26 to 33, you describe a 2003 experiment involving the Searchlight newspaper in Prentiss, **MS**, which is edited by NNA member Patsy Speights. In that experiment, Mrs. Speights shifted her Outside County mail out of sacks and into flats tubs. In your testimony on page 15, lines 5 to 6, you state, 'Mrs. Speights has reduced her container use from 68 sacks to 26-27 tubs.'

(a) Please describe the 68 sacks prepared by Mrs. Speights prior to the experiment by reference to the sacks' i) presort level. and ii) average size, in terms of pieces.

(b) Of the 68 sacks, approximately how many contained fewer than 24 pieces?

(c) Please describe the 26-27 flats tubs prepared by Mrs. Speights as a result of the experiment by reference to the tubs' i) presort level, and ii) average size, in terms of pieces.

(a-c) I do not have access to the specifics of Mrs. Speights's mailing profile. My description of her sack reduction comes from her oral reports to me, as I was an informal consultant to newspapers in Mississippi at the time of this experiment, trying to help them improve very poor in-state delivery of newspapers.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES **POSTAL SERVICE**

USPSINNA-TI-8

- (a) Please describe the usage of sacks by newspapers following the promulgation of the 24-piece sack rule.
- (b) What are the approximate median piece counts of sacks prepared by a typical LCNI, and an NNA-member, newspaper?
- (c) Based on typical mail piece characteristics, what is an approximate or median quantity of pieces that such newspapers are able to place in a flat tub?

RESPONSES:

(a) I am not sure what usage you refer to here, but I can confirm that newspapers I am aware of continue to use them. Newspapers now must comply with the 24-piece sack rule, at considerable degradation of service, I might add. Therefore sack use has been cut considerably, as much as half at some papers I am familiar with, less at others. The range is from about 22% reduction to as high as 71%, depending on volume.

(b) Median piece counts for a typical LCNI newspaper are approximately 35 per sack. Most of that is outside the trade area of the newspaper, as we typically do unsacked bundles to DDU within the county and sometimes extended trade area. I could not estimate a typical piece count for an NNA newspaper.

(c) Depending on the size in pages and sections, i.e. the bulk of a newspaper, a newspaper can put as many as 200 pieces of a small two-fold tabloid in a flats tub. Larger, bulkier broadsheet papers may be limited to as few as 15-20 per tub. So it can run the gamut from 20 to 200.

**RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T1-9 In your testimony on page 15, lines 10 to 11, you state in reference to the experiment in Maine, "I understand it is still ongoing and has produced container reductions and improved service." Please quantify the "container reductions" that have occurred as a result of the experiment.

Response:

My company does not own newspapers in Maine. I have not directly consulted with Maine newspapers on this experiment. I do not have a container count for Maine newspapers. But I have been told by **NNA** members there that it has greatly improved service within the state and may have resulted in a small container reduction based on preferred sortations to certain postal operations.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-10 In your testimony on page 16, lines 19 to 20, you state, "I believe tubs actually do avoid some expense for the Postal Service and for mailers, besides the apparent service improvements, compared to sacks." **Also**, in your testimony on page 17, lines 16 to 17, you propose that the Commission "reject the proposed charge on [flats tubs] altogether."

(a) Please confirm that a flats tub is a container. If you do not confirm, please explain.

(b) Please confirm that flats tubs do cause the Postal Service to incur some costs for handling them. If you do not confirm, please explain.

(c) Please confirm that if the container charge is imposed on flats tubs, it would provide mailers with an incentive to utilize tubs more efficiently, which would thereby reduce the number of tubs that are entered. If you do not confirm, please explain.

RESPONSES:

(a) Confirmed.

(b) I presume that there are costs, but I am unaware of any quantification by the Postal Service of such costs. USPS operational personnel have frequently told me that trays are easier to unload, handle, and sort, often with the use of a Low Cost Tray Sorter, and that leads to quicker processing times. Ease and speed for USPS should equal minimal costs. USPS has repeatedly complained about newspapers' use of sacks, and sack "surcharges" were suggested to be appropriate. To me, providing a more efficient, easier-to-use alternate container like a tray and then sticking it with the same charge as the supposedly highly inefficient sack is a "bait and switch tactic of the worst order.

(c) I cannot confirm. A charge might induce mailers already using tubs to use fewer tubs, but it also would discourage mailers presently using sacks from shifting to tub use, so it might not encourage efficiency with regard to tub use at all. Newspaper mailers are more interested in getting timely delivery for their non-local subscribers, and may well choose to use more tubs if that works best for delivery. But if USPS wants to eliminate sacks, the pricing signal should not be the same for trays as sacks.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS **HEATH** TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-11 In your testimony on pages 17 and 18 you assert that the container charge should not be applied to "uncontainerized mail." Please confirm that by "uncontainerized mail," you mean unsacked bundles entered at the delivery unit pursuant to DMM 707.23.4. If you do not confirm, please explain.

RESPONSES:

I mean unsacked bundles. If loose copies were permitted to be entered in some smaller post offices, these would also fit into the "uncontainerized mail" category.

**RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T1-12 In your testimony at page 18, lines 23 to **24**, you state in reference to applying the Outside County container charge to "uncontainerized mail," "A surcharge gives me no incentive to push this practice further." Please also refer to the Postal Service's response to Presiding Officer's Information Request No. 30 (Tr. 7/1615-18) and to Tr. 7/1857. Please confirm that a mailer who enters mail in unsacked bundles rather than in sacks or tubs would pay a lower container charge in situations where the number of 5-digit ZIP Codes to which the mail is destined is lower than the number of containers that would be required to hold the mail. If you do not confirm, please explain.

RESPONSE:

Confirmed as the hypothetical you pose, but for many community newspapers, only one container would be used at many 5-digit zip entry points. So the number of hypothetical containers in many cases would equal the number of 5 digit ZIP codes.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-13 Please confirm that mailers utilizing flats tubs and unsacked bundles pay the same piece rates as all other Outside County mailers. If you do not confirm, please explain.

RESPONSE:

If you mean Outside County mailers using flats tubs and unsacked bundles, confirmed.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-14 In your testimony on page 19, lines 13 to 14, you state, "Many publishers who have consulted with me for budgets are finding similar ranges of impact."

- (a) How many publishers are you referring to?
- (b) Please provide the percentage changes that they reported, and provide the underlying calculations supporting those percentage changes.

RESPONSES:

(a) I speak to or e-mail with **5-6** publishers in a typical week, in addition to conducting mail seminars for larger groups a half dozen times within a typical year. Those that produce highly-efficient newspaper mail, high-density walk-sequenced and entered at a delivery office, are simply getting larger percentage increases than less efficient mail not meeting those characteristics.

(b) I do not ask them for their calculations and therefore do not have them, but the ranges I am hearing from publishers run from 25% to **31%**. Please see also Appendix B of my testimony.

**RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T1-16 Please refer to page 19, line 30, of your testimony. Based on your experience, please provide your best estimate as to the typical weight of a weekly community newspaper that utilizes Within County rates.

RESPONSE:

In my experience, I believe 4 to 8 ounces would be a valid mean range.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-17 Please refer to page 20, lines 16 to **22**, of your testimony.

(a) Please explain the derivation of the **1.7** cents figure, with specific citations to supporting materials.

(b) Please confirm that discounts are based on the costs avoided by the Postal Service rather than the costs incurred by a mailer.

RESPONSES:

(a) **1.7** cents is the amount of the DU entry discount, pound and piece combined, for a paper weighing about **5** oz. That is an ounce more than stated in colleague Sosniecki's testimony, but perhaps he was estimating.

(b) Not confirmed. The Postal Service **seems** to measure its avoided costs, but to apply an array of passthroughs in deciding how much of that cost savings to pass on. I would say the discounts are not wholly based on either, from that perspective.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-18 Please refer to your testimony from page 20, line 24, to page 21, line 4.

(a) Please confirm that the Postal Service's proposed rate differential between the carrier route basic piece rate and the carrier route high density rate is the same as the differential in current rates.

(b) Considering your answer to part (a), please explain how can it be said that the Postal Service's proposal "punish[es]" high density mail?

RESPONSES:

(a) confirmed.

(b) because the percentage increase is significantly higher for high density mail entered at a DDU (22-27% from 1-16oz.) than for carrier route entered at DDU (33-31%).

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-19 In your testimony on page 22, lines 10 to 12, you state, "For the 22% of Within County mail that remains at the basic, 5-digit, and 3-digit levels, 170.8 million pieces are nonautomation flats, which is about 14% of the subclass." Please confirm that the correct figure is 107.9 million non-carrier route nonautomation pieces rather than 170.8. If you do not confirm, please explain your derivation of the 170.8 million figure, with citations to supporting materials.

RESPONSE:

Confirmed.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-21 Based on your experience, please describe those Within
County newspapers that typically use the non-carrier-routerate categories.

RESPONSE:

Most community newspapers I am familiar with use non-carrier-routerate categories. Generally those categories are used because the mail in a given carrier route does not achieve the density required for the discounts and therefore, even if the mail is sorted to the carrier route, it would not be reported as carrier route mail in the billing determinants.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-TI-22

(a) Please approximate, or provide your best estimate of, the percentage of i) LCNI newspapers, and ii) NNA newspapers, that **use** the carrier route rate categories.

(b) Please approximate, or provide your best estimate of, the percentage of i) LCNI newspapers, and ii) NNA newspapers, that use the carrier route high density category.

RESPONSES:

(a) (i) In my company, it is 100%. (ii) I can only guess at it, but from seeing numerous postage statements, it is probably 95% or more.

(b) For LCNI Newspapers, it is about 64% of titles that have some high density rate usage, representing 50% of our in-county volume. (ii) I can only guess at it, but from my viewing of member postage statements, it may be closer to 50%.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-23 Please refer to page 5, lines 30 to 31, of your testimony. Please confirm that the base year in Docket No. R94-1 was FY 1993 rather than FY 1996. If you **do** not confirm, please explain.

RESPONSE:

Confirmed.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-25 In your testimony on page 13, lines 12 to 13, you state, "If the Commission used a four year look-back, as it did in the past, the average number of pieces would be 791,553 for the base year." Please explain how this figure was estimated, with specific citations to supporting materials.

RESPONSE:

I calculated this figure from the volume data for Within-County mail provided by witness Pafford in LR-L-20, the Revenue, Piece, Weight system summary report. The total annual volumes provided there for 2002-2005 are as follows:

2005	762,763
2004	760,020
2003	793,521
2002	849,911

The total of those years' volumes equals 3,166,215. Divided by four, the average volume total would be 791, 553.8

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

1

USPSINNA-TI-26. Please refer to interrogatory USPS/NNA-T1-2(b), which directed you attention to DMM 707.7.3, entitled "Advertising Copies". Your response to USPS/NNA-T1-2(b) states, "I do not understand what is meant by 'advertising copies[beyond what is referenced in USPS/NNA-T1-2(f-g)].'" In your testimony, p. 9, lines 11- 14, you state, 'Advertisers may, for their own marketing reasons, choose to purchase copies for their own customers. Under DMM 707.7.3, these copies are required to travel at the outside County postage rate as well, but would appear to IOCS, [sic] again, as a Within County periodical.' You appeared to understand the import of DMM 707.7.3 in your testimony, while it escapes your understanding when faced with interrogatory USPS/NNA-T1-2(b). Please assume that the reference to 'advertising copies' in the title of DMM 707.7.3 refers to those copies as described in that section of the DMM.

- a. Please confirm that DMM 707.7.3 expressly identifies copies purchased by advertisers "or others" for advertising purposes as nonsubscriber (or nonrequester) copies.
- b. Please confirm that your testimony does not address requester publications or nonrequester copies.
- c. Please identify the language in DMM 707.7.3 that requires advertising copies. or copies related to advertising, to be entered at Outside-County rates.
- d. Please confirm that nonsubscriber copies may be entered at Within-County rates, subject to the 10 percent limit on nonsubscriber copies described in DMM 707.11 and 707.7.
- e. Please confirm that the Postal Service provides a tool found at http://pe.usps.com/10_rule.xls that facilitates counting of subscriber and nonsubscriber copies so that publishers can keep track of when a periodical's annual pieces approach or exceed the applicable 10 percent limit.

RESPONSES:

- a. Confirmed.
- b. Confirmed.
- c. DMM 707.7.3 makes clear that these copies are considered non-subscriber copies. Therefore, they would generally travel at Outside County rates.
- d. Confirmed. However, publishers carefully reserve the 10 percent allowance, usually called the sampling allowance, for use in targeting potential new subscribers just before, or during a direct mail campaign for new subscribers. They would not generally wish to consider the copies mailed under 707.7.3 as part of their sampling allowance, therefore. So while the DMM permits 707.7.3 copies to be mailed at Within County rates, such usage would waste the sampling allowance in the view of most newspaper publishers. And, to clarify my understanding of "advertising copies," my customary usage of that term refers to copies mailed by the publisher to advertisers, not to copies identified under 707.7.3.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-TI-27. In your response to **USPS/NNA-T1-6(a)** you state, "An Outside County mailpiece so qualified because of one of the conditions I explain in my testimony is not likely to be considered by the publisher to be a 'sample copy' within the 10 percent allowance and therefore would not be mailed at Within County rates." However, in your response to **USPS/NNA-T1-2**, in all but one part you confirmed that the DMM allows mailers to mail nonsubscriber copies at Within-County rates within the 10 percent allowance.

a. Please confirm that if the number of nonsubscriber copies mailed is less than 10 percent of the annual number of subscriber copies paying Within-County rates, then those nonsubscriber copies need not pay Outside-County rates but may be mailed at Within-County rates. If you do not confirm, please explain fully, referring to your response to **USPS/NNA-T1-2(a)**.

b. Please confirm that the examples from your testimony, p. 8, lines 19-27, are nonsubscriber copies described in DMM 707.7.7, 'Complimentary Copies'. If you do not confirm, please explain fully.

c. Please confirm that the examples from your testimony, p. 9 lines 1-9, are nonsubscriber copies described in DMM 707.7.6, 'Expired Subscription'. If you do not confirm, please explain fully.

d. Please confirm that the examples from your testimony, p. 9, lines 11-14, are nonsubscriber copies described in DMM 707.7.3, 'Advertising Copies'. If you do not confirm, please explain fully.

e. Please confirm that according to DMM 707.7.1 'Sample Copies' are nonsubscriber copies and can be mailed at Within-County rates subject to the limitation in part (a). If you do not confirm, please explain fully.

f. Please confirm that if the number of nonsubscriber copies mailed is fewer than 10 percent of the annual number of subscriber copies, then all nonsubscriber copies defined in DMM 707.7, including 'Sample Copies', 'Complimentary Copies', 'Expired Subscription' and 'Advertising Copies' destined to the origin entry county can all be mailed at Within-County rates. If you do not confirm, please explain fully, referring to your responses to **USPS/NNA-T1-2**, parts (c)-(g) and to **USPS/NNA-T1-27**.

RESPONSES:

a. Confirmed, but see my response to **USPS/NNA T1-26d**.

b. Confirmed.

c. Confirmed.

d. Confirmed.

e. Confirmed that these copies are permitted by the DMM to be mailed at Within County rates, but please see my response to **USPS/NNA T1-26d**.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

f. Confirmed. but it would be a foolish use of the sampling allowance if a publisher claimed these categories as Within County mail.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-TI-28. Please refer to interrogatory **USPS/NNA-T1-6(b)**, which you declined to answer based on your belief "that the USPS would not know how many such pieces there are in the Postal mail stream at any given time." Please answer the question as a hypothetical, regardless of your belief about what the Postal Service could or could not know. If you are unable to answer hypothetically, then:

- a. Explain why you, ostensibly an expert witness in this proceeding, are unable to answer questions of the type that expert witnesses are expected to be able to answer;
- b. Identify all pieces of information or data elements that you would need to know so that you could answer the hypothetical question;
- c. Hypothecate as necessary each piece of information, or value for each data element that you need, and answer the question.
- d. If you have any trouble answering the hypothetical as stated in the body of this interrogatory, or as supplemented in parts (a) through (c), then please assume that the Postal Service can count how many "such pieces" there are, and answer the question.

RESPONSES:

a. Perhaps the problem is that my expertise is in advising newspapers on the use of the mail, rather than in testifying before the Postal Rate Commission. My response in USPS/NNA T1-6(b) was given as such because the hypothetical laid out in part (a) seemed unlikely and unreasonable to me, for the reasons I explained, and therefore a confirmation would have been misleading. If the hypothetical demands that I assume conditions that I do not believe reasonably would exist for a typical publication, I confirm.

b-d. See my response to subsection a

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-29 Please refer to Appendix **B** in your response to USPS/NNAT1-1, and to Table 6 in the testimony of witness Tang (USPS-T-35).

(a) Please confirm that the section of Appendix **B** headed "Periodicals In- County Rates, R2006-1 USPS Proposed mid-2007" contains, at Column C (the "None" column), a piece rate of 0.142. If you do not confirm, please explain.

(b) Please confirm that the Postal **S**ervice has not proposed a piece rate of 0.142 for any rate category in Within County Periodicals. If **you** do not confirm, please explain.

(c) Please explain why you used a piece rate of **0.142**, and explain how it was derived. Please provide any necessary corrections to Appendix **B**.

RESPONSES:

(a) Confirmed. That was an error on my part.

(b) Confirmed.

(c) The cell was inadvertently completed wrongly, and a corrected Exhibit **B** is attached, showing a piece rate of ,117 for None-entry, basic rate in-county presort. I also double-checked my 2006 rate chart, which is used for comparison, and found it to be correct for this rate cell. I see that the error correction actually makes **NNA's** arguments stronger, since the essence of our argument is that the most efficient mail gets hit harder than less efficient. The correction to ,117 lowers the percentage increase for the least efficient mail (None entry, basic presort) to a range of '14.6% to 20.8%. rather than the inadvertent 31-37% previously shown, for 1-16 oz.

Periodicals In-County Rates

R2006-1 USPS Proposed mid-2007

01-Nov-06

(USPS2007)

NOTE: High Density W/S rate based on 25% of active possible del. rates

Piece Rate	0.117	0.050	0.060	0.044	0.032
DU Discount	0.117	0.060	0.052	0.044	0.035
Pound Rate	0.179	0.179	0.142	0.179	0.142

Discounts	None	Carrier Route	Carrier Route Del O/c	Carrier Route HDW/S	Carrier Route HDW/S Del O/c	Carrier Route Sat W/S Del O/c
1 oz	0.1282	0.0712	0.0609	0.0552	0.0449	0.0329
2 oz	0.1394	0.0824	0.0698	0.0664	0.0538	0.0418
3 oz	0.1506	0.0936	0.0786	0.0776	0.0626	0.0506
4 oz	0.1618	0.1048	0.0875	0.0888	0.0715	0.0595
5 oz	0.1729	0.1159	0.0964	0.0999	0.0804	0.0684
6 oz	0.1841	0.1271	0.1053	0.1111	0.0893	0.0773
7 oz	0.1953	0.1383	0.1141	0.1223	0.0981	0.0861
8 oz	0.2065	0.1495	0.1230	0.1335	0.1070	0.0950
9 oz	0.2177	0.1607	0.1319	0.1447	0.1159	0.1039
10 oz	0.2289	0.1719	0.1408	0.1555	0.1248	0.1128
11 oz	0.2401	0.1831	0.1496	0.1671	0.1336	0.1216
12 oz	0.2513	0.1943	0.1585	0.1783	0.1425	0.1305
13 oz	0.2624	0.2054	0.1674	0.1894	0.1514	0.1394
14 oz	0.2736	0.2166	0.1763	0.2006	0.1603	0.1483
15 oz	0.2848	0.2278	0.1851	0.2118	0.1691	0.1571
16 oz	0.2960	0.2390	0.1940	0.2230	0.1780	0.1660

PERCENTAGE CHANGES -- New Rates over Old Rates

R2006-1 USPS Proposed mid-2007

01-Nov-06

Discounts	None	Carrier Route	Carrier Route Del O/c	Carrier Route HD W/S	Carrier Route HD W/S Del O/c	Carrier Route Sat W/S Del O/c
	22.21%	31.79%	32.72%	18.20%	20.58%	27.69%
	23.18%	30.79%	32.31%	20.58%	22.17%	23.32%
	23.94%	30.08%	32.02%	22.17%	23.32%	24.18%
	24.56%	29.56%	31.80%	23.32%	24.18%	24.85%
	25.06%	29.16%	31.63%	24.18%	24.85%	25.39%
	25.48%	28.84%	31.49%	24.85%	25.39%	25.83%
	25.84%	28.58%	31.38%	25.39%	25.83%	26.20%
	26.15%	28.37%	31.29%	25.83%	26.20%	26.51%
	26.42%	28.18%	31.21%	26.20%	26.51%	26.78%
	26.66%	28.03%	31.14%	26.51%	26.78%	27.01%
	26.87%	27.89%	31.09%	26.78%	27.01%	27.21%
	27.05%	27.78%	31.03%	27.01%	27.21%	27.39%
	27.22%	27.67%	30.99%	27.21%	27.39%	27.55%
	27.37%	27.58%	30.95%	27.39%	27.55%	27.69%
	27.51%	27.50%	30.91%	27.55%	27.69%	
	27.63%	27.43%	30.88%	27.69%		

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-30 Please refer to Appendix **B** in your response to **USPS/NNAT1-1**, and to Table 6 in the testimony of witness Tang (USPS-T-35).

(a) Please confirm that the section of Appendix B headed "Periodicals In-County Rates. R2006-1 USPS Proposed mid-2007" contains, at Column H (the "Carrier Route Sat W/S Del Ofc" column), a piece rate of 0.033. If you do not confirm, please explain.

(b) Please confirm that the piece rate for Carrier Route Saturation proposed by the Postal Service is 0.032. If you **do** not confirm, please explain.

RESPONSES:

(a) Confirmed. That was an error on my part

(b) Confirmed. The cell was inadvertently completed wrongly, and a correct Exhibit B is attached, showing the .032 piece rate for saturation. The percentage changes are relatively small, now 18.2% up to 27.7%, as compared to 21.8% to 28.5% for 1-16 oz. I also double-checked my 2006 rate chart, used for comparison, and found it to be correct for this rate cell.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-31 In your testimony at page 19, lines 23 to 26. you state, "a periodical sorted to carrier route high density presort that is not entered at the delivery office could experience a 47.3% increase, while a lower presort periodical also not DU entered would experience a 24.1% increase." Please refer to Appendix B in your response to NNA/USPS-T1-1.

(a) Please confirm that the range of percentage increases over current rates for carrier route high density presort not entered at the DU that you provide in Appendix B is 27.43 percent to 31.79 percent. If you do not confirm. please explain.

(b) Please provide the underlying calculations specifically supporting your statement that a carrier route high density periodical not entered at the DU could experience a 47.3 percent increase.

(c) Please confirm that when you state on lines 25 to 26 that "a lower presort periodical also not DU entered would experience a 24.1% increase." you are referring to a 5 oz Carrier Route Basic publication. If you do not confirm, please identify with specificity (i.e., weight and presort level) the periodical that you are referring to.

RESPONSES:

(a) Confirmed

(b) I have corrected this calculation in my testimony The increase is 29.56%.

**Not Delivery Unit Entered but CR High
Density**

Pound rate	0.0355	0.04475	
Piece rate	0.033	0.044	
	0.0685	0.08875	29.56%

(c) I was using a 4 oz paper as an example. for simplicity. That number has also been corrected, and my point remains that the lower presort piece receives a lower increase. My calculations are below:

Not Delivery Unit Entered; Not Automated; Basic rate

	2005	2007	% increase
Pound rate	0.0355	0.04475	
Piece rate	0.103	0.117	
	0.1385	0.16175	16.79%

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-TI-32 In your testimony at page 19, lines 27 to 29, you state, "a 5 digit auto newspaper would see a 39.71% increase while the same newspaper without a barcode would see an 18.11% increase." Appendix B in your response to NNA/USPS-T1-1 does not appear to provide the underlying calculations supporting these statements (if it does, please provide the specific cell references).

(a) Please identify with specificity (i.e., weight and shape) the 5 digit auto publication that you are referring to.

(b) Please identify with specificity (i.e., weight) the 5 digit nonauto publication that you are referring to.

RESPONSES:

My calculations for this example are below and have been corrected in my testimony

5 digit automation flat

Pound rate	0.0355	0.0448	
Piece rate	0.065	0.093	
	0.1005	0.1378	37.06%

5 digit nonauto flat

pound rate	0.0355	0.04475	
piece rate	0.085	0.098	
	0.1205	0.14275	18.46%

a. I was assuming a **4** ounce newspaper that would fit within automated flat sorting specifications. I did not assume any other dimensions

b. I was assuming a **4** ounce newspaper that would fit within automated flat sorting specifications. I did not assume any other dimensions.

Periodicals In-County Rates

R2006-1 USPS Proposed mid-2007

01-Nov-06

NOTE: High Density W/S rate based on 25% of active postal employees

(USPS2007)

Piece Rate	0.117	0.060	0.060	0.044	0.044	0.032
DU Discount	0.117	0.060	0.052	0.044	0.044	0.032
Pound Rate	0.179	0.179	0.142	0.179	0.142	0.142

Discounts	None	Carrier		Carrier		Carrier		Carrier	
		Route	Del Ofc						
1 02	0.1282	0.0712	0.0609	0.0552	0.0449	0.0379			
2 02	0.1394	0.0824	0.0698	0.0664	0.0538	0.0418			
3 02	0.1506	0.0936	0.0786	0.0776	0.0626	0.0505			
4 02	0.1618	0.1048	0.0875	0.0888	0.0715	0.0595			
5 02	0.1729	0.1159	0.0964	0.0999	0.0804	0.0684			
6 02	0.1841	0.1271	0.1053	0.1111	0.0893	0.0773			
7 02	0.1953	0.1383	0.1141	0.1223	0.0981	0.0861			
8 02	0.2065	0.1495	0.1235	0.1335	0.1070	0.0950			
9 02	0.2177	0.1607	0.1329	0.1447	0.1159	0.1039			
10 02	0.2289	0.1719	0.1429	0.1555	0.1248	0.1128			
11 02	0.2401	0.1831	0.1496	0.1671	0.1336	0.1216			
12 02	0.2513	0.1943	0.1585	0.1783	0.1425	0.1305			
13 02	0.2624	0.2054	0.1674	0.1894	0.1514	0.1394			
14 02	0.2736	0.2166	0.1763	0.2006	0.1603	0.1483			
15 02	0.2848	0.2278	0.1851	0.2118	0.1691	0.1571			
16 02	0.2960	0.2390	0.1940	0.2230	0.1780	0.1660			

PERCENTAGE CHANGES -- New Rates over Old Rates

R2006-1 USPS Proposed mid-2007

01-Nov-06

Discounts	None	Carrier		Carrier		Carrier		Carrier	
		Route	Del Ofc						
1 02	14.58%	23.00%	22.21%	31.79%	32.72%	18.20%			
2 02	15.42%	23.41%	23.18%	30.79%	32.31%	20.58%			
3 02	16.15%	23.72%	23.94%	30.08%	32.02%	22.17%			
4 02	16.79%	23.96%	24.56%	29.56%	31.80%	23.32%			
5 02	17.35%	24.16%	25.06%	29.16%	31.63%	24.18%			
6 02	17.84%	24.33%	25.48%	28.84%	31.49%	24.85%			
7 02	18.28%	24.47%	25.84%	28.58%	31.38%	25.39%			
8 02	18.68%	24.58%	26.15%	28.37%	31.29%	25.83%			
9 02	19.04%	24.68%	26.42%	28.18%	31.21%	26.20%			
10 02	19.36%	24.77%	26.66%	28.03%	31.14%	26.51%			
11 02	19.66%	24.85%	26.87%	27.89%	31.09%	26.78%			
12 02	19.93%	24.92%	27.05%	27.78%	31.03%	27.01%			
13 02	20.18%	24.98%	27.22%	27.67%	30.99%	27.21%			
14 02	20.41%	25.04%	27.37%	27.58%	30.95%	27.39%			
	20.62%	25.09%	27.51%	27.50%	30.91%	27.55%			
	20.82%	25.13%	27.63%	27.43%	30.88%	27.69%			

*** print only columns A-H, lines 5-62

Periodicals In-County Rates

R2006-1 USPS Proposed mid-2007
 05-NOV-06
 (USPS2007)
 NOTE: High Density W/S rate based on 25% of active possible deliveries

Piece Rate	0.117	0.060	0.080	0.044	0.044	0.032
DU Discount	0.117	0.060	0.052	0.044	0.036	0.024
Pound Rate	0.179	0.179	0.142	0.179	0.142	0.142

Final

05-Nov-06

COPY RESULTS FROM COLUMNS A-H BY / R/V

Discounts	None	Carrier Route	Carrier Route Del O/c	Carrier Route HD/W/S	Carrier Route HD/W/S	Carrier Route Sat W/S	Carrier Route Sat W/S
1 0z	0.1282	0.0712	0.0609	0.0552	0.0449	0.0329	0.1119
2 0z	0.1394	0.0824	0.0698	0.0664	0.0538	0.0418	0.1208
3 0z	0.1506	0.0936	0.0786	0.0776	0.0626	0.0506	0.1296
4 0z	0.1618	0.1048	0.0875	0.0888	0.0715	0.0595	0.1385
5 0z	0.1729	0.1159	0.0964	0.0990	0.0804	0.0684	0.1474
6 0z	0.1841	0.1271	0.1053	0.1111	0.0893	0.0773	0.1563
7 0z	0.1953	0.1383	0.1141	0.1223	0.0941	0.0861	0.1651
8 0z	0.2065	0.1495	0.1230	0.1335	0.1010	0.0950	0.1740
9 0z	0.2177	0.1607	0.1319	0.1447	0.1079	0.1039	0.1829
10 0z	0.2289	0.1719	0.1408	0.1559	0.1148	0.1128	0.1918
11 0z	0.2401	0.1831	0.1496	0.1671	0.1216	0.1216	0.2006
12 0z	0.2513	0.1943	0.1585	0.1783	0.1285	0.1305	0.2095
13 0z	0.2624	0.2054	0.1674	0.1894	0.1354	0.1394	0.2184
14 0z	0.2736	0.2166	0.1763	0.2006	0.1423	0.1483	0.2273
15 0z	0.2848	0.2278	0.1851	0.2118	0.1491	0.1571	0.2361
16 0z	0.2960	0.2390	0.1940	0.2230	0.1560	0.1660	0.2450

PERCENTAGE CHANGES -- New Rates over Old Rates

R2006-1 USPS Proposed mid-2007
 05-NOV-06

Discounts	None	Carrier Route	Carrier Route Del O/c	Carrier Route HD/W/S	Carrier Route HD/W/S	Carrier Route Sat W/S	Carrier Route Sat W/S
1 0z	14.58%	23.00%	22.21%	31.79%	32.72%	18.20%	20.58%
2 0z	15.42%	23.41%	23.18%	30.79%	32.31%	20.58%	22.17%
3 0z	16.15%	23.72%	23.94%	30.08%	32.02%	22.17%	23.32%
4 0z	16.79%	23.96%	24.56%	29.56%	31.80%	23.32%	24.18%
5 0z	17.35%	24.16%	25.06%	29.16%	31.63%	24.18%	25.02%
6 0z	17.84%	24.33%	25.48%	28.84%	31.49%	24.85%	25.89%
7 0z	18.28%	24.47%	25.84%	28.58%	31.38%	25.39%	26.78%
8 0z	18.68%	24.58%	26.15%	28.37%	31.29%	25.83%	27.67%
9 0z	19.04%	24.68%	26.42%	28.18%	31.21%	26.20%	28.56%
10 0z	19.36%	24.77%	26.66%	28.03%	31.14%	26.51%	29.45%
11 0z	19.66%	24.85%	26.87%	27.89%	31.09%	26.78%	30.34%
12 0z	19.95%	24.92%	27.05%	27.78%	31.03%	27.01%	31.23%
13 0z	20.18%	24.98%	27.22%	27.67%	30.99%	27.21%	32.12%
14 0z	20.41%	25.04%	27.37%	27.58%	30.95%	27.39%	33.01%
15 0z	20.62%	25.09%	27.51%	27.50%	30.91%	27.55%	33.90%
16 0z	20.82%	25.13%	27.63%	27.43%	30.88%	27.69%	34.79%

Periodicals In-County Rates

R2006-1 USPS Proposed mid-2007

01-Nov-06 NOTE: High Density W/S rate based on 25% of active possible del. w/ses (USPS2007)

Piece Rate	0.117	0.060	0.060	0.044	0.032
DU Discount	0.117	0.060	0.052	0.044	0.034
Pound Rate	0.179	0.179	0.142	0.142	0.142

Discounts	Carrier	Carrier	Carrier	Carrier	Carrier	Carrier	Carrier
	None	Route	Route	Route	Route	Route	Route
		Del. O/c	Del. O/c	HD W/S	HD W/S	HD W/S	Sat W/S
1 oz	0.1282	0.0712	0.0609	0.0552	0.0449	0.0329	
2 oz	0.1394	0.0824	0.0698	0.0664	0.0538	0.0418	
3 oz	0.1506	0.0936	0.0786	0.0776	0.0626	0.0506	
4 oz	0.1618	0.1048	0.0875	0.0888	0.0715	0.0595	
5 oz	0.1729	0.1159	0.0964	0.0999	0.0804	0.0684	
6 oz	0.1841	0.1271	0.1053	0.1111	0.0893	0.0773	
7 oz	0.1953	0.1383	0.1141	0.1223	0.0981	0.0861	
8 oz	0.2065	0.1495	0.1230	0.1335	0.1070	0.0950	
9 oz	0.2177	0.1607	0.1319	0.1447	0.1159	0.1039	
10 oz	0.2289	0.1719	0.1408	0.1559	0.1248	0.1128	
11 oz	0.2401	0.1831	0.1496	0.1671	0.1336	0.1216	
12 oz	0.2513	0.1943	0.1585	0.1783	0.1425	0.1305	
13 oz	0.2624	0.2054	0.1674	0.1894	0.1514	0.1394	
14 oz	0.2736	0.2166	0.1763	0.2006	0.1603	0.1483	
15 oz	0.2848	0.2278	0.1851	0.2118	0.1691	0.1571	
16 oz	0.2960	0.2390	0.1940	0.2230	0.1780	0.1660	

PERCENTAGE CHANGES -- New Rates over Old Rates

R2006-1 USPS Proposed mid-2007

01-Nov-06

Discounts	Carrier	Carrier	Carrier	Carrier	Carrier	Carrier	Carrier
	None	Route	Route	Route	Route	Route	Route
		Del. O/c	Del. O/c	HD W/S	HD W/S	HD W/S	Sat W/S
1 oz	14.58%	23.00%	22.21%	31.79%	32.72%	18.20%	
2 oz	15.42%	23.41%	23.18%	30.79%	32.31%	20.58%	
3 oz	16.15%	23.72%	23.94%	30.08%	32.02%	22.17%	
4 oz	16.79%	23.96%	24.56%	29.56%	31.80%	23.32%	
5 oz	17.35%	24.16%	25.06%	29.16%	31.63%	24.18%	
6 oz	17.84%	24.33%	25.48%	28.84%	31.49%	24.85%	
7 oz	18.28%	24.47%	25.84%	28.58%	31.38%	25.39%	
8 oz	18.68%	24.58%	26.15%	28.37%	31.29%	25.83%	
9 oz	19.04%	24.68%	26.42%	28.18%	31.21%	26.20%	
10 oz	19.36%	24.77%	26.66%	28.03%	31.14%	26.51%	
11 oz	19.66%	24.85%	26.87%	27.89%	31.09%	26.78%	
12 oz	19.93%	24.92%	27.05%	27.78%	31.03%	27.01%	
13 oz	20.18%	24.98%	27.22%	27.67%	30.99%	27.21%	
14 oz	20.41%	25.04%	27.37%	27.58%	30.95%	27.39%	
15 oz	20.62%	25.09%	27.51%	27.50%	30.91%	27.55%	
16 oz	20.82%	25.13%	27.63%	27.43%	30.88%	27.69%	

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPSINNA-TI-5. Please refer to your testimony, page 9. lines 16-17, where you state. "All of these circumstances could combine, in an environment where small errors loom large, to cause a tally to be wrongly marked." Please also refer to the response to the interrogatory **NNA/USPS-T1-16**.

- a. Do you agree that there were 193 direct Within-County tallies in FY2005? If not, please explain.
- b. Do you agree that an error in one tally would affect the estimated costs of Within-County Periodicals on average by less than 1 percent—i.e., approximately 1/193? If not, please explain.

RESPONSE:

- a. I have not examined the tally total. I understand from **NNA** Witness Siwek that there were 193 direct tallies relating specifically to Clerks and Mail Handlers Mail Processing costs and to City Carrier In-Office costs for Within County.
- b. I neither agree nor disagree. I have not examined the full scope of IOCS tallies for Within County.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T1-20 In your testimony on page 23, lines 2 to 4, you state that the Postal Service's proposed Within County rates "**do**] not provide sufficient incentive for high density mail, which is the category that publishers should be aiming for by increasing their readership on routes where they could achieve the density targets."

(a) Is it your testimony that the passthrough for the high density rate should be increased in order to provide publishers with an incentive to seek out new subscribers on particular carrier routes? If this is not your testimony, please explain.

(b) Do you agree that increasing the passthrough for the high density rate would increase the rates for other types of pieces assuming a fixed Within County revenue requirement? If you do not agree, please explain.

(c) Do you agree that a newspaper's incentive to increase its circulation is independent of any desire to qualify for a particular postage rate? If you *do* not agree, please explain

RESPONSES:

(a) That would make a lot of sense. It would benefit both the Postal Service and the mailer.

(b) I agree. Witness Siwek has proposed a number of adjustments within the subclass that make more sense than the rate design proposed here.

(c) I do not agree. Publishers have many reasons to seek subscribers, but I often work with publishers to concentrate their subscription campaigns in carrier routes where they might gain a discount with an increase in subscribers. The 25% level needed for high density is a realistic and acceptable level of mail delivery route penetration to be strived for, for many reasons, postage savings included.

**RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS HEATH TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE**

1

USPS/NNA-T1-24 In your testimony on page 6, lines 24 to 25, you state, "I have a high degree of confidence that newspaper mailing practices remain relatively stable over time." However, at lines 26 to 28 of that same page, you state that the newspaper industry is "more sophisticated, and engages in a much higher degree of mail preparation," and at lines 27 to 28 of page 21 you state that the billing determinants "show how highly efficient this subclass has become."

Please explain what you mean when you state that "newspaper mailing practices remain relatively stable over time" in light of your other statements.

RESPONSE:

I mean that newspapers use the mail for relatively the same purposes from year to year, as opposed to other delivery options--such as single copy or private carrier delivery. Thus, the apparent fluctuations in volumes make no sense to me. I find that the subscriber numbers remain relatively stable over time, which drives the mailing practices for carrier route, high density, DU entry, etc.

1 CHAIRMAN OMAS: Is there any additional
2 written cross-examination for Witness Heath?

3 (No response.)

4 CHAIRMAN OMAS: This brings us to oral
5 cross-examination.

6 One participant asked to cross-examine
7 Witness Heath, the U.S. Postal Service. Mr. Weidner?

8 MR. WEIDNER: Thank you, Mr. Chairman.

9 CROSS-EXAMINATION

10 BY MR. WEIDNER:

11 Q Good morning, Mr. Heath.

12 A Good morning.

13 Q Could you describe types of mailers who
14 utilize the within county subclass?

15 A Well, in my industry, of course, the ones
16 that I'm most familiar with are weekly newspapers that
17 probably average I think as we testified 3,000 to
18 5,000 range circulation.

19 There are also a limited amount of twice
20 weeklies and tri-weeklies, more twice weeklies than
21 tri-weeklies, and there are a number of dailies that
22 for reasons of geography or historical locations in
23 the trayed area they try to serve also use the in
24 county mails.

25 Also as I mentioned in my testimony, there's

1 a slight trend toward afternoon dailies moving toward
2 in county mail from a standpoint of high gas costs, so
3 we think there's some opportunity for the class to
4 continue to grow, but it's mainly used by weeklies.

5 There are also some nonprofits and so forth
6 in there, city and regional magazines and church
7 publications, I believe.

8 Q So not all within county mailers are
9 newspapers, correct?

10 A Not all, no.

11 Q For the non-newspaper portion of the within
12 county mail stream do you have any understanding as to
13 their ability to take advantage of presort discounts
14 and the like?

15 A Well, most everybody in the industry, and I
16 would wager to say that in the non-newspaper side of
17 the industry that most people other than perhaps
18 churches, but the nonprofits and the majority of the
19 mailers that represent more sophisticated associations
20 or something that have an arrangement for that
21 particular subscription to go to their members under a
22 Postal rule, I find them to be fairly sophisticated
23 and to use pretty good software.

24 So it would be my belief, and we've
25 testified so, that we think the majority of the class

1 uses presort software in some manner in the source of
2 the carrier route and so forth. Does that speak to
3 your question?

4 Q Yes. The less sophisticated the
5 publication, the more likely it's going to be that
6 they will not qualify for the higher presort levels by
7 carrier route. Is that correct?

8 A Well, NNA has over the years tried to
9 represent the smallest paper in Nebraska, as I like to
10 say.

11 We have developed with the cooperation of
12 some very good people in the Postal Service in Mailing
13 Standards some optional processes whereby a small
14 paper can obtain walk sequence information from its
15 local post offices and can get that certified on a
16 form provided by the Postal Service with written
17 letter permission and get it recertified every 90
18 days.

19 So it is possible and there are people who
20 do use optional processes that allow them to qualify
21 for carrier route rates without more expensive presort
22 software. I can't qualify exactly how many are using
23 that optional process, but I'm always pleased and
24 surprised as I go around making visits around the
25 country. I find people that are using it.

1 We train on it, and then a lot of times
2 after I leave we'll find somebody that then decides
3 they can use it and lets me know, so there are
4 optional processes that allow carrier routes to be
5 done without the expensive presort software.

6 Q All right. But clearly there are within
7 county mailers who don't use the carrier route as the
8 billing determinants show?

9 A It's always a great shock to me frankly. My
10 company just bought a newspaper in Florida, and I was
11 shocked to find out that these people had just
12 continued to send their mail out as five digit mail
13 into the local post office and pay those higher rates.

14 We're in the process of fixing that this
15 very week, getting them into the carrier route presort
16 environment. I guess there are some people that kind
17 of go to sleep.

18 Q And you're speaking there of newspapers,
19 correct?

20 A Newspapers, yes.

21 Q All right.

22 A I'm not familiar with anybody else.

23 Q Okay. From a newspaper perspective, or if
24 you can speak to other type of within county mailers
25 that are not newspapers, what type are generally going

1 to use the basic level or the three digit level?

2 A Well, most every publication has a certain
3 amount of residual mail, the mail that doesn't fall
4 into the carrier route sort with six or more on
5 carrier route.

6 Depending on the coverage of their area, I
7 think some of the city and business and regional
8 magazines, they typically would not have a large
9 circulation base. They're not of general circulation
10 as much they are specific circulation that is angled
11 towards a business or a court or commercial legal type
12 environment where businesses want to see this
13 information.

14 Some of those that I've observed, and
15 they're part of NNA actually. Some of those I've
16 observed will have more five digits scattered around
17 throughout their trayed area just because they can't
18 mass **up** as many copies except in maybe the business
19 zones, the downtown zones and some other sometimes
20 suburban park zones where the businesses are located,
21 and their subscribers don't subscribe to those.

22 They would tend to fit more into the mode of
23 people who have a higher percentage of five digit,
24 three digit and basic.

25 Q And given your understanding, you mentioned

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1 church bulletins earlier. Do you know what they would
2 typically qualify for?

3 A Well, I think they could operate as either
4 standard or periodicals under certain circumstances.
5 I don't really have a broad knowledge of what they
6 operate under.

7 I do notice in some of the tallies that
8 we've seen in the testimony that there's some
9 publications that look like church bulletin type
10 material, you know. I'm really not sure exactly how a
11 church bulletin meets periodical status.

12 I am familiar, however, with the mega
13 churches that have periodical nonprofit status and put
14 a standard community type newspaper out to serve that
15 church. I know that was started in 1996 for a mega
16 church in Louisville. It's about 25,000 a week.

17 That particular one does serve a church in
18 more of a newspaper format than a bulletin format and
19 so it is clearly as much a periodical as any other
20 community newspaper, a newspaper periodical.

21 Q You mentioned the smallest newspaper in
22 Nebraska is a member of NNA, and you have provided
23 optional carrier route processing for them.

24 For a newspaper that's not a member of NNA
25 that's a small weekly or daily community newspaper,

1 would you have any understanding as to their ability
2 to qualify for carrier route rates?

3 A Well, generally speaking, most people have
4 got this carrier route thing down.

5 It's a rare occurrence. It's a shocking
6 thing to me to find a paper like we found in Florida
7 recently when we bought a paper that was not sorting
8 to the carrier route. The postmaster and I discussed
9 it and realized it certainly needed to be done.

10 Generally speaking, as I travel around the
11 country doing seminars -- I'm doing 15 this year. I
12 just counted up last night. Usually it's more like
13 six to 10, but this rate case has sort of increased
14 some anxiety among mailers who have asked us to come
15 and talk to them.

16 As you visit people and we ask them to bring
17 their Postal forms and we look at them, we rarely see
18 a paper that is not making some effort at carrier
19 route sorting so it's a fairly rare situation, but it
20 is one that I do run into.

21 Q Okay. Moving on, Mr. Heath, is it fair to
22 say from your testimony and your interrogatory
23 responses that service is of particular importance to
24 newspapers, correct?

25 A Yes. That is the service though that is

1 outside the county of origin because inside the county
2 of origin we take most of our mail directly to the
3 delivery office. We strongly encourage people to do
4 that. The Postal Service to some degree incenses
5 people to do that.

6 We take it to other operations that are post
7 offices that are within the trayed area, but not in
8 the county. County line newspapers can have some
9 particular problems with that because they're paying
10 much higher rates if they're right near that county
11 line.

12 Most of it is delivery office entered. The
13 problems that we have are with working mail that's
14 sent through an SCF and beyond, especially since the
15 24 piece sack rule was imposed on us by the last rate
16 case settlement.

17 Q So for those pieces that are delivered
18 outside the trayed zone, would you agree that a
19 typical newspaper mailer will use whatever container
20 -- be it a sack, tub, whatever -- that will ensure the
21 most timely delivery of their newspaper?

22 A Well, they'd certainly like to. The
23 understanding on the use of sacks and tubs even within
24 the Postal Service for a tub option is one that's been
25 a little slow to take hold even though it was optional

1 since October 25, 2005, yes, but we'd like to, and I
2 think most people would like to.

3 Q And service is a big reason why, as you
4 state in your testimony, you have encouraged
5 newspapers to switch to tubs, right?

6 A Right because of several experiments that we
7 refer to in our testimony here that have been done
8 just to fix within state service, for instance, in I
9 think we first reported on Mississippi. I first
10 encountered it a few years ago in Houston, Texas.
11 North Houston District was encouraging newspapers to
12 go to tubs for service reasons.

13 One of our NNA board members worked with
14 people in Maine to get about nine newspapers working
15 out of one particular area all going into trays or
16 tubs as people commonly call them for service reasons
17 within that state.

18 Those initial things were done within a
19 state. They weren't done nationwide.

20 Q Okay. As you mention at page 15 of your
21 testimony, the main experiment, for example, has
22 produced what you understand to be container
23 reductions and improved service. Is that correct?

24 A That's correct, yes. Tubs are easier to
25 handle and are handled more quickly and not deferred

1 like sacks.

2 A lot of people I ve talked to in the Postal
3 Service informally that wou d be on the workroom floor
4 confirmed that fact.

5 Q Okay. Could you turn to your response to
6 Interrogatory 8(b), please?

7 A Okay.

8 Q You actually talk about it earlier. You
9 talk about how for your company, LCNI, you typically
10 do unsacked bundles to the trayed area, and outside
11 the trayed area you use sacks. Is that correct?

12 A That's right. According to the rules, you
13 can't use trays for any three digit or five digit mail
14 outside the trayed area or in the trayed area, for
15 that matter.

16 Q Right. For the typical community newspaper,
17 is the mailing profile something like a concentration
18 of addressees in the local zips, the local zips in the
19 trayed area, and with the rest of the addressees
20 dispersed throughout the country as people move away
21 from their hometown, but want to maintain a connection
22 with it?

23 A I think that's a fair statement. We see
24 sort of a concentration of course of snowbirds in
25 Florida for most of the eastern markets that we have

1 in the southeast, and we'll see certain communities
2 where people will move from the south and the upper
3 south to places like Aurora, Illinois, and Cincinnati,
4 Ohio.

5 We've got carrier route presort mail in
6 Cincinnati because so many people from one of our
7 weeklies moved up there in the 1950s and 1960s. It's
8 strange. You can see little pockets where people end
9 up relocating.

10 Q Again, the newspapers that are sent to the
11 trayed areas are generally going to be sent within
12 county, and the others outside of the trayed area is
13 typically you said outside county, correct?

14 A Well, it varies somewhat. If there's enough
15 volume going to a post office that is important to the
16 readers and advertisers because of its traffic
17 patterns I advise people, and most people I think tend
18 to follow the practice, that you need to be taking
19 that mail to the delivery unit, especially since the
20 24 piece rule. I strongly encourage people to open up
21 more delivery unit drops and take advantage of the
22 rates.

23 This is particularly tough on county line
24 newspapers because they have a lot of mail that's not
25 getting the in county rate, so they need to really

1 pick it up and not depend on the Postal Service to do
2 it if it goes into working mail that takes two or
3 three days, four days.

4 Q Right. Typically with that exception, say a
5 newspaper in Mississippi has some subscribers in
6 southern Florida. They're typically not going to go
7 to the delivery unit in that circumstance, right?

8 A No, absolutely not.

9 Q All right.

10 A You can't go beyond Zone 1 and 2 anyway. We
11 got it expanded a little bit a couple years ago to go
12 that far, but most people except in west Texas don't
13 drive it over maybe 30, 40, 50 miles probably,
14 somewhere in that range.

15 Q Okay. Also sticking with a typical
16 community newspaper and sticking to those pieces that
17 are going to be traveling at outside county rates to
18 addressees probably dispersed throughout the country,
19 what type of sacks are we generally talking about?
20 I'm speaking here in terms of presort level.

21 A Well, in the current environment since
22 May 11, 2006, since the 24 piece sack rule advent,
23 it's a different world, but up until that point there
24 were a lot of six piece sacks heading to three digit
25 zip codes, occasionally to five digit zip codes, and

1 more frequently to area distribution center zip codes.

2 Today it's a different environment where
3 because of the 24 piece sack rule there's fewer and
4 fewer five digit sacks, fewer three digit sacks and
5 more mixed ADC mail and origin mixed ADC mail, which
6 is the new permissive tray product that has been a
7 very positive thing for us.

8 Q Okay. Could you turn to part (c) of that
9 same interrogatory?

10 A Okay.

11 Q Is it fair to say that when you're talking
12 about the ability to place newspapers in flat tubs and
13 you discuss a small, twofold tabloid and then large,
14 bulkier broad sheets, you're talking about a spectrum
15 of newspaper sizes with maybe a small tabloid on the
16 low end and the broad sheet on the high end in terms
17 of size?

18 A Uh-huh.

19 Q Is that a fair statement?

20 A Right. We have college sports publications.
21 We own seven titles. These magazines are not very
22 large in page count and so we found we can get as many
23 as 200 of those, and there are other small tabloids of
24 that size that qualify as periodicals, but, generally
25 speaking, that's not a common thing. It can run

1 anywhere from 15 or 20 up to 200.

2 Q Right. Based on your experience, what is
3 the most common? Where would you expect the typical
4 community paper to fall in that spectrum?

5 A Well, for an ADC flats tub the minimum is
6 24, and most of the people can default to that level
7 in their software.

8 However, I encourage our people to try to
9 minimize the number of tubs that they use instead of a
10 higher number if the average weight -- excuse me. The
11 average size of that paper, the bulk of that paper,
12 comes at a place that they can figure out that they
13 can get 40 or 50 in a tray on a regular basis with the
14 maximum size of the paper we encourage them to run up
15 a little higher.

16 It's a little bit new to us and we're still
17 adjusting, quite frankly, but I think it's probably
18 closer to 40 or 50 for the average newspaper.

19 Q Okay. Could you turn to your response to
20 Interrogatory 12, please?

21 A I'm there.

22 Q Just so I understand your response
23 correctly, are you saying that regardless of the
24 container or lack of container that the newspaper uses
25 they typically will have one container for each DDU

1 drop? Is that the import of this answer?

2 A For offices other than the origin entry
3 office that is probably more likely to be so than not.

4 The Postal Service allows 40 pounds of mail
5 in a DDU bundle, whereas they only allow 20 pounds of
6 mail in a sack bundle and so those unsacked bundles of
7 40 pounds will usually accommodate a fairly high
8 number of papers so there would be, you know, two or
9 three bundles at the most probably for most DDUs.

10 Did that answer your question?

11 Q Yes. You say in the last sentence talking
12 about unsacked bundles the number of hypothetical
13 containers in many cases would equal the number of
14 five digit zip codes, so I took from that and I think
15 you just confirmed that it's typically one container
16 per five digit zip code. Is that correct?

17 A It's typically one noncontainer.

18 Q Yes.

19 A Or what some people call an air container or
20 virtual container.

21 Q I'm sorry. We were just pointing out. We
22 noticed the error in the actual question. It's
23 actually Presiding Officer's Ruling No. 30, but it's
24 no matter.

25 Kind of changing gears here, I'd like to

1 discuss your interrogatory responses dealing with
2 Section 1(a) and 1(b) of your testimony where you
3 discuss nonsubscriber copies and their ability to
4 qualify for within county rates.

5 A 1(a) and 1(b)?

6 Q Yes. That's the section of your testimony.

7 A Yes. Right. Let me get there. Right.

8 Okay.

9 Q Okay. It is correct, isn't it, that the DMM
10 allows nonsubscriber pieces to be sent at within
11 county rates so long as the number sent at those rates
12 does not exceed 10 percent of the within county
13 subscriber volume? Is that correct?

14 A That's correct.

15 Q You state in your response to Interrogatory
16 6 and 26 that publishers often reserve that allowance
17 for the purpose of sending out copies to potential new
18 subscribers. Is that correct?

19 A That's the highest and best use, yes.

20 Q So when you say it's the highest and best
21 use, you do confirm, do you not, that it's not the
22 only use that a publisher may make of that allowance,
23 correct?

24 A It's not the only use. There are people who
25 mail single copies to rural outlets that are a little

1 too hard to drive to. There's nothing between here
2 and there, 30 miles of bad road.

3 There are places where we take Newspapers in
4 Education copies to schools during the high school
5 season using in county mail. They are in county
6 copies, but many of those -- they get to a certain
7 point of the year, somewhere about the midpoint of the
8 year. They go over to paying out of county copies
9 because they have exceeded that entitlement.

10 Q Do you agree that different publishers will
11 have different numbers of nonsubscriber copies
12 relative to subscriber copies in a given year? That
13 is, some publishers will send more nonsubscriber
14 copies relative to subscriber copies than others. Do
15 you agree?

16 A Absolutely. Yes.

17 Q So based on that it stands to reason that
18 the 10 percent limit is going to be a bigger issue for
19 some publishers over others? Is that correct?

20 A I think that's a fair statement. I get a
21 lot of people that want to try to figure out how to
22 get as close as they can without going over both the
23 10 percent in county rule and the 50 percent when they
24 use the regular rate rule.

25 A lot of people are fighting for circulation

1 out there, so we see people. People call me all the
2 time saying how many can I send out without violating
3 the 50 percent rule?

4 There are people eager to pay outside county
5 rates in order to get copies out there to build their
6 advertising volume and build their total circulation.

7 Q You would agree that some publishers, maybe
8 many publishers, won't have to worry about exceeding
9 the 10 percent limit?

10 A Certainly. Possibly, yes.

11 Q Okay. Of course, if a publisher is not
12 going to reach the 10 percent allowance in a given
13 year it's not necessary for them to reserve the
14 allowance for the purpose you mentioned in the
15 interrogatory responses since all those copies are
16 going to be able to go on within county rates. Isn't
17 that correct?

18 A I suppose that's correct, but again
19 practices do vary widely because of the competition
20 and even the competition on the internet. A lot of
21 papers are fighting hard trying to get the circulation
22 maximized that they've got.

23 I'm a little surprised that I find quite a
24 few people who are willing to pay the regular rate in
25 order to get the total number of copies out that are

1 distributed, so they're paying outside county rates.

2 Q Publishers do have, don't they, a pretty
3 strong incentive to utilize within county rates
4 whenever they can because they are significantly lower
5 than outside county rates?

6 A Yes, about a third I think I've estimated.
7 About a third lower than regular rates.

8 There are a lot of requests for publications
9 of course that use those rates because they want to
10 hit every household so I believe there are, but there
11 are times that business plans dictate that certain
12 things you do maybe cause you to use more regular rate
13 mail than maybe you would wish to use.

14 Q Right. But you're always going to try to
15 use within county whenever you can?

16 A Absolutely. You should certainly. You
17 absolutely should.

18 Q Would you agree that the likelihood of a
19 nonsubscriber piece paying within county rates is
20 dependent on whether or not the publisher is going to
21 break what you termed the sampling allowance or the 10
22 percent allowance?

23 A Would I agree that --

24 Q I can repeat it if you want.

25 A Yes. Let me hear that again.

1 Q Yes. It's basically a matter of logic that
2 the likelihood that a nonsubscriber piece paying
3 within county rates is dependent on whether or not the
4 publisher is going to break the allowance. That is,
5 if a publisher has a chance of breaking the allowance
6 -- excuse me. Okay. I'll repeat it since I confused
7 even myself there briefly.

8 Would you agree that the likelihood of a
9 nonsubscriber piece paying within county rates is
10 dependent on whether or not the publisher breaks the
11 sampling allowance or is going to break the sampling
12 allowance?

13 A Generally speaking, yes, although I find
14 occasions where people inadvertently break it. They
15 don't think this thing through. They're not using the
16 Postal Service tools to track that or they don't track
17 it.

18 It's sometimes poorly enforced, so people
19 break it without thinking about it. Maybe they break
20 it for a year or two and get by with it. The next
21 thing you know they've got to fix it. It's broken on
22 purpose, it's broken inadvertently, and some people
23 don't break it. It's all over the board.

24 Q You mentioned the Postal Service does
25 provide a tool on the internet that facilitates the

1 counting of subscriber **and** nonsubscriber copies so
2 that publishers can keep track of when their annual
3 pieces are approaching the 10 percent limit, correct?

4 A That's right. I worked with Joel Walker of
5 Manning Standards to develop that and put it up there.
6 Yes.

7 Q All right. And that was asked in
8 Interrogatory 26 (e).

9 We know that some publishers are going to
10 have an issue with the 10 percent allowance. Some
11 aren't. Do you agree that from the perspective of
12 IOCS the fewer nonsubscriber pieces there are that
13 actually exceed the 10 percent limit the less
14 potential there is for IOCS to misclassify those
15 pieces as within county when they have in fact paid
16 outside county rates?

17 A I think that's a logical statement, yes.

18 Q One last thing. **Could** you turn to your
19 response to Interrogatory 17?

20 A Okay.

21 Q **And** particularly part (b). It is your
22 understanding, isn't it, that discounts in within
23 county and in other subclasses are derived by passing
24 through a certain percentage of Postal Service avoided
25 costs?

1 A Yes, I do agree, although sometimes we think
2 the Postal Service keeps a little bit too much for the
3 house.

4 Q But mailer costs are not taken into account
5 in that equation? Is that correct?

6 A Mailer what?

7 Q Mailer costs are not taken into account when
8 setting discounts. That is, how much it costs a
9 mailer to incur to do whatever worksharing activity
10 there is.

11 A Are you talking about by the Postal Service?
12 The Postal Service doesn't take mailer cost into
13 account?

14 Q When discounts are created in the rate
15 schedule, mailer costs are not taken into account.
16 You're only going to look at Postal Service avoided
17 costs. Is that correct?

18 A Okay. I think that. would be correct, yes.

19 Q So discounts are in fact based on Postal
20 Service avoided costs rather than the costs incurred
21 by a mailer, correct?

22 A I guess that's true. I'm not sure, frankly.

23 MR. WEIDNER: All right. That's it. Thank
24 you.

25 CHAIRMAN OMAS: Thank you, Mr. Weidner

1 Is there any other participant who would
2 like to cross-examine Witness Heath?

3 (No response.)

4 CHAIRMAN OMAS: Are there any questions from
5 the bench? Commissioner Acton?

6 COMMISSIONER ACTON: Thank you, George.

7 Good morning, Mr. Heath.

8 THE WITNESS: Good morning.

9 COMMISSIONER ACTON: I have a question for
10 you regarding the seminars you mentioned during the
11 course of your testimony. Can you tell us a bit about
12 the frequency, the scope and the general nature of
13 those seminars?

14 THE WITNESS: Well, we put together a
15 program, a hard copy handout, that we call Maximizing
16 Your Postage Savings and Delivery. We started out in
17 1988 because we were asked to save some money for the
18 Sacred Press Association's mailing of their monthly
19 Kentucky Press magazine.

20 Some other people were there, some other
21 associations, and they said they'd like us to come and
22 do something for their members so it sort of took off
23 there. We didn't come up with a plan to do this, but
24 it just sort of happened.

25 What we try to do there is to show people

1 what the costs are and to show people what the cost
2 saving opportunities are such as barcoding. That's an
3 opportunity that people still have out there that not
4 everybody is caught up with yet.

5 We show what their opportunity is for
6 carrier route savings to get to the high density
7 level, which is a big thing that we stress to people.
8 We try to stress to people that newspapers are in the
9 walk sequence business. They're not in just the
10 carrier route sort business. They need to walk
11 sequence their mail.

12 We tell them about such things as firm
13 packages that save 100 percent of the piece rate and
14 some other rules and things that: can help them both
15 with interpretations of some of the rules that they
16 might want to run across to keep them out of trouble,
17 and then we also talk about how to maximize their
18 delivery by making sure that they take advantage of
19 the current rules and some of the options that have
20 been made available by the good people of Mailing
21 Standards on behalf of the NNA members. Actually it's
22 distributed only by the NNA members.

23 Then we do a little third class piece too
24 with our standard mail piece because there are many of
25 our papers that are heavy mailers of standard mail and

1 also mail renewal notices, as well as shopper
2 material, advertising material to nonsubscribers or
3 all of the subscribers in their market on another day
4 of the week.

5 **COMMISSIONER ACTON:** How about the switch to
6 tubs? Is that an issue that you guys addressed in the
7 context of --

8 **THE WITNESS:** Very much so. Following a
9 summit that we held here on the 11th of August, I
10 realized that I needed -- even though I had been
11 preaching it through my monthly column, that people
12 needed to prepare for this 24 piece rule change and
13 needed to open up more delivery office drops, and they
14 needed to make sure they were barcoding all their mail
15 and making sure they were using paid certified
16 software with Postal Service approval.

17 We then also realized that the OMX was not
18 well understood within the Postal Service. As we
19 tried to encourage people to do this, they would go
20 down say in Mississippi, and nobody in the State of
21 Mississippi knew about OMX.

22 We developed a piece that showed them
23 exactly how a tray looks prepared, and we give them 10
24 steps to work through, the first one being educate
25 your postmaster that it was in the *Postal Bulletin* of

1 October 25, 2005. Three types of tubs are allowed.
2 You need to go there. It's an option, but for you
3 it's mandatory if you want good service.

4 COMMISSIONER ACTON: Thank you, Mr. Heath.

5 CHAIRMAN OMAS: Commissioner Goldway?

6 COMMISSIONER GOLDWAY: Thank you, Mr.
7 Chairman.

8 I have a question about the inconsistency
9 with zip codes following or not following county
10 borders. You've indicated in your testimony that
11 there is a problem in the IOCS tallies because of the
12 misidentification.

13 I'm wondering if you have any ideas for how
14 the Postal Service might be able to identify perhaps
15 in the subsequent four digits or some other way the
16 county delineation which would help at least one of
17 the problems in the IOCS tallies.

18 THE WITNESS: Well, when they're doing those
19 tallies -- I hate to be too much of a technical expert
20 for them, but if they're doing those tallies if they
21 would simply do an address look up on that paper that
22 they record it, if they do in fact record the
23 addresses of any subscribers they're looking at.

24 They could actually iheck on the USPS
25 website, and if they were a matched address it shows

1 the county of origin in a click on box there once you
2 get a match of that address.

3 It's pretty tough out in the country. You
4 know, I'm from Kentucky where we have small counties.
5 There's 120 counties crammed in that area, so it's not
6 uncommon at all for those routes to meander, you know,
7 out of the county.

8 The biggest thing, and I always ask for a
9 show of hands on this, is how many people are on
10 county line newspapers. They're the ones that grumble
11 to us quite a bit because they're having to pay out of
12 county rate because a half or a third of their
13 circulation, maybe two-thirds sometimes, is in another
14 county.

15 Our company owns a paper in Dunnellon,
16 Florida, that is right on a river, the Withlacoochee
17 River, and right across that river is Citrus County
18 and so about a third of the circulation of that
19 Dunnellon Post Office is in Citrus County, and another
20 part of it is over in Levy County to the northwest and
21 so it has some percentage -- I don't know which; a
22 smaller percentage.

23 Even though the largest amount of it is in
24 Marion County where Dunnellon is physically located,
25 these county line newspapers that are located often

1 near rivers because they end up being used as county
2 demarcation lines, they have a real problem with the
3 rate structure, and I would say it could be
4 problematic for people that are trying to figure out
5 whether their paper is really in county or not.

6 Anybody looking at the *Dunnellon News*, the
7 *Riverland News* and the *Dunnellon*, it would look like
8 an in county paper, but a good part of its circulation
9 is actually in another county.

10 COMMISSIONER GOLDWAY: There would be no way
11 to have a certain kind of address overlay for
12 communities, you think? Have you thought of that?

13 THE WITNESS: Well, are you talking about
14 some physical markings?

15 COMMISSIONER GOLDWAY: Some sort of
16 identification within the addressing system of the
17 Postal Service that could identify a community even if
18 it's split by a county line.

19 THE WITNESS: The addresses are recorded in
20 the Postal Service database as to what county they're
21 in.

22 COMMISSIONER GOLDWAY: I know, but could
23 there also be some identification of this community
24 that they're in since by historical happenstance they
25 wind up being split into two counties even though it

1 turns out to be more or less one community?

2 THE WITNESS: Well, I'm not sure what you're
3 asking that they might do there. What are you
4 suggesting?

5 COMMISSIONER GOLDWAY: Do you have any other
6 ideas of how the IOCS tallies might be improved?

7 THE WITNESS: Well, since there aren't a lot
8 of them I guess I would think that the piece that they
9 have, they ought to take a picture of the address and
10 have them physically check on the Postal Service
11 website. That would be my suggestion.

12 COMMISSIONER GOLDWAY: And one more general
13 question for you. You indicate in your testimony that
14 your papers have increased in circulation by 7.9
15 percent. There was a big article in the paper just
16 two days ago about newspaper circulation declining as
17 much as five percent around the country. How are you
18 doing it?

19 THE WITNESS: Well, we've worked awful hard
20 at it for one thing, and we happen to be in some
21 growth markets. We specialize in weekly papers, and
22 some of the work that I do in acquisitions, we're only
23 buying weekly papers. We think the future of the
24 small dailies is kaput, frankly, and the larger
25 dailies is even more kaput.

1 COMMISSIONER GOLDWAY: Is it email? What is
2 it that's changing the nature of the newspaper?

3 THE WITNESS: Well, it's the distribution of
4 news on websites largely in my opinion is having a lot
5 to do with it and people's time. People get their
6 information from other sources.

7 COMMISSIONER GOLDWAY: What is it about the
8 weekly papers that's --

9 THE WITNESS: Well, they're community based.
10 They're typically in rural areas that are not **as** fully
11 deployed into high speed internet, although that is
12 gradually changing. We're beginning to see some
13 effects of that.

14 Don't get me wrong. This year for 2006 was
15 the first year I've ever had a decline in circulation
16 in my division -- we just finished figuring that out
17 last week -- of 1.3 percent, but prior to every other
18 year we have grown. We think we can continue to grow
19 with proper effort.

20 We sell a lot of subscriptions off the
21 internet. If you set the internet up right, you can
22 actually get people to subscribe to your paper through
23 the internet and overcome a lot of the problem that
24 the internet caused us, if you want to call it a
25 problem.

1 It is a new channel for all newspapers. Our
2 association recently approved internet memberships.
3 That's a distribution channel that's going to be
4 increasingly important to us, and in fact many of our
5 members are using the internet to redeem a
6 subscription that is totally electronic and has a
7 complete facsimile of every page of the newspaper.

8 They go there and either send out a file to
9 the subscriber once a week, or the subscriber is
10 prompted with an email message to click on something
11 and see that subscriber. This is used primarily for
12 distance subscribers who don't get good mail service,
13 so the internet is competing with the Postal Service,
14 not just competing with the newspaper business.

15 People that make an effort to grow
16 newspapers can grow newspapers -- I'll put it that way
17 -- at least in the small weekly segments. It's a
18 little tough in the big daily segment.

19 COMMISSIONER **GOLDWAY**: Thank you for your
20 answers.

21 CHAIRMAN **OMAS**: Ms. Rush, would you like
22 some time with your witness?

23 MS. RUSH: Mr. Chairman, maybe about three
24 minutes?

25 CHAIRMAN **OMAS**: Well, why don't we take

1 about a five minute break and we'll be back. Thank
2 you.

3 (Whereupon, a short recess was taken.)

4 CHAIRMAN OMAS: Ms. Rush?

5 MS. RUSH: Mr. Chairman, thank you. We have
6 no redirect.

7 CHAIRMAN OMAS: Thank you.

8 Mr. Heath, that completes your testimony
9 here today. We appreciate your appearance before the
10 Commission. and we thank you for your contribution to
11 the record. You are now excused. Thank you very
12 much.

13 (Witness excused.)

14 CHAIRMAN OMAS: Ms. Rush, would you identify
15 your next witness, please?

16 MS. RUSH: Mr. Chairman, NNA would like to
17 call Witness Stephen Siwek.

18 CHAIRMAN OMAS: Would you raise your right
19 hand?

20 Whereupon,

21 STEPHEN E. SIWEK

22 having been duly sworn, was called as a
23 witness and was examined and testified as follows:

24 CHAIRMAN OMAS: Be seated.

25 Ms. Rush?

1 MS. RUSH: Mr. Chairman, Mr. Siwek's
2 testimony appears in two parts. I'll proceed with the
3 first part.

4 DIRECT EXAMINATION

5 (The document referred to was
6 marked for identification as
7 Exhibit No. NNA-T-3.)

8 BY MS. RUSH:

9 Q Mr. Siwek, I am presenting to you Direct
10 Testimony of Stephen E. Siwek on Behalf of the
11 National Newspaper Association and asking you if this
12 testimony was prepared by you or under your direction?

13 A Yes, it was.

14 Q If you were to testify today, would your
15 testimony be the same?

16 A Yes.

17 MS. RUSH: Mr. Chairman, I offer the
18 testimony of Stephen E. Siwek into evidence.

19 CHAIRMAN OMAS: Without objection.

20 However, first of all I did omit as I
21 understand it Witness Siwek sponsored an exhibit that
22 is under seal.

23 Ms. Rush, I understand in addition to his
24 testimony Witness Siwek sponsored material subject to
25 protective conditions. Please introduce the material

1 **sub** j ct to protective conditions separately, which I
2 think you are about to do, but we'll go on.

3 Without objection, we will receive into
4 evidence the first.

5 (The document referred to,
6 previously identified as
7 Exhibit No. NNA-T-3, was
8 received in evidence.)

9 MS. RUSH: Thank you, Mr. Chairman. I'm
10 about to present to the witness Appendix E to his
11 testimony, which was filed under protective conditions
12 pursuant to Presiding Officer's Ruling No. 51.

13 (The document referred to was
14 marked for identification as
15 Exhibit No NNA-T-3, Appendix
16 E.)

17 BY MR. RUSH:

18 Q Mr. Siwek, was this appendix also written by
19 you or under your supervision?

20 A Yes, it was.

21 Q And if you were to testify today would your
22 testimony be the same?

23 A Yes, it would.

24 MS. RUSH: Mr. Chairman, I'd like to also
25 move this into evidence under protective conditions.

1 I m pla ing it in the envelope, and I trust you want
2 me to seal the envelope at this time?

3 CHAIRMAN OMAS: Please.

4 Is there objection?

5 (No response.)

6 CHAIRMAN OMAS: Hearing none, I will direct
7 counsel to provide the reporter with two copies of the
8 corrected direct testimony of Stephen E. Siwek.

9 That testimony is received into evidence.
10 However, as is our practice, it will not be
11 transcribed.

12 This is the protective conditions testimony
13 that is received into evidence. The reporter shall
14 mark this material and return it to the Commission
15 under seal.

16 (The document referred to,
17 previously identified as
18 Exhibit No. NNA-T-3, Appendix
19 E, was received in evidence.)

20 CHAIRMAN OMAS: Mr. Siwek, have you had an
21 opportunity to examine the packet of designated
22 written cross-examination made available to you this
23 morning?

24 THE WITNESS: Yes, I have.

25 CHAIRMAN OMAS: If the questions contained

1 in that packet were posed to you orally; today would
2 they be the same as those you provided us in writing?

3 THE WITNESS: Yes, they would.

4 CHAIRMAN OMAS: Are there any additions or
5 corrections you would like to make?

6 THE WITNESS: No, sir, not at this time.

7 CHAIRMAN OMAS: Counsel, would you please
8 provide two copies of the corrected designated written
9 cross-examination of Witness Siwek to the reporter?

10 That material is received into evidence and
11 is to be transcribed into the record.

12 (The document referred to was
13 marked for identification as
14 Exhibit No. NNA-T-3 and was
15 received in evidence.)

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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Postal Rate and **Fee** Changes, 2006

Docket No. R2006-1

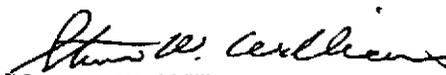
DESIGNATION OF WRITTEN CROSS-EXAMINATION
OF NATIONAL NEWSPAPER ASSOCIATION
WITNESS STEPHEN E. SiWEK
(NNA-T-3)

Interrogatories

United States Postal Service

USPS/NNA-T3-1, 3-14, 16-22, 24-29

Respectfully submitted,



Steven W. Williams
Secretary

INTERROGATORY RESPONSES OF
NATIONAL NEWSPAPER ASSOCIATION
WITNESS STEPHEN E. SIWEK (T-3)
DESIGNATED AS WRITTEN CROSS-EXAMINATION

Interrogatory

Designating Parties

USPS/NNA-T3-1	USPS
USPS/NNA-T3-3	USPS
USPS/NNA-T3-4	USPS
USPS/NNA-T3-5	USPS
USPS/NNA-T3-6	USPS
USPS/NNA-T3-7	USPS
USPS/NNA-T3-8	USPS
USPS/NNA-T3-9	USPS
USPS/NNA-T3-10	USPS
USPS/NNA-T3-11	USPS
USPS/NNA-T3-12	USPS
USPS/NNA-T3-13	USPS
USPS/NNA-T3-14	USPS
USPS/NNA-T3-16	USPS
USPS/NNA-T3-17	USPS
USPS/NNA-T3-18	USPS
USPS/NNA-T3-19	USPS
USPS/NNA-T3-20	USPS
USPS/NNA-T3-21	USPS
USPS/NNA-T3-22	USPS
USPS/NNA-T3-24	USPS
USPS/NNA-T3-25	USPS
USPS/NNA-T3-26	USPS
USPS/NNA-T3-27	USPS
USPS/NNA-T3-28	USPS
USPS/NNA-T3-29	USPS

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-1. Please refer to your testimony at page 4, lines 2-3. You state, "Absent a known extraordinary event, cost increases of this magnitude, occurring within so limited a time frame are simply not believable."

- a. Do you consider the IOCS redesign, which you mention at lines 13-14 on the same page, to be a "known extraordinary event"?
- b. Did you consider the possibility that the change of the IOCS instrument could contribute to the increase in measured costs? If not, why not?

RESPONSE:

- a. No. In this statement, I meant a known and extraordinary event that was external to the cost measurement systems of the **USPS** and that actually increased postal costs. The IOCS redesign itself would not increase actual postal costs for a given subclass.
- b. Yes, I considered the possibility that the change of the IOCS instrument could contribute to the increase in measured costs.

RESPONSE ~~OF~~ NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-3. Please refer to your testimony, section VIII(d), p. 16, where you state "... a margin of error equal to only 3% is generally used in surveys where a 95% confidence interval is measured." and in footnote 3 quote Dr. Lohr "For many surveys of people in which a proportion is measured, $e = 0.03$ and $\alpha=0.05$;" also refer to your testimony at page 17, lines 18-19. Please also refer to USPS-T-1 at pages 14-15.

- a. Please confirm that, based on Postal Service methods, Within-County Periodicals constitute 0.156 percent of mail processing volume-variable costs reported in Dr. Czigler's Table 1. If you do not confirm, please explain.
- b. Please confirm that, based on Postal Service methods, Within-County Periodicals constitute 0.303 percent of city carrier in-office volume-variable costs reported in Dr. Czigler's Table 2. If you do not confirm, please explain.
- c. Do you believe that in her textbook Dr. Lohr referred to estimates of proportions of the magnitudes of the Within-County cost proportions from parts a and b?
- d. Do you propose that the CV for the costs of the Within-County Periodicals subclass should be about 1.5 percent, so that the confidence interval about the point estimate is ± 3 percent?
- e. If in part (d) you do not agree the CV should be no greater than 1.5 percent. what do you recommend as the maximum value for the CV for estimate of costs of Within-County Periodicals?
- f. Do you agree that the CVs of the pooled estimates you propose on page 17 (8.81 percent for mail processing, 9.13 percent for city carrier), which require two full years of data, are much greater than 1.5 percent? If you do not agree, please explain fully.
- g. Are the CVs of the pooled estimates you propose less than the maximum CV value you recommend in part(e)?
- h. Do you propose that the cost estimates for all subcategories of mail measured by the IOCS, no matter how small, should have a CV no greater than the value you recommend in part (e)?

RESPONSE:

- a. Confirmed.
- b. Confirmed.
- c. In this context, I did not find any reference to magnitudes of proportions in Dr. Lohr's textbook. Absent such a reference, I have no basis upon which to speculate as to what magnitudes she may have been referring to.
- d. No
- e. I do not recommend a "maximum" value for the CV for estimate of costs of Within-County Periodicals.

- f. Yes, I agree the CVs for the pooled estimates are still much greater than 1.5%, but they are noticeably lower than reported in Mr. Czigler's Table 1 and Table 2.
- g. See my response to Part (e) above.
- h. See my response to Part (e) above.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-4. Please refer to your testimony at page 5, lines 9-10.

a. Please confirm that the entire sentence from which you quoted is "Within-County Periodicals were not studied separate from Outside-County Periodicals in the beta test because the test would not be expected to produce sufficient Within-County tallies to support statistical inference."

b. Do you disagree with Dr. Bozo's conclusion that the expected sample of Within-County Periodicals pieces from the Postal Service study would be too small to 'support statistical inference'? Explain the basis for any disagreement.

c. In your opinion, how many observations of Within-County Periodicals pieces would be needed to validate the Postal Service procedures?

d. Assume the pre-deployment tests of the redesigned IOCS data collection instrument had been expanded to produce sufficient observations of Within-County Periodicals by the standard of your response to part (c). Would the additional costs of the expanded tests be borne by Within-County Periodicals?

Please explain completely any answer other than a simple affirmative.

RESPONSE:

a. Confirmed.

b. I have not attempted to evaluate whether Dr. Bozo's conclusions regarding statistical inference in this context were or were not correct. My point was that these studies were simply not done for Within-County Periodicals.

c. Analysis as well as new observations would likely be needed to "validate" the Postal Service's procedures in this context. I have not attempted to assess whether and to what extent a specific number of new observations would be needed. However, as noted above, the Postal Service analyzed no observations for Within County Periodicals in its beta tests.

d. If you mean that the pre-deployment costs should be borne fully by Within-County Periodicals, the answer is No, The Within-County Periodicals subclass now bears a disproportionate risk that it is paying excessive postal rates because the Within-County CV's are so high relative to other subclasses. If the USPS were to reduce this risk by improving Within-County CV's and, at the same time: impose additional cost burdens solely on the Within-County Periodicals subclass, Within County mailers would have simply traded one form of unequal treatment for another. For the reason, any new study costs should not be borne entirely by the Within County subclass.

If **you** mean that these pre-deployment costs should be shared among the Within County subclass and other mail classes, I would not object in principle to such a policy.

RESPONSE OF NNA WITNESS SIWEK TC INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-5.

- a. Please confirm that the Within-County piece rates are less than Outside-County piece rates by percentages ranging from 64% to 85%. and that Outside-County piece rates are higher than Within-County piece rates by factors of 2.74 to 6.8. If you **do** not confirm, please provide the correct ranges **of** differences.
- b. Do you agree that the Periodicals rate structure provides publishers with a price incentive to mail eligible pieces at the lower Within-County rates rather than higher Outside-County rates? Please explain any negative answer.
- c. Please describe any circumstances known **to** you where a Periodicals piece is eligible to claim a Within-County rate but nevertheless was mailed at an Outside-County rate. Explain each circumstance fully, in particular the frequency with which such situations occur in the real world.

RESPONSE:

- a. I have not attempted to systematically compare Within-County piece rates with Outside County piece rates in my testimony or since it was filed.
- b. I believe that such an incentive exists **for** eligible pieces but I have not attempted to confirm its existence.
- c. I personally know of no such circumstances, but I cannot speak for other **NNA** witnesses. The concerns that I raise in **my** testimony center on a somewhat different circumstance, namely one in which a mailer actually paid Outside County rates on **a** mail piece that appeared to the USPS to be eligible for Within-County rates but was not.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-6. Please refer to your testimony, where on p. 8 you state, 'Mr. Heath also points out that in a costing environment **for** a lower volume subclass like Within-County Periodicals, 'small errors loom large.'" Also, please also refer to Dr. Czigler's response to NNA/USPS-T1-16 (Tr. 10/2402).

- a. Do you agree that the Postal Service analysis produced 193 direct tallies for Within-County Periodicals in FY2005? Please explain any disagreement.
- b. Do you agree that an error in one tally would **affect** the estimated costs of Within-County Periodicals on average by less than 1 percent—i.e., approximately 1/193? If not, please explain.
- c. Please identify which of the 193 Within-County tallies in the Postal Service's dataset you would propose to recode as Outside-County Periodicals. Please describe all **criteria** you would apply for the purpose, and explain why you believe your classification to be more accurate than the Postal Service's.

RESPONSE:

- a. It is my understanding that 193 direct tallies were ultimately used for Within-County Periodicals in FY2005.
- b. No. It is my understanding that the **193** direct tallies relate specifically to Clerks and Mail Handlers Mail Processing costs and to City Carrier In-Office costs. An error in one of these tallies would affect these cost segments directly and other cost segments indirectly through the USPS' cost allocation process. However, I do not believe that all of Within-County costs would fall by approximately 1/193.
- c. I don't propose to recode any specific Within-County tallies in the case since, like the USPS, I do not possess all the data required to assess these tallies accurately. Rather, as noted in my Direct Testimony, I propose either that the Commission reject the USPS' proposed rate increase for Within County Periodicals in its entirety or in the alternative, that the Commission accept my recommendations for cost adjustments and significantly reduce the proposed Within-County rate.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-7. Please refer to your testimony at page **6**, lines **4-6**. You state:
By choosing to ignore actual postage payments and to focus only on eligibility, the USPS has introduced the possibility that the Within-County pieces that it analyzed were eligible for Within-County rates but were not assessed postage at those preferred rates.

a. Please confirm that if a mailer indicates pieces at Within-County rates on a mailing statement, the mailer has actually paid Within-County rates for those pieces. If **you** do not confirm, please explain.

b. If a mailer indicates Within-County pieces on a mailing statement, is it appropriate to infer that the mailer was eligible to claim Within-County rates for those pieces? If not, why not?

c. Please also refer to Dr. Czigler's response to **NNA/USPS-T1-17 (Tr. 10/2403)**, where Dr. Czigler states, "The count of 129 [tallies]... is the number of tallies identified by the **recode.f** program where **PostalOne!** reported a positive volume at Within-County rates in the same county as the destination of the periodical."

(i) Please confirm that for a majority of the Within-County Periodicals tallies, the Postal Service determined that the mailers had, in fact, actually paid Within-County rates. If you do not confirm, please explain.

(ii) Please reconcile your claim that the Postal Service "**choos[es]** to ignore actual postage payments" with Dr. Czigler's statement.

RESPONSE:

a. Confirmed.

b. Yes.

c. I cannot confirm this statement. As I understand the Postal Service's procedure, if, after the **recode.f** processing has been completed and if the origination and destination county of a particular tally match, the Postal Service considers whether the publication has recorded 2005 volumes at Within-County Periodicals rates in the Postal One system at the **office** where the tally was recorded. If such volumes were recorded in the Postal One system during the first 11 months of 2005, the Postal Service concludes that it has verified the tally. However, as I understand this procedure, the Postal Service does not determine whether the actual tallied piece was included within the Postal One Within County volume for that publication. As noted both in my testimony and in the testimony of NNA witness Heath, there are a number of **circumstances** in which a publication whose origin and destination counties are the same would still not qualify for



Within County rates. The *Postal One* procedure cited in this question does nothing to solve those problems since it does not capture the actual postage paid by each tallied piece.



RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-8. Please refer to your testimony at page 6, lines 14-19, where you criticize the Postal Service analysis for not assessing Within-County rate eligibility on an issue-by-issue basis. Please provide any quantitative information you have on the extent to which eligibility for Within-County Periodicals rates actually varies from issue-to-issue for titles that claim Within-County rates at some point during a year.

RESPONSE:

Like the USPS, I have no data on the extent to which eligibility for Within County rates varies from issue-to-issue for titles that claim Within-County rates at some point during the year. I do note that in the June 2002 issue of the USPS' Handbook for Applying for Periodicals Mailing Privileges (Handbook DM-204), at Appendix B, the Postal Service includes the following: "**NOTE:** In-County rate eligibility is determined on an **issue-by-issue** basis and remain subject to your total paid distribution. Changes in paid circulation can affect In-County rate eligibility. Make **copies** of this worksheet and **use it regularly** to determine whether your publication remains eligible for IN-County rates." (Emphasis Added).

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-9. Please refer to your testimony at page 7, lines 3-13.

- a. Please explain your understanding of the number of Within-County tallies where the classification was made on the basis of circulation figures obtained from publication directories.
- b. Please explain in detail your understanding of the **extent** to which the circulation of the affected titles fluctuates over time.
- c. Do you have more current circulation figures for any of the tallies listed in **USPSLR-L-9**, file 'hand2005.xls' that were classified as Within-County Periodicals based on circulation figures obtained from publication directories? If so, please provide the more current figures and describe your **source(s)** in detail.
- d. Are there other sources you would consider to be authoritative on the question of the circulation of Periodicals publications?

RESPONSE:

- a. As I understand it, the USPS uses **publication** directories **to** support its assumption that a given tally was eligible for Within-County Periodical rates as part of its manual checking process. Directories are used **to** determine a publication's circulation if other manual checks have failed to generate a definitive subclass.
- b. I have no data on the extent to which circulation figures for these 'affected' publications varies over time but neither, I believe, **does** the USPS. According **to** USPS witness Bozo, the exact date of the circulations taken from these directories was not determined. In addition, the USPS only appears to have recorded from the directories **a** single circulation value for each publication. See Response of USPS witness **Bozzo** (USPS-T46-24) to NNA/USPS-T46-24.
- c. No. I do not have more current circulation figures for any of these publications.
- d. If you mean total circulation, I would imagine that more recent directories would provide more timely data on total circulations than the directories used by the USPS in this case. In addition, I would imagine that the publishers of each publication possess recent data on total circulations.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-10. Please refer to your testimony at page 7, line 19 to page 8, line 3. Please describe in detail the basis (e.g., DMM references) for your claim that the Postal Service "limits the time period during which Periodicals sent to such late-paying subscribers could actually qualify for Within-County rates."

RESPONSE:

My understanding from NNA witness Max Heath is that the relevant reference is DMM 707.7.6. A typographical error appeared in witness Heath's testimony. An erratum is being filed to correct the citation from DMM 708.7.6 to DMM 707.7.6.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-11. Please refer to your testimony at page 8, line 20-21. You state, "For Within-County Periodicals, the Postal **Service** assumes that original entry and destination counties should be the same."

a. Please confirm that this is a requirement for Within-County rate eligibility. If you do not confirm, please explain.

b. Please confirm that for each tally whose original entry and destination county match, the Postal Service subjected that tally to additional scrutiny to confirm its status as Within-County.

RESPONSE:

- a. Confirmed.
- b. Confirmed.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-12. Please refer to your testimony at page 9, lines 5-9. Please also refer to USPS-LR-L-9, file 'hand2005.xls.'

- a. Please explain your understanding of the number of Within-County tallies classified on the basis of prior years' identifications.
- b. For each of the affected tallies, do you have evidence that the publications had not been eligible to claim Within-County rates in FY 2005? If so, please describe it in detail.

RESPONSE:

- a. As referenced in f/n 19 of my Direct Testimony, in USPS-LR-L-9, at Appendix D, page D-3, the USPS describes its manual checking process for IOCS Periodicals tallies. As part of this process, the USPS stated that 174 out of 7,671 Periodicals tallies required manual checks. Among the manually reviewed tallies, the USPS considered tallies where the original entry or destination county could not be determined. For these tallies, the USPS states "Third, if a publication was mailed at Within-County Periodicals rates at least once in the previous two years, it is assumed that it is still eligible to mail at Within County Periodicals rates."
- b. I have not attempted to determine whether the individual tallies sampled by the USPS from publications that were classified by the USPS as being eligible for Within County rates on the basis of prior years' identifications had actually come from publications that were no longer eligible in FY 2005. I would note that even if such publications remained eligible for Within County rates, such eligibility need not extend to the individual tally at issue.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-13. Please refer to your testimony at page 9, lines **14-21**.

a. Is it your testimony that the Gonzales Tribune does not claim Within-County rates for pieces it mails to addresses in Sonoma County, CA? If so, please provide all evidence to support your claim.

b. Please confirm that the Gonzales Tribune tally is the only tally subject to the "local appeal" criterion in FY 2005. If you do not confirm, please explain.

RESPONSE:

a. No.

b. I cannot confirm this statement. I have not attempted to determine the number of tallies that were classified on the *basis* of the "local appeal" criterion in FY 2005.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-14. Please refer to your testimony, page 10. You state, "Since the Postal Service has not identified actual Within-County Periodicals in its cost studies, it has not measured the actual costs of Within-County Periodicals for use in this proceeding."

- a. Would you recommend, for instance, that every copy of a Periodical actually mailed at Within-County rates have identifying markings, which would enable data collectors to directly identify Periodical copies that were actually mailed at Within-County rates?
- b. Would you recommend a special study focused specifically on the costs of Within-County Periodicals?
- c. If your answer to part (b) is yes, do you agree that the costs for such a study should be attributed to Within-County Periodicals?

RESPONSE:

- a. I do not make such a recommendation in this case.
- b. I believe that the USPS study entitled "IOCS Periodicals Tally Edits" that is described in Appendix D of USPS-LR-L-9 already attempts to address the costs of Within County and Outside County Periodicals. I also believe that a study of this basic topic will likely be needed in the future.
- c. I believe that the costs of such a study should not be borne solely by Within County Periodicals but that these costs might be shared among the Within-County subclass and other mail classes.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-16. Please refer to your testimony, section VIII d), p. 17, where you quote "If it is desired that the sample contain a certain number of members from the rare population, the initial sample could be used to obtain a preliminary estimate of prevalence, and that estimate of prevalence is used to estimate the necessary size of the second sample."

- a. Please confirm that it is Within-County Periodicals that are the rare members that you wish to sample. Please explain if you do not confirm.
- b. What is the number of rare Within-County Periodicals that in your judgment should be obtained in the second sample? Please justify your response.
- c. Please refer to USPS-LR-L-9, page 10, Table 3. Do you agree that there were **725,184** readings taken by the IOCS in FY2005?
- d. Please estimate the number of IOCS readings that would need to be taken in the second sample in order to obtain your desired number of readings with Within-County Periodicals.

RESPONSE:

- a. Yes.
- b. I have not estimated such a number.
- c. Agreed based on page 10 of USPS-LR-L-9_R2006-1_IOCS.pdf.
- d. I have not estimated such a number.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-17. Please refer to your testimony, section VIII(d) where you state, "Effectively, my cost estimates are based on a pooled sample combining the Shaw sample and the Czigler sample."

- a. Do you believe that it is valid to pool data from two distinct populations to obtain a pooled estimate when those populations are significantly different from each other? If so, please provide justification from a standard statistics reference that supports your opinion.
- b. Do you agree that FY2005 estimated costs should reflect the FY2005 population of mail processed by FY2005 Postal Service operations? If not, why not?
- c. Please refer to Dr. Bozzo's testimony, USPS-T-46, section IV.C.I. p. 35. Do you accept Dr. Bozzo's statement that "The Within-County increase appears to have resulted from new methods to facilitate identification of Periodicals in the redesigned Question 23?" If not, please explain in detail the basis for disagreement.
- d. Do you agree that if Dr. Bozzo's statement quoted in part (d) is true (whether or not you agree with it), it implies that the costs for Within-County Periodicals were understated in FY2004?

RESPONSE:

- a. No.
- b. Ideally FY2005 estimated costs should reflect the FY2005 population of mail processed by FY2005 Postal Service operations.
- c. Yes, new methods to facilitate identification of Periodicals in the redesigned Question 23 could be one of the reasons that *contributed* to the increase in the Within-County cost estimates.
- d. No. Costs for Within-County Periodicals were not necessarily understated in FY2004. Dr. Bozzo's statement implies only that the new estimates of Within County costs based on the Postal Service's new methods were higher than previous estimates that were based on prior methods

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-18. Please confirm that, while the pound rates you propose in Appendix D to your testimony (at *I0*), increase current Within-County rates by less than 4 percent, all of the piece rates in your proposal (other than Ride-Along) would increase current rates by more than 30 percent, and that the piece rates for Basic Automation Flats, Basic Automation Letters, 3-Digit Automation Flats, 5-Digit Automation Flats, and 5-Digit Automation Letters would increase **by** more than **80** percent. If you do not confirm, please explain why not.

RESPONSE:

a. Confirmed. My rate proposal for Within County Periodicals shifts revenue recovery from pound rates to piece rates. For this reason, as compared with the USPS proposal, my proposed rate design increases the revenue to be recovered from piece rates and reduces the revenue to be recovered **by** pound rates. Note however that my rate design proposal also maintains the same level of overall revenue recovery from the Within County subclass as that proposed **by** the USPS in this case.

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-19. In section VII(b) of your testimony you appear to recognize that comparisons between IOCS costs presented by witness Shaw in Docket No. R2005-1 and by witness Czigler in Docket No. R2006-1 present some difficulties (although they are for respective base years 2004 and 2005 – not 2005 and 2006 as you state in your analysis). Do you agree with this characterization?

- a. ~~Is~~ one difficulty the fact that different IOCS instruments were used to generate the respective cost estimates?
- b. Please provide justification from authoritative sources for your applying confidence intervals developed by witness Shaw for FY 2004 to estimates for FY 2005 using a revised instrument.

RESPONSE:

Yes.

- a. Yes.
- b. I did not simply apply confidence intervals developed by **witness** Shaw for **FY** 2004 to estimates for FY 2005. I made adjustments to the confidence intervals to reflect the increase in total cost estimates between the two years. See my Tables **1A** and **1B**.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS SIWEK TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-20. On page 4 of your testimony, lines 4-6, you claim that apparent cost increases for Within County "far more likely ... result from .. deficiencies" in Postal Service "processes and data used... [for] the Within County Periodical [sic] subclass." Please refer to library references R2005-1/LR-K-9, Appendix D and R2006-1/LR-L-9, Appendix D.

- a. Are you claiming that between BY2004 and BY2005 the Postal Service changed any of the processes specifically applicable to Within-County Periodicals, as opposed to general IOCS changes affecting all Periodicals?
- b. If your answer to part (a) is affirmative, please explain in detail what changes you believe were made, and please provide citations to USPS-LR-K-9, Appendix D, and USPS-LR-L-9, Appendix D, to support your claims.
- c. If your answer to part (a) is negative, please explain how you believe processes that did not change between BY 2004 and BY 2005 can account for the measured cost increase.

RESPONSE

a. **No.** I have not tried to distinguish changes in the **IOCS** processes that were "specifically applicable" to Within-County Periodicals from "general IOCS changes" affecting all Periodicals.

b. See my response to (a) above.

c. The processes that affected all Periodicals did change and those changes appear to have contributed to the dramatic cost increases for the Within County subclass that are claimed by the Postal Service in this case. For one example of how these changes might have affected the Within County subclass, I note that at lines 7-8 of page 35 of Mr. *Bono's* Direct Testimony (USPS-T-46), Mr. *Bono* states "The Within-County increase appears to have resulted from new methods to facilitate identification of Periodicals in the redesigned Question 23."

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS SIWEK TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-21. Please refer *to* your response to **USPS/NNA-T3-9(a)**, which asks for your understanding of a number of tallies rather than a description of how circulation information is used to assign subclass. How many of the 193 direct tallies were assigned to the Within-County Periodicals subclass based on circulation figures obtained from publication directories?

RESPONSE:

In his response to **NNA/USPS-T46-24**, USPS witness Bozo stated that "Titles for which circulation counts were collected, the circulation count and the edited activity code are listed in the table below. An exact date of the circulations cannot be determined, but the most recent editions (2005) of the publication directories cited in **USPS-LR-L-9** were used to determine circulation." By my count, the list provided in this response included 35 different publications whose circulations were determined on the basis of the publication directories cited in **USPS-LR-L-9**. Of this total, there were 22 publications that were ultimately given an edited 2211 (Within County) activity code and 13 publications that were ultimately given an edited 2212 (Outside County) activity code.

I believe that the USPS did not use the circulations reported above as the sole basis upon which to assign each of the publications to a Periodical subclass. For example, in the response cited above, the USPS collected circulation data for the Gonzales Tribune from the publications directories that it listed in **USPS-LR-L-9**. The reported circulation for the Gonzales Tribune was 13,000, While this total exceeds the 10,000 circulation threshold for Within County publications, it is certainly far below, say 200,000. Nevertheless, in his response to **NNA/USPS-T46-26**, Mr. Bozzo stated that the Gonzales Tribune was classified as a Within County publication "based on the assumed local appeal of a community newspaper." (Emphasis Added). In this circumstance are we therefore *to* assume that the circulation data that the USPS compiled on this publication had nothing to do with the USPS' assumption that the publication had local appeal? Suppose the circulation of the Gonzales Tribune were 200,000. In that Circumstance, would the USPS still assume that the publication had local appeal?

Given the sequential nature of the USPS tally editing process and the data that I have reviewed, I cannot report how many of the 193 direct tallies that were ultimately

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS SIWEK TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

assigned to the Within County subclass were assigned there "based on" the publication directory circulation figures or for another reason or perhaps for more than one reason.

RESPONSES OF NATIONAL NEWSPAPER ASSOCIATION WITNESS SIWEK TO
INTERROGATORIES OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-22. Please refer to your response to USPS/NNA-T3-12(a), which asks for your understanding of a number of tallies rather than a description of how historical data is used to assign subclass. How many of the 193 direct tallies were assigned to the Within-County Periodicals subclass based on prior years' identifications?

RESPONSE:

Based on the data that I have reviewed, I cannot report how many of the **193** direct tallies that were ultimately assigned to the Within County subclass were assumed to be eligible to mail at Within-County Periodicals rates "based on" whether the publication had been mailed at Within-County Periodicals rates at least once in the previous **two** years.

**RESPONSE OF NATIONAL NEWSPAPER ASSOCIATION WITNESS STEVE
SIWEK TO INTERROGATORY OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T3-24. Please refer to Appendix D of your testimony.

(a) Please confirm that USPS-LR-L-126 was revised on July 13, 2006, and August 8, 2006, prior to its receipt into evidence. If you do not confirm, please explain.

(b) Please confirm that Appendix D does not reflect the revisions to the "TYAR B.D.", "Rate Design Input" and "Piece Discounts 2" worksheets in USPS-LR-L-126 that were filed on July 13, 2006. If you do not confirm, please explain.

(c) If you confirm part (a), and putting aside Appendix D's increase of the proportion of revenue derived from the piece side on pages 4 and 8 and increase of the passthroughs for carrier route basic and high density on pages 6 and 9, was Appendix D's failure to reflect the revisions to USPSLR-L-126 intentional? If it was intentional, please explain.

(d) If it was not intentional, please provide an updated version of Appendix D incorporating the revisions that were made to USPS-LR-L-126 where appropriate.

RESPONSE:

(a).Confirmed

(b).Confirmed

(c).No. It was not my intention to omit the USPS' revisions to USPS-LR-L-126.

(d) See enclosed "Appendix D Revised (October 18, 2006)."

TYAR BILLING DETERMINANTS - AFTER RATES VOLUME & REVENUES WITHIN COUNTY PERIODICALS			
Pounds	TY AR Pounds	Proposed Rates	Postage (Rate*Pounds)
Delivery Unit - Pound Rate	105,321,546	\$ 0.142	\$ 14,955,660
General - Pound Rate	126,766,452	\$ 0.179	\$ 22,691,195
Presort Rate Pieces	TY AR Pieces	Proposed Rates	Postage (Rate*Pieces)
BASIC NON-AUTOMATION	15,294,097	\$ 0.117	\$ 1,789,409
BASIC AUTOMATION LETTER	497,774	\$ 0.057	\$ 28,373
BASIC AUTOMATION FLAT	902,094	\$ 0.108	\$ 97,426
3-DIGIT NON-AUTOMATION	15,339,480	\$ 0.108	\$ 1,656,664
3-DIGIT AUTOMATION LETTER	4,004,446	\$ 0.050	\$ 200,222
3-DIGIT AUTOMATION FLAT	3,533,813	\$ 0.097	\$ 342,780
5-DIGIT NON-AUTOMATION	68,412,119	\$ 0.098	\$ 6,704,388
5-DIGIT AUTOMATION LETTER	3,910,481	\$ 0.051	\$ 199,435
5-DIGIT AUTOMATION FLAT	41,099,272	\$ 0.093	\$ 3,822,232
CARRIER ROUTE BASIC	404,946,190	\$ 0.060	\$ 24,296,771
CARRIER ROUTE HIGH DENSITY	108,177,430	\$ 0.044	\$ 4,759,807
CARRIER ROUTE SATURATION	34,022,501	\$ 0.032	\$ 1,088,720
WKSHARING DISCNTDELIVERY OFFICE ENTRY	258,307,013	\$ (0.008)	\$ (2,066,456)
Total Pieces & Calculated Revenue	700,139,698		\$ 80,566,626
Ride-along Pieces	597,775	0.155	\$ 92,655
Adjusted Total Revenue including Ride-along			\$ 80,687,773
TYAR Fees			\$ 1,666,370
Calculated Revenue+TYAR Fees			\$ 82,354,143
TYAR Cost			\$ 79,513,462
Cost Coverage after calculation of new rates			103.6%
Revenue per piece			\$ 0.118

APPENDIX D, Revised Page 2 of 10

Inputs to Within County Rates Development

Line #	Item	Amount	Source / Notes
5	TY Before Rates Volume	722,431,237	USPS-LR-L-63, Witness Thress
6	TY After Rates Volume	853,535,270	USPS-LR-L-63, Witness Thress
7	TYBR Cost, Without Contingency	81,056,095	USPS-LR-L-7, Witness Waterbury
8	TYAR Cost, Without Contingency	78,726,200	USPS-LR-L-7, Witness Waterbury
9	Contingency Factor	101%	USPS-T-10, Witness Waterbury
10	TYBR Cost, (Including Contingency)	\$ 81,868,658	Calculated (Line 7*Line 9)
11	TYAR Cost, (Including Contingency)	\$ 79,513,482	Calculated (Line 8*Line9)
12	Desired Cost Coverage	103.70%	One-Half of Initial Cost Coverage for Outside County
13	TYBR Fees	\$ 1,650,649	USPS-T-39, Witness Berkeley
14	TYAR Fees	\$ 1,666,370	USPS-T-39, Witness Berkeley
15	Proportion of Revenue From Piece Rates	53.5%	Assumption
16	MULTIPLIER TO GET ACTUAL REVENUE	100.035%	Base Year Worksheet
17	Transportation Cost, Without Contingency	95,825	USPS-LR-L-7, Witness Waterbury
18	Transportation Cost, With Contingency	\$ 97,592	Calculated (Line 17*Line 9)
19	Proportion of Transportation Cost That is Distance Related	0.5946	USPS-LR-L-39, Witness Ke
20	Distance Related Transportation Cost	\$ 58,028	Calculated (Line 18*Line 19)

CALCULATION OF PIECE DISCOUNTS, SHEET 2

Line #

3	Presort Level	Unit Cost Savings (From Discounts W/S)	Passthrough
5	BASIC NONAUTOMATION	\$ -	(Benchmark unit cost)
6	BASIC AUTOMATION LETTER	\$ 0.296	20.2%
7	BASIC AUTOMATION FLAT	\$ 0.013	70%
8	3 DIGIT NONAUTOMATION	\$ 0.073	12%
9	3 DIGIT AUTOMATION LETTER	\$ 0.304	19%
10	3 DIGIT AUTOMATION FLAT	\$ 0.012	86%
11	5 DIGIT NONAUTOMATION	\$ 0.081	12%
12	5-DIGIT AUTOMATION LETTER	\$ 0.315	15%
13	5 DIGIT AUTOMATION FLAT	\$ 0.003	166%
14	CARRIER ROUTE	\$ 0.066	58%
15	HIGH DENSITY	\$ 0.024	65%
16	SATURATION	\$ 0.043	64%
17	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 0.0138	55%
18		Final Unit Cost Savings	Notes
19	BASIC NONAUTOMATION	\$ -	
20	BASIC AUTOMATION LETTER	\$ 0.060	Passthroughs Times Unit Cost Savings
21	BASIC AUTOMATION FLAT	\$ 0.009	Passthroughs Times Unit Cost Savings
22	3 DIGIT NONAUTOMATION	\$ 0.009	Passthroughs Times Unit Cost Savings
23	3 DIGIT AUTOMATION LETTER	\$ 0.058	Passthroughs Times Unit Cost Savings
24	3 DIGIT AUTOMATION FLAT	\$ 0.011	Passthroughs Times Unit Cost Savings
25	5 DIGIT NONAUTOMATION	\$ 0.010	Passthroughs Times Unit Cost Savings
26	5-DIGIT AUTOMATION LETTER	\$ 0.047	Passthroughs Times Unit Cost Savings
27	5 DIGIT AUTOMATION FLAT	\$ 0.005	Passthroughs Times Unit Cost Savings
28	CARRIER ROUTE	\$ 0.038	Passthroughs Times Unit Cost Savings
29	HIGH DENSITY	\$ 0.016	Passthroughs Times Unit Cost Savings
30	SATURATION	\$ 0.028	Passthroughs Times Unit Cost Savings
31	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 0.008	Passthroughs Times Unit Cost Savings
32		TY BR Leakage	Notes
33	BASIC NONAUTOMATION	\$ -	
34	BASIC AUTOMATION LETTER	\$ 30,817	Final Discount times Volume
35	BASIC AUTOMATION FLAT	\$ 8,377	Final Discount times Volume
36	3 DIGIT NONAUTOMATION	\$ 212,455	Final Discount times Volume
37	3 DIGIT AUTOMATION LETTER	\$ 239,653	Final Discount times Volume
38	3 DIGIT AUTOMATION FLAT	\$ 40,110	Final Discount times Volume
39	5 DIGIT NONAUTOMATION	\$ 2,223,628	Final Discount times Volume
40	5-DIGIT AUTOMATION LETTER	\$ 189,644	Final Discount times Volume
41	5 DIGIT AUTOMATION FLAT	\$ 212,039	Final Discount times Volume
42	CARRIER ROUTE	\$ 32,180,293	Final Discount times Volume
43	HIGH DENSITY	\$ 1,785,947	Final Discount times Volume
44	SATURATION	\$ 982,961	Final Discount times Volume
45	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 2,132,249	Final Discount times Volume
46	Total Discount Leakage	\$ 40,238,173	Sum Line 33-45
47	Revenue Required from Pieces + Discount Leakages	\$ 84,706,940	Line 46 plus Line 4 from Piece Discounts
48	TYBR Pieces	722,431,237	
49	Revenue Requirement + Leakage Per Piece (Base Rate)	\$ 0.117	Line 47/Line 48

Inputs to Within County Rates Development

Line #	Item	Amount	Source / Notes
5	TY Before Rates Volume	722,431,237	USPS-LR-L-63, Witness Thress
6	TY After Rates Volume	853,535,270	USPS-LR-L-63, Witness Thress
7	TYBR Cost, Without Contingency	81,056,095	USPS-LR-L-7, Witness Waterbury
8	TYAR Cost, Without Contingency	78,726,200	USPS-LR-L-7, Witness Waterbury
9	Contingency Factor	101%	USPS-T-10, Witness Waterbury
10	TYBR Cost, (Including Contingency)	\$ 81,866,656	Calculated (Line 7*Line 9)
11	TYAR Cost, (Including Contingency)	\$ 79,513,462	Calculated (Line 8*Line9)
12	Desired Cost Coverage	103.70%	One-Half of Initial Cost Coverage for Outside County
13	TYBR Fees	\$ 1,650,649	USPS-T-39, Witness Berkeley
14	TYAR Fees	\$ 1,666,370	USPS-T-39, Witness Berkeley
15	Proportion of Revenue From Piece Rates	62.5%	Assumption
16	MULTIPLIER TO GET ACTUAL REVENUE	100.035%	Base Year Worksheet
17	Transportation Cost, Without Contingency	96,625	USPS-LR-L-7, Witness Waterbury
18	Transportation Cost, With Contingency	\$ 97,592	Calculated (Line 17*Line 9)
19	Proportion of Transportation Cost That is Distance Related	0.5546	USPS-LR-L-39, Witness Kelly
20	Distance Related Transportation Cost	\$ 58,028	Calculated (Line 18*Line 19)

N A R BILLING DETERMINANTS - AFTER RATES VOLUME & REVENUES WITHIN COUNTY PERIODICALS			
Pounds	TYAR Pounds	Proposed Rates	Postage (Rate*Pounds)
Delivery Unit - Pound Rate	105,321,548	\$ 0.109	\$ 11,480,049
General - Pound Rate	126,766,452	\$ 0.146	\$ 18,507,902
Presort Rate Pieces	WAR Pieces	Proposed Rates	Postage (Rate*Pieces)
BASIC NON-AUTOMATION	15,294,097	\$ 0.128	\$ 1,957,644
BASIC AUTOMATION LETTER	497,774	\$ 0.068	\$ 33,849
BASIC AUTOMATION FLAT	902,094	\$ 0.119	\$ 107,349
3-DIGIT NON-AUTOMATION	15,339,480	\$ 0.119	\$ 1,825,398
3-DIGIT AUTOMATION LETTER	4,004,446	\$ 0.061	\$ 244,271
3-DIGIT AUTOMATION FLAT	3,533,813	\$ 0.108	\$ 381,652
5-DIGIT NON-AUTOMATION	68,412,119	\$ 0.109	\$ 7,456,921
5-DIGIT AUTOMATION LETTER	3,910,481	\$ 0.062	\$ 242,450
5-DIGIT AUTOMATION FLAT	41,099,272	\$ 0.104	\$ 4,274,324
CARRIER ROUTE BASIC	404,946,190	\$ 0.071	\$ 28,751,179
CARRIER ROUTE HIGH DENSITY	108,177,430	\$ 0.055	\$ 5,949,759
CARRIER ROUTE SATURATION	34,022,501	\$ 0.043	\$ 1,462,968
WKSHARING DISCNTDELIVERY OFFICE ENTRY	258,307,013	\$ (0.008)	\$ (2,066,456)
Total Pieces & Calculated Revenue	700,139,698		\$ 80,609,259
Ride-along Pieces			
Adjusted Total Revenue including Ride-along			\$ 80,730,420
TYAR Fees			\$ 1,666,370
Calculated Revenue+TYAR Fees			\$ 82,396,790
NAR Cost			\$ 79,513,462
Cost Coverage after calculation of new rates			103.6%
Revenue per piece			\$ 0.118

CALCULATION OF PIECE DISCOUNTS, SHEET 2

Line #

3	Presort Level	Unit Cost Savings (From Discounts W/S)	Passthrough (Benchmark unit cost)
5	BASIC NONAUTOMATION	\$ -	
6	BASIC AUTOMATION LETTER	\$ 0.296	20.2%
7	BASIC AUTOMATION FLAT	\$ 0.013	70%
8	3 DIGIT NONAUTOMATION	\$ 0.073	12%
9	3 DIGIT AUTOMATION LETTER	\$ 0.304	19%
10	3 DIGIT AUTOMATION FLAT	\$ 0.012	86%
11	5 DIGIT NONAUTOMATION	\$ 0.081	12%
12	5-DIGIT AUTOMATION LETTER	\$ 0.315	15%
13	5 DIGIT AUTOMATION FLAT	\$ 0.003	166%
14	CARRIER ROUTE	\$ 0.066	100%
15	HIGH DENSITY	\$ 0.024	70%
16	SATURATION	\$ 0.043	64%
17	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 0.0138	55%
18		Final Unit Cost Savings	Notes
19	BASIC NONAUTOMATION	\$ -	
20	BASIC AUTOMATION LETTER	\$ 0.060	Passthroughs Times Unit Cost Savings
21	BASIC AUTOMATION FLAT	\$ 0.009	Passthroughs Times Unit Cost Savings
22	3 DIGIT NONAUTOMATION	\$ 0.009	Passthroughs Times Unit Cost Savings
23	3 DIGIT AUTOMATION LETTER	\$ 0.058	Passthroughs Times Unit Cost Savings
24	3 DIGIT AUTOMATION FLAT	\$ 0.011	Passthroughs Times Unit Cost Savings
25	5 DIGIT NONAUTOMATION	\$ 0.010	Passthroughs Times Unit Cost Savings
26	5-DIGIT AUTOMATION LETTER	\$ 0.047	Passthroughs Times Unit Cost Savings
27	5 DIGIT AUTOMATION FLAT	\$ 0.005	Passthroughs Times Unit Cost Savings
28	CARRIER ROUTE	\$ 0.066	Passthroughs Times Unit Cost Savings
29	HIGH DENSITY	\$ 0.017	Passthroughs Times Unit Cost Savings
30	SATURATION	\$ 0.028	Passthroughs Times Unit Cost Savings
31	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 0.008	Passthroughs Times Unit Cost Savings
32		TY BR Leakage	Notes
33	BASIC NONAUTOMATION	\$ -	
34	BASIC AUTOMATION LETTER	\$ 37,317	Final Discount times Volume
35	BASIC AUTOMATION FLAT	\$ 8,377	Final Discount times Volume
36	3 DIGIT NONAUTOMATION	\$ 212,455	Final Discount times Volume
37	3 DIGIT AUTOMATION LETTER	\$ 239,653	Final Discount times Volume
38	3 DIGIT AUTOMATION FLAT	\$ 40,110	Final Discount times Volume
39	5 DIGIT NONAUTOMATION	\$ 2,222,628	Final Discount times Volume
40	5-DIGIT AUTOMATION LETTER	\$ 189,644	Final Discount times Volume
41	5 DIGIT AUTOMATION FLAT	\$ 212,039	Final Discount times Volume
42	CARRIER ROUTE	\$ 47,988,156	Final Discount times Volume
43	HIGH DENSITY	\$ 1,897,568	Final Discount times Volume
44	SATURATION	\$ 982,961	Final Discount times Volume
45	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 2,132,249	Final Discount times Volume
46	Total Discount Leakage	\$ 56,157,658	Sum Line 33-45
47	Revenue Required from Pieces + Discount Leakages	\$ 100,626,425	Line 46 plus Line 4 from Piece Discounts
48	TYBR Pieces	722,431,237	
49	Revenue Requirement + Leakage Per Piece (Base Rate)	\$ 0.139	Line 47/Line 48

TYAR BILLING DETERMINANTS -AFTER RATES VOLUME & REVENUES WITHIN COUNTY PERIODICALS			
Pounds	TY AR Pounds	Proposed Rates	Postage (Rate*Pounds)
Delivery Unit - Pound Rate	105,321,546	\$ 0.142	\$ 14,955,660
General- Pound Rate	126,766,452	\$ 0.179	\$ 22,691,195
Presort Rate Pieces	TY AR Pieces	Proposed Rates	Postage (Rate*Pieces)
BASIC NON-AUTOMATION	15,294,097	I 0.139	\$ 2,125,880
BASIC AUTOMATION LETTER	497,774	\$ 0.079	\$ 39,324
BASIC AUTOMATION FLAT	902,094	\$ 0.130	\$ 117,272
3-DIGIT NON-AUTOMATION	15,339,480	\$ 0.130	\$ 1,994,132
3-DIGIT AUTOMATION LETTER	4,004,446	\$ 0.072	\$ 288,320
3-DIGIT AUTOMATION FLAT	3,533,813	\$ 0.119	\$ 420,524
5-DIGIT NON-AUTOMATION	68,412,119	\$ 0.120	\$ 8,209,454
5-DIGIT AUTOMATION LETTER	3,910,481	\$ 0.073	\$ 285,465
5-DIGIT AUTOMATION FLAT	41,099,272	\$ 0.115	\$ 4,726,416
CARRIER ROUTE BASIC	404,946,190	\$ 0.054	\$ 21,867,094
CARRIER ROUTE HIGH DENSITY	108,177,430	\$ 0.037	\$ 4,002,565
CARRIER ROUTE SATURATION	34,022,501	\$ 0.026	\$ 884,585
WKSHARING DISCNTDELIVERY OFFICE ENTRY	258,307,013	\$ (0.008)	\$ (2,066,456)
Total Pieces & Calculated Revenue	700,139,698		\$ 80,541,430
Adjusted Total Revenue including Ride-along			\$ 80,662,568
N A R Fees			\$ 1,666,370
Calculated Revenue+TYAR Fees			\$ 82,328,938
N A R Cost			\$ 79,513,462
Cost Coverage after calculation of new rates			103.5%
Revenue per piece			\$ 0.118

Inputs to Within County Rates Development

Line #	Item	Amount	Source / Notes
5	TY Before Rates Volume	722,431,237	USPS-LR-L-63, Witness Thress
6	TY After Rates Volume	853,535,270	USPS-LR-L-63, Witness Thress
7	TYBR Cost, Without Contingency	81,056,095	USPS-LR-L-7, Witness Waterbury
8	TYAR Cost, Without Contingency	78,726,200	USPS-LR-L-7, Witness Waterbury
9	Contingency Factor	10.1%	USPS-T-10, Witness Waterbury
10	TYBR Cost, (Including Contingency)	\$ 81,866,856	Calculated (Line 7*Line 9)
11	TYAR Cost, (Including Contingency)	\$ 79,513,482	Calculated (Line 8*Line9)
12	Desired Cost Coverage	103.70%	One-Half of Initial Cost Coverage for Outside County
13	TYBR Fees	\$ 1,650,649	USPS-T-39, Witness Berkeley
14	TYAR Fees	\$ 1,666,370	USPS-T-39, Witness Berkeley
15	Proportion of Revenue From Piece Rates	62.5%	Assumption
16	MULTIPLIER TO GET ACTUAL REVENUE	100.035%	Base Year Worksheet
17	Transportation Cost, Without Contingency	96,625	USPS-LR-L-7, Witness Waterbury
18	Transportation Cost, With Contingency	\$ 97,592	Calculated (Line 17*Line 9)
19	Proportion of Transportation Cost That is Distance Related	0.5945	USPS-LR-L-39, Witness Kelly
20	Distance Related Transportation Cost	\$ 58,028	Calculated (Line 18*Line 19)

CALCULATION OF PIECE DISCOUNTS, SHEET 2

Line #

3	Presort Level	Unit Cost Savings (From Discounts W/S)	Passthrough
4			(Benchmark unit cost)
5	BASIC NONAUTOMATION	\$ -	
6	BASIC AUTOMATION LETTER	\$ 0.296	20.2%
7	BASIC AUTOMATION FLAT	\$ 0.013	70%
8	3 DIGIT NONAUTOMATION	\$ 0.073	12%
9	3 DIGIT AUTOMATION LETTER	\$ 0.304	19%
10	3 DIGIT AUTOMATION FLAT	\$ 0.012	86%
11	5 DIGIT NONAUTOMATION	\$ 0.081	12%
12	5-DIGIT AUTOMATION LETTER	\$ 0.315	15%
13	5 DIGIT AUTOMATION FLAT	\$ 0.003	166%
14	CARRIER ROUTE	\$ 0.066	100%
15	HIGH DENSITY	\$ 0.024	70%
16	SATURATION	\$ 0.043	64%
17	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 0.0138	55%
18		Final Unit Cost Savings	Notes
19	BASIC NONAUTOMATION	\$ -	
20	BASIC AUTOMATION LETTER	\$ 0.060	Passthroughs Times Unit Cost Savings
21	BASIC AUTOMATION FLAT	\$ 0.009	Passthroughs Times Unit Cost Savings
22	3 DIGIT NONAUTOMATION	\$ 0.009	Passthroughs Times Unit Cost Savings
23	3 DIGIT AUTOMATION LETTER	\$ 0.058	Passthroughs Times Unit Cost Savings
24	3 DIGIT AUTOMATION FLAT	\$ 0.011	Passthroughs Times Unit Cost Savings
25	5 DIGIT NONAUTOMATION	\$ 0.010	Passthroughs Times Unit Cost Savings
26	5-DIGIT AUTOMATION LETTER	\$ 0.047	Passthroughs Times Unit Cost Savings
27	5 DIGIT AUTOMATION FLAT	\$ 0.005	Passthroughs Times Unit Cost Savings
28	CARRIER ROUTE	\$ 0.066	Passthroughs Times Unit Cost Savings
29	HIGH DENSITY	\$ 0.017	Passthroughs Times Unit Cost Savings
30	SATURATION	\$ 0.028	Passthroughs Times Unit Cost Savings
31	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 0.008	Passthroughs Times Unit Cost Savings
32		TY BR Leakage	Notes
33	BASIC NONAUTOMATION	\$ -	
34	BASIC AUTOMATION LETTER	\$ 30,817	Final Discount times Volume
35	BASIC AUTOMATION FLAT	\$ 8,377	Final Discount times Volume
36	3 DIGIT NONAUTOMATION	\$ 212,455	Final Discount times Volume
37	3 DIGIT AUTOMATION LETTER	\$ 239,653	Final Discount times Volume
38	3 DIGIT AUTOMATION FLAT	\$ 40,110	Final Discount times Volume
39	5 DIGIT NONAUTOMATION	\$ 2,223,628	Final Discount times Volume
40	5-DIGIT AUTOMATION LETTER	\$ 189,644	Final Discount times Volume
41	5 DIGIT AUTOMATION FLAT	\$ 212,039	Final Discount times Volume
42	CARRIER ROUTE	\$ 47,988,156	Final Discount times Volume
43	HIGH DENSITY	\$ 1,897,568	Final Discount times Volume
44	SATURATION	\$ 982,961	Final Discount times Volume
45	WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ 2,132,249	Final Discount times Volume
46	Total Discount Leakage	\$ 56,157,658	Sum Line 33-45
47	Revenue Required from Pieces + Discount Leakages	\$ 108,107,152	Line 46 plus Line 4 from Piece Discounts
48	TYBR Pieces	722,431,237	
49	Revenue Requirement + Leakage Per Piece (Base Rate)	\$ 0.150	Line 47/Line 48

Pounds	TY AR Pounds	Proposed Rates	Postage (Rate*Pounds)
Delivery Unit - Pound Rate	105,321,546	\$ 0.109	\$ 11,480,049
	126,766,452	\$ 0.146	\$ 18,507,902
Presort Rate Pieces	TY AR Pieces	Proposed Rates	Postage (Rate*Pieces)
BASIC NON-AUTOMATION	15,294,097	\$ 0.150	\$ 2,294,115
BASIC AUTOMATION LETTER	497,774	\$ 0.090	\$ 44,800
BASIC AUTOMATION FLAT	902,094	\$ 0.141	\$ 127,195
3-DIGIT NON-AUTOMATION	15,339,480	\$ 0.141	\$ 2,162,867
3-DIGIT AUTOMATION LETTER	4,004,446	\$ 0.083	\$ 332,369
3-DIGIT AUTOMATION FLAT	3,533,813	\$ 0.130	\$ 459,396
5-DIGIT NON-AUTOMATION	68,412,119	\$ 0.131	\$ 8,961,988
5-DIGIT AUTOMATION LETTER	3,910,481	\$ 0.084	\$ 328,480
5-DIGIT AUTOMATION FLAT	41,099,272	\$ 0.126	\$ 5,178,508
CARRIER ROUTE BASIC	404,946,190	\$ 0.065	\$ 26,321,502
CARRIER ROUTE HIGH DENSITY	108,177,430	\$ 0.048	\$ 5,192,517
CARRIER ROUTE SATURATION	34,022,501	\$ 0.037	\$ 1,258,833
WKSHARING DISCNTDELIVERY OFFICE ENTRY	258,307,013	\$ (0.008)	\$ (2,066,456)
Total Pieces & Calculated Revenue	700,139,698		\$ 80,584,063
Ride-along Pieces	597,775	0.155	\$ 92,655
Adjusted Total Revenue including Ride-along			\$ 80,705,216
TYAR Fees			\$ 1,666,370
Calculated Revenue+TYAR Fees			\$ 82,371,586
TYAR Cost			\$ 79,513,462
Cost Coverage after calculation of new rates			103.6%
Revenue per piece			\$ 0.118

**RESPONSE OF NATIONAL NEWSPAPER ASSOCIATION WITNESS STEVE
SIWEK TO INTERROGATORY OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T3-25. In your testimony at page 27, lines 20 to 21, you state, "I recommend that the Commission accept the Within County rate design shown on page 10 of Appendix D."

(a) Please complete the following table showing the postage rates that would apply to a 4-ounce Within County publication under the rates you propose on page 10 of Appendix D of your testimony, as well as the percentage changes over current rates that those rates would represent. If possible, please provide in Excel format.

<u>Presort Level</u>	<u>Rate</u>	<u>% Change from Current</u>
Basic Nonauto		
Basic Auto Flat		
Basic Auto Letter		
3D Nonauto		
3D Auto Flat		
3D Auto Letter		
5D Nonauto		
5D Auto Flat		
5D Auto Letter		
CR Basic (DU entered)		
CR Basic (not DU entered)		
CR HD (DU entered)		
CR HD (not DU entered)		
CR SAT (DU entered)		
CR SAT (not DU entered)		

(b) Please provide tables in the same format as in part (a) showing the rates and percentage changes over current **rates** for a **4-ounce** Within County publication that would result from the rates shown on i) page 5 of Appendix D of your testimony, and ii) page 7 of Appendix D of your testimony. If possible, please provide in Excel format.

RESPONSE:

- (a). See attached spreadsheet – Responses to USPS/NNA-T3-25.
 (b). See attached spreadsheet – Responses to USPS/NNA-T3-25

Response of NNA Witness Siwek
 to
 USPS/NNA-T3-25 (a)

PERIODICALS WITHIN COUNTY
 CURRENT vs. PROPOSED RATES
 Appendix D Revised at page 10.

Delivery Unit	Current Rates	Rates Proposed at page 10 of Appendix D	Current Rates for a 4 oz. piece	Proposed Rates for a 4 oz. piece	Percent Change
General	<input type="radio"/> 109 <input type="radio"/> 142	<input type="radio"/> 103 <input type="radio"/> 14E			
Pieces					
BASIC NON-AUTOMATION	0.103	0.150	0.1385	0.1865	34.66%
BASIC AUTOMATION LETTER	0.049	0.090	0.0845	0.1265	49.70%
BASIC AUTOMATION FLAT	0.075	0.141	0.1105	0.1775	60.63%
3-DIGIT NON-AUTOMATION	0.095	0.141	0.1305	0.1775	36.02%
3-DIGIT AUTOMATION LETTER	0.047	0.083	0.0825	0.1195	44.85%
3-DIGIT AUTOMATION FLAT	0.071	0.130	0.1065	0.1665	56.34%
5-DIGIT NON-AUTOMATION	0.085	0.131	0.1205	0.1675	39.00%
5-DIGIT AUTOMATION LETTER	0.045	0.084	0.0805	0.1205	49.69%
5-DIGIT AUTOMATION FLAT	0.065	0.126	0.1005	0.1625	61.69%
CARRIER ROUTE BASIC (at DU)	0.049	0.065	0.0763	0.0923	20.98%
CARRIER ROUTE BASIC (No DU)	0.049	0.065	0.0845	0.1015	20.12%
CR HIGH DENSITY (at DU)	0.033	0.048	0.0603	0.0753	24.90%
CR HIGH DENSITY (No DU)	0.033	0.048	0.0685	0.0845	23.36%
CR SATURATION (at DU)	0.027	0.037	0.0543	0.0643	18.43%
CR SATURATION (No DU)	0.027	0.037	0.0625	0.0735	17.60%

Response of NNA Witness Siwek
to
USPS/NNA-T3-25 (b)(i)

PERIODICALS WITHIN COUNTY
CURRENT vs. DESCRIBED RATES
Appendix D Revised at page 5

	Current Rates	Rates Described at page 5 of Appendix D	Current Rates for a 4 oz. piece	Described Rates for a 4 oz. piece	Percent Change
Pounds					
Delivery Unit	0.109	0.109			
General	0.142	0.146			
Pieces					
BASIC NON-AUTOMATION	0.103	0.128	0.1385	0.1645	18.77%
BASIC AUTOMATION LETTER	0.049	0.068	0.0845	0.1045	23.67%
BASIC AUTOMATION FLAT	0.075	0.119	0.1105	0.1555	40.72%
3-DIGIT NON-AUTOMATION	0.095	0.109	0.1305	0.1555	19.16%
3-DIGIT AUTOMATION LETTER	0.047	0.081	0.0825	0.0975	18.18%
3-DIGIT AUTOMATION FLAT	0.071	0.108	0.1065	0.1445	35.68%
5-DIGIT NON-AUTOMATION	0.085	0.109	0.1205	0.1455	20.75%
5-DIGIT AUTOMATION LETTER	0.045	0.062	0.0805	0.0985	22.36%
5-DIGIT AUTOMATION FLAT	0.065	0.104	0.1005	0.1405	39.80%
CARRIER ROUTE BASIC (at DU)	0.049	0.071	0.0763	0.0983	28.85%
CARRIER ROUTE BASIC (No DU)	0.049	0.071	0.0845	0.1075	27.22%
CR HIGH DENSITY (at DU)	0.033	0.055	0.0603	0.0823	36.51%
CR HIGH DENSITY (No DU)	0.033	0.055	0.0685	0.0915	33.58%
CR SATURATION (at DU)	0.027	0.043	0.0543	0.0703	29.49%
CR SATURATION (No DU)	0.027	0.043	0.0625	0.0795	27.20%

**Response of NNA Witness Siwek
to
USPS/NNA-T3-25 (b)(ii)**

**PERIODICALS WITHIN COUNTY
CURRENT vs. DESCRIBED RATES
Appendix D Revised at page 7**

	Current Rates	Rates Described at page 7 of Appendix D	Current Rates for a 4 oz. piece	Described Rates for a 4 oz. piece	Percent Change
Pounds					
Delivery Unit	0.109	0.142			
General	0.142	0.179			
Pieces					
BASIC NON-AUTOMATION	0.103	0.139	0.1385	0.18375	32.67%
BASIC AUTOMATION LETTER	0.049	0.079	0.0845	0.12375	46.45%
BASIC AUTOMATION FLAT	0.075	0.130	0.1105	0.17475	58.14%
3-DIGIT NON-AUTOMATION	0.095	0.130	0.1305	0.17475	33.91%
3-DIGIT AUTOMATION LETTER	0.047	0.072	0.0825	0.11675	41.52%
3-DIGIT AUTOMATION FLAT	0.071	0.119	0.1065	0.16375	53.76%
5-DIGIT NON-AUTOMATION	0.085	0.120	0.1205	0.16475	36.72%
5-DIGIT AUTOMATION LETTER	0.045	0.073	0.0805	0.11775	46.27%
5-DIGIT AUTOMATION FLAT	0.065	0.115	0.1005	0.15975	58.96%
CARRIER ROUTE BASIC (at DU)	0.049	0.054	0.0763	0.0895	17.38%
CARRIER ROUTE BASIC (No DU)	0.049	0.054	0.0845	0.09875	16.86%
CR HIGH DENSITY (at DU)	0.033	0.037	0.0603	0.0725	20.33%
CR HIGH DENSITY (No DU)	0.033	0.037	0.0685	0.08175	19.34%
CR SATURATION (at DU)	0.027	0.026	0.0543	0.0615	13.36%
CR SATURATION (No DU)	0.027	0.026	0.0625	0.07075	13.20%

**RESPONSE OF NATIONAL NEWSPAPER ASSOCIATION WITNESS STEVE
SIWEK TO INTERROGATORY OF UNITED STATES POSTAL SERVICE**

USPS-NNA-T3-26. Please refer to page 7 of Appendix D of your testimony, where you propose rates after increasing the passthrough for carrier route basic and high density. Please provide the percentage increases over current rates for the (a) non-carrier route piece rates and (b) carrier route piece rates on that page.

RESPONSE:

The Table below provided the requested comparison for the rates described at page 7 of Appendix D as revised in USPS-LR-L-126.

PERIODICALS WITHIN COUNTY CURRENT vs. PROPOSED RATES			
Pounds	Current Rates	Proposed Rates	Percent Change
Delivery Unit	\$ 0.109	\$ 0.142	30.28%
General	\$ 0.142	\$ 0.179	26.06%
Pieces			
BASIC NON-AUTOMATION	\$ 0.103	\$ 0.139	34.95%
BASIC AUTOMATION LETTER	\$ 0.049	\$ 0.079	61.22%
BASIC AUTOMATION FLAT	\$ 0.075	\$ 0.130	73.33%
3-DIGIT NON-AUTOMATION	\$ 0.095	\$ 0.130	36.84%
3-DIGIT AUTOMATION LETTER	\$ 0.047	\$ 0.072	53.19%
3-DIGIT AUTOMATION FLAT	\$ 0.071	\$ 0.119	67.61%
5-DIGIT NON-AUTOMATION	\$ 0.085	\$ 0.120	41.18%
5-DIGIT AUTOMATION LETTER	\$ 0.045	\$ 0.073	62.22%
5-DIGIT AUTOMATION FLAT	\$ 0.065	\$ 0.115	76.92%
CARRIER ROUTE BASIC	\$ 0.049	\$ 0.054	10.20%
CARRIER ROUTE HIGH DENSITY	\$ 0.033	\$ 0.037	12.12%
CARRIER ROUTE SATURATION	\$ 0.027	\$ 0.026	-3.70%
WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ (0.006)	\$ (0.008)	33.33%
RIDE-ALONG PIECES	\$ 0.131	\$ 0.155	18.32%

**RESPONSE OF NATIONAL NEWSPAPER ASSOCIATION WITNESS STEVE
SIWEK TO INTERROGATORY OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T3-27. Please refer to page 5 of Appendix D of your testimony, where YOU propose rates after increasing the percent of revenue derived from the piece side to 62.5 percent. Please provide the percentage increases over current rates for the (a) pound rates and (b) piece rates on that page.

RESPONSE:

The Table below provided the requested comparison for the rates described at page 5 of Appendix D as revised to reflect the USPS' revisions in USPS-LR-L-126.

Pounds	Current Rater	Proposed Rater	Percent Change
Delivery Unit	\$ 0.109	\$ 0.109	0.00%
General	\$ 0.142	\$ 0.146	2.82%
Pieces			
BASIC NON-AUTOMATION	\$ 0.103	\$ 0.128	24.27%
BASIC AUTOMATION LETTER	\$ 0.049	\$ 0.068	38.78%
BASIC AUTOMATION FLAT	\$ 0.075	\$ 0.119	58.67%
3-DIGIT NON-AUTOMATION	\$ 0.095	\$ 0.119	25.26%
3-DIGIT AUTOMATION LETTER	\$ 0.047	\$ 0.061	29.79%
3-DIGIT AUTOMATION FLAT	\$ 0.071	\$ 0.108	52.11%
5-DIGIT NON-AUTOMATION	\$ 0.085	\$ 0.109	28.24%
5-DIGIT AUTOMATION LETTER	\$ 0.045	\$ 0.062	37.78%
5-DIGIT AUTOMATION FLAT	\$ 0.065	\$ 0.104	60.00%
CARRIER ROUTE BASIC	\$ 0.049	\$ 0.071	44.90%
CARRIER ROUTE HIGH DENSITY	\$ 0.033	\$ 0.055	66.67%
CARRIER ROUTE SATURATION	\$ 0.027	\$ 0.043	59.26%
WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ (0.006)	\$ (0.008)	33.33%
RIDE-ALONG PIECES	\$ 0.131	\$ 0.155	18.32%

**RESPONSE OF NATIONAL NEWSPAPER ASSOCIATION WITNESS STEVE
SIWEK TO INTERROGATORY OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T3-28. Please refer to page 5 of Appendix D of your testimony, where you propose rates after increasing the percent of revenue derived from the piece side to 62.5 percent. What would those rates be if you set the proportion of revenue derived from the piece side on page 4 of Appendix D to 60 percent rather than 62.5 percent? Please provide the percentage increases over current rates for the (a) pound rates, and (b) piece rates that these rates would represent.

RESPONSE:

The Table below provided the requested comparison for the rates described at page 5 of Appendix D as revised to reflect the USPS' revisions in **USPS-LR-L-126** with the proportion of revenue derived from the piece side to 60% rather than 62.5%.

CURRENT vs. PROPOSED RATES			
Pounds	Current Rates	Proposed Rates	Percent Change
Delivery Unit	\$ 0.109	\$ 0.118	8.26%
General	\$ 0.142	\$ 0.155	9.15%
Pieces			
BASIC NON-AUTOMATION	\$ 0.103	\$ 0.125	21.36%
BASIC AUTOMATION LETTER	\$ 0.049	\$ 0.065	32.65%
BASIC AUTOMATION FLAT	\$ 0.075	\$ 0.116	54.67%
3-DIGIT NON-AUTOMATION	\$ 0.095	\$ 0.116	22.11%
3-DIGIT AUTOMATION LETTER	\$ 0.047	\$ 0.053	23.40%
3-DIGIT AUTOMATION FLAT	\$ 0.071	\$ 0.105	47.89%
5-DIGIT NON-AUTOMATION	\$ 0.085	\$ 0.106	24.71%
5-DIGIT AUTOMATION LETTER	\$ 0.045	\$ 0.059	31.11%
5-DIGIT AUTOMATION FLAT	\$ 0.065	\$ 0.101	55.38%
CARRIER ROUTE BASIC	\$ 0.049	\$ 0.068	38.78%
CARRIER ROUTE HIGH DENSITY	\$ 0.033	\$ 0.052	57.58%
CARRIER ROUTE SATURATION	\$ 0.027	\$ 0.040	48.15%
WKSHARING DISCNTDELIVERY OFFICE ENTRY	\$ (0.006)	\$ (0.008)	33.33%
RIDE-ALONG PIECES	\$ 0.131	\$ 0.155	18.32%

**RESPONSE OF NATIONAL NEWSPAPER ASSOCIATION WITNESS STEVE
SIWEK TO INTERROGATORY OF UNITED STATES POSTAL SERVICE**

USPS/NNA-T3-29. Please refer to your testimony at page 2, lines 10 to **16**. Please confirm that the TYBR and **TYAR** cost and revenue figures you discuss there do not reflect the revisions to witness OHara's exhibits made on August 25, 2006. If you do not confirm, please explain. Was this intentional? If it was intentional, please explain.

RESPONSE:

I confirm that the TYBR and TYAR cost and revenue figures referenced at page 2 of my testimony do not reflect the **revisions to** witness OHara's exhibits made on August 25, 2006. It was not my *intention* **to** omit the **USPS'** revisions to these exhibits.

CHAIRMAN OMAS: There are a 30 responses to
2 the following interrogatories that I would like to
3 enter into the evidentiary record at this time. They
4 are USPS/NNA-T3-15 and USPS/NNA-T3-23.

5 Ms. Rush, would you consult with your
6 witness, please, Witness Siwek, and notify the record
7 if he wishes to change his answer to any of these
8 questions?

9 THE WITNESS: 23 and 15? My answers would
10 be the same as appear.

11 CHAIRMAN OMAS: All right. Thank you, Mr.
12 Siwek.

13 I have already provided two copies of the
14 answers to the reporter and direct that they be
15 admitted into evidence and transcribed.

16 (The documents referred to
17 were marked for
18 identification as Exhibit
19 Nos. USPS/NNA-T3-15 and
20 USPS/NNA-T3-23 and were
21 received in evidence.)

22 //

23 //

24 //

25 //

RESPONSE OF NNA WITNESS SIWEK TO INTERROGATORIES
OF UNITED STATES POSTAL SERVICE

USPS/NNA-T3-15. Please refer to your testimony, NNA-T-3, section VIII d), p. 17, where you write, "If the 2006 sample is not large enough to obtain accurate and reliable estimates for this low volume subclass, ...".

- a. Do you believe that sample size affects the accuracy of an estimate?
- b. If so, please explain how sample size affects the accuracy, as opposed to the precision, of an estimate.

RESPONSE:

- a. Yes.
- b. I have used the word "accuracy" as equivalent to the word "precision" in my testimony. The larger the sample size, the more **accurate/precise** an estimate can be.

**RESPONSE OF NATIONAL NEWSPAPER ASSOCIATION WITNESS STEVE
SIWEK TO INTERROGATORY OF UNITED STATES POSTAL SERVICE**

USPS-NNA-T3-23. In your testimony at page 22. lines 6 to 9, you state, "Ms. Tang thus failed to identify any functionally 'different' Within County costs that could help to explain why the USPS has proposed a 24.2 percent increase for Within County periodicals and only an 11.7 percent increase for Outside County periodicals." Please confirm that the Postal Service determines subclass-level costs independently for Within County and Outside County Periodicals. If you do not confirm, please explain.

RESPONSE:

I personally would not characterize the Postal Service's determinations of subclass-level costs for Within County and **Outside** County Periodicals as "independent." The Postal Service first attempts to identify Periodicals "tallies." Subsequently, the USPS attempts to determine which of these tallies reflect **the** handling of Periodicals that are eligible for Within County rates and which are not. Therefore, at least as I see this process, the determination of subclass level costs for both Within County and Outside County Periodicals is "dependent" upon the initial identification of tallies for "Periodicals."

1 CHAIRMAN OMAS: Is there any additional
2 written cross-examination for Witness Siwek?

3 (No response.)

4 CHAIRMAN OMAS: This now brings us to oral
5 cross-examination.

6 One participant has requested oral cross-
7 examination of Witness Siwek. Mr. Weidner?

8 MR. **HOLLIES**: This is Mr. Hollies for the
9 Postal Service.

10 CHAIRMAN OMAS: Mr. Hollies, please
11 introduce yourself.

12 CROSS-EXAMINATION

13 BY MR. HOLLIES:

14 Q Good morning, Mr. Siwek. I'm Ken Hollies
15 for the Postal Service.

16 A Good morning.

17 Q I have a few questions for you. The first
18 couple of mine are I think housekeeping matters.

19 Could you take a look please at your
20 response to Interrogatory 25 from the Postal Service?
21 That's USPS/MNA-T3-25.

22 This interrogatory asks you to calculate the
23 rates for a four ounce within county publication that
24 would result from your proposed rates and to compare
25 those rates to the current rates. **Is** it safe to say

1 that's accurate?

2 A That's accurate as it regards part (a) of
3 that answer.

4 Q Okay. And specifically for the carrier
5 route rate categories it asks you to calculate the
6 current rates and your proposed rates for a four ounce
7 publication assuming delivery unit entry and
8 nondelivery unit entry, correct?

9 A That's correct.

10 Q There are no tricks here, so relax. Now, it
11 is correct, is it not, that the current and proposed
12 carrier route delivery unit entry rates that you
13 present in your response do not include the DDU
14 discount?

15 A I would have to check that.

16 Q I would like to quote for you -- just a
17 second -- DMCS Section 423.45, Destination Entry
18 Discount. "A destination delivery unit discount
19 applies to within county carrier route category mail
20 which is destined for delivery within the destination
21 delivery unit, DDU, in which it is entered as defined
22 by the Postal Service."

23 I do believe that you failed to include that
24 in your exhibit, and that was an inadvertent error.
25 That's the thrust of my immediate questions. The

1 pieces we asked you about do include the delivered
2 unit pound rate. Is that correct?

3 A Yes.

4 Q And is it possible that you may have left
5 something out in your calculations?

6 A Yes, it's possible. These calculations were
7 derived from an exhibit prepared by Ms. Tang so I
8 would have to go look at that, but certainly it is
9 possible that part of the DDU discount may not have
10 been included here, in which case the percentage
11 increases would be lower.

12 Q That is **my** point. Thank you. If you would
13 agree to take a look at that and file updated answers
14 if you find something, that would be appreciated.

15 A Yes.

16 Q Okay. Mr. Siwek, you propose a pass through
17 for within county carrier route basic of 100 percent.
18 Is that correct?

19 A I believe that's **correct**, yes.

20 Q And that pass through is relative to a five
21 digit nonauto?

22 A It would help if you gave me a reference to
23 this in the testimony.

24 Q Well, I don't have that with me. To
25 rephrase that, if the rate difference between five

1 digit nonauto and the carrier route basic reflects 100
2 percent of the calculated cost savings of carrier
3 route over five digit nonauto.

4 A Again subject to check, I believe that's
5 correct.

6 Q Yes. If you would look at the top of page
7 27 of your testimony, I think that would anchor you.

8 A Yes. There are my proposed pass throughs.

9 Q All right. The Postal Service has proposed
10 a pass through of 58 percent for carrier route basic.
11 Is that correct? You might want to look at page 3 of
12 your revised Appendix D.

13 A Yes, that's correct.

14 Q Okay. The Postal Service has proposed a
15 pass through of 65 percent for high density relative
16 to carrier route basic. Is that correct?

17 A I believe that's correct, yes.

18 Q Are you aware of what the Commission has
19 recommended in the past with respect to these two pass
20 throughs?

21 A Not in any detail. I looked at I believe
22 the last decision on this, but I focused mainly on the
23 current proposals.

24 Q I have a copy of library references, PRC
25 library references, from the last two litigated cases

1 that we're going to hand out here.

2 The last two litigated cases of course were
3 R2000-1 and R97-1, and we're handing out a sheet from
4 PRC Library Reference 14 in the R2000-1 docket and
5 from PRC Library Reference 11 in the R97 docket, which
6 you'll have in a moment.

7 Looking at Library Reference 14 from
8 R2000-1, is it correct that the Commission recommended
9 a 50 percent pass through for carrier route basic?

10 A Just give me a second. I'm just getting it
11 now.

12 MS. RUSH: Mr. Chairman, may I query the
13 Postal Service here?

14 Are we looking at nonprofit pass throughs
15 here, or are we looking at within county rates?

16 MR. HOLLIES: Within county.

17 THE WITNESS: Well, this is a bit confusing
18 because it does say for nonprofit on these sheets.

19 MR. HOLLIES: I'm given to understand that
20 the nonprofit costs were used as a proxy, and that's
21 why they are so labeled.

22 THE WITNESS: So you're saying in the last
23 two cases the nonprofit costs were used as a proxy for
24 within county costs and in this case the regular rate
25 costs were used as a proxy, so that's the difference

1 here?

2 **MR. HOLLIES:** Yes, that is correct.

3 **THE WITNESS:** Okay.

4 **BY MR. HOLLIES:**

5 Q So looking to the **R2000** library reference --

6 A Yes.

7 Q -- the carrier route basic pass through was
8 50 percent?

9 A For nonprofit, yes That's what this sheet
10 says.

11 Q And what about for carrier route high
12 density? Is that **42** percent?

13 A Yes. The number is **42** percent on the sheet
14 here, the input sheet.

15 Q **And** if you look at the sheet from Commission
16 Library Reference 11 in the **R97-1** docket, the carrier
17 route basic and the high density pass throughs are
18 both 50 percent there, are they not?

19 A Yes, for nonprofit.

20 Q So for the carrier route basic do you agree
21 that the pass through you propose of 100 percent is
22 double what the Commission recommended in both Docket
23 No. **R97**, 50 percent, and Docket No. **R2000**, again 50
24 percent?

25 A You're asking me if the pass through is

1 double, but it is being applied to a different cost
2 base so I'm not sure that it applies to apples, your
3 question.

4 Q Okay. Well, I think we can work with that
5 in the brief.

6 For the high density, would you agree that
7 the pass through you propose of 70 percent is
8 approximately two-thirds greater than what the
9 Commission recommended in R2000?

10 A Yes, again with the caveat that that was for
11 nonprofit, a different cost base than is being used
12 here.

13 Q Okay. I think we'll be able to show that it
14 is actually within county, but I can understand the
15 labeling being troubling at **this** point. Okay. That's
16 all I have for that. Thank you.

17 CHAIRMAN OMAS: Is there anyone else who
18 wishes to --

19 MR. HOLLIES: I'm sorry, Mr. Chairman. I'm
20 not done asking. I'm done with that line of
21 questioning.

22 BY MR. HOLLIES:

23 Q In your testimony, Mr. Siwek, you use
24 various terms regarding the IOCS cost increases
25 referring to them as alleged increases, that they are

1 claimed increases, that they are supposedly increases.

2 Are the within county IOCS costs calculated
3 in this docket developed in ways that are markedly
4 different from how they were developed in previous
5 omnibus cases?

6 A I believe to the extent the IOC costs in
7 this docket reflect changes in the IOCS questions they
8 would be different than costs estimated in prior
9 dockets.

10 Q Okay. The IOCS instrument changed. I think
11 that's what you're referring to?

12 A Yes.

13 Q Okay. And using the IOCS costs that
14 resulted from the new instrument, the mechanics of the
15 calculations were nonetheless the same **as** they were in
16 previous dockets, were they not?

17 A I guess I'm not sure what you mean by
18 mechanics of the calculation.

19 Q Well, in terms of using the cost pools, the
20 estimates of costs that derive from IOCS and building
21 up the proposed rates and discounts.

22 That type of approach has been used before
23 and does not change markedly. We use it the same in
24 this case.

25 A I haven't explored that question in detail.

1 I will accept your representation, but clearly the
2 instruments have changed, and Mr. Bozzo has testified
3 that they were fairly dramatic changes.

4 Q What standard do you apply to distinguish
5 true costs from alleged costs?

6 A I don't know that I use the word true cost.
7 I am attempting to come **up** with the best estimate of
8 costs for within county, within county periodicals.

9 What I'm observing ~~in~~ the Postal Service's
10 proposal here is a failure to really address the
11 mechanics of the costs in the first instance. In
12 other words, you haven't correctly studied the costs,
13 so that's what I meant.

14 Q If periodical costs were previously
15 undercounted by IOCS, what impact would that have when
16 such costs are counted more accurately?

17 A Well, by assumption if they were previously
18 undercounted in the past and you corrected that
19 undercount, the cost would increase.

20 Q Should the Commission issue its opinion and
21 recommended decision based on costs that you
22 characterize as alleged, would you still characterize
23 them that way?

24 A You're asking me if I were in a position to
25 comment after the fact on the Commission's decision?

1 I don't know that I've been in that position. I don't
2 know how I would characterize it.

3 Q A little further into your testimony -- this
4 would be page 3, line 14 -- you've introduced some
5 more colorful language. At what threshold do reported
6 cost changes become "dramatic"?

7 A I don't know that I've identified a
8 particular point, but I've given examples and
9 percentages of what I believe are dramatic cost
10 increases.

11 Q Is that a term of art to an economist?

12 A I don't believe so, no. We could use
13 significant or large. Those would apply.

14 Q At the bottom of page 3 of your testimony
15 you switch your discussion of reported cost changes
16 from a focus on cost segments to a focus on unit
17 costs, Look at lines 20 and 21.

18 A I do, yes.

19 Q Your characterizations of reported costs
20 extend the familiar use of alleged cost increase to
21 include the claim that per unit increases are "even
22 more outlandish." Is that right?

23 A Yes.

24 Q What's the threshold you apply to
25 distinguish dramatic increases from outlandish

1 increases?

2 A Well, if you'll look at the cited sentences
3 the within county periodical increase under a unit
4 cost analysis is 65 percent, which is a higher
5 percentage than any of the prior percentages which
6 I've identified, so by that measure I am saying that
7 the increase is even greater if you accept unit costs
8 are more significant.

9 Q Is your point that a cost increase analyzed
10 at the level of cost segments is "dramatic," but when
11 you instead look at that increase at the level of unit
12 costs that it becomes more outlandish?

13 A Not specifically. My point is that by the
14 measure of unit cost the percentage increases is
15 greater by a significant factor than it is when you
16 look at the cost segments.

17 By either measure, the increase in costs
18 that is claimed for within county periodicals is very
19 large.

20 Q On page 4 you state, "Absent a known
21 extraordinary event, cost increases of this magnitude
22 occurring with so limited a timeframe are simply not
23 believable." Is that right?

24 A Yes, that's what I state.

25 Q And I think you've already indicated your

1 familiarity with Witness Bozzo's **USPS-T-46** testimony?

2 A Yes, I've reviewed his testimony.

3 Q And what's your general understanding of
4 that testimony?

5 A My general understanding of Mr Bozzo's
6 testimony, T-46, is a description of changes in the
7 IOCS that are presented in this case and a
8 presentation of some of the results of those changes,
9 and in particular from my point of view a discussion
10 of the increases that would apply to within county
11 periodicals.

12 Q If within county IOCS costs were previously
13 underreported and given that a new IOCS questionnaire
14 and an enhanced look **up** table for periodicals has been
15 implemented, could these have had any impact on the
16 size of reported increases for within county?

17 A I think that's possible. Indeed, I think
18 that's what Mr. Bozzo suggests.

19 Q Later on page 4 you write, "It is far more
20 likely that these cost increases result from
21 significant deficiencies in the processes and data
22 used by the" Postal Service. You use **USPS**. How did
23 you arrive at this probabilistic judgment?

24 A By focusing on what was done by the Postal
25 Service in the latter portion of their cost analysis

1 related to within county periodicals, also noting as I
2 do on this same page that there was a failure by the
3 Postal Service to pretest the effects of these changes
4 on within county, so --

5 Q We' ll be discussing that.

6 A Okay.

7 Q On page 5, lines 13 and 14, you claim that
8 the validity and reliability of within county cost
9 estimates are just assumed. Is that right?

10 A Yes.

11 Q Could you identify each specific assumption
12 that led to that conclusion?

13 A I will try. As I mentioned, it is assumed
14 by the failure of the Postal Service to pretest for
15 within county problems that the new cost method
16 appropriately captures within county periodical costs
17 in a way that was not done in the past, so the Postal
18 Service by failing to look at any pretests has ruled
19 out any other possibility that might have been
20 discovered through such pretests.

21 Secondly, when we move to the
22 characterization of the checking process for
23 periodicals, the process which ends up as a manual
24 process to distinguish in county from outside county
25 periodicals, I have a series of difficulties with how

1 that was done, most notably the fact that the Postal
2 Service has not attempted to study the actual payment
3 of a particular rate for a particular piece.

4 In other words, the tally that comes to the
5 Postal Service is not assessed as even whether a
6 within county or outside county rate was paid.

7 After that we look at how the Postal Service
8 determined eligibility, and I have a number of
9 concerns with assumptions and judgments and a lack of
10 timely data that were used in that context and so all
11 of these together represent really a summation of why
12 I believe that these cost estimates are unreliable.

13 Q If I heard you correctly, you mean to say
14 also then that the point estimates and the confidence
15 intervals reported for IOCS cost measures in USPS-T-1,
16 the testimony of Witness Ziegler, together with the
17 body of underlying data also constitute assumptions
18 with respect to within county. Is that right?

19 A Well, I don't know that I've criticized
20 precisely the calculation by Mr. Ziegler on
21 coefficients and variants.

22 Basically the way I see that, that is a
23 criticism that kind of assumes, notwithstanding
24 everything that I said previously, that the Postal
25 Service got it right on within county costs. Even

1 assuming that's true, you are left with a coefficient,
2 a variance, that is basically so wide as to leave open
3 a wide range of uncertainty on the cost estimate.

4 Q So is that confidence interval larger than
5 it has been in past proceedings?

6 A It is larger than it has been in some past
7 proceedings and not larger than in others, but in any
8 case it's substantially larger than most other
9 subclasses have **shown**.

10 Q That would be true for any small subclass,
11 would it not?

12 A I suppose, based on how the Postal Service
13 looks at this, yes, that would be true.

14 Q Are the data collected during an IOCS
15 reading also assumptions?

16 A Well, they're certainly assumptions that go
17 into the sampling process. The Postal Service makes
18 assumptions as to each stage of its sample and when
19 that sample will be taken throughout the year, so
20 assumptions go into the precise act of taking a tally.

21 Q And those assumptions are all different from
22 what's happened in previous proceedings?

23 A I'm not saying they are different, no.

24 Q They're the same?

25 A I haven't studied that in detail.

1 Q You haven't look at how within county costs
2 were done in previous dockets?

3 A I looked briefly, but not in great detail,
4 no.

5 Q So your comments about IOCS in this case are
6 based largely, if not totally, on your examination of
7 what's happened in this case?

8 A Well, but bear in mind that you have at
9 least Witness Bozzo who talks about what's happening
10 in this case relative to the prior case vis-a-vis the
11 IOCS.

12 Q So your knowledge of what's happened in
13 previous cases regarding IOCS is derived from your
14 understanding of Witness **Bozzo's** testimony?

15 A Well, I've also looked at and indeed
16 summarized I think somewhere in my testimony what the
17 CVs were for within county going back some period of
18 time, so I did look at and tally up those indications.

19 I guess what you were asking me is did I
20 look at the actual sampling strata from the prior
21 case. No, I didn't do that.

22 Q No. I was asking if you had looked at how
23 the IOCS within county costs were developed in
24 previous cases.

25 A Beyond what I've just explained, no, I don't

1 believe I have.

2 Q Let's look for a moment at the logical
3 structure of Roman numeral part V on pages 4 and 5 of
4 your testimony.

5 A I have it.

6 Q Would you agree that the first paragraph
7 centers on mail processing and in-office city carrier
8 cost increases measured by IOCS for within county
9 periodicals?

10 A Yes.

11 Q You do of course mention the IOCS redesign
12 and the absence of certain testing, which turned out
13 to predicate the content of the next two paragraphs.
14 Is that right?

15 A Yes.

16 Q But can you agree that those statements
17 still relate to the reported within county cost
18 increases?

19 A The changes on the beta tests? Do you have
20 a specific sentence in mind?

21 Q No. I'm looking at the paragraph, the first
22 paragraph of that section.

23 A Yes.

24 Q In the second paragraph you delve further
25 into the IOCS redesign, and in the third paragraph you

1 make the point that none of the testing performed by
2 the Postal Service during the redesign effort
3 considered without county periodicals exclusively. Is
4 that a fair assessment?

5 A Yes, that's fair

6 Q The single sentence fourth paragraph
7 summarizes your conclusion for this section that the
8 "basic validity and reliability of the USPS within
9 county cost estimates cannot simply be assumed." Is
10 that accurate?

11 A Yes, that's what I say.

12 Q So Section V of your testimony could be
13 summarized as because 1) IOCS shows substantial cost
14 increases for the within county subclass when 2) that
15 subclass was not studied in isolation from other
16 subclasses before implementation of a new instrument,
17 then 3) IOCS estimates for within county constitute
18 assumptions that lack any validity or liability.

19 Is that right?

20 A Not exactly. You omitted the statement in
21 the beginning in which I indicate that the cost
22 increases reflect a substantial redesign of the Postal
23 Service's in-office cost system, which is part of my
24 argument here. If there were no substantial redesign
25 perhaps these things might be easier to explain.

1 Q Ok y. With that additional material, the
2 summary is fairly accurate then, is it not?

3 A With the addition of the salient fact that
4 there was a substantial redesign.

5 Q I'm having a little trouble with the logic
6 here. Did each of the 197 IOCS tallies underlying the
7 within county cost estimates also consist of
8 assumptions?

9 A I don't know that I could speak to each and
10 every one of the 197, but there are assumptions that
11 go into the process by which the 197 tallies were
12 derived.

13 Q So for at least some of those the mail piece
14 characteristics collected in those tallies were also
15 assumptions? That would be your conclusion, right?

16 A Well, the mail piece characteristics were to
17 some extent ignored by the Postal Service as the
18 process unfolded, so there is a process of a
19 preliminary identification of various characteristics
20 and then a subsequent attempt to verify whether those
21 are accurate or not so that periodical counts were
22 thrown out by the Postal Service even though
23 preliminary estimates suggested there were periodicals
24 in there.

25 Q What was thrown out?

1 A Counts of periodicals. In other words,
2 there was an initial count of in county plus outside
3 county periodicals.

4 There was an elimination of a number of
5 those tallies because of rules that the Postal Service
6 has relative to things like whether they were
7 developed from a software redesign, and then finally
8 there was an elimination of a number of tallies which
9 were unverifiable which were eliminated from the
10 periodical counts which were the results of the
11 answers provided in the IOCS.

12 All of this precedes the discussion of
13 whether it's within county or not.

14 Q So you would assert that verification on
15 those tallies to confirm whether they were within
16 county rather than outside county also consisted of
17 assumptions?

18 A That's where the assumptions were most
19 clearly made, but all I'm saying is there were
20 assumptions prior to that by which the Postal Service
21 decided to ignore the fact that periodical tallies
22 didn't really belong, even though that was the answer
23 that came from the question.

24 Q Were the publication names recorded in
25 respect of tallies also assumptions?

1 A don t know he nswer to th t. I assume
2 they were faithfully recorded from the tally, so I
3 suppose there's an assumption that they were
4 accurately recorded, but I don't think that's what I
5 mean by assumption.

6 Q How do the within county tallies differ from
7 tallies relating to other subclasses? Are all IOCS
8 tallies assumptions?

9 A I haven't looked at all IOCS tallies. I'm
10 telling you that in the process of identifying
11 periodical tallies assumptions are made as to whether
12 or not a particular response should or should not be
13 included, and that happens prior to the discussion of
14 within county and outside county volumes.

15 Q On page 5 of your testimony you first assert
16 that the Postal Service conducted two tests and two
17 studies of the revised IOCS instrument -- that would
18 be lines 4 through 12 -- while in the following
19 section you criticize "the USPS' failure to pretest
20 the IOCS redesign" at line 19.

21 Is your intended point that the pre beta
22 test, the beta test, the photocopy study and the
23 keying study, that none of these constitutes a pretest
24 that you assert was a necessary precondition to the
25 IOCS redesign?

1 A For within county mail, yes.

2 Q Please look at the sentence that starts on
3 page 5 and concludes on page 6 of your testimony. The
4 sentence starts with, "In this case..." in case you
5 have the Word version rather than the pdf version.

6 A Yes. I have it.

7 Q Okay. Is it your testimony that an IOCS
8 tally is invalid or unusable when the Postal Service
9 fails to verify the actual postage paid for each piece
10 described as part of an IOCS reading?

11 A Based solely on that fact, I don't know that
12 I would want to go so far as to say it was totally
13 unreliable, but it does in any case raise substantial
14 question as to how reliable it would be because you
15 would have to think about the reasons why the breaks
16 may differ from other information on the tally, so not
17 necessarily in all cases, but certainly a serious
18 concern in any case.

19 Q So you assert that there should be some
20 mechanism of recording the actual postage paid for
21 each piece sampled in IOCS?

22 A I'm not saying that. I'm saying that the
23 Postal Service has failed to study that, so the Postal
24 Service does not know what mail revenue, what mail
25 postage, was paid on any of these pieces.

1 Q And to the best of your understanding, what
2 portion of IOCS tallies meet your standard?

3 A Again, I haven't looked beyond periodicals
4 generally and within county and outside county.

5 Q Would you agree that as a practical matter
6 most IOCS periodical test readings do not occur as
7 pieces are entered, so identifying that actual postage
8 paid and the subclass of the piece is necessarily
9 problematic?

10 A I don't know that I could agree or disagree
11 with that statement.

12 Q Do you understand how IOCS works in a
13 general sense?

14 A In a general sense I believe I do, yes, but
15 certainly there are --

16 Q And that would include, for example, looking
17 at a piece of mail that a worker is actually touching
18 at the time of a reading perhaps?

19 A Yes.

20 Q How can one determine what postage was
21 actually paid for a periodical piece?

22 A There are some ways that I might consider
23 thinking about this question. but my point is simply
24 that the Postal Service has not determined that
25 postage.

1 We now base for example, on one of the
2 examples that Mr. Heath was describing a few minutes
3 ago that there are any number of situations in which
4 the postage is not obvious for within county mail.
5 It's not obvious from some of these other criteria.

6 So I think that as you get down to the fine
7 grained analysis of within county mail that there
8 should be or should have been some way to check this
9 against postage paid.

10 Q Well, I'm asking you a very practical
11 question. The postage is not indicated on a
12 periodicals piece. Is that correct?

13 A It may or may not be.

14 Q You don't know?

15 A I don't know if it always is or it always
16 isn't, particularly on other forms of periodicals.

17 Q What do you know about postage indication on
18 periodicals pieces?

19 A There are any number of data that are
20 recorded from markings that indicate the type or class
21 of piece, and I know that the IOCS focuses on those
22 markings as part of its attempt to identify
23 periodicals.

24 I guess what I'm not certain of is what
25 exactly the markings show beyond some indication that

1 it's a periodical.

2 Q Okay. I'm still stuck on this practical
3 problem. You've set up a standard indicating that the
4 Postal Service needs to check the actual postage paid
5 for a periodicals piece sampled in IOCS, and I'm
6 asking you how that can be done.

7 A All right. First of all, I'm not setting
8 the standard. The Postal Service has proposed costs
9 and wants to raise rates based on those costs. What I
10 said is the basis of that cost claim is inadequate for
11 a number of reasons, including the fact that the
12 Postal Service doesn't know what postage was paid.

13 Now, to get to the specifics of the question
14 we recognize that within county periodicals the Postal
15 Service already does substantial manual checking of
16 the relatively limited number of tallies that exist
17 and so what I'm suggesting if need be is a further
18 look at that manual checking process and perhaps a way
19 to check it against whether the postage was actually
20 paid on a given piece.

21 That's one of a number of criticisms that I
22 have of the Postal Service's process.

23 Q I guess I misheard. I thought you indicated
24 that one standard that should be applied in looking at
25 the quality of the IOCS periodical data is the fact

1 that the actual postage paid for a piece is not
2 recorded. Didn't you lodge that criticism?

3 A The criticism extends to the process of
4 coming up with a cost of within county mail. I think
5 you're making a distinction here between manual versus
6 IOCS process.

7 Q No. No, I'm not. You are. I'm asserting
8 that you established a standard; that is, the
9 recordation of actual postage paid for a piece.
10 You're using that as a criticism for the IOCS results.

11 A Yes, that's fair, although again it's the
12 overall results. I guess the question is do you
13 include the manual periodical checking as part of IOCS
14 or not because in my answer I'm including that.

15 Q Well, we're getting back to the question
16 that I have, which is you've asserted a standard; that
17 is, recordation of actual postage paid, and I'm asking
18 you how that standard can ever be met?

19 A I'm not proposing recordation of revenue.
20 I'm proposing at some point the need to check against
21 actual postage paid just as the Postal Service adopts
22 any number of other attempts to check the periodicals
23 paid.

24 It may extend to contacting the mailers.
25 Again, this is not my proposal as to what the costs

1 are. I'm simply criticizing what you've done because
2 that's the basis of the rate increase.

3 Q Right, and I'm asserting a standard that
4 ought to be applied which can't ever be met.

5 A I disagree.

6 Q Okay.

7 A You have to tell me that, for example --

8 Q How then can it be recorded? How do you
9 find that piece of information?

10 A You would have to think about what in your
11 question I already have. Are you assuming I already
12 have everything that the Postal Service gathers?

13 Q I'm asking how the actual postage paid could
14 be determined so that it could be recorded as part of
15 an IOCS tally.

16 A The process that I envision would ultimately
17 require some sort of checking back to the individual
18 periodicals mailer and his mail statements and his
19 internal records.

20 I understand that the Postal Service already
21 audits such periodicals mailers, and I am envisioning
22 some way in which the data that are maintained for
23 that purpose would be considered.

24 Also, I'm envisioning perhaps even the point
25 of surveys or questions to the mailer that would

1 attempt to focus on the postage paid for that
2 particular mail piece. That's how it could be done.

3 Q Are you familiar with the mailing practices
4 of periodicals mailers?

5 A To some extent. Again, not as much as Mr.
6 Heath is, but yes.

7 Q Do you have enough of an understanding to
8 tell me how a mailer would answer that question, how
9 that mailer would determine the actual postage paid
10 for a specific piece of mail?

11 A Okay. I'm not sure that I would ask the
12 question exactly as you have phrased it.

13 Q Okay.

14 A You're asking me how would I improve the
15 system, and I'm giving you some ideas as to how I
16 would proceed.

17 Q You set up a standard by which IOCS should
18 be evaluated, and I'm trying to get you to focus on
19 how that standard could ever be met.

20 MS. RUSH: Mr. Chairman, I'd like to break
21 in here.

22 Counsel is asking the witness to solve a
23 problem that really is the Postal Service's to solve.
24 The scope of his testimony is to identify flaws in the
25 costing basis, and I think he has.

1 Counsel may not agree with them, but it
2 doesn't necessarily mean that the burden now shifts to
3 the witness to solve the problem.

4 MR. HOLLIES: It's still a fair question,
5 Mr. Chairman. He's asserting that there's a standard
6 that should be applied, and I'm just asking him how it
7 could be applied.

8 CHAIRMAN OMAS: If you can answer the
9 question, would you answer the question, please?

10 THE WITNESS: Again, I am not the Postal
11 Service. I don't have the resources to know precisely
12 what's available to them vis-a-vis abilities to
13 communicate data they may have that we haven't really
14 identified, but what I think is the case is that this
15 problem with not identifying postage paid is a serious
16 one and requires some checking beyond what is now
17 done.

18 I have given you some suggestions as to how
19 that checking ought to be considered.

20 MR. HOLLIES: You have.

21 THE WITNESS: I don't know for a fact that
22 that would solve the problem. Again, I haven't done
23 the analysis.

24 BY MR. HOLLIES:

25 Q You have, and one of those suggestions was

1 to go back to the mailer and ask the mailer what the
2 postage was on that piece. I've asked you to answer
3 the question of how the mailer would do that.

4 A I haven't suggested that as the question.
5 I've suggested we would have to work with the mailers
6 to identify questions that could be answered, which
7 may or may not include the question you've posed.

8 For example, the mailer may not know the
9 postage on a particular piece, but he may know that
10 generally a piece of this timeframe, of this
11 publication, generally would qualify for within county
12 based on some other information that he has or at
13 least could present.

14 That's the kind of thing I'm talking about.
15 It's sort of a cooperative process. There aren't that
16 many tallies here to be considered,

17 Q On pages 5 and 6 of your testimony you first
18 criticize the Postal Service for failing to determine
19 the actual postage paid for a periodicals mail piece
20 and then criticize the verification procedures
21 employed by the Postal Service as "detailed and
22 multidimensional." That would be page 6, lines 12 and
23 13.

24 At least I think the "detailed and
25 multidimensional" is intended as criticism. Is it

1 criticism

2 A I don't believe so. I'm suggesting the
3 process of determining eligibility is complicated.

4 I suppose it's criticism in the sense that
5 you leap into this problem because you don't solve it
6 for the revenue, but once you've made the leap into
7 determining eligibility I think that's a bit of a
8 difficult issue.

9 Q So I take it you still don't have any
10 suggestions on how you think the Postal Service should
11 determine actual postage paid?

12 A Okay. Well, I think we've talked about
13 this, but let me try again.

14 I think that what we are considering is a
15 relatively few number of within county tallies. I
16 think you used the number of **1.93** direct tallies for
17 clerk mail handler costs and in carrier cities.

18 There are within that **193** types of tallies
19 different degrees of concern over the lack of postage.
20 In other words, some of the criterion used on
21 eligibility are probably more judgmental than others,
22 so I would take a look at that, and then I would
23 attempt to see what is available from periodicals
24 mailers to the extent one could follow up on a
25 particular tally from a particular periodical from a

1 particular part of the county and look at data that's
2 going to be far more direct and timely other than, for
3 example, as the Postal Service has done looked at data
4 publications directories from two years ago.

5 I think that there's an awful lot of room to
6 improve here that might not necessarily go to the
7 standard that you continue to attribute to me, but
8 nevertheless could improve the situation.

9 Q When an IOCS data collection technician
10 takes a reading does he or she know what subclass a
11 periodicals piece is within at that time?

12 A I don't believe so, no.

13 Q So if the Postal Service were to follow up
14 on your suggestion, looking as it were to see what
15 information is available or could be obtained, it
16 wouldn't be just for the 190 some odd tallies
17 associated with within county, but it would be for all
18 periodicals tallies. Is that right?

19 BY MR. HOLLIES:

20 A Well not necessarily. It would depend upon
21 how comfortable you are with all the processes leading
22 up to that point. I envisioned it as kind of a final
23 check I guess.

24 Q Are you aware that one of the reasons IOCS
25 was redesigned was to take judgment out of the data

1 collection technician's hands as to the subclass of a
2 piece?

3 A That may be the case. Yes. I think Mr.
4 Bozzo says that in sum and substance.

5 Q I think he does. My point is that we're not
6 talking about 190 some odd detailed checks because you
7 can't isolate within county from outside county at
8 that point in time. We're talking about doing it for
9 7,000 tallies.

10 A I'm telling you I don't think that's true.

11 Q Why?

12 A Because as I envisioned this this is the
13 final check. The Postal Service seeks to impose a 25
14 percent rate increase on within county periodicals and
15 it would just seem to me that In order to avoid that
16 if it were at all unnecessary that it would require
17 additional efforts on the part of being finally sure
18 that those are within county pieces that we're looking
19 at.

20 Q Can we agree that verification of the actual
21 postage paid for a periodicals piece that's sampled in
22 IOCS is not easy?

23 A Sure. I agree it's not easy.

24 Q Can we also agree that regardless of the
25 difficulty you still maintain your criticism and that

1 fa lure to ver fy actual postage paid is in your view
2 problematic?

3 A Yes.

4 Q So once again looking at your logic you
5 identify or create a standard for evaluating IOCS, a
6 standard that is difficult to satisfy and which has
7 not previously been used, then based on the IOCS
8 failure to meet your standard you characterize IOCS
9 within county cost estimates variously as allegations,
10 outlandish, dramatic and consisting of assumptions.

11 Is that an accurate summary of the structure
12 of your criticism?

13 A Not really because I've also criticized a
14 variety of the bases used by the Postal Service to
15 determine within county eligibility, so the failure to
16 understand the revenue is only part and parcel of the
17 total of criticisms that I have.

18 Q On page 7 you reference the Gale and Bowker
19 directories of publications. How much variation do
20 these directories show in the circulations of
21 respected publications from one year to the next?

22 A I haven't looked at the updated directories.
23 I just noted the Postal Service's directories were out
24 of date. I don't know that I would use directories at
25 all for that matter. Another problem that I've

1 identified is that circulation is supposed to be
2 determined on an issue by issue basis.

3 Q We'll get to that, too.

4 A Okay.

5 Q How much do periodical circulations
6 typically vary from year to year?

7 A I don't know typically how much they vary
8 from year to year.

9 Q In Section 6(d), page 10, you claim that the
10 Postal Service has, "no data", as to the real costs of
11 within county periodicals.

12 A I'm sorry. What page was that?

13 Q Ten.

14 A Page 10. Yes. I'm sorry. Could I have the
15 question again?

16 Q I was just summarizing what you said and
17 you've now looked at it. I'm figuring out which way
18 I'm going to go with it. I think we've talked about
19 the number of tallies that underlie within county
20 periodicals IOCS costs. You lodge various criticisms
21 of the tallies based on what you describe as various
22 coding problems with those tallies.

23 How many of those tallies underlying within
24 county costs have the earmarks of one of those coding
25 problems you criticize?

1 A Can you give me reference? I'm not sure
2 what you mean by my reference to coding problems.

3 Q That's fair enough. I'm talking about pages
4 5 to 10 of your testimony, that is Section 6, which
5 your heading for that section is the USPS's failure to
6 identify actual within county periodicals.

7 A Yes. Okay. I have it.

8 Q So I'm asking how many of the 197 tallies
9 underlying within county costs suffer from one of the
10 shortcomings you identify in that section of your
11 testimony?

12 A It's not clear how many suffer. Potentially
13 all of them. For example the Postal Service has
14 failed to study circulation on an issue by issue
15 basis. Has no data. That potentially means all the
16 circulation counts for every one of the 197 is off. I
17 don't know how many were actually off. I don't have
18 the data either.

19 Q Wouldn't that depend upon the volatility in
20 circulation counts?

21 A Yes.

22 Q So if there's no volatility the criticism
23 doesn't hold any water, does it?

24 A But you don't know and I don't know that
25 there's no volatility. The Postal Service makes it

1 cle r to mailers th t eligibility is based on an issue
2 by issue basis.

3 Q We'll be getting to that.

4 A All right.

5 Q So you don't know how many tallies suffer
6 from the problems that you identified?

7 A And neither does the Postal Service.

8 Q Please assume as is factually correct that
9 different IOCS instruments underlie IOCS estimates of
10 within county costs for fiscal years 2004 and 2005.
11 Let's further assume that the new IOCS instrument is
12 acknowledged as being better, that is the new
13 instrument improves the allocation of costs to
14 products or subclasses.

15 If there are also changes in within county
16 volume between fiscal year **2004** and fiscal year 2005
17 how can one isolate changes in cost allocations to
18 subclasses due to the volume changes from those due to
19 the new instrument?

20 A Well, I guess you've asked me to assume that
21 the new instrument is better, so if I assume that I
22 don't know why one needs to separate those changes in
23 the first place. In other words then you could simply
24 focus on volume changes.

25 Q Well, would you agree that the Postal

1 Service concluded when putting together its request in
2 this case that the new IOCS system was improved, but
3 that changes that might be due to that new IOCS
4 instrument warranted coverage in direct testimony?
5 Would you agree?

6 A I would agree that the Postal Service
7 described the changes. I don't know that they
8 precisely said it's improved, but I suppose they did.

9 Q I believe if you look in USPS-ST-1 and 46
10 you might find several examples of that.

11 A Okay.

12 Q Well, I'm about to pile on on this question,
13 so rather than getting stuck here I'll give it a
14 chance to get stuck on the next one.

15 A Okay.

16 Q If we further assume that there are changes
17 in the mix of within county shapes between FY 2004 and
18 2005 how can we isolate changes in cost allocation to
19 subclasses from shape changes, and from the volume and
20 from the instrument change?

21 A That would be more difficult to do. You're
22 talking about changes between 2004 and 2005?

23 Q Yes.

24 A Yes. That would be difficult to do.

25 Q Further -- we're not done yet -- if changes

1 in operations also occur & do we base those on
2 from the three other sources of change?

3 A Presumably your changes would be picked up
4 in your improved IOCS or are these outside of the IOCS
5 entirely? In other words improved operational changes
6 ought to result in different taily counts I would
7 think.

8 Q Well, one would like to think that perhaps
9 the operational changes are made for reasons of
10 efficiency and that as a result costs might decrease.
11 Is that a fair statement?

12 A You're asking me if that's a fair statement
13 in general? Yes.

14 Q In your opinion which of these factors
15 impact the reported changes in IGCS costs for within
16 county periodicals between **FY 2004** and **FY 2006**?

17 A Of all of these changes? I don't know that
18 I have attempted to isolate each change. My reading
19 of the Postal Service testimony suggests that the
20 Postal Service believes overwhelmingly the changes
21 were caused by the instrument change in fiscal 2005,
22 so I would think that is the dcminant cause.

23 In fact I think Mr. **Bozzo** had an analysis of
24 this which basically could prove that far and away the
25 fiscal **2005** instrument changes resulting in the higher

un costs were muc more import than c h r issues.

2 Again, I don't know that he studied mixes.

3 Q I'm not sure I'd agree with you to the
4 extent you're taking those, but he does address the
5 issue. Yes. Where in your combination of Witness
6 Shaw's **IOCS** data and Witness Ziegler's **IOCS** data do
7 you take account of changes caused by the change to
8 the new instrument?

9 A I don't. That's the concern is that the new
10 instrument is driving those costs.

11 Q Please take a look at your response to
12 **USPS/MMA-T3-19, Part B.**

13 A I have it.

14 Q Part B of this interrogatory asked if you
15 could cite to authoritative sources supporting your
16 aggregation of FY 2004 and FY 2005 IOCS data. Is that
17 correct?

18 A Yes.

19 Q Does the fact you identify no authoritative
20 sources in your response mean that you were unable to
21 find any?

22 A I believe we provided in another
23 interrogatory authoritative responses to step by step
24 sampling processes. I think, I don't know that
25 there's statistical literature that focuses as

1 precis ly on postal fiscal year cost determination as
2 I interpreted this question to ne asking, but I think
3 we gave you a cite in an earlier response to the
4 general notion of pooling in the way I proposed.

5 Q Could you find that for me, please?

6 A Sure. Actually, it might have been in my
7 testimony. If you look at page 17 of my testimony
8 there are some quotes to or taken from a book entitled
9 Sampling Design and Analysis written by Sharon L.
10 Lohr, L-O-H-R, and the quote there comes from her
11 description of what she calls sequential sampling
12 which is used in a case such as this one where there
13 are members of a rare population that are not being
14 captured frequently in the normal sampling process.

15 Q In that situation the first sampling in the
16 sequence is used to improve the results in the second.
17 Is that right?

18 A I believe that's actually explained, so yes.

19 Q How does your combination of IOCS data
20 follow that model?

21 A Because we are improving the sample size, in
22 effect we're more than doubling the sample size, and
23 we are downplaying the possible defects or errors
24 brought about by the Postal Service's change in its
25 IOCS instruments.

1 Q I disagree, but we'll save that for brief.
2 Please turn to your response to Postal Service
3 interrogatory to you 5(b) .

4 A No. 5(b) . I have it.

5 Q That question poses a fairly simple question
6 about the fact that within county rates are lower than
7 outside county rates meaning that as is generally true
8 in all subclasses mailers will pay a lower rate if
9 they can, situ paribas. Your answer however states,
10 "I believe that such an incentive exists for eligible
11 pieces but I have not attempted to confirm its
12 existence".

13 A Yes.

14 Q Could you explain your understanding of the
15 question?

16 A I guess the question as I read it differed
17 from the question you've just asked me. The question
18 you've just asked me assumes situs paribas. I don't
19 know that I interpreted this interrogatory as assuming
20 situs paribas and what I was referring to was the
21 general fact that periodicals mailers face different
22 incentives or additional incentives beyond the pure
23 price incentive as Mr. Heath testified about earlier
24 today.

25 There are reasons that periodicals mailers

1 want to have circulation in places that would require
2 them to pay outside county rates much as they may not
3 want to pay outside county rates. I guess I didn't in
4 this question sense that there was that situs paribas
5 assumption.

6 Q Okay. What would your answer be if as I did
7 in my paraphrase I reinsert or I insert for the first
8 time the situs paribas?

9 A Yeah. Well, situs paribas such an incentive
10 would exist. All else equal you would want to go for
11 lower postage rather than pay higher postage, again
12 all else equal.

13 Q For the record I've asked you questions
14 about a number of tallies in IOCS for within county
15 I think I was using the number of 197, and you were
16 using 193 and I think you're probably right.

17 A No. You used 193 as well. It is 193,
18 though.

19 Q All right. Thank you. Please turn to your
20 response to Question 6(b) from the Postal Service.
21 That would be USPS/MMA-T3-6(b).

22 A Yeah. I have it.

23 Q This question is again straightforward
24 asking you whether an error in one of the 193 IOCS
25 tallies which within county IOCS costs are based would

1 affect on average 1/193 of within county IOCS costs?
2 You answered no. Approximately what portion of within
3 county IOCS costs would on average be affected?

4 A I don't know that I have studied that
5 percentage, but that's why I answered no.

6 Q Well, this is a fairly straightforward
7 proposition. I'm wondering why --

8 A Because you've asked me for the overall cost
9 effect on within county periodicals in total and yet
10 here on the tallies we're only talking about mail
11 processing costs and city carrier and office costs for
12 within county, and so what I'm worried about with a
13 simple yes answer is that this question doesn't
14 address the nonmail processing and in office cost
15 segments.

16 Q Okay. So if the question is restated and
17 refers not to the estimated costs of within county
18 periodicals but to the estimated IOCS costs of within
19 county periodicals what would your answer be?

20 A I don't know that I'd accept even IOCS
21 costs. I mean, my problem is there are other cost
22 segments that may be affected by this change. It just
23 is odd for me to calling them IOCS costs because
24 they're really costs in other segments

25 Q Is it not correct that IOCS is used to both

1 quantify costs in plants and by city carriers in
2 office that are attributed to products, to subclasses?

3 A Yes. That's true. I'm not trying to be
4 difficult. The problem here is you have direct
5 tallies which is what we're talking about and then you
6 have other allocations based on those direct tallies
7 that occur in other cost segments than what we're
8 studying and I don't know that it's all linear as I
9 sit here.

10 Q Well, let me limit the question then to what
11 you characterize as the direct costs measured by IOCS
12 and not costs that are distributed to products based
13 on proportions of IOCS tallies. Would your answer be
14 yes if we changed the question to apply only to the
15 direct IOCS costs for within county periodicals?

16 A Yes. I believe with that correction that
17 would be fine.

18 Q Thank you. I wasn't trying to be difficult
19 either. Please turn to the next, that is Postal
20 Service Question No. 7 to you.

21 A I have it.

22 Q I think we were in agreement that as a
23 general matter if a periodicals mailer has a choice of
24 paying outside county or within county postage that
25 mailer would normally choose the lower postage. Is

1 that right?

2 A Again, all else equal which may or may not
3 be the normal situation.

4 Q Just as a matter for the record take a look
5 at the second to last word on page 1 of this response
6 and tell me if you think there's a typo in that word?
7 The word on my copy is quality.

8 A Qualify. I'm sorry.

9 Q That should be qualify?

10 A Qualify. Yes.

11 Q Thank you.

12 A I did not catch that one.

13 Q Let's move on to Question No. 8 to you.
14 That would be USPS/MMA-T3-8.

15 A I have it.

16 Q In response to this interrogatory you state
17 that you have no data on the issue to issue
18 eligibility for within county rates. Is that correct?

19 A That's true.

20 Q Do you have any experience dealing with
21 within county mailers?

22 A I've certainly spoken to Mr. Heath on a
23 number of occasions as well as Ms. Rush, who is also a
24 mailer as I understand it.

25 Q Are you the recipient, are you a subscriber

1 to any such publications?

2 A I am not a subscriber. I am on occasion a
3 recipient. I live in Alexandria and I do get weekly
4 papers delivered to my home.

5 Q Do you claim to have any expertise regarding
6 within county mailers?

7 A I have expertise in assessing the basis upon
8 which the rate proposal to within county mailers **was**
9 developed and I've also reviewed such things as this
10 handbook that's cited in this answer to inform me
11 additionally as to how eligibility is determined.
12 Beyond that I have no additional expertise.

13 Q Okay. You're jumping about 10 questions
14 ahead. We'll get there.

15 A Okay.

16 Q What about expertise regarding use of the
17 mail by within county mailers? Do you have any?

18 A Just that I've picked up in discussions with
19 people like Mr. Heath and other mailers.

20 Q Is it safe to say that your background and
21 experience do let you understand that within county
22 mailers routinely mail periodicals pieces to their
23 subscribers?

24 A Well, I have done quite a bit of work in a
25 variety of media including newspapers more generally,

1 so sure I understand at some level of detail
2 advertising versus subscription requirements for
3 newspapers.

4 Q I would hope that you understand that some
5 subscribers to within county periodicals are located
6 in the same county as that mailer?

7 A Yes, I understand that.

8 Q Do within county mailers need to maintain a
9 list of subscribers?

10 A Certainly they have business needs to
11 maintain such a list. Whether they have a Postal
12 Service requirement for that I'm not certain.

13 Q Would you think it's safe to assert that
14 within county mailers generally seek to increase the
15 number of their subscribers?

16 A Again, all else equal. yes, they would like
17 to do that. They would not give away the subscription
18 prices necessarily to achieve that however.

19 Q That's goes to the nominal rate which
20 recently changed, but that's an aside.

21 A Well, I'm talking about the subscription
22 rate for the newspaper.

23 Q I understand. How much does the subscriber
24 list for a within county mailer change from one
25 mailing to the next?

1 A I don't know the answer to that question
2 which I think you asked me already.

3 Q Do you think that such changes would likely
4 involve a large proportion of a within county mailer's
5 subscribers?

6 A I don't know.

7 Q Well, I think it's fairly intuitive. For
8 the most part within county newspapers such as those
9 that Mr. Heath talked about earlier are serving the
10 local community of interest and typically they are
11 sustained by having a regular group of subscribers
12 from the local area. If the mailers saw a great deal
13 of volatility in subscribers they might not have a
14 business that was a going affair. Does that sound
15 fair?

16 A Well, I suppose it would depend upon the
17 general trend in the volatility. In other words I
18 could imagine that there would be a large reduction in
19 subscribers if the newspaper increased subscription
20 prices say, so there would be that volatility and
21 whether or not that was a profitable thing to do or
22 not would be based on the economics of the newspaper.

23 Q Sure and you're probably not going to see
24 much in the way of subscription price changes on
25 successive issues, right?

1 A Well, but at some point there will be a
2 change and from that point forward there will be new
3 subscription prices and a new number of subscribers.

4 Q I can appreciate that, especially as an
5 economist. That's one of the classic things that you
6 might be looking at in response to a price change, but
7 I'm really trying to get at here what I think you can
8 agree with me on and that is that on the whole the
9 number of subscribers is going to be relatively stable
10 over time.

11 There may be such events such as a
12 subscription price change that induce a change in the
13 number of subscribers, but you're not going to lose 20
14 percent of your subscribers between Issue 1 and Issue
15 2 and then get 40 percent of them back again between
16 Issue 2 and Issue 3. Does that sound fair?

17 A Well, you're asking me on the whole and
18 relatively stable. I mean, these are things that
19 neither of us know and that's the concern with using
20 them in the costing. I certainly would agree that is
21 unlikely, but I don't have a basis for reaching that
22 conclusion and my concern is neither does the Postal
23 Service and yet you're making that assumption and
24 imposing these rates.

25 Q Well, I did ask you a while back about

1 whether you had looked at issues of the Gale Bowker
2 directories to see whether they show volatility in the
3 circulation counts for respected papers and you had
4 not checked that. Is that correct?

5 A I looked at the directories or at least one
6 of the directories and I am aware that the directories
7 show a single annual figure for circulation, so you
8 don't have in the directories issue by issue
9 circulation at any rate. So having looked at the
10 directories is still not going to answer the question
11 how much volatility is there on an issue by issue
12 basis?

13 Yet that is how the eligibility is
14 determined. I mean, in a nutshell that's my
15 criticism.

16 CHAIRMAN OMAS: Mr. Hollies, could you tell
17 us about how much longer you have with this witness
18 approximately?

19 MR. HOLLIES: Fifteen to 20 minutes.

20 CHAIRMAN OMAS: Okay. Well, then we'll just
21 go afoot and finish that before the lunch break.
22 Thank you very much, Sorry to interrupt.

23 BY MR. HOLLIES:

24 Q If as you say those directories record a
25 single number for annual circulation were you to look

1 at earlier examples, earlier annual issues of one of
2 those directories and see that the annual numbers
3 jumped around a lot for publications that would be
4 some indication of volatility in the circulation
5 numbers, would it not?

6 A Perhaps, but again it's really not going to
7 tell you much since we're talking about weekly
8 newspapers that have 52 issues.

9 Q No. I'm talking about year to year
10 volatility. I'm not talking about issues.

11 A All right. Okay. I understand that. So it
12 would tell you that there might be or might not be
13 some volatility.

14 Q Thank you. Now, at the end of your response
15 to this interrogatory, we're still here on No. 8, you
16 point to Postal Service Handbook **DM104** which is
17 entitled Handbook For *Applying For* Periodicals Mailing
18 Privileges. Is that right?

19 A It's **DM204**.

20 Q I'm sorry. It is. I wrote 104, but it is
21 204. Thank you.

22 A Yes.

23 Q With that correction?

24 A Yes.

25 Q You include in your response a quotation

1 from an appendix in that handbook. Is that correct?

2 A I believe so. Yes. Appendix B.

3 Q Appendix B?

4 A Yes.

5 Q My colleague is currently handing out copies
6 of Appendix B to Handbook DM204. While we're waiting,
7 Mr. Siwek, if you would compare the quotation in your
8 answer with the actual words on the form that would be
9 helpful.

10 A I have it. Yes.

11 Q Do you see any typographic errors in your
12 quote?

13 A Yes. I had the word remain.

14 Q Which should be remains?

15 A Remains. Yes.

16 Q There's actually another, although it's not
17 substantive. In the first occurrence of in county you
18 do not capitalize the first Nand in the second
19 instance you do capitalize --

20 A Yes. That's right.

21 Q Okay. Now, as a general matter what happens
22 to a publisher who falsely claims within county
23 eligibility?

24 A I believe that there are audit provisions
25 and penalty provisions including paying back I believe

1 what was owed to the Postal Service, but I don't have
2 more specific details on that. I'm sure Mr. Heath
3 would know that.

4 Q Yes, and Mr. Heath touched on that briefly
5 this morning and was amused to hear that the 10
6 percent limit is not avidly enforced. Somehow I
7 thought that it was, but it was interesting to hear.
8 I'm asking my colleague to hand out another item.
9 This is a portion of the *Domestic Mail Manual*, Section
10 707.11.3.3 which is actually on the second page. I
11 believe it was on the second page.

12 I didn't keep a copy here. Section
13 707.11.3.3. is entitled nonsubscriber copies.

14 A I have it.

15 Q There is an aspect of mail piece eligibility
16 for within county rates that is cumulative across
17 issues. Isn't that right?

18 A I believe that's true. Yes.

19 Q This section, that is DMM 707.11.3.3,
20 establishes a limit or ceiling on the number of
21 nonsubscriber copies that may be entered at within
22 county rates during a calendar year. Is that right?

23 A I believe that's correct. Yes.

24 Q So for a prudent within county mailer to
25 know whether that limit is approached or exceeded the

1 mailer must keep records of cumulative totals. Does
2 that sound about right?

3 A Yes.

4 Q Indeed we heard from Mr. Heath this morning
5 that sometimes a newly acquired newspaper does not
6 exhibit this particular trait. ■ believe he stated
7 that.

8 A I believe that's what he said. Yes.

9 Q Indeed a prudent within county mailer also
10 needs to be aware of the limit embodied in DMM Section
11 707.7.0 which we know if only because it's mentioned
12 there at the bottom of not the DMM 707.11.3.3 the
13 nonsubscriber copies section. Is that correct?

14 A I'm afraid you lost me there with the
15 quotes.

16 Q Okay. I think that DMM Section 707.7.0 is
17 mentioned within the body of the first handout that's
18 707.11.3.3 entitled nonsubscriber copies?

19 A I guess I don't see it on this page. There
20 we are. 212.4, that's requestor publication. I don't
21 think that's what you mean.

22 Q All right: I'm looking at page 1368 in the
23 lower left-hand corner.

24 A Okay.

25 Q The second section from the bottom,

1 nonsubscriber copies --

2 A Yes?

3 Q -- cross-references a 10 percent allowance
4 under 7.0.

5 A Yes. I see that.

6 Q Okay. Though it may not necessarily be
7 obvious if don't know DMM nomenclature that's a
8 reference to 707.7.0.

9 A Okay.

10 Q So we know that there is another limit. I
11 mean, I could share with you copies of that other
12 section, but it's not really that constructive. As
13 indicated in 11.3.3 there's a 10 percent allowance in
14 terms of the total number of nonsubscriber copies
15 mailed at in county rates over the period of a year
16 and there's also a 10 percent allowance in that other
17 section that also needs to be attended to.

18 So to reprise for a moment we agreed a while
19 back that your response to Postal Service Question No.
20 8 quotes from Appendix B of Handbook 204, correct?

21 A Yes.

22 Q Now, looking at Appendix B would you agree
23 that its purpose is verifying that subscriber copies
24 also known as paid circulation are eligible for within
25 county rates?

1 A Yes.

2 Q Now, I think Appendix B could help you
3 answer this, although it may not be necessary. In
4 your experience with periodicals mailers have you come
5 across any situations in which eligibility for within
6 county rates bounced back and forth from issue to
7 issue, perhaps eligible in month one, ineligible in
8 month two, then eligible again in month three? Have
9 you ever seen something like that?

10 A I personally have not. No.

11 Q You quote from Appendix B in your response
12 to Postal Service Interrogator] No. 8 because the
13 question inquires about issue to issue eligibility for
14 within county rates. Is that right?

15 A Yes.

16 Q Appendix B addresses situations in which
17 paid subscriber copies may not retain eligibility for
18 within county rates. Is that right?

19 A That's correct.

20 Q Now, do the questions you raise in your
21 testimony about whether specific pieces sampled by
22 IOCS are eligible for within county rates, do those
23 involve subscriber copies or nonsubscriber copies?

24 A Both. Postal Service has studied neither.

25 Q Well, I would submit to you that you

1 actually talk about nonsubscriber copies in your
2 testimony.

3 A Well, I cite Appendix B which I think we
4 both agreed were talking about circulation.

5 Q Yes, and you got interrogatories from the
6 Postal Service about the fact that nonsubscriber
7 copies can be entered at within county rates up to the
8 maximum specified in this section of the DMM called
9 nonsubscriber copies. Is that right?

10 A Yes.

11 Q Would you agree that perhaps the purpose in
12 the Postal Service asking you those questions was to
13 get you to agree that as long as the 10 percent limit
14 was not exceeded those nonsubscriber copies could be
15 answered at within county rates?

16 A I don't know what the Postal Service
17 intended with that question.

18 Q Okay. Well, if I tell you that was the
19 intention does that sound reasonable to you?

20 A I suppose. Yes. Which answer was this
21 again?

22 Q There were several. I wasn't going to the
23 specifics.

24 A Okay.

25 Q My point is that Appendix B deals with

1 subscriber copies and the issues that you raise in
2 your testimony, the questions that had tried to raise
3 about the IOCS sample pieces, relate solely to
4 nonsubscriber copies.

5 A Well, that's not my intention. I'm pointing
6 out that the Postal Service has not gathered data on
7 subscribers on an issue by issue basis. Separate and
8 apart from that the Postal Service has not gathered
9 data on nonsubscribers.

10 Q Why does the Postal Service need data on
11 subscribers?

12 A It needs data to maintain eligibility as we
13 see in Appendix B.

14 (Pause)

15 Thank you I have no further questions.

16 CHAIRMAN OMAS: Thank you, Mr. Hollies. Is
17 there anyone else who would like to cross-examine
18 Witness Hollies. Ms. Rush, would you like some time
19 with your witness?

20 MS. RUSH: Mr. Chairman, I think we can wrap
21 up before lunch if you'll give us five minutes and
22 five minutes of redirect.

23 CHAIRMAN OMAS: I'm sorry I didn't ask the
24 bench -- the permission to go away is the question.

25 MS. RUSH: But thank you. The previous

1 witness had thought it might be possible to improve
2 the ICOS data by actually scanning in the addresses
3 that the piece was marked for and therefore being able
4 to identify more accurately whether it was in-county
5 or outside county. Do you have an opinion on that?

6 MR HOLLIES: I have not personally studied
7 that question. That could be addressed by
8 understanding in some detail how the destination
9 location is put into the ICOS. I have not explored
10 that particular question but whether or not it could
11 be improved or not would depend on whether it's
12 inadequate at this point and that's at least one area
13 that I haven't really criticized.

14 CHAIRMAN RUSH: Thank you.

15 CHAIRMAN OMAS: Ms. Rush?

16 MS. RUSH: Yes, Mr. Chairman. We would like
17 to endeavor to complete before lunch. We'll have some
18 very short redirects and I'd like about five minutes,
19 please?

20 CHAIRMAN OMAS: *Very* good. Ms. Rush, before
21 we begin with redirect, I just would like to ask Mr.
22 Hollies much earlier the possibility of revising your
23 response to a designated interrogatory was mentioned.
24 Would you please provide any such revision to the
25 Commission within seven days, please?

1 MR. HOLLIES: Of course. Absolutely.

2 CHAIRMAN OMAS: Ms. Rush, would you please
3 proceed.

4 MS. RUSH: Thank you, Mr. Chairman. And in
5 fact we will have no redirect.

6 CHAIRMAN OMAS: Oh, thank you very much.
7 Well, at that point, we will break for lunch and why
8 don't we come back at let's say 1:30. Thank you.

9 (Whereupon, at 12:20 p.m., the hearing in
10 the above-entitled matter was recessed, to reconvene
11 at 1:30 p.m. this same day, Monday, November 6, 2006.)

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1 testimony?

2 A Two minor changes. -- draft of the letter.

3 CHAIRMAN OMAS: Your mic, please?

4 THE WITNESS: Okay. Thought the green light
5 was on. Professor Kelegian had originally drafted an
6 appendix to my testimony. Upon a ruling by Commission
7 that was changed to direct testimony by Professor
8 Kelegian. Then secondly in order to make my testimony
9 consistent with an answer that I gave to an
10 interrogatory from DMA I estimated revenue losses for
11 two different versions of my proposal for GCA, one
12 under linking and one under delinking.

13 BY MR. HORWOOD:

14 Q Are those the changes that are reflected in
15 the revised testimony?

16 A Yes, they are.

17 Q Do you have any other changes as a result of
18 a matter that was called to our attention this morning
19 by Mr. Koetting?

20 A Mr. Koetting is correct on that. There is a
21 typo in connection with an elasticity and his
22 correction is correct. It should be .07, not .7.

23 Q Are those on page 8, lines 6 and 8?

24 A Yes.

25 Q With those changes would your testimony if

1 given today be as indicated in the direct testimony?

2 A Yes.

3 Q Do you sponsor Library Reference LR-L-2
4 which is a Category II library reference?

5 A Yes.

6 MR. HORWOOD: Mr. Chairman, I would like to
7 have Dr. Clifton's testimony and library reference
8 admitted into evidence. The changes he indicated this
9 afternoon have been physically made on the testimony.

10 CHAIRMAN OMAS: Is there any objection?

11 Mr. Levy, put your mic on.

12 MR. LEVY: I have a question of
13 clarification of either counsel or the witness. The
14 corrected number on lines 6 and 8 of page 8 is what?
15 I didn't hear the corrected number.

16 THE WITNESS: It should read on line 6, Mr.
17 Levy, .07, not .7.

18 MR. LEVY: Thank you.

19 CHAIRMAN OMAS: Without objection, Mr.
20 Horwood, would you please provide the reporter with
21 two copies of the corrected direct testimony of James
22 A. Clifton. That testimony is received into evidence.
23 However as is our practice it will not be transcribed.

24 //

25 //

1 (The document referred to,
2 previously identified as
3 Exhibit No. GCA-T-1, was
4 received in evidence.)

5 CHAIRMAN OMAS: Mr. Clifton, have you had an
6 opportunity to examine the packet of designated
7 written cross-examination that was made available to
8 you in the hearing room today?

9 THE WITNESS: Yes, I have.

10 CHAIRMAN OMAS: If those questions in that
11 packet were posed to you orally today would your
12 answers be the same as those you provided previously
13 in writing?

14 THE WITNESS: Yes, they would.

15 CHAIRMAN OMAS: Are there any additions or
16 corrections you'd like to make to those answers?

17 THE WITNESS: Not at this time.

18 CHAIRMAN OMAS: Okay. Counsel, would you
19 please provide two copies of the corrected designated
20 written cross-examination of Witness Clifton to the
21 reporter. That material is received into evidence and
22 is to be transcribed into the record.

23 //

24 //

25 //

1 (The document referred to was
2 marked for identification as
3 Exhibit No. GCA-T-1 and was
4 received in evidence.)

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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

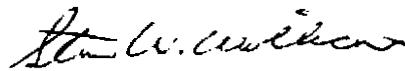
Postal Rate and Fee Changes, 2006

Docket No. R2006-1

DESIGNATION OF WRITTEN CROSS-EXAMINATION
OF GREETING CARD ASSOCIATION
WITNESS JAMES A. CLIFTON
(GCA-T-1)

Party	<u>Interrogatories</u>
Alliance of Nonprofit Mailers	DMA/GCA-T1-1-9 NAA/GCA-T1-1, 5 USPS/GCA-T1-2-3, 9, 20-21, 40-41, 45-46, 49-50, 52, 55, 72, 84, 87, 89
Newspaper Association of America	DMA/GCA-T1-7-8 NAA/GCA-T1-1-5
United States Postal Service	USPS/GCA-T1-1-62, 63a, 64-65, 67-70, 72-95

Respectfully submitted,



Steven W. Williams
Secretary



Interrogatory

USPSIGCA-TI-93

USPSIGCA-TI-94

USPSIGCA-TI-95

Desianatina Parties

USPS

USPS

USPS



REVISED OBJECTION AND RESPONSE OF GREETING CARD ASSOCIATION
 WITNESS CLIFTON TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION
 Revised: October 20,2006

DMA/GCA-T-1-1. Please assume for the purpose of responding to this interrogatory that your proposed rates for First-class Single-Piece Letter Mail were accepted by the Postal Rate Commission.

- a) How much revenue would be lost in First-class Single-Piece Letter Mail as compared to the rates proposed by the Postal Service?
- b) Please calculate the implicit coverage for First-class Single-Piece Letter Mail under your proposed rates.
- c) Please calculate the average rate increase for First-class Single-Piece Letter Mail under your proposal.
- d) Please confirm that you propose collecting the revenue lost from First-Class Single-Piece Letter Mail from Standard Regular Mail.
- e) Please calculate the coverage for Standard Regular Mail under your proposal.
- f) Please calculate the average rate increase for Standard Regular Mail under your proposal.
- g) Do you have recommendations as to how the increase in Standard Regular Mail rates should be distributed among letters, flats, and parcels? If so, please provide them and your rationale.
- h) Does your proposal apply to all shapes in First-Class Single-Piece Letter Mail or only to a selected set of shapes? If only to a selected set, please specify the shapes to which it applies.

RESPONSE:

a.-c. and e.-g. To answer your questions would require me to re-do the entire Thress forecasting model in LR-L-66, not **just** the single piece demand equation that I did re-estimate. Such a large task was and is beyond the scope of my testimony. What is clear from my testimony, however, is that witness Thress' model does not produce reliable results for ratemaking purposes for single piece First Class letters.

d. Confirmed.

h. **USPS** witness Thress' own price demand elasticities are based on data for "all shapes". **My** proposal is limited to First Class single piece letter mail and Standard A Regular letter mail.

REVISED OBJECTION AND RESPONSE OF GREETING CARD ASSOCIATION
WITNESS CLIFTON TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION
Revised: October 20, 2006

DMA/GCA-T-1-2. Please assume that the Postal Rate Commission accepted your proposal for First-class Single-Piece Letter Mail, but also decided that the overall coverage for First-class Mail Letters as proposed by the Postal Service was correct.

- a) Please confirm that this would result in an increase in rates for Presort Letters.
- b) Please confirm that you have sponsored testimony on behalf of the American Banker's Association in this case.
- c) Please confirm that banks use First-class Presort Mail for both operational and marketing purposes.
- d) Would banks that use First-class Presort Mail for statement and marketing pay increased postage under this scenario?
- e) Do you believe that banks would be pleased with this outcome? Please explain any affirmative answer.

RESPONSE:

- a. Not confirmed. I stated in my testimony for GCA at page 58, lines 16-21. I had all First-class Automation Presort rates be **set at** the levels proposed **by** the Postal Service in this case. Your hypothetical is in my view inconsistent with de-linking First Class workshared rates from single piece rates. With de-linking in First Class, the Postal Service has emphasized separate unit cost contributions made to institutional costs, not any single overall cost coverage. Across classes, as I state in my testimony for GCA at page 59, lines 4-13, not only is there a substantial gap of well over a dime between the low unit cost contribution of Standard A Regular Mail and the high unit cost contribution of First Class single piece mail. That gap has increased by 1.5 cents since the last litigated rate case according to an interrogatory response provided by USPS witness O'Hara..
- b. Confirmed that I have sponsored testimony on behalf of the American Banker's Association for automation First Class presort letter rates only, and not for any other rates.
- c. Please **see** my answer to 3.b. below.

- d. Please see my response to a.
- e. GCA objects on grounds of relevance, burden and harassment to discovery on what witness Clifton “believe[s]” with respect to matters that he has not opined on in his GCA testimony. Without waiving its objections, GCA provides witness Clifton's response as follows: Please see my response to a.

REVISED OBJECTION AND RESPONSE OF GREETING CARD ASSOCIATION
WITNESS CLIFTON TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION
Revised: October 20, 2006

DMA/GCA-T-1-3. Please assume that the Postal Rate Commission accepted your proposal for First-class Single-Piece Letter Mail to reduce the price by a penny, shifting the resulting burden to Standard Regular.

- a) Please confirm that banks also use Standard Regular Mail for marketing mail. If you are unable to do so, you may wish to refer to various NSA testimony in which banks discuss their use of Standard Regular Mail for marketing.
- b) Do you believe that banks would be pleased with this outcome? Please explain any affirmative answer.

RESPONSE:

- a. In terms of material use, confirmed for some very large banks
- b. GCA objects on grounds of relevance, burden and harassment to discovery on what witness Clifton "believe[s]" with respect to matters that he has not opined on in his GCA testimony. Without waiving its objections, GCA provides witness Clifton's response as follows:

The banking industry, if not each and every individual bank, should be pleased with such an outcome. I do not represent any individual banks. I represent ABA, the industry trade association representing small, medium-sized, as well as large banks. From the latest publicly available reliable data I have seen, a majority of the banking industry's mail volume in First Class continues to be mailed at the full single piece rate. This probably reflects the fact that banks outside of urban and suburban areas do not necessarily have access to a presort bureau and do not have enough mail volume to warrant leasing or purchasing automation machinery. Less than 6% of the banking industry's volume of mail and cost of mail is posted at Standard A Regular Rates according to the publicly available reliable data I have seen. This latter figure may have increased in very recent years despite the NSAs, but I do not have any reliable data source to confirm that. In any event I do not represent ABA or any banks on Standard A Regular rates, as is clear from my answer to 2.b. above.

REVISED OBJECTION AND RESPONSE OF GREETING CARD ASSOCIATION
WITNESS CLIFTON TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION
Revised: October 20, 2006

DMA/GCA-T-1-4. Please consider how banks market their credit cards

- a) **As** an economist, would you agree that it would be rational for them to evaluate the efficiency of alternative marketing channels? Please fully explain any disagreement.
- b) As an economist, would you agree that if prices of Standard Regular Mail increase relative to the prices of alternative marketing channels. some marketing will shift to the alternatives. all **else** being equal?

RESPONSE:

a. and b. Yes. However, the present mix of marketing mail between First **Class** and Standard A Regular is in my opinion as an economist due to incorrect relative price signals being sent to such mailers. First Class mail pays a disproportionate share of the Postal Service's delivery costs (attributable plus "institutional"), **so** marketing mail that would be sent by First Class under correct relative price signals **is** instead sent by Standard A Regular rates. which are artificially low because of the delivery cost subsidy they receive. In recent years. NSAs were formed in part to reduce the flow of such marketing mail from First Class to Standard A Regular caused by the relative rate problem. Profit maximizing or cost minimizing firms, if rational, **will** always take advantage of such rate disequilibria. To date, I do not believe the NSAs have solved this fundamental relative rate problem.

REVISED OBJECTION AND RESPONSE OF GREETING CARD ASSOCIATION
WITNESS CLIFTON TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION
Revised: October 20, 2006

DMA/GCA-T-1-5. You estimate the elasticity of First-class Single-Piece Letter Mail to be -0.456. GCA-T-1 at 3.

- a) Please confirm that if some segments of this mail stream are more elastic than this, others must be less elastic. If you do not confirm, please explain fully.
- b) Please confirm that if rates increased from their current level to 43 cents and your elasticity is correct, Postal Service revenues would increase all else being equal. If you do not confirm, please explain fully.
- c) Please confirm that if rates increased from their current level to 43 cents and your elasticity is correct. Postal Service costs would decrease all else being equal. If you do not confirm, please explain fully.
- d) Please confirm that with increased revenues and decreased costs, the contribution to overhead would increase all else being equal. If you do not confirm, please explain fully.

RESPONSE:

- a. Confirmed, with the caveat that the Postal Service is losing substantial volumes of single piece mail such as bill payments in areas that appear to me to be the more elastic areas, an outcome that raises "the contribution to overhead" that Standard A Regular mailers as well as First Class letters subclass mailers end up paying. Under current market conditions, when the Postal Service refuses to compete on price as aggressively for single piece mail as it does for other mail, every mailer ends up losing.
- b. and c. Confirmed that raising the rates of any inelastic rate category, including Standard A Regular, will lead to higher revenue and reduced costs. What my elasticity findings make clear, however, is that it is relatively easier to raise rates on Standard A Regular mail than on First Class single piece because the former is relatively more price inelastic. Moreover, Standard A Regular mail can afford the modest increase in its unit cost contribution burden as volume growth is healthy, whereas volume continues to fall since the last litigated rate case for single piece mail due to intensified price and non-price competition in the markets in which it competes. Raising prices on products



for which the demand is markedly falling, and in areas that may exhibit relatively high elasticity such as bill payments, is a mistake.

d. Please see my answer to a.

REVISED OBJECTION AND RESPONSE OF GREETING CARD ASSOCIATION
 WITNESS CLIFTON TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION
 Revised: October 20, 2006

- DMA/GCA-T-1-6.** Your testimony seems to suggest that based on the elasticities you estimate for Standard Regular Mail and First-class Single-Piece Letter Mail, the Rate Commission should reduce the Postal Service's proposed rate by one cent for First-class Single-Piece Letter Mail and increase Standard Regular Mail rates to offset the revenue leakage.
- a) Please confirm that this is an accurate representation. If you do not confirm, please provide cites to your testimony that explain why you do not confirm.
 - b) Do you believe that the Postal Rate Commission should consider all the pricing factors of the Act in setting rates?
 - c) Is there a pricing factor that deals exclusively with price elasticity? If so, please provide a citation to it.
 - d) Please provide any example of an instance when the Postal Rate Commission based its recommended coverage for classes or subclasses exclusively on the basis of the elasticities for these classes and subclasses.
 - e) To the best of your knowledge, did the Postal Service ever propose Ramsey prices in rate cases? If so, please explain why and when it stopped doing so.

RESPONSE:

- a. Confirmed
- b. – e. All factors in the Act should be considered in rate making and generally are (if not always in the right proportions), including elasticities. The purpose of my testimony was to point out that the Postal Service has been using highly flawed elasticities as one of the factors used in its proposed rate increases. In the face of intensified electronic competition for single piece letters, and to some degree for the entire First Class letters subclass, I believe that the Postal Service should compete more aggressively on price in key volume-driver markets like the U. S. payments market than they have been with respect to single piece letters especially. Recognizing these competitive factors just leads to smart pricing, it is not any mechanistic application of the inverse elasticity rule derived from Frank Ramsey's 1925 Economic Journal article.

Revised: October 20, 2006

DMA/GCA-T1-7. Please refer to your response to DMA/GCA-T1-1. Please assume for the purpose of responding to this interrogatory that your proposed rates for First-class Single-Piece Letter Mail were accepted by the Postal Rate Commission. Also, please assume that mail volumes do not change in response to your proposed decrease in First-Class Single Piece rates and your proposed increase in Standard Mail rates.

- a) How much revenue would be lost in First-class Single-Piece Letter Mail as compared to the rates proposed by the Postal Service?
- b) Please calculate the implicit coverage for First-class Single-Piece Letter Mail under your proposed rates.
- c) Please calculate the average rate increase for First-class Single-Piece Letter Mail under your proposal.
- d) Please calculate the coverage for Standard Regular Mail under your proposal.
- e) Please calculate the average rate increase for Standard Regular Mail under your proposal.
- f) Do you have recommendations as to how the increase in Standard Regular Mail rates should be distributed among letters, flats, and parcels? If so, please provide them and your rationale.

RESPONSE:

- a. – e. Please see my response to DMA/GCA-T-1 a. You are asking me in a. to assume there is no relationship between volume and price, but my entire testimony contradicts such a premise under the new types of competitive conditions faced by single piece letter mail. My testimony for GCA and my rate proposal for GCA was based on an implicit assumption of de-linking. The GCA testimony stands insofar as I am assuming de-linking. Without de-linking, I still propose a one cent cut in the single piece rate proposed by the Postal Service, but under the traditional "linked rates" discount methodology as between single piece and workshared, I must also propose an identical one cent cut in all of the USPS-proposed

worksharing rates for **FCLM**. The revenue loss from that under my proposal without de-linking would also fall on Standard **A** Regular letter mail rates. I can easily justify this based on the same unit cost contribution arguments made in my testimony for single piece, and because workshared FCLM as well as single piece have been negatively impacted by Internet diversion. However, USPS witness Thress' forecasting model equations are built only around an assumption of linked rates, which is inconsistent with the proposal for de-linking submitted by the USPS in this case.

With all of these caveats, I attempt to respond to your question below utilizing spreadsheets from USPS witnesses Thress and Taufique. I cannot verify the accuracy of the numbers because of fundamental flaws with the Thress model.

Under de-linking, without the **GCA** proposal to cut single piece rates by one cent from the USPS proposed rates, the institutional cost burden as measured by unit cost contributions would drift upward for single piece since the last litigated rate case. I measure this burden as the difference between the unit cost contribution of single piece and Standard **A** Regular. That difference was 12.7 cents in **R2000-1**. Under the USPS proposed rates it would rise to 13.5 cents (and with witness O'Hara's use of revised data to 14.2 cents). Under the **GCA** rate proposal it would be **12.8** cents, a little more than in **R2000-1**. Without volume changes, the resulting implicit cost coverage for single piece would be 183.2% compared to the **USPS**

proposed implicit cost coverage of **186.4%**. Intense competition from Internet diversion causing falling volumes in FCLM is the reason behind the GCA proposal. The revenue **loss** of **\$337,676,000** would be shifted to Standard A Regular mail, whose cost coverage would increase from the USPS proposed **176.5%** to the GCA proposed **180%**. The unit cost contribution for Standard A Regular would increase from **10 cents** to **10.5 cents**.

Under "linked rates" , all First Class **letters** subclass first ounce rates would decline by one cent. Under this variant of the GCA rate proposal, the unit cost contribution difference between single piece and Standard A Regular would be **12.7cents**, identical to **R2000-1**. The resulting implicit cost coverage for single piece would be **183.8%** compared to the USPS proposed implicit cost coverage of **186.4%**. The resulting implicit cost coverage for workshared FCLM would be **307.6%** compared to the USPS proposed implicit cost coverage of **312.3%**. Intense competition from Internet diversion causing falling volumes in FCLM is the reason behind the GCA proposal. The revenue **loss** of **\$519,259,000** would be shifted to Standard A Regular mail, whose cost coverage would increase from the USPS proposed **176.5%** to the GCA proposed **181.8%**. The unit cost contribution for Standard A Regular would increase from **10 cents** to **10.7 cents**.

- f. **Standard A Regular Letters only with de-linking. Without de-linking, possibly ECR as well, in part because I believe the elasticity *for* ECR. while clearly greater than Standard A Regular, is also inelastic.**

Table Two
R2006-1
GCA Proposal with "De-Linked" Rates

First-Class Mail
Financials for Single-Piece and Presort Letters
SP Price Reduced to 41 Cents from USPS Proposed
42 Cents without Accounting for Volume Changes

FY 2008 Test Year After Rates Financials		Presort	
Postage Revenue	\$ 18,880,310,989	\$ 16,376,070,440	
NSA Adjustment			\$ 37,803,000
Fees	\$ 213,324,435	\$ 26,528,032	
Total Revenue	\$ 19,093,635,434	\$ 16,440,401,472	
Volume 1	\$ 37,206,438,437	\$ 48,542,758,437	
Revenue Per Piece	0.513	0.339	
Rollforward Cost	\$ 10,423,260,976	\$ 5,265,124,393	
Cost Per Unit	\$ 0.280	\$ 0.108	
Per Unit Contribution	0.233	0.230	
Implicit Cost Coverage	183.2%	312.3%	

Standard Mail
Financials for Standard Mail Regular

FY 2008 Test Year After Rates Financials		Total Regular*	
Total Revenue	\$ 17,701,803	\$ 17,701,803	
Volume	75,188,113	75,188,113	
Revenue per Piece	0.235	0.235	
Rollforward Cost	\$ 9,836,572	\$ 9,836,572	
Cost per Unit	\$ 0.131	\$ 0.131	
Per Unit Contribution	\$ 0.105	\$ 0.105	
Implicit Cost Coverage	180.0%	180.0%	

* Revenue loss of \$337,676 (in 1,000) due to SP price reduction is added to the Standard Regular R2006-1 baseline revenue

R2006-1

GCA Proposal with "De-Linked" Rates

First-Class Mail
Financials for Single-Piece and Presort Letters
SP Price Reduced to 41 Cents from USPS Proposed
42 Cents and Accounting for Volume Changes

FY 2008 Test Year After Rates Financials		Presort	
Postage Revenue	\$ 18,942,349,733	\$ 16,132,605,168	
NSA Adjustment			\$ 37,803,000
Fees	\$ 213,324,435	\$ 26,528,032	
Total Revenue	\$ 19,155,674,168	\$ 16,196,936,200	
Volume 1	\$ 37,328,755,707	\$ 49,293,592,008	
Revenue Per Piece	0.513	0.329	
Rollforward Cost	\$ 10,423,260,976	\$ 5,265,124,393	
Cost Per Unit	\$ 0.279	\$ 0.107	
Per Unit Contribution	0.234	0.222	
Implicit Cost Coverage	183.8%	307.6%	

FY 2008 Test Year After Rates Financials

FY 2008 Test Year After Rates Financials		Total Regular*	
Total Revenue	\$ 17,863,386	\$ 17,863,386	
Volume	75,188,113	75,188,113	
Revenue per Piece	0.238	0.238	
Rollforward Cost	\$ 9,836,572	\$ 9,836,572	
Cost per Unit	\$ 0.131	\$ 0.131	
Per Unit Contribution	\$ 0.107	\$ 0.107	
Implicit Cost Coverage	181.8%	181.8%	

* Revenue loss of \$337,676 (in 1,000) due to SP & WS price reduction is added to the Standard Regular R2006-1 baseline revenue

Source: FCM Data are obtained from R2006-1, USPS-LRL-129, WP-FCM-12 Revised after making appropriate changes to WP-FCM-11a

Revised: October 20, 2006

DMA/GCA-T1-8. Please refer to your response to DMA/GCA-T1-4, where you state, ". . . Standard A Regular rates . . . are artificially low because of the delivery cost subsidy they receive." Please define "subsidy" as you use the term in that response. Please discuss whether this definition corresponds with the standard economic usage of the word.

RESPONSE:

My use of the word "subsidy" corresponds with standard economic usage. First Class Mail subsidizes the **total** delivery costs of Standard Mail. One cannot "see" the subsidy by looking at attributable delivery costs because most delivery costs are "declared" to be non-attributable even though common sense would dictate that a straightforward distribution key such as "per piece by shape" could make most all delivery costs attributable. Because of ~~the~~ higher cost basis from which higher cost coverages for First Class are imposed under postal ratemaking, compared to what are imposed for Standard A Regular, namely lower cost coverages from a lower cost basis, First Class Mail ends up paying a disproportionately large share of most delivery **costs**, those that are buried in so-called "institutional costs" of the USPS. Nearly all delivery costs could easily be made attributable by class and subclass by **introducing** a straightforward distribution key as stated above. Once a carrier has First Class letter mail and Standard A Regular letter mail in **his/her** hands, there is no difference in costs delivering one versus the other. **As** matters now stand, even on several days per week when I get only Standard Regular Mail in my mailbox, it is the high First Class Mail letter rates that are paying a good share of the costs for that delivery through the higher institutional cost contribution of FCM. Formally, the clearest way to make the American subsidy for Standard A Regular Mail directly visible would be to apply the European mathematical models of full liberalization and

look at the total costs for the entrant's delivery system. The resulting assignment of costs by the entrant as between First Class and Standard would **look** entirely different than today's USPS assignments of so-called non-attributable delivery costs and attributable costs. Given respective volumes, the share of **First Class** delivery costs in **the** entrant's delivery system would be less and the share of **Standard A** Regular mail would be considerably more.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION

Revised: October 20, 2006

DMAIGCA-TI-9. Please provide a complete cite to the Frank Ramsey 1925 article that you cite in your response to DMA/GCA-T1-6. Please provide a copy of the article.

RESPONSE:

The editing process missed a typo and the correct year is 1927. The full citation

is: F.P. Ramsey, *The Economic Journal*. Vol. 37, No. 145. (Mar., 1927),

pp. 47-61. The article is available from:

<http://links.jstor.org/sici?sici=0013-0133%28192703%2937%3A145%3C47%3AA>

[CTTTO%3E2.0.CO%3B2-K](#). Because it is subject to copyright protection, a copy

is not being provided, but is available for inspection at GCA counsel's office.

Revised: October 20, 2006

NAA/GCA-T1-1: Please refer to pages 2 and 3 of your testimony, where you state that an incorrect elasticity estimate "...leads to flaws in rate proposals and the revenue requirement, and flaws in the assignment of institutional cost coverages based on faulty demand elasticities and other perceptions of market conditions." One of the components used to determine rates and to determine an appropriate institutional cost contribution for a mail subclass is that subclass's value to mailers.

- (a) Were one to know only the correct own-price elasticity of demand for a particular mail subclass, would that information be sufficient to accurately determine the value of that subclass to mailers? Put differently, are there factors other than the elasticity of demand that determine the overall value of the subclass and therefore inform the appropriate contribution of that subclass to institutional costs?
- (b) Is it possible that a mail subclass with a demand that is significantly more elastic (at current price of that subclass) than some other mail subclass (at the current price of that other subclass) offers value to mailers that significantly exceeds the value to mailers of the other (more inelastic) subclass? Please explain, and in particular explain the role played by the volume of each subclass in **determining** the total value of that subclass.

RESPONSE:

- a. Yes, there are other factors that matter in determining the value of that subclass to mailers beyond own price demand elasticities in general. However, with respect to the particular situation described in my testimony, it is my belief that the Commission especially, but also the USPS itself, must be far more savvy **about** pricing in light of market conditions rather than business-as-usual cost plus pricing than it seems to have been in the past or with its proposals for the single piece rate in this case. In its recommendation for the First Class single piece rate in this case the Commission cannot realistically assume that we are in the same market environment that existed, or was perceived to exist in the last litigated case in **R2000-1**. We have seen dramatic drop-offs in single

piece volumes since that last rate case, future uncertainties are high with respect to further large drop-offs, and those are the key realities that need to be considered in setting the single piece rate in this case. The rate should be set it as low as possible, even below the **41** cent rate **GCA** proposes, given the competitive realities. Please see my entry under "competitive market processes" in The New Palgrave, 1987 edition, **MacMillan**, New York and London. for a fuller discussion of the intensity of modern competitive processes such as those **USPS** faces.

- b. What I discovered using **VES** demand curves that overcome most all the flaws of the Thress model is that First Class single piece mail is somewhat more elastic than Standard **A** Regular and, correspondingly, more elastic than was heretofore believed. The previous belief was that single piece was more inelastic. In either calculation, we are speaking about roughly 39 billion pieces of single piece and **51** billion pieces of Standard **A** Regular, utilizing actual **PFY2005** billing determinant data. Single piece, even with the corrected elasticity, offers more value than a Standard letter; privacy, return, **forwarding**, priority in sortation. However, there is a wide gap between single piece rates and Standard **A** Regular rates at USPS proposed rates in this case, and that relative rate difference greatly exceeds the relative value difference in my view. To bring the relative rates into closer alignment with the relative values, the single piece rate should be lower than the USPS proposed rates and Standard **A** Regular rates should be higher than those proposed by the

USPS in this case.

Revised: October 20, 2006

NAA/GCA-T1-2: Is it a fair interpretation of your testimony that the emergence of the Internet, including email and electronic payment systems, should have (and did) make the own-price elasticity of demand for single-piece First Class letters relatively more elastic over time, but that the Postal Service's volume forecasts would suggest that that demand has become *less* elastic?

RESPONSE:

Yes.

NAA/GCA-T1-3: Please explain your qualitative understanding as to why the price elasticity of Standard Regular mail appears to be declining during the periods of time covered by your testimony. Please address what effect you believe that the growth of the Internet may have on Standard Regular mail.

RESPONSE:

I am not an expert on Standard mail, so I am speculating here in my answer. The competitive alternatives to Standard Mail are well known, have been in place for a long time, are not in rapid and unpredictable evolution as is the Internet as a competitive alternative for single piece (and workshared) FCLM. Possibly, price and non-price factors for competing alternatives to marketing mail, like the price of a 30 second spot during the Super Bowl, have rendered mail as an especially desirable medium with higher value added over time, as demonstrated by the falling elasticity in Standard A Regular. My impression is that advertising on the Internet has not been a particular success, and that would be a very close substitute for mail advertising. Internet selling having been tried but found wanting, possibly the recent growth of marketing mail is a direct result of advertisers redirecting resources from the Internet and back toward the tried and true method of Standard Mail. And perhaps that shift has also demonstrated higher than previously recognized value of Standard A Regular mail, as also reflected in its falling elasticity.

Revised: October 20, 2006

NAA/GCA-T1-4: Please refer to page 53, lines 17 to 21, of your testimony. Please explain what you mean by "At the margin for the R2005-1 rate **case**" and the meaning of the **-0.765** and -0.190 price elasticities presented there.

RESPONSE:

By "at the margin" I mean that the elasticity number from **our** VES regression runs shows a value at the last margin of time (namely 2005) in **that** data series equal to -0.765. See Appendix Table A2. Similarly, see Appendix Table A6 for the -0.190 number.

NAA/GCA-T1-5: Please refer to page 59 of your testimony, where you compare the unit contributions to institutional costs of First-Class single piece and Standard Regular mail. Please explain how comparisons of unit contributions should be used in postal ratemaking.

RESPONSE:

The Postal Service itself seems to have highlighted the concept of "unit contributions" in its approach to ratemaking for this case for the FCLM subclass, namely expressing a desire to make them equal as between single piece and workshared under de-linking.

It occurred to me that the same principle ought, possibly, to be emphasized across classes and subclasses, not just within a **subclass**, in lieu of or in addition to the more traditional "cost coverage" or mark-up ratios approach. As a result a unit cost contributions table was created for a **GCA** interrogatory, **GCA/USPS-T31-1**, which looked at a time series of unit cost contributions for single piece and workshared in FCLM, and in addition for Standard A Regular as well. The table showed that the unit cost contributions for single piece and workshared were not only substantially greater than that for Standard A Regular, but that the gap since the last litigated rate case assuming the **USPS** proposed rates in this case for **TY2008** would grow. USPS witness O'Hara's response to the **GCA** interrogatory confirmed the table's results generally, and his updated data for some cells in the table showed the gap was widening even more than seen from the original table. Reducing that growing gap in unit cost contributions is one of the reasons for my rate proposals for **GCA** (1) assuming de-linking; and (2) assuming no de-linking. Please see my response to **DMA/GCA-T1-7**.

USPS/GCA-T1-1. On page 3 at line 6 of your testimony, you refer to witness Thress's estimate of the own-price elasticity of First-class single-piece letters as "biased."

- a. Please define the term "biased" as it is used in formal statistical or econometric analysis.
- b. Was your use of the term "biased" on page 3, line 6, of your testimony consistent with the definition in a.?
- c. If your use of the term "biased" was consistent with the definition in a., please provide the mathematical and statistical evidence which you used to arrive at this conclusion.
- d. If your use of the term "biased" was not consistent with the definition in a., please define the term "biased" as you intended it to be understood on page 3 at line 6 of your testimony.

RESPONSE:

- a. $\text{Bias} = E(\hat{\beta}) - \beta \neq 0$. Thus, bias means that the expected value of the estimated coefficient of a parameter is not equal to the parameter's value.
- b. Yes.
- c. The incorrect and unnecessary Box-Cox specification of the ISP variable is a source of the bias, since it dampens the true estimates. Furthermore, even if Box-Cox is correctly specified, its coefficients should be estimated along with the other coefficients using an appropriate econometric technique such as the maximum-likelihood estimation rather than least square technique. Otherwise, this could also be another source of bias.
- d. Not applicable.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-2. Please define the "payments market" as you use the term on page 3 at line 20 of your testimony and elsewhere. Within your answer, please address whether the following payments would be part of the "payments market" as you use the term in your testimony.

- a. Payment for groceries at point of purchase
- b. Payment for clothing at point of purchase
- c. Payment for a newspaper subscription
- d. Payment to an employee
- e. Payment to mail a package
- f. Payment for theater tickets
- g. For the items listed in a - f., what is your best guess as to how such payments are made in 2006?
- h. For the items listed in a - f., what is your best guess as to how such payments were made in 1975?
- i. Do you believe that payment for any of the items listed in a - f would have ever been sent through the mail? If so, approximately what percentage of such payments would you estimate were sent through the mail at the peak of such usage? What percentage of such payments would you estimate are currently sent through the mail?
- j. If you contend that debit cards are currently used for any of the above transactions, or any point-of-sale transactions. how would such use of debit cards affect the volume of First-class Mail? Please explain fully

RESPONSE:

The definition of the U. S. payments market I adopt is based on that of the 2004 Federal Reserve Bank of Atlanta study

a. - f. Yes.

g. - j. I do not have the level of detail to answer these questions

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-3. Please define "pricing power" as you use the term on page 4, line 1, of your testimony.

RESPONSE:

The term "pricing power" is an economic term referring to the effect that a change in a firm's production price has on the quantity demanded of that product. Pricing power relates to the "Price Elasticity of Demand" Generally speaking, if a company doesn't have much pricing power, then an increase in their prices would substantially lessen the demand for its products. See (<http://financial-dictionary.thefreedictionary.com/Pricing+Power>)

- USPS/GCA-T1-4.**
- a. Do you believe that a firm has "pricing power" if its share of a market exceeds 50 percent? Please explain.
 - b. Do you believe that a firm lacks "pricing power" if its share of a market is less than 50 percent? Please explain.
 - c. Are there any conditions under which a firm could lack "pricing power" despite having a market share in excess of 50 percent? If so, what are the conditions?
 - d. Are there any conditions under which a firm could have "pricing power" despite having a market share that is less than 50 percent? If so, what are the conditions?

RESPONSE:

a. - d. Please see my response to 3. Furthermore. I would have to know the specifics of any market situation before I could answer your questions

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-5.** a. Please confirm that the use of electronic alternatives to mailed bills and statements requires Internet access by both the sender and recipient of electronic bills and statements.
- b. What percentage of First-class workshared mail is sent to households?
- c. Please confirm that, in order for a business to send an electronic bill or statement to a household, that household must have Internet access.
- d. In light of your responses to parts a. - c. of this interrogatory, please explain your statement on page 6 of your testimony at lines 23 and 24. that "[t]he inclusion of a broadband variable for workshared letters makes no economic sense."

RESPONSE:

- a. Confirmed.
- b. No data are available to answer this question so far as I am aware.
- c. Confirmed.
- d. You have taken my remarks out of context. Please read lines 19-27 on page 6, and lines 1-4 on page 7. Since T1 technology has been in widespread use since well before 2002, witness Thress should have used that as an explanatory variable in the workshared letters equation. not starting in 2002. but much earlier. The inclusion of a broadband variable in the single piece equation should be made when that trend started to ramp up. roughly after 2000, which was much later than the ramping up of T1 connections in office buildings.

USPS/GCA-T1-6. In his testimony at page 27, lines 10 – 23, witness Thress makes the following statement:

"I am not asserting here that the use of broadband Internet access leads directly to a proportional decrease in mail volume. Rather, I am suggesting that the historical pattern of the adoption of broadband Internet access has mirrored electronic substitution out of certain types of mail. In some cases, mail loss may be a direct result of the use of broadband. For example, higher-speed connections, which allow for faster downloads of graphical images, may make online magazines a more attractive alternative to Periodicals mail. In other cases, however, it may simply be the case that the adoption of these technologies is occurring along a similar time path. This similarity may be more than coincidental, of course, and may be the result of common technological advancements. Recent increases in electronic bill presentment may have aspects of both of these factors. That is, while higher-speed connections may make it more feasible to receive bills and statements online, it is also the case that the technology which allows for such things has also developed more or less over this same time period."

Do you agree with Mr. Thress's statement here? If not, why not? If so, why do you believe that "[t]he inclusion of a broadband variable for workshared letters makes no economic sense"?

RESPONSE:

Please see my response to 5. d. above.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-7.** a. What percentage of businesses currently has access to "high speed T1 technology"?
- b. What percentage of businesses had access to "high speed T1 technology" in 2001?
- c. What is the basis for your assertion at page 6, line 25, through page 7, line 1 that "any business that operates in a commercial office environment has had access to high speed T1 line technology for many, many years and certainly well before the rate increase in 2002"?
- d. What is the basis for your assertion at page 7, lines 1 - 3, that "[t]he broadband deepening that has gone on in recent years since 2000 is almost exclusively in the household or residential sector"?

RESPONSE:

- a. - b. I do not have such precise numerical data.
- c. My general knowledge and experience.
- d. My general knowledge and experience.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-8.** a. Do you believe that there is an immediate and universal shift from mail to electronic alternatives for all households when they acquire Broadband Internet access? Please explain.
- b. Do you believe that the loss of mail due to electronic alternatives must be proportional to the overall level of Broadband usage in the United States? If so, please explain why you believe this to be the case. If not, please explain why you believe that the number of Broadband subscribers "should be included in the single piece equation"?

RESPONSE:

- a. No. There is a learning curve. The substitution effect probably resembles a standard "S" shaped growth curve. It is interactive. For example, on-line banking is made more feasible once households have broadband.
- b. Not necessarily. The point is accelerating adoption of broadband by households is becoming the major dynamic explaining further Internet diversion. I would expect at some point as this process unfolds, unless the USPS becomes more aggressive in competing, one will see another large drop off in First Class Mail volume such as that experienced in the recent past, and again it will be focused in a further loss of bill payments mail.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-9.** a. Please confirm that the demand equation which is used by you to produce your estimate of the own-price elasticity of First-Class single-piece letters of -0.456 does not include the number of Broadband subscribers as an explanatory variable.
- b. Please reconcile your decision to omit the number of Broadband subscribers within the demand equation for First-Class single-piece letters with your assertion on page 7 that "on economic grounds, it should be included in the single-piece equation."

RESPONSE:

- a. Confirmed.
- b. In this model I was merely trying to investigate whether Mr. Thress' estimated price elasticity is dampened due to: (1) the use of a mislabeled Box-Cox transformation; and (2) the stochastically imposed workshared discount coefficient.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-10. Please explain in detail the "other problems" which are created "whenever a time trend dummy variable ... is re-introduced into a demand equation" to which you refer on page 7 of your testimony.

RESPONSE:

Inclusion of a time trend variable could introduce further autocorrelation in the model. Furthermore, the time trend variable may cause multicollinearity, resulting in some variables becoming insignificant.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-11.** a. Please confirm that the demand equation which is used by you to produce your estimate of the own-price elasticity of First-Class single-piece letters of **-0.456** includes an interaction between a linear time trend starting in **2002Q4** and consumption expenditures on Internet Service Providers.
- b. Would the inclusion of a linear time trend starting in **2002Q4** interacted with consumption expenditures on Internet Service Providers represent "a time trend dummy variable capturing everything and nothing"? If not, to what variable in witness Thress's First-class single-piece letters equation were you referring when you denigrated (page 7) his use of "a time trend dummy variable capturing everything and nothing"?
- c. Given the inclusion of the linear time trend starting in **2002Q4** interacted with consumption expenditures on Internet Service Providers as an explanatory variable in your proposed demand equation for First-class single-piece letters, is your demand equation subject to the problems to which you refer on page 7 of your testimony at lines 19 - 21, which are created "whenever a time trend dummy variable ... is re-introduced into a demand equation"? If not, why not?

RESPONSE:

- a. Confirmed.
- b. I was referring to the long-term trend that interacts with the ISP variable.
- c. It could, but at a lesser degree than over-the-whole-period time trend.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-12. Please refer to your testimony at page 9, lines 3-4.

a. Is it your testimony that the 2005 Household Diary Study indicates that of total First-class Mail sent by households, only 13 percent constitute payments? If so, please show the full derivation of this percentage. If not, please explain fully, and provide the correct percentage of First-class Mail sent by households that constitutes payments.

b. What percentage of First-class single-piece letters are payments sent by households? Please explain fully.

RESPONSE:

a. - b. The text above table 4.1 in the HHD talks about “[t]ransactions sent and received” and says they are 53 percent of household First-class Mail. Part (a) of the question appears to read the testimony as asserting that payments are 13 percent of FCM sent by households. If the 10.8 billion comes from the 2005 column for bill payments, as I assume it does, then household bill payments do constitute $10.8 / (42.7 + 0.53) = 13.4$ percent of all household First-class Mail (sent and received). But the question asks whether it is 13.4 percent of First-Class Mail sent by households.

I have not found a good way of estimating the FCM sent by households, but the following is suggestive. The categories are the ones that seem likely to originate with households (the numbers come from HHD tables 3.1 and 4.1):

Total HH to HH correspondence	5.870 billion
Total HH to NHH correspondence	2.119
Total correspondence sent	7.989
Bill payments	10.809
Orders	0.769
Donations	0.560
Total transactions sent	12.138
Total sent	20.127

So the 10.8 billion bill payments would be 53.7 percent of the outgoing.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-13. Do you understand witness Thress's own-price elasticity estimate for First-class single-piece letters to be an estimate of the "market own-price elasticity of demand or an estimate of the "own-price elasticity of demand for [a] single competitor" as you use those terms on page 10, lines 17 - 19, of your testimony?

RESPONSE:

The latter.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-14. Do you believe that witness Thress has ever asserted that the payments market is highly price inelastic? If so, please provide evidence of such an assertion.

RESPONSE:

Yes. See Tr., page 1322, lines 2 -25, and particularly lines 17-25.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-15. On page 14 of your testimony at lines 16 – 18, you hypothesize that "[p]ayments made by check are an excellent proxy for payments made by mail, because at the point of sale, checks are rarely used anymore, having been displaced by credit and debit cards."

- a. Do you believe that "payments made by check are an excellent proxy for payments made by mail" in the year 2000? Please explain.
- b. Do you believe that "payments made by check are an excellent proxy for payments made by mail" in the year 1990? Please explain.
- c. If the percentage of checks which are mailed, as opposed to being used at the point of sale, has been increasing over time, could the number of checks which are mailed have increased even as the total number of checks has decreased? Please explain
- d. Please confirm that Table 2 on page 15 of your testimony does not provide any direct evidence on the 'USPS market share in the U.S. payments market." If not confirmed, please explain.

RESPONSE:

- a. - b. Yes, increasingly over the 1970-2000 period. Not based on statistical data but on "common knowledge" observations of what people do. I do not see many people pay by check anymore, they use credit or debit cards, general purpose or special issue. At the end of the month, however, in paying bills sent by mail, people write checks generally. Automatic debit may be substituting for check writing, particularly if the amount is identical each month, such as a fixed mortgage payment. On-line banking may be substituting for some check writing, but in the main I believe most checks written to pay bills are sent through the mail.
- c. I do not have the data to answer your question, but it does not follow that just because point of sale check percentage has declined, it would lead consumers to increase usage of checks sent by mail.
- d. Not confirmed. Table 2 lists checks. Even if every check were mailed, the USPS market share in the U. S. payments market would be well under 50%. It is highly unlikely that every check is mailed. I pay a lot of workmen around my home by check on the spot. Those checks come back to me in a single monthly statement from my bank. Most but not all of the checks I write are for bill payments and are sent through the mail.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPSIGCA-TI-16. On page 17, at lines 18 - 20, you claim that "[a] direct estimate of that cross price elasticity, b_2 , would greatly sharpen the estimate for b , the own-price elasticity of demand for single piece payments mail." Please explain in detail why you believe this to be the case.

RESPONSE:

See footnote 11 of my testimony. In particular Carlton and Perloff state 'All else the same, the larger a cross-elasticity of demand. the larger in absolute value is the direct elasticity of demand.' In their footnote 23, the reason for this is explained. "This result follows because the sum of the direct elasticity plus all cross-elasticities of demand equals 0." In the case of First Class single piece mail, we are speaking about a single substitute. and hence a single cross elasticity. Thus, my statement follows.

USPSIGCA-TI-17. On page 17, at line 20 through page 18, line 2, you claim that "[o]ther things being equal, a further property of the demand specification in equation (2) is that when the cross price elasticity b_2 is high, the absolute value of the own price elasticity, b , will also tend to be high."

- a. Please explain why you believe this to be true.
- b. What conditions are necessary for this expected relationship to hold true?
- c. If P and P_2 in equation (2) are uncorrelated. would you expect the own-price elasticity, b , to be dependent on the level of the cross-price elasticity b_2 ? If your answer is yes, please provide citations from mathematical or statistical sources that would support your answer.
- d. If the Postal Service "refuses to compete on price" with electronic alternatives. would you expect P and P_2 to be correlated? Please explain your answer.

RESPONSE:

a. - d. Please see my answer to 16. Further, in a properly specified demand equation for First Class single piece letters, the price of the competing substitute would be explicit, and not captured by vague non-price variables or time trend variables. In the long run, the USPS has no choice but to compete on price with electronic substitutes, they have just refused to do so thus far. Thus, fundamentally, there is a correlation

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-18. On page 17, line 6 of your testimony you present the following equation (1):

$$(1) \log(Q) = a - b \log(P) + Z(t)$$

On page 18, line 3 of your testimony you present the following equation (2):

$$(2) \log(Q) = a - b \log(P) + b_2 \log(P_2)$$

- a. Please confirm that equation (1) is mathematically identical to equation (2) if $Z(t) = b_2 \log(P_2)$. If not confirmed, please explain.
- b. Please confirm that the estimated value of b will be identical in equations (1) and (2) if $Z(t)$ is perfectly correlated with $b_2 \log(P_2)$. If not confirmed, please explain.

RESPONSE:

- a. Confirmed.
- b. Confirmed.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPSIGCA-TI-19. Please refer to your testimony at page 9, lines 5 to 9, where you refer to the response to GCA/USPS-T8-1.c and you state that "Postal Service witness Peter Bernstein notes that an alternative approach to elasticity measurement is to 'decompose First-class Mail individual mail and make a segment-by-segment projection of diversion.'"

a. By "elasticity" are you referring to the change in First-class Mail volume in response to a change in First-class Mail price? If not, what do you mean by the term "elasticity" in your statement?

b. Please confirm that witness Bernstein in his response to GCA/USPS-T8-1.c was not referring to an alternative approach to measuring the price elasticity of First-class Mail, but rather, as requested in the question, to an alternative approach to measuring the level of electronic diversion of First-class Mail. If you cannot confirm, please explain fully.

c. Please confirm that witness Bernstein in his response to GCA/USPS-T8-1.c stated that his belief that this alternative segment-by-segment approach to estimating the level of electronic diversion was inferior to the econometric approach employed by witness Thress to estimate the level of electronic diversion. If you cannot confirm, please explain fully.

RESPONSE:

a. By "elasticity" I am referring to percentage change in First-class single piece mail volume in response to a percentage change in the single piece First-Class Mail price.

b. The issues of electronic diversion and [changing] own price elasticities for First Class single piece mail are inextricably joined at the hip. Under oral cross examination in connection with his response to GCA/USPS-T8-1, witness Bernstein engaged in a discussion that included questions surrounding electronic diversion of payments mail and the elasticity of payments mail. See Tr. at 1452, lines 14-25, through 1453, lines 1-5.

c. **Mr.** Bernstein's statement about the alleged superiority of Thress' econometric approach was made before GCA-T-1 was filed.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20,2006

USPS/GCA-T1-20. Please refer to the first sentence of page 57 of your testimony.

a. If you truly believe that single piece First-class Mail is "clearly" more elastic in demand than Standard Regular Mail. doesn't that suggest that what you refer to as "the statutory monopoly" can no longer provide any valid justification for mitigating the institutional cost share of First-class single piece mail "in today's competitive market environment," at least relative to Standard Regular Mail? If not, why not?

b. Please confirm that the Private Express Statutes (what you refer to as "the statutory monopoly") are not specific to any mail class, and to the extent that they apply, they apply as equally to letters carried as Standard Mail as to letters carried as First-class Mail. If not confirmed. please explain fully.

RESPONSE:

- a. As worded, I take the question to mean that the statutory monopoly has resulted in a mitigation of First Class institutional costs relative to Standard. This is obviously not true as institutional costs are much higher for First Class than for Standard A Regular. On a unit cost basis. the disparity is actually widening.
- b. Confirmed. Nonetheless, the impact of my findings for rate-making are correct.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-21. Please refer to the first paragraph of page 57 of your testimony. Please assume for purposes of this question that the Commission does not adopt your view that single piece First-class Mail is "clearly" more elastic than Standard Regular, and instead relies upon relative elasticities more in accord with those employed by the Commission historically (such as the elasticities estimated by witness Thress). Under this hypothetical, would your conclusion be that the single piece First-class Mail should "be looked at first as a source of extra revenue when there is a general revenue deficiency in postal finances"? If not, why not? Specifically, do you agree that the appropriate role of relative elasticities of demand in the pricing process should not depend on which particular categories of mail get favored or disfavored by this measure in a particular case? If not, why not?

RESPONSE:

The hypothetical is completely unrealistic, particularly because no confidence can be placed on elasticities for FCM estimated by witness Thress in this case. However, even accepting the hypothetical, I do not agree that single piece First-Class Mail should "be looked at first as a source of extra revenue when there is a general revenue deficiency in postal finances." As Postmaster General Potter stated in Congressional testimony in 2005, quoted at page 28 of my testimony, "electronic diversion continues to erode First-class Mail volume, this product will become more price-sensitive than ever. Higher rates will likely increase the pace of change, accelerating the volume decline, resulting in falling revenue and the need, again, to increase rates." As I noted on pages 26-29, the Postal Service's competitors are competing on price, it is only USPS that is not. Price is one of the few ways, and the only way the Commission can undertake, in which the Postal Service can compete. (In footnote 29 on pages 56 - 57 I identify other ways the Postal Service may be able to cut single piece rates.) But irrespective of price elasticity is the matter of the role of relative institutional cost contributions of classes of mail in rate setting. On page 59 of my testimony I discuss the "longstanding inequity in institutional unit cost contributions between First Class and Standard Mail that calls for such a redistribution of unit cost contributions even in the absence of the own price elasticity comparisons.."

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-22. On page 21 at lines 10 – 11, you state that the BEA deflator in the GDP accounts for computers and peripheral prices "performed appreciably better" than the BLS series for computer prices.

- a. What do you mean when you say it "performed appreciably better"? Please provide all of the statistical evidence which was used in making this claim.
- b. Did you perform any studies, statistical or otherwise, to assess whether "the BEA deflator in the GDP accounts for computers and peripheral prices" was a suitable proxy for the price of electronic payment instruments? If so, please provide all such studies.

RESPONSE:

- a. The GDP deflator has a higher correlation with the single-piece volume compared to the BLS series.
- b. No.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-23. On page 23 of your testimony at lines 18 – 20, you state, "Statements mail exceeding one ounce has fallen because of electronic alternatives to checks and because broadband more recently has made on-line banking an attractive alternative to paying by check."

- a. Are you aware that many banks do not return cancelled checks to their customers within their monthly bank statements?
- b. If banks no longer return cancelled checks to their customers, could statements mail exceeding one ounce fail, even if the number of checks remained constant or grew?
- c. Have you performed any studies, statistical or otherwise, to support the causal relationship hypothesized above?

RESPONSE:

a. - c. I am aware that most banks offer a simplified checking account product which does not return any checks. and other products which print several checks per page by reduced facsimile image. High extra ounce rates for letter mail that cannot be justified by costs are one reason why such products were developed. Notwithstanding these factors, the descriptive statistics I developed in my testimony are one such exercise which supports the causal relationship that increases in extra ounce rates in recent years caused a fall in check volumes

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-24. With respect to your equation which models commercial check volume as a function of the First-class additional-ounce rate,

- a. Why was the additional-ounce rate not deflated prior to its inclusion in this equation?
- b. Were any other explanatory variables investigated as possible explanatory variables, such as the price and availability of alternatives to checks (e.g., credit cards, debit cards) or any measures of on-line banking?
- c. Did you conduct any analyses, statistical or otherwise, which attempted to explain the number of First-class additional ounces as a function of the First-class additional-ounce rate?
- d. Did you conduct any analyses, statistical or otherwise, which attempted to relate the number of commercial checks and the number of First-class additional ounces?
- e. If your answers to any of b., c., or d. were affirmative, please provide details of all such analysis. If your answers to any of b., c., or d. were negative, please explain fully why you failed to perform such analyses.

RESPONSE:

a. - e. This work was descriptive statistics and no other explanatory variable was included. The timing between changes in extra ounce rates and volume declines in checks indicated a close correlation. Clearly, other factors have been impacting check volumes, but data was not readily available to investigate their relative importance. In periods of low inflation such as the limited period examined here, business and consumer decision making may reflect nominal rates as much or more than it reflects real rates.

Revised: October 20, 2006

USPS/GCA-T1-25. On page 27 of your testimony at lines 12 -14. you state the following, "In general one expects that the own-price elasticity of a demand curve for a market is less elastic than the own-price elasticity faced by an individual competitor. The reverse appears to be the case here."

- a. What is your best estimate for the own-price elasticity for the "payments market" as you have defined it?
- b. Please explain how you arrived at your answer.
- c. Please provide all evidence, statistical or otherwise, in support of your assertion that "[t]he reverse appears to be the case here."

RESPONSE:

a. - c. I only have descriptive statistics for the payments market, which indicate own price elasticities for the payments market could be well above -1.0. I am confident, however, that the payments market elasticity for single piece is well above our overall estimate for single piece mail. I would need more data for more variables than I was able to find to determine a magnitude, however.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPSIGCA-TI-26. On page 27, starting at line 17, you make the following statement:

"When an estimate of the own price elasticity for single piece mail is made, because the USPS chooses not to compete on price, little correlation is found between variations (i.e. declines) in single piece volumes and variations in single piece prices. However, the market demand curve, which is the aggregation of all individual demand curves. is not single piece mail. It is single piece mail plus all competing substitutes. The own-price elasticity that single piece mail faces in its problematic areas such as payments mail, statements mail and on-line banking derives from conditions in those markets."

- a. Please define the "own-price elasticity that single piece mail faces" as you use that term here.
- b. What do you believe witness Thress's estimate of the own-price elasticity for First-class single-piece letters of -0.184 is intended to measure?
- c. What is your best estimate of the "own-price elasticity that single piece mail faces"?
- d. What "demand" do you believe witness Thress is estimating with his First-Class single-piece letters demand equation?

RESPONSE:

- a. I am referring to the market demand curve USPS faces in, for example. the U.S. payments market, and the associated own price elasticity of that market demand curve.
- b. The individual demand curve USPS faces for all single piece mail. is an aggregation of various individual demand curves it faces in various markets where single piece mail is one product competing with other products for market share.
- c. I have not calculated, or been able to calculate, the own price elasticity of a market demand curve in a market in which mail is one of the competing substitutes. See also my answer with respect to the payments market in USPSIGCA-T1-25 a-c.
- d. The demand for single piece mail in all the markets in which it competes.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-27. Please define *to* whom you are referring when you use the term "firm" on page 28 at line 23.

RESPONSE:

An oligopolist as defined in the theory of the *firm* in microeconomics.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-28.** a. Please confirm that witness Thress uses the real price of First-class single-piece letters to calculate his estimated own-price elasticity for First-class single-piece letters.
- b. Please confirm that the real price of First-class single-piece letters has declined on numerous occasions over the time period over which witness Thress estimates the own-price elasticity for First-class single-piece letters.
- c. Please confirm that witness Thress's First-class single-piece letters demand equation in this case therefore represents "statistical data that would allow one to calculate an own-price elasticity for single piece mail when prices are cut."

RESPONSE:

- a. Confirmed.
- b. Confirmed. By definition, it always declines [until the next nominal and real rate increase] once a nominal rate is set by the Commission and ratified by the Governors, so long as inflation exceeds zero.
- c. Not confirmed, Please see the context of the passage you cite by reading in addition page 29, lines 2-8. I am talking about a cut in the nominal price of stamps.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-29** a. Please confirm that each of the demand equations estimated by witness Thress in past rate cases, outlined in Table 5 on page 31 of your testimony could, in fact, be summarized by equation (1) on page 17 of your testimony:

$$(1) \log(Q) = a - b \log(P) + Z(t)$$

- b. Please confirm that equation (1) is mathematically identical to equation (2) on page 18, line 3 of your testimony:

$$(2) \log(Q) = a - b \log(P) + b_2 \log(P_2)$$

if $Z(t) = b_2 \log(P_2)$. If not confirmed, please explain.

- c. Please confirm that the experiments outlined in Table 5 on page 31 could therefore be viewed as attempts by witness Thress to model the price of competing alternatives to First-class single-piece mail. If not confirmed, please explain.

RESPONSE:

- a. Confirmed
- b. Confirmed.
- c. Mr. Thress' R2006-1 internet variable does not reflect or even capture the price of competing substitutes to First-class single-piece mail. It is merely the number of subscribers reflecting the trend in the use of the internet per se. and nothing more.

- USPS/GCA-T1-30.** a. Please confirm that the number of Broadband subscribers, as presented by witness Thress in his testimony (Table IV-17. page 354) was equal to 1.165 million in 1999Q3. If not confirmed, please explain.
- b. Please confirm that the number of Broadband subscribers, as presented by witness Thress in his testimony (Table IV-17. page 354) was equal to 15.654 million in 2002Q3. If not confirmed. please explain.
- c. Please confirm that the number of Broadband subscribers grew by 1,243.7% over the three years from 1999Q3 through 2002Q3. If not confirmed, please explain.
- d. Please confirm that the number of Broadband subscribers, as presented by witness Thress in his testimony (Table IV-17. page 354) was equal to 40.211 million in 2005Q3. If not confirmed. please explain.
- e. Please confirm that the number of Broadband subscribers grew by 156.9% over the three years from 2002Q3 through 2005Q3. If not confirmed, please explain.
- f. Please explain why you believe it is appropriate to focus uniquely upon the "post-2002 period during which broadband has become more widely used" in light of the numbers presented in a. – e. above.

RESPONSE:

- a. Confirmed.
- b. Confirmed.
- c. Confirmed.
- d. Confirmed.
- e. Confirmed.
- f. Because it has been or during the last few years that consumers have accelerated their use of broadband. However. it is important to note that even a broadband variable is not a good proxy for the price of competing substitutes. This broadband variable merely measures the number of broadband subscribers and nothing more.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-31. Please define the term "empirically significant" as you use it at line 10 of page 30 of your testimony.

RESPONSE:

By "empirically significant", I mean from the standpoint of using basic principles of theory to choose what should be empirically significant, as contrasted with throwing anything into a model that produces a lower MSE.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-32. Please define the term "arbitrary" as you use it at line 9 of page 32 of your testimony.

RESPONSE:

Arbitrary means without theoretical, econometric, or economic justification, that is, a choice "Based on or subject to individual judgment or preference."

(<http://www.answers.com/topidarbitrally>). Witness Thress' E-views model solves whether the form of the ISP variable is non-linear or not. It is not a necessary transformation, but it certainly greatly reduces the own price elasticity of single piece mail, especially in his model in R2005-1

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-33** .a. Please confirm that witness Thress's specification of ISP consumption, ISP^A , does not preclude the possibility of entering **ISP** consumption directly into the First-class single-piece letters demand equation. That is, please confirm that using witness Thress's specification with $A = 1$ is identical to simply entering ISP consumption directly into the First-class single-piece letters demand equation. If not confirmed, please explain.
- b. Please confirm that the value for A is estimated mathematically by witness Thress and is not simply chosen arbitrarily. If not confirmed, please explain.
- c. Please confirm that the value for A which is estimated mathematically by witness Thress is significantly different from 1. If not confirmed, please explain.
- d. Please provide all evidence, statistical and otherwise, which would suggest to you that the value for A as used by witness Thress should be equal to 1.
- e. Please confirm that if one constrains the value of one coefficient within an econometric equation to an incorrect value that this may bias the estimated coefficients on the other variables within that equation. If not confirmed, please explain.
- f. Please confirm that your constraint of the value of A to be equal to 1 in your demand equations for First-class single-piece letters has biased your estimates of the own-price elasticity for First-class single-piece letters. If you cannot confirm, please provide all evidences, statistical and otherwise, upon which you relied to reach your conclusion, that your own-price elasticity estimates are not biased.

RESPONSE:

- a. Confirmed.
- b. Not confirmed. Mr. Thress just estimates A econometrically. He did not derive A from any mathematical principle. What I am disputing is the arbitrary choice of his non-linear form (X^A) for this particular variable without any reasonable justification, such as Box-Cox or any econometric tests.
- c. Partially confirmed. Mr. Thress just estimates A econometrically. He did not derive A from any mathematical principle. It is confirmed that the estimated value is different from 1. However, this is not the Box-Cox coefficient.
- d. The coefficient of a properly transformed Box-Cox variable $[(X^A - 1)/\lambda]$ has a specific property. When A approaches zero the variable is transformed to log form $[\ln(X)]$ and when it approaches 1, it transforms to linear form (X). A **Box-**

Cox coefficient is expected to have a value between **-2** to **+2**. Mr. Thress' non-linear specification (X^A) can assume any value between $-\infty$ to $+\infty$. Thress' estimated [so-called] Box-Cox coefficient of **0.122** has no theoretical, empirical or economic meaning in this context. Furthermore, if this value approaches zero, the value of ISP variable becomes 1 not log form. Obtaining a value of **0.122** is not a sufficient reason to assume that the ISP variable is best represented by a non-linear form. The attempted use of Box-Cox to justify his non-linear form (X^A) is therefore without any merit, since Mr. Thress did not correctly specify his variable as Box-Cox. Furthermore, Mr. Thress has provided no other theoretical, empirical, or economic justification for the non-linear specification he in fact did use. Or, the contrary, there is a reasonable justification to enter the ISP variable as a simple linear form (ISP¹).

- e. Confirmed.
- f. Not confirmed. My model is a non-log linear form. I did not perform any tests to see if each individual variable should be written in non-linear form. Possibly, it would have been better for both Mr. Thress and me to specify every variable, other than the dummy variables, in the Box-Cox form and estimate the model. This is far too difficult to do.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPSIGCA-TI-34. a. Please confirm that the Internet variable(s) used by witness Thress were different in R2001-1, R2005-1, and R2006-1. If not confirmed, please explain.
- b. Please confirm that a coherent discussion of an alleged "trend" in the coefficient estimates of a variable requires the definition of the variable to be consistent for each coefficient estimate under discussion. If not confirmed, please explain.

RESPONSE:

- a. Confirmed. as clearly shown in Table 5 of my testimony.
- b. Confirmed. However, this does not refute the fact that these elasticities were used in past rate cases for rate-making purposes and at the time were considered to be true estimates, even if later some of them were disavowed once they had served their purpose. With respect to the issues I am concerned with in my testimony, it is important to examine how these elasticities have evolved over time and whether that accords with economic principles and known business facts.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-35. On lines 16 and 17 of page 33, you indirectly assert that "Mr. Thress' choice criterion 'could very well lead to an incorrect model.'"

- a. Please provide all evidence, statistical or otherwise, that Mr. Thress's choice criterion did, in fact, lead to an incorrect model.
- b. Please confirm that the demand equation which you present in your testimony uses the same explanatory variables as the model presented by Mr. Thress in his testimony.
- c. Based on ~~the~~ selection criteria of your choosing, which of the First-class single-piece letters models presented by witness Thress in LR-L-65 would you choose?
- d. If your choice is different from the model used by witness Thress in this case, please explain the basis for your choice and describe the ways in which your chosen model is superior to the model used by witness Thress.
- e. If your choice is different from the model used by witness Thress in this case, please explain why you did not use that model as the starting point in developing your estimate of the own-price elasticity for First-class single-piece letters.

RESPONSE:

- a. The mislabeled Box-Cox transformation can affect the MSE value
Furthermore, autocorrelation problems which still continue to be present in the estimated models can lead to lower standard errors and lower MSE. thus, making a model to be wrongly chosen
- b. Partially confirmed. My model is similar to Thress. except that my model does not include the time trend interaction with the ISP variable. Further, my work sharing discount variable is allowed to be estimated endogenously rather than being stochastically imposed from the worksharing equation.
- c. - e. I did not consider any of those models, since it would not allow me to observe the changes in elasticity over time. Furthermore, they all had imposed restrictions on them.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-36. To what specifically are you referring when you claim that “Mr. Thress’ model . . . includes prolonged periods in the **1970s**” at line **4** on page 35 of your testimony.

RESPONSE:

There was no impact on the volume of First Class single piece mail during the 1970s and **1980s** which caused it to decline in the way it has with Internet diversion and electronic payments options since the mid-**1990s**.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

- USPS/GCA-T1-37.** a. Please define the term "long run own-price elasticities" as you use in at line 9 on page 35 of your testimony.
- b. Please explain your understanding of witness Thress's use of the term "long-run price elasticities" as you quote him at lines 7-8 on page 34 of your testimony.

RESPONSE:

- a. The distinction between long run and short run demand curves is clear from any elementary textbook of economic principles, and focuses on whether ceteris paribus conditions hold in the main, or not. Elasticities are generally thought to be greater for true long run demand curves than short run demand curves.
- b. In each rate case, witness Thress adds several more quarterly observations to a database which starts with 1983 data for the single piece demand equation. I believe this is an inappropriate approach when short run market demand conditions are in rapid flux as the impact on postal volumes from current competitive conditions gets diluted and distorted because, for example, there is 1983 data influencing the determination of the elasticity.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-38. At page 36 of your testimony, you make the following claim:

"One interpretation of witness Thress' models over the span of several rate cases is that demand is not simply inelastic for the FCLM subclass, but becoming increasingly price inelastic over time."

- a. Please confirm that witness Thress has never himself made this particular interpretation of his work. If not confirmed, please explain.
- b. Please confirm that witness Thress, in fact, explicitly rejected this particular interpretation of his work under oral cross-examination from the GCA (Tr. 6/1325, l. 16 – p. 1326, l. 2). If not confirmed, please explain.

RESPONSE:

a. - b. In fact, in this case Mr. Thress has refuted his own previous work in R2005-1 and considers it flawed with respect to the own price elasticity of workshared mail in the FCLM subclass. GCA (Tr. 6/1326, l. 3-7.) If he does not have confidence in his own previous work on which basis rates were increased in R2005-1, how can the Commission have confidence in his current elasticities. at least in the problematic areas I identify?

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-39. At page 36 of your testimony you claim that witness Thress "defends" the interpretation that "demand is not simply inelastic for the FCLM subclass, but becoming increasingly price inelastic over time" by "claiming that customers who stop using single piece mail are at any point in time the marginal customers, the ones whose own individual price elasticities are higher, on average, than those of the customers who continue to use the mail."

- a. Please confirm that you are referring here to Thress's response to **GCA/USPS-T7-8(e)** where he says "the introduction of a new product may induce more price-elastic consumers to stop using the old product, leaving the average own-price elasticity of the product's remaining customers lower than before the introduction of the new product, even when one accounts for the increasing own-price elasticity of these individual consumers relative to their own individual elasticities prior to the introduction of the new product." If you cannot confirm, please provide an exact citation to the statement by witness Thress to which you were referring.
- b. Please confirm that **GCA/USPS-T7-8**, the interrogatory to which Mr. Thress was responding when he made the statement to which you refer on page 36 of your testimony, made **no** reference to First-class Mail.
- c. Please confirm that Mr. Thress's hypothesis that "the introduction of a new product **may** induce more price-elastic consumers to stop using the old product, leaving the average own-price elasticity of the product's remaining customers lower than before the introduction of the new product" (emphasis added) was purely hypothetical and made **no** specific reference to any category or user of mail. If not confirmed, please explain.
- d. Please confirm that Mr. Thress, in his response to **GCA/USPS-T7-8**, explicitly stated that "[t]he extent to which two goods are substitutes and the extent to which consumers would be expected to substitute between two goods because of changes in the relative price of the goods is ultimately an empirical question that can not be answered generally, but can best be answered in a specific case via rigorous econometric investigation." If not confirmed, please explain.

RESPONSE:

- a. - d. Mr. Thress, at (Tr 6/1291, 116), specifically, refers to "first class single piece letters."

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPSIGCA-T1-40. In footnote 25 at the bottom of page 37 of your testimony you make the following assertion:

"If [the hypothesis that the own-price elasticity of First-class Mail were declining over time] were true, there is no reason why the real prices of stamps should not also be increasing over time. The fact that they have not been — in the presence of competing substitutes due to Internet diversion and electronic payments substitutes for the mail — demonstrates that the own (real) price elasticity of single piece mail is higher than what witness Thress has calculated over recent rate cases."

- a. What are the factors which you believe determine the real price of stamps?
- b. If the Postal Service does not go to the Postal Rate Commission and seek an increase in the real price of stamps, is there any mechanism by which stamp prices will increase? Please explain.
- c. If mail volume declines as a result of an increasing "presence of competing substitutes due to Internet diversion and electronic payments substitutes for the mail" when nominal stamp prices remain unchanged. what do you believe this indicates about the own-price elasticity for First-Class Mail? Please explain why you believe this.

RESPONSE:

a. - c. My observations from looking at real single piece prices over the past 10-15 years is that the USPS did at one time make an effort to keep real prices steady. It has not stopped additional lost volume due to Internet diversion and the growth of electronic payments, and it looks to me as if USPS management is not interested any more in keeping real prices of single piece mail constant, has given up trying to do so, and/or feels it cannot do so. That is my interpretation of why "price caps" find widespread support in current postal reform legislation. namely to keep real prices from rising in the future, now that the will and/or ability are lacking at USPS.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-41. Your footnote 27 on page 41 says the following, 'In the experiments we conducted, the exponential specification of the elasticity and functional form of the equations produced the wrong sign associated with the high absolute value. This circumstance does not alter the conceptual merit of the critique, however.'

- a. Are you saying here that the experimental own-price elasticities which you found necessary to "bring the forecasted volume curve to the actual volume curve" had values which were greater than zero? If not, please explain what you meant here.
- b. If your answer to a. was affirmative, please confirm that own-price elasticities greater than zero are theoretically untenable. If not confirmed, please explain.
- c. If your answer to a. was affirmative, please confirm that if the experimental elasticities necessary to "bring the forecasted volume curve to the actual volume curve" had values greater than zero, this indicates that the own-price elasticities estimated by witness Thress in recent cases were not too close to zero. If not confirmed, please explain.

RESPONSE:

- a. Yes.
- b. Confirmed.
- c. It could simply mean that the demand equation is either not properly specified or is estimated improperly, It does not necessarily mean that Thress' forecasting estimates are correct and **without** bias. In fact, he himself does not believe his own previous estimates to be correct.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2005

USPS/GCA-T1-42. At page 43, lines 20-21, you say that "it made no sense to introduce any other non-linear specification of the Internet variable."

- a. Do you believe that it would make sense to introduce a non-linear specification for a variable if there was strong statistical evidence that the variable was related to mail volume in a non-linear fashion? If not, why not?
- b. Did you investigate any evidence, statistical or otherwise, with regard to whether the relationship between First-class single-piece letters volume and the Internet was linear or non-linear? If so, please describe all such evidence. If not, why not?

RESPONSE:

- a. No. Because the power coefficient of a variable is significant does not necessarily mean that the variable should be entered in a non-linear form. The non-linearity should be justified before it is attempted on theoretical, economic, or econometric theory. The whole model should be tested to see if a linear or a non-linear form results in a better mode. The non-linear form should be based on a correct premise. If Box-Cox transformation is a method to introduce the variable into the model in a non-linear form, then it should be done properly and estimated with the proper technique, such as maximum likelihood estimation. Simply entering a variable in non-linear form (ISP^A) without the appropriate test for that particular variable can produce unnecessary bias in the model. Including a variable as non-linear without some reasonable justification is nothing but an arbitrary choice. A correct Box-Cox transformation and proper estimation of a Box-Cox coefficient along with the other coefficients is justifiable with the caveat that one needs to test whether the Box-Cox transformation improves the efficiency of the forecasting ability of the model.
- b. My model by its structure is in a non-log linear form and thus, it does not require transformation of any variables.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-43. On page 47 of your testimony you state that a linear demand function "accommodates our expectation of varying elasticities due both to the changing level of postal rates and the changing availability and strength of competing substitutes."

- a. What is your expectation of how elasticities will vary due to the changing availability and strength of competing substitutes?
- b. What is the precise mathematical relationship between the own-price elasticity and the "availability and strength of competing substitutes" in your demand equation?

RESPONSE:

- a. The own price elasticity of single piece mail should **increase** as the number and intensity of competition from substitutes increases.
- b. In my model I kept Mr. Thress' ISP variable and its interaction with the time trend 200204. There is currently no good proxy for the price of competing substitutes such as Internet to include in the model. One purpose of staying as close as possible to Mr. Thress' model was to investigate how his inappropriate and unnecessary *transformation of the* ISP variable and certain stochastic imposition had dampened the single-piece own-price elasticity. Carlton and Perloff state "The direct price elasticity ~~-not~~ the cross elasticity of demand-determines market power. ... There is a lot of discussion in court decisions as to the importance of ~~cross-elasticity~~ of demand in defining markets. Courts often use the term [cross elasticity] loosely to indicate that products are substitutes." (Carlton and Perloff. 2005, page 647.)

Revised: October 20, 2006

USPS/GCA-T1-44. Please refer to Table A-8 on page 9 of Appendix A of your testimony.

- a. Please confirm that the volume of First-class single-piece letters lagged two quarters is included as an explanatory variable in the demand equation presented in Table A-8.
- b. You state at the top of Table A-8 that the volume of First-class single-piece letters lagged two quarters ~~is~~ included as an explanatory variable "to correct for autocorrelation." Please provide a citation to an econometric textbook or other econometric literature that suggests that merely adding the lagged dependent variable as an explanatory variable is an appropriate means of correcting for autocorrelation.

RESPONSE:

- a. Confirmed.
- b. According to Granger and Newbold (1974) the usual approaches to autocorrelation are either (i) to ~~include~~ a lagged dependent variable; or (ii) to take first differences of the variables; or (iii) to assume a simple-first-order autoregressive process for the ~~residuals~~. The last two were not practical for us. Autocorrelation and partial ~~autocorrelation~~ that Mr. Thress has provided in his output file ~~demandequations.txt~~ for each mail category in LR-L-64 reveals that his econometric program is incapable of ~~dealing~~ with the autocorrelation problems. Furthermore, in most cases the calculated Durbin Watson values are in the indeterminate range of critical values. The Durbin Watson ~~critical~~ values exist up to only 20 explanatory variables. For example, at the 5% level the critical values for a sample of size 90 are $D_L = 1.16$ and $D_U = 2.21$; and for a sample size of 70 they are $D_L = 0.971$ and $D_U = 2.362$. We know that the greater the number of explanatory variables the wider the range becomes. We also know that there are more than 20 explanatory variables in Thress' models. Thus, this range is much wider than the above two ranges. The reason for some of the autocorrelations to continue to persist in Mr. Thress' estimated models could be due to the arbitrary specification of his autocorrelation structure (AR1, AR2, & AR4). I therefore did not use Mr. Thress' program. At the same time we decided to preserve the integrity of his specification of seasonal variables. As a result of this, we were not able to

use the built in procedures of E-views to deal with the autocorrelation. The approach we took was to introduce the lagged dependent variable into the equation when necessary.

Granger, C.W.J. and P. Newbold, "Spurious Regressions in Econometrics," *Journal of Econometrics*, Vol. 2, 1974, 111-120.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-45. Please provide a **95%** confidence interval for the own-price elasticity value of **-0.456** which you present in your testimony at page 3, line 6, and elsewhere.

RESPONSE:

The **95%** confidence intervals for the sum of the **two** price coefficients with **68** degrees of freedom are:

-1.055226 ± 2*0.224174 or

-0.6069 to -1.5036

Evaluating this at the average price and average volume for the **1983-2005** period we obtain the **95%** confidence interval for the own-price elasticity to be:

-0.262 to -0.650

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-46. On page 38 of your testimony, at lines 13 – 15, you make the following statement:

"To imply that major structural changes in market conditions faced by single piece mail have not changed the elasticity of single piece mail at all is ... incredible"

- a. Please confirm that your estimate of the own-price elasticity for First-class single-piece letters in **1983** as shown in Table A-8 on page 9 of Appendix A is -0.428.
- b. Please confirm that your estimate of the own-price elasticity for First-class single-piece letters in **1995** as shown in Table A-8 on page 9 of Appendix A is -0.425.
- c. Do you believe that the availability and strength of competing substitutes for First-class single-piece mail was greater in **1995** than in **1983**? Please explain fully.
- d. Do you believe that your own-price elasticity estimates for **1983** and **1995** are credible, in light of your statement on page 38 quoted above? Please explain fully.

RESPONSE:

- a. Confirmed.
- b. Confirmed
- c. - d. I did not investigate, and had no reason to investigate, the period between **1983** and **1990**. My point elasticity estimates from VES demand assumptions show that the elasticity increased between **1990** and **1995**. My own focus was on the post-1995 period when Internet Diversion is acknowledged to have become a growing and significant competitive threat to single piece mail.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-47. Please refer to page 24 of your testimony, line 3. Please explain the distinction between "commercial checks" as you use that term, and any other types of checks.

RESPONSE:

"Commercial checks" is the terminology used in The 2004 Federal Reserve Payments Study. Please refer to that study for the distinctions you request, especially Appendix A. See also

<http://www.federalreserve.gov/paymentsystems/checkservices/commcheckcolqtr.htm>

RE RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIF
 TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE
 Revised. October 20, 2006

USPSIGCA-T1-48. On page 39 of USPS-T-7, lines 5 - 8, witness Thress testified as follows:

"Given the current level of real First-Class letters prices and the price elasticities presented in Tables 13 and 16 below, a 10 percent increase in the price of First-class single-piece letters, holding the price of First-class workshared letters constant, will lead to a 5.9 percent reduction in First-class single-piece letters volume"

The derivation of this 5.9 percent figure is as follows:

- (i) For GFY 2005, the nominal price of First-class single-piece letters, as shown in LR-L-63 at page 27, Table 63-5, was \$0.453295. For GFY 2005, the average value of the price deflator used by witness Thress in this case had a value of 1.104693 (LR-L-63, Table 63-16, page 65). Dividing the nominal price by the price deflator produces a real price of First-class single-piece letters for GFY 2005 of \$0.410336.
- (ii) A 10 percent increase in the price of First-class single-piece letters would lead to a price for First-Class single-piece letters of \$0.451369, which is equal to \$0.410336 * 1.10.
- (iii) The sum of the coefficients on the current and lagged price of First-Class single-piece letters in witness Thress's equation (called the "long-run own-price elasticity" by witness Thress) is equal to -0.183741.
- (iv) Given the functional form of witness Thress's demand equation, the impact of a 10 percent increase in the price of First-class single-piece letters would be equal to the following:

$$\text{Percent change in volume} = (\$0.451369 / \$0.410336)^{-0.183741} - 1 = -1.736\%$$
- (v) The nominal value for the average First-Class worksharing discount for GFY 2005 is equal to \$0.079713 (LR-L-63, Table 63-8, page 41). Dividing by the price deflator (1.104693) produces a real discount for GFY 2005 of \$0.072158.
- (vi) An increase in the average price of First-class single-piece letters of \$0.041034 (\$0.451369 - \$0.410336), holding the price of First-Class workshared letters constant, will increase the average worksharing discount from \$0.072158 to \$0.113192 (\$0.072158 + \$0.041034).

(vii) The coefficient on the average worksharing discount in witness Thress's First-class single-piece letters equation is -0.095656.

(viii) Given the functional form of witness Thress's demand equation, the impact of a change in the average worksharing discount from \$0.072158 to \$0.113192 would be equal to the following:

$$\text{Percent change in volume} = (\$0.113192 / \$0.072158)^{-0.095656} - 1 = -4.215\%$$

(ix) Combining the impacts shown in steps (iv) and (viii) above, the full impact of a 10 percent increase in the price of First-class single-piece letters, holding the price of First-class workshared letters constant, will be equal to the following:

$$[1 + (-1.736\%)] \cdot [1 + (-4.215\%)] - 1 = -5.9\%$$

- a. Please confirm that steps (i)–(ix) presented above are mathematically correct, and correctly reproduce the result (i.e., the 5.9 percent reduction) described by witness Thress. If you cannot confirm, please explain fully.
- b. Turning to your analysis, please confirm that the demand equation which you present in Table A-8 on page 9 of Appendix A of your testimony is the demand equation for First-class single-piece letters which you are proposing be adopted in this case. If you cannot confirm, please explain fully.
- c. Please confirm that the sum of the coefficients on the current and lagged price of First-class single-piece letters in your equation, which you present in Table A-8 on page 9 of Appendix A of your testimony, is equal to -1.0552 (-0.9076 plus -0.1476). If you cannot confirm, please explain fully.
- d. Please confirm that, given the functional form of your equation, the impact of a 10 percent increase in the price of First-Class single-piece letters would be equal to the following:

$$\text{Change in volume (pieces per adult per day)} = (\$0.451369 - \$0.410336) \cdot (-1.0552) = -0.0433$$

If you cannot confirm, please explain fully.

- e. Please confirm that the coefficient on the average worksharing discount in your equation is identified as C(31) in Table A-8 on page 9 of Appendix A

of your testimony and has a value of 1.268284. If you cannot confirm, please explain fully.

- f. Please reconfirm from step (vi) above that an increase in the average price of First-class single-piece letters of \$0.041034 (\$0.451369 - \$0.410336), holding the price of First-class workshared letters constant, will increase the average worksharing discount from \$0.072158 to \$0.113192 (\$0.072158 + \$0.041034). If you cannot confirm, please explain fully.
- g. Please confirm that, given the functional form of your equation, the impact of a change in the average worksharing discount from \$0.072158 to \$0.113192 would be equal to the following:

$$\begin{aligned} \text{Change in volume (pieces per adult per day)} &= (\$0.113192 - \$0.072158) * (1.2683) \\ &= +0.0520 \end{aligned}$$

If you cannot confirm, please explain fully.

- h. Please confirm that, combining the impacts shown in d. and g. above, the total change in the volume of First-class single-piece letters (pieces per adult per day) predicted by your model, given a 10 percent increase in the price of First-class single-piece letters, holding the price of First-class workshared letters constant, will be equal to an increase of 0.0087 (minus 0.0433 plus 0.0520). If you cannot confirm, please explain fully.
- i. Please confirm that the calculations presented above show that your demand equation would predict that an increase in the price of First-class single-piece letters, holding the price of First-class workshared letters and everything else constant, would be expected to lead to an increase in the volume of First-class single-piece letters. If you cannot confirm, please explain fully.
- j. Please confirm that the result postulated in part h. – that your model suggests that an increase in the price of First-class single-piece letters would lead to an increase in the volume of First-class single-piece letters – would be true for any change in the price of First-class single-piece letters which leads to an equal change in the average First-class worksharing discount. If you cannot confirm, please explain fully.
- k. Please confirm that your model would predict that a reduction in the price of First-class single-piece letters, coupled with an equal reduction in the average First-class worksharing discount, would predict a reduction in the volume of First-class single-piece letters. If you cannot confirm, please explain fully.

- I. Please confirm that the results identified in parts h. – k. of this question are at odds with basic economic theory. If you cannot confirm, please explain fully.

RESPONSE:

a. Confirmed.

b-f. Not confirmed. It seems you are calculating the change in volume for a percentage change in price. The sum of the coefficients of single-piece price and its lag which I have estimated gives the change in volume for one unit change in price not the change in volume for 1% change in price. Note that 1 unit change means $(X+1)$ whereas 1% change means $(X+0.01*X = 1.01*X)$. The values you are using are not elasticities but slopes which should be evaluated at the average price and average volume over the entire period to obtain the elasticities and then to perform the exercise. My single-piece own-price elasticity is -0.456 and for the workshared discount in the single-piece equation it is $+0.0795$ with the sum of these two elasticities being -0.3765 . The impact cannot be positive.

To simplify the process and to be comparable to your results, I will reproduce your steps (i)-(ix) below. The only difference is that I am replacing Thress' own-price elasticity of -0.183741 with my own-price elasticity of -0.455699 and the Thress workshared discount elasticity of -0.095656 with my workshared discount elasticity of $+0.0794552$. The latter elasticity was calculated as follows:

Workshared Discount Elasticity = Workshared Discount Coefficient * (Average Workshared Discount over 1983-2005 divided by the Average Single-Piece Volume over 1983-2005)

Workshared Discount Coefficient = 1.268284

Average Workshared Discount = 0.0610

Average SP Volume = 0.9737

Workshared Discount Elasticity = $1.268284 \cdot (0.061/0.9737) = +0.0795$

(i) For GFY 2005, the nominal price of First-class single-piece letters, as shown in LR-L-63 at page 27, Table 63-5, was \$0.453295. For GFY 2005, the average value of the price deflator used by witness Thress in this case had a value of 1.104693 (LR-L-63, Table 63-16, page 65). Dividing the nominal price by the price deflator produces a real price of First-class single-piece letters for GFY 2005 of \$0.410336.

(ii) A 10 percent increase in the price of First-class single-piece letters would lead to a price for First-class single-piece letters of \$0.451369, which is equal to $\$0.410336 \cdot 1.10$.

(iii) The sum of the coefficients on the current and lagged price of First-Class single-piece letters in witness Thress's equation (called the "long-run own-price elasticity" by witness Thress) is equal to -0.183741 .

(iv) Given the functional form of witness Thress's demand equation, the impact of a 10 percent increase in ~~the~~ price of First-class single-piece letters would be equal to the following:

$$\text{Percent change in volume} = (\$0.451369 / \$0.410336)^{-0.455699} - 1 = -4.25\%$$

(v) The nominal value for the average First-Class worksharing discount for GFY 2005 is equal to \$0.079713 (LR-L-63, Table 63-8, page

41). Dividing by the price deflator (1.104693) produces a real discount for GFY 2005 of \$0.072158.

(vi) An increase in the average price of First-class single-piece letters of \$0.041034 ($\$0.451369 - \0.410336), holding the price of First-Class workshared letters constant, will increase the average worksharing discount from \$0.072158 to \$0.113192 ($\$0.072158 + \0.041034).

(vii) The coefficient on the average worksharing discount in witness Thress's First-class single-piece letters equation is 0.0794552.

(viii) Given the functional form of witness Thress's demand equation, the impact of a change in the average worksharing discount from \$0.072158 to \$0.113192 would be equal to the following:

$$\text{Percent change in volume} = (\$0.113162 / \$0.072158)^{0.0794552} - 1 = 3.64\%$$

(ix) Combining the impacts shown in steps (iv) and (viii) above, the full impact of a 10 percent increase in the price of First-class single-piece letters, holding the price of First-Class workshared letters constant, will be equal to the following:

$$[1 + (-4.25\%)] * [1 + (3.64\%)] - 1 = -0.76\%$$

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised. October 20, 2006

USPS/GCA-T1-49. Please refer to Table 3 on page 20 of your testimony

- a. Please confirm that the years 2000 - 2003 identified in Table 3 refer to calendar years 2000 - 2003. That is, please confirm that "2000" refers to the time period from January 1, 2000 through December 31, 2000. If you cannot confirm, please identify what time period is covered by the year identified as "2000" in Table 3.
- c. What is the source of the data identified as "Commercial checks"?
- d. Why are "Bill Payments by SP Mail" only provided for the years 2002 and 2003?
- e. Please provide an updated version of Table 3 which includes "Bill Payments by SP Mail" data for 2000 and 2001.
- f. Are data available for any of the payment instruments presented in Table 3 for any years more recent than 2003? If so, please provide all such data.
- g. You cite "Thress R2005-1" as the source for the 'SP Volume' and "SP Prices" data in this Table. Why did you not use data from the current rate case?
- h. You state in a note that 'USPS quarterly SP volume & price are converted to regular annual data to correspond to other annual data given in above table.' Please provide a step-by-step example of how these data were converted to "regular annual data."
- i. Are you aware that the Fiscal Years for which Household Diary Studies report data are Postal Fiscal Years? That is, the 2004 Household Diary Study reports data for the time period from October 1, 2003 through September 30, 2004. Did you convert this data to 'regular annual data' in the same way as was done for 'USPS quarterly SP volume & price' data? If not, why not? If not, please produce, if feasible, an updated version of Table 3 which uses volume, price, and Household Diary Study data from consistent time periods.
- j. Please confirm that First-class Mail volumes and price data are available through 2005.
- k. Please confirm that Household Diary Study data are available through 2005.
- l. Please provide an updated version of Table 3 which includes data through 2005 wherever such data are available.

RESPONSE:

- a. Most of the data in the columns you refer to are annual, calendar year data. The only exceptions are the data from the HHD Study, which are fiscal year numbers for the rows labeled "Bill Payments..." and "Statements Per...". In the revised Table 3 submitted with this

interrogatory response, I have used **fiscal** year data for the rows 'SP Volume...' and 'SP Real Price...' so that the **cross** price elasticities for Bill Payments and Statements with respect to the single piece mail price are based on consistent definitions of years. The intention was to convert all the above-mentioned data to annual. The **SP** real price and volume data were so converted, and should have been converted back to **fiscal** data when it was determined the HHD data could not **be** converted from a postal fiscal year to annual year **basis**. The revised data in Table 3 are consistent with respect to my **testimony** and do not alter it in any material way. With respect to the revised **cross** elasticities, they are very close and well above an absolute value of **1.0** using pure **fiscal** year data or mixed **fiscal/annual** year data for the time **periods** 2000-2003 and 2001-2003. For the 2002-2003 period, the values **differ**, **but** the revised cross elasticity is still well above an absolute value of 1.0.

- b. N/A – **No** pending question.
- c. See my answer to 47.
- d. To the best of our knowledge, **this** information is not available from the HHD Study for those years, which was our **source** for the 2002 and 2003 data.
- e. See my answer to d.
- f. Not to my knowledge. The FED study has not been updated past the year **2003**.
- g. We did not have the corresponding data for electronics payments instruments to update the table beyond the **years** covered in the table.
- h. See my answer to **a.**, and the revised Table 3.
- i. Yes. Please see my answer to **a.** and the revised Table 3.
- j. Confirmed.
- k. Confirmed.
- l. This is not possible for reasons explained in **f.** and **g.** Further, for the few cells of data where it is possible, it is unclear from your question what **base year(s)** and **end year(s)** you are asking for.

Table 3
Descriptive Statistics Estimating Arc Elasticities for Single-Piece Mail and Electronic Payments

Arc Elasticities 2000-2003
Revised September 28, 2006

Number of payments (millions)	Annual Data				Cross Price Elasticities With Respect to Single-Piece Price			Own Price Elasticities With Respect to GDP Computer Price Deflator			Own Price Elasticities With Respect to BLS Computer Price Index		
	2000	2001	2002	2003	2000- 2003	2001- 2003	2002- 2003	2000- 2003	2001- 2003	2002- 2003	2000- 2003	2001- 2003	2002- 2003
Payment Instrument													
General Purpose Credit Cards	12,300	13,203	14,172	15,212	4.83	3.20	4.53	-0.82	-0.62	-0.81	-0.42	-0.39	-0.36
Private Label Credit Cards	3,301	3,445	3,586	3,753	2.68	1.88	2.70	-0.38	-0.37	-0.37	-0.24	-0.23	-0.22
Signature Debit	5,269	6,580	8,218	10,283	18.54	11.78	15.37	-2.50	-2.29	-2.08	-1.69	-1.44	-1.24
PIN Debit	3,010	3,644	4,410	5,338	15.12	9.78	12.99	-2.04	-1.90	-1.76	-1.38	-1.20	-1.04
ACH	6,211	7,045	7,990	9,062	8.98	6.02	8.28	-1.21	-1.17	-1.12	-0.82	-0.74	-0.67
EBT	538	621	716	827	10.52	6.99	9.52	-1.42	-1.36	-1.29	-0.86	-0.86	-0.77
Total	30,629	34,678	39,263	44,455	8.83	5.93	8.16	-1.19	-1.15	-1.10	-0.60	-0.73	-0.68
Checks (Own Price)	41,900	40,090	38,357	36,700	-2.43	-1.78	-2.67						
Commercial checks	16,993	16,905	16,588	15,805	-1.37	-1.37	-2.81						
Bill Payments by SP mail (FY)			11,998	11,088									
Bill Payments Per Household Per Week (FY)	2.9	3.2	3.4	3.2									
Statements Per Household Per Week (FY)	1.1	1.4	1.2	1.1									
SP Volume /Pop/Days (FY)													
SP Real Price (FY)													
SP Volume /Pop/Days	3.53669	3.36397	3.23447	3.04258	-2.73	-2.01	-3.66						
SP Real Price	0.40889	0.41030	0.42295	0.42980									
GDP Deflator for Computers	100.00	82.19	70.54	62.10									
BLS Price Index for Computers	70.62	50.64	38.78	30.96									

Notes: USPS quarterly SP volume & price are converted to regular annual data to correspond to other annual data given in above table
FY denotes Postal Fiscal Year.

The shaded area shows the revised numbers based on the Postal Fiscal Year. All other data are based on calendar year.

Sources:

Payment Instruments data are obtained from 2004 Electronic Payments Study
Commercial checks are obtained from the Bureau of Economic Analysis & various The Household Diary Study reports.
SP Volume and SP prices are obtained from Thress R2005-1.
GDP deflator and BLS price index for computers are from BEA & BLS.

WITNESSES (GREETING CARD ASSOCIATION WITNESS CL
 TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE
 Revised: October 20, 2006

USPS/GCA-T1-50. At page 18, line 15, you describe the elasticity estimates presented in Table 3 on page 20 of your testimony thusly, "This estimation assumes short run economic conditions, where ceteris Paribus conditions are presumed to hold for all other factors affecting the demand for electronic payments other than their own prices and postal prices."

- a. Please confirm that the numbers presented in Table 3 under the columns identified as "Cross Price Elasticities" attribute all of the change in the number of payments to the real price of First-class single-piece letters. Specifically, please confirm that these "Cross Price Elasticity" estimates assume that changes in the price of the electronic payments themselves have no effect on the volume of electronic payments. If not confirmed, please explain fully.
- b. Please confirm that the numbers presented in Table 3 under the columns identified as "Own Price Elasticities" attribute all of the change in the number of payments to the price of electronic payments, as measured by the implicit GDP price deflator for computers. If not confirmed, please explain fully.
- c. In light of your answers to a. and b. above, please confirm that the "Cross Price Elasticities" and "Own Price Elasticities" presented in Table 3 are not consistent. That is, please confirm that, for example, if the own-price elasticity for general purpose credit cards is equal to -0.62, then the cross-price elasticity for general purpose credit cards with respect to postage prices is not equal to 4.63. If not confirmed, please explain fully.
- d. Please confirm that, based on how the numbers in your Table 3 were calculated, if the own-price elasticity for general purpose credit cards is equal to -0.62, then the cross-price elasticity with respect to the price of First-class single-piece letters is equal to **zero**. If not confirmed, please explain fully.
- e. Please confirm that, based on how the numbers in your Table 3 were calculated, that if the own-price elasticities for electronic payment instruments were all equal to the numbers shown in Table 3, then the cross-price elasticity with respect to the price of First-Class single-piece letters would be equal to zero for all of the electronic payment instruments presented in Table 3. If not confirmed, please explain fully.
- f. Did you make any attempts to estimate own- and cross-price elasticities jointly for any of the payment instruments shown in Table 3? If so, please provide the results of such experiments. If not, why not?

RESPONSE:

- a. Not confirmed. These are descriptive statistics only, and do not purport to correct for all other possible influences on the volume of electronic

payments instruments. Moreover, they are point estimates, not linear regressions of the theoretical equation (2) on page 18.

b. Please see my answer to a.

c.-f. Not confirmed. I have not yet identified the full universe of competing substitutes for payments mail. Had I been able to do so, the sum of the cross price elasticities would approximate the own price elasticity. What your numbers suggest is that the intensity of competition in the payments market faced by the Postal Service is even greater than I discuss in my testimony.

SED RESPONSES OF GREETING CARD ASSOCIATION WITH
 TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE
 R I C

CLIFTON
 20,2006

USPSIGCA-TI-51. Please refer to Table 3 on page 20 of your testimony. Please calculate price elasticities with respect to the GDP Computer Price Deflator for Checks, Commercial Checks, Bill Payments by SP Mail, Bill Payments per Household per Week, Statements per Household per Week. SP Volume / Pop / Days, and WS Volume / Pop / Days.

RESPONSE:

The data for own price elasticity of payments instruments with respect to Commercial Checks, Bill Payments by SP mail, and SP Volume all have a positive sign, as expected, since economic theory predicts the higher the price of the competing substitute the greater the volume of the other good. The corresponding data with respect to Bill Payments and Statements is erratic, inconsistent, and one cannot draw any inference from it

Number of payments (millions)	Annual Data				Own Price Elasticities With Respect to GDP Computer Price Deflator		
	2000	2001	2002	2003	2000- 2003	2001- 2003	2002- 2003
Payment Instrument							
Checks (Own Price)	41.900	40.090	38.357	36.700	0.327	0.346	0.361
Commercial checks	16.993	16.905	15.585	15.805	0.184	0.286	0.393
Bill Payments by SP mail (FY)			11.956	11.096			0.608
Bill Payments Per Household Per Week (FY)	2.9	3.2	3.4	3.2	-0.272	0.000	0.477
Statements Per Household Per Week (FY)	1.1	1.4	1.2	1.1	0.000	0.803	0.676
SP Volume / Pop / Days (FY)	3.56344	3.44667	3.27098	3.05866	0.373	0.422	0.540
GDP Deflator for Computers (FY)	102.94	87.09	72.84	63.86			
GDP Deflator for Computers	100.00	82.19	70.54	62.10			

Note: FY denotes Postal Fiscal Year.

Revised: October 20, 2006

USPS/GCA-T1-52. Please refer to Table 3 on page 20 of your testimony. You calculate a price elasticity of Statements per Household per Week with respect to the First-class single-piece letters price.

- a. What percentage of statements sent to households are sent as First-class single-piece letters?
- b. If most statements sent to households are sent as First-class workshared letters, wouldn't it make more sense to estimate the price elasticity of statements with respect to the price of First-class workshared letters? In [sic] not, why not?

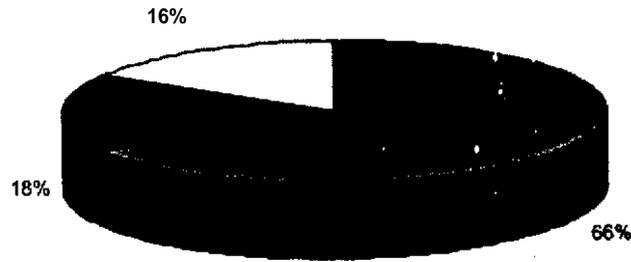
RESPONSE:

a. and b. I do not have "global" evidence on this from all industry statements sent to households, but the attached "Figure 5: Banking Industry's Outgoing First Class Mail Volume", page 8, from a survey by the American Bankers Association, "Postal Operations Survey Report—2000". is a strong indication that a great deal of statements mail is sent at the full single piece rate.

ABA POSTAL OPERATIONS SURVEY REPORT

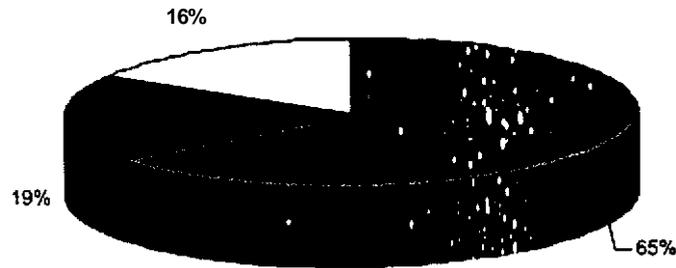
FIGURE 5: BANKING INDUSTRY'S OUTGOING
FIRST CLASS MAIL VOLUME
1999

By Program Type



■ Full Postage ■ Delivery Point Bar Code □ Nonautomation Retail Presort

By Weight



■ Up to 1 Ounce ■ 1+ to 2 Ounces □ More than 2 Ounces

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20.2006

USPSIGCA-TI-53. Please refer to Table 3 on page 20 of your testimony. Why did you calculate an elasticity for First-class workshared letters volume (WS Volume \div Pop / Days) with respect to the price of First-Class single-piece letters? What was your expectation with respect to the magnitude and sign of this elasticity? Why?

RESPONSE:

The inclusion of the row labeled "WS Volume/Pop/Days" was inadvertent and has been dropped in the revised Table 3 attached to the answer to 49. a. That data was not used for any calculation in Table 3.

USPS/GC [redacted] at page [redacted], line [redacted], you [redacted] the [redacted] g, with [redacted] it to the [redacted] estimates presented in Table 3 on page 20 of your testimony, "This estimation is [redacted] short run economic conditions. where ceteris paribus conditions are presumed to hold for all other factors affecting the demand for electronic payments other than their own prices and postal prices."

- a. Please confirm that the National Bureau of Economic Research stated that the U.S. economy was in recession from [redacted] through November, 2001.
- b. Please confirm that total private employment in the U.S. was [redacted] at the end of 2003 than it was at the end of 2000.
- c. Isn't it true that the [redacted] confirmed in a. and b. indicate that the assumption of ceteris paribus [redacted] was not correct.
- d. If you attempted to control for [redacted] in economic conditions from 2000 to 2003, how do you think this would have affected [redacted] at least [redacted] as shown in Table 3 of your testimony? [redacted], how would you think [redacted] for changes in economic conditions would [redacted] on our estimates of the elasticities of [redacted] statements, and total First-class mail volume with respect to the [redacted] of First-class [redacted] letters?

RESPONSE:

- a. Confirmed.
- b. Confirmed.
- c. Not confirmed. People have to pay most recurrent bills at the same volume even if they are cutting back on their overall level of expenditure. For example, during a recession or during a personal period of unemployment, a household may have a much smaller credit card bill to pay each month. However, they still have a bill to pay, which can be paid on-line or through the mail.
- d. I don't know.

REVISED RESPONSES OF GREETING CARD ASSOCIATION WITNESS CLIFTON
TO INTERROGATORIES OF UNITED STATES POSTAL SERVICE

Revised: October 20, 2006

USPS/GCA-T1-55. At page 18, line 15, you state the following, with respect to the elasticity estimates presented in Table 3 on page 20 of your testimony, "This estimation assumes short run economic conditions. where ceteris paribus conditions are presumed to hold for all other factors affecting the demand for electronic payments other than their own prices and postal prices."

- a. Please confirm that the price elasticities associated with checks, bills, statements, and First-class mail volume, presented in Table 3, attribute all of the change in these volumes to the real price of First-class single-piece letters. Specifically, please confirm that these elasticity estimates assume that changes in the price of electronic payments have no effect on these volumes.
- b. Do you believe that the volume of bill and statement mail is affected by the availability and strength of competing substitutes? Specifically, do you believe that the volume of bill and statement mail would be affected by the availability and price of electronic payments even if the real price of First-Class Mail remained constant?
- c. If you attempted to control for changes in the availability and strength of electronic payment alternatives to the mail from 2000 to 2003, how do you think this would have affected the elasticities presented in Table 3 of your testimony? Specifically, what effect do you think controlling for changes in the availability and strength of electronic payment alternatives would have on your estimates of the elasticity of bills, statements, and total First-class Mail volume with respect to the price of First-Class single-piece letters?

RESPONSE:

- a. See my answer to 50. a.
- b. Yes, because by "availability", I am assuming what you mean is that electronic substitutes compete on price and non-price grounds with First Class Single Piece Mail. The point I am making in my testimony, however, is that the intensity of this combination of competitive forces aligned against single piece mail absolutely requires the Postal Service to do better than keeping the real price of single piece letters constant, in addition to competing on non-price grounds as well. I am deeply concerned, however, that the rate proposals for single piece letters in R2005-1 and again in R2006-1 suggest USPS is throwing in the towel against electronic competition for payments mail, and giving up trying to achieve even a constant real price for single piece mail.
- c. I don't know.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPSIGCA-TI-56: You have stated in several places in your testimony and in your responses to USPS/GCA-T1-9, USPS/GCA-T1-33, and USPS/GCA-T1-42 that the non-linear transformation which witness Thress applies to consumption expenditures on Internet Service Providers in his testimony 'is not a Box-Cox transformation.'

- a. Please confirm that witness Thress's model can be expressed as follows:

$$\ln(V) = a + b(X^\lambda) + \dots$$

- b. Please confirm that a Box-Cox model can be expressed as follows:

$$\ln(V) = a' + b'[(X^\lambda - 1) / \lambda] + \dots$$

- c. Please confirm that the Box-Cox model equation in b. could be re-written as follows:

$$\ln(V) = a' + (b'/\lambda)(X^\lambda) - (b'/\lambda) + \dots$$

- d. Please confirm that the Box-Cox model equation in c. could be re-written as follows:

$$\ln(V) = [a' - (b'/\lambda)] + (b'/\lambda)(X^\lambda) + \dots$$

- e. Please confirm that the Box-Cox model equation in d. could be re-written as follows:

$$\ln(V) = a + b(X^\lambda) + \dots$$

$$\text{Where } a = a' - (b'/\lambda) \text{ and } b = (b'/\lambda)$$

- f. Please confirm that witness Thress's model equation in a. is identical to the Box-Cox model equation in e.
- g. Please confirm that your statements that witness Thress's transformation "is not a Box-Cox transformation" (e.g., page 31, line 3 of your testimony) are not correct.
- h. Would the fact that witness Thress does, in fact, use a correct Box-Cox transformation in his work change your answer to USPS/GCA-T1-33?
- i. Would the fact that witness Thress does, in fact, use a correct Box-Cox transformation in his work change your answer to USPS/GCA-T1-42?

RESPONSE:

a-i. Please see Dr. Kelegian's response to USPS/GCA-2, redirected to GCA witness Kelegian. Before I continue, I should make it clear that, Mr. Thress nowhere in his testimony shows or states that he has reformulated the Box-Cox transformation, In addition to Dr. Kelegian's response and assuming that Mr. Thress has deliberately reformulated his Box-Cox specification, I will show below

that this reformulation of Box-Cox in R2006-1 has resulted in two relevant variables being omitted from his model. This results in a mis-specified model. This can introduce serious bias in the model with severe consequences.

To begin with, let's write the complete Internet variables in the Single-Piece equation for R2006-1 with the correct Box-Cox specification:

$$L(n) = a_0 + (b_0 + b_1 * T_1 + b_2 * T_2) (ISP^{\lambda} - 1) / \lambda$$

Where $T_1 = \text{Trend}$, $T_2 = \text{T02Q4}$, and $ISP = \text{CS_ISP}$

Let's reformulate this specification and regroup relevant terms:

$$L(n) = [(a_0 - b_0 / \lambda)] + [(b_0 / \lambda + b_1 / \lambda * T_1 + b_2 / \lambda * T_2) * (ISP^{\lambda})] + [(-b_1 / \lambda) * T_1 + (-b_2 / \lambda) * T_2]$$

Let $a_0' = a_0 - b_0 / \lambda$ in the first bracket; $b_0' = b_0 / \lambda$, $b_1' = b_1 / \lambda$, and $b_2' = b_2 / \lambda$ in the second bracket; and $c_1' = b_1 / \lambda$, and $c_2' = b_2 / \lambda$ in the third bracket. Now we get

$$L(n) = [a_0'] + [(b_0' + b_1' * T_1 + b_2' * T_2) * (ISP^{\lambda})] + [c_1' * T_1 + c_2' * T_2]$$

Below I have provided Thress's Single-Piece equation given in LR-L-64, file, `demandequations.prg`:

```
equation singlepiece2.ls bgvol01sp = c01sp(1) + c01sp(2)*employ(-1) + c01sp(3)*empl_t(-1) +
(c01sp(4)+c01sp(26)*trend+c01sp(25)*t02q4)*(cs_isp^lcoef(1)) + c01sp(7)*msadj +
c01sp(8)*mc95 + c01sp(9)*d2004_05q1 + x_d*d1_3ws + c01sp(10)*px01sp +
c01sp(11)*px01sp(-1) + c01sp(12)*sep1_15 + c01sp(13)*sep16_30 +
c01sp(14)*(oct+nov1_dec10) + c01sp(15)*(dec11_12+dec13_15+dec16_17+dec18_19) +
c01sp(16)*(dec20_21+dec22_23+dec24) + c01sp(17)*(dec25_jan1+jan_feb) + c01sp(18)*march
+ c01sp(19)*apr1_15 + c01sp(20)*apr16_may + c01sp(22)*gqtr1 + c01sp(23)*gqtr2 +
c01sp(24)*gqtr3 + (0-c01sp(22)-c01sp(23)-c01sp(24))*gqtr4 + 100000000*(lcoef(1) -
@abs(lcoef(1))) + 100000000*((1-lcoef(1)) - @abs(1-lcoef(1)))
```

Comparing the correctly reformulated Box-Cox specification with Mr. Thress's reformulated Box-Cox, the terms in the second bracket are similar to those that Mr. Thress has given in his equation. However, those terms in the third bracket,

that is, the two time trend variables of T1 & T2 are missing from Thress's demand equation above. To be considered a correctly reformulated Box-Cox specification, these two relevant variables must be **explicitly** included in this equation. Given that these two relevant time trend variables are omitted, Mr. Thress's model is mis-specified, thus, **leading** to biased estimates. (Please see William H. Greene, Econometric Analysis, 1993, Second Edition, Macmillan Publishing Company, New York. section 8 4 2 'Omission of Relevant Variables, pages 245-247.)

What are the empirical consequences of Thress's omitted variables? I did a preliminary investigation by adding the two trend variables of TREND and T02Q4 to Mr. Thress's equation above and **re-estimated** the model using his program given in LR-L-64. Table One provides partial output for the correctly reformulated Box-Cox transformation as **well** as Mr. Thress's original estimation in Panels A & B, respectively.

	Panel A Thress's Model with Correctly Reformulated Box-Cox Transformation			Panel B Thress's Original Model		
	Coefficients	Std. Error	T-Ratio	Coefficients	Std. Error	T-Ratio
CONSTANT	0.59774	0.20964	2.85129	0.01562	0.12514	0.12482
EMPLOY(-1)	1.01400	0.33120	3.06157	0.67930	0.10804	6.28755
EMPL_T(-1)	4.00780	0.00322	-2.42465	-0.00221	0.00079	-2.79245
CS_ISP_L01SP	0.69108	0.06837	10.10860	0.75321	0.04588	16.41696
CS_ISP_L01SP_T	-0.00856	0.00089	-9.58340	-0.01109	0.00058	-19.00949
CS_ISP_L01SP_T02	0.12634	0.01535	9.46331	-0.00814	0.00171	-47.6793
MSADJ	0.01766	0.00523	3.37763	0.02046	0.00795	2.57555
MC95	0.02917	0.01594	1.83019	0.05861	0.01076	5.44669
D2004_05Q1	0.03946	0.01526	2.58561	0.04349	0.014%	2.90700
D1_3WS	0.01567	0.05529	0.28333	-0.09566	0.00993	-9.63352
TREND	-0.00625	0.00251	-2.48955			
T02Q4	-0.09542	0.00938	-10.17524			
PX01SP	4.27598	0.11929	-2.31360	-0.07115	0.10636	-0.66891
lag1	4.055%	0.08192	-0.68310	-0.11259	0.10189	-1.10501
lag2	0	0	0	0	0	0
lag3	-0	0	0	0	0	0
lag4	0	0	0	0	0	0
Own Price Elasticity	-0.331938			-0.18374		

I can make several observations comparing the two estimation results within the Thress model :

- i) Coefficient of the interaction between ISP variable and the time trend (CS_ISP_L01SP_T02) becomes positive.
- ii) Coefficient of the worksharing discount becomes positive and insignificant using a correctly reformulated **Box-Cox** even though Mr. Thress's program stochastically restricts that coefficient to be around -0.0956.
- iii) The two time trends, TREND and T02Q4 are both negative and highly significant, therefore, they are relevant variables. Yet, Thress's arbitrary non-linear transformation of his R2006-1 ISP variable excludes these two time trends, which are necessary aspect of a correctly reformulated **Box-cox**.
- iv) Significantly, the sum of the own price elasticity of the Single-Piece mail becomes -0.332 within Thress's own R2006-1 model compared to his -0.184 using an arbitrary non-linear transformation of his R2006-1 ISP variable.

To further investigate the consequence of Thress's mis-specification of **Box-Cox**, in Table Two I have also provided a preliminary examination of the impact of the Internet on the volume of the Single-Piece mail for my correctly reformulated Box-Cox transformation (Column A) as well as for Mr. Thress's original model (Column B) over several time periods.

Table Two					
R2006-1					
Impact of Internet on the Volume of Single-Piece Mail Letters					
				Column A	Column B
				Reformulated	Thress's
				Box-Cox Model	Original Model
				Coefficients	Coefficients
CS_ISP				0.691079	0.75321
CS_ISP*T				-0.008557	-0.01109
CS_ISP*T02Q4				0.126344	-0.00814
Box-Cox				0.145734	0.122
Period	CS_ISP	Trend	T02Q4	ISP-impact	iSP-impact
1983Q1	0.0000000	49	0	0.0000	0.00000
1988Q2	0.0000451	70	0	0.02142	-0.00674
2000GQ1	0.0409519	117	0	-0.19465	-0.36817
2002GQ3	0.0637703	127	0	-0.26492	-0.46785
2002GQ4	0.0632438	128	1	-0.18583	-0.48110
2003GQ1	0.0655523	129	2	-0.10762	-0.49700
2004GQ1	0.0786080	133	6	0.21472	-0.56452
2004GQ2	0.0791217	134	7	0.29631	-0.57908
2004GQ3	0.0821951	135	8	0.37980	-0.59595
2004GQ4	0.0818597	136	9	0.46136	-0.60982
2005GQ1	0.0826809	137	10	0.54394	-0.62474
2005GQ2	0.0852990	138	11	0.62870	-0.64136
2005GQ3	0.0874551	139	12	0.71357	-0.65760
2005GQ4	0.0895049	140	13	0.79885	-0.67378

As it is shown in Table Two, using **Box-Cox**, the impact of the internet on the single-piece volume is initially positive, then becomes negative and then becomes positive again beginning in 2004GQ1. These results are at odds with the economic reality surrounding the Internet's impact on mail but they are the results of using a correctly reformulated **Box-Cox**.

There are three non-exclusive possibilities as to why Mr. Thress used the R2006-1 non-linear form (ISP^A) form that he used:

- (1) Erroneous understanding of the **Box-Cox** transformation or erroneous **Box-Cox** "reformulation".

- (2) Intentionally choosing his non-linear form (ISP^λ) rather than properly specified Box-Cox transformation $[(X^\lambda - 1)/\lambda]$, because he could not obtain empirical results that were plausible with the latter.
- (3) An arbitrary choice on this particular variable.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPSIGCA-TI-57: In your response to USPS/GCA-T1-42, you indicate that you believe that "[i]ncluding a variable as non-linear without some reasonable justification is nothing but an arbitrary choice."

At line 3 of page 18 of your testimony you present the following hypothetical equation for modeling the demand for First-class single-piece letters.

$$(2) \log(Q) = a - b \log(P) + b_2 \log(P_2)$$

where P is the price of First-class single-piece letters and P₂ is the price of competing electronic alternatives. You go on to state that 'price data for competing substitutes ... is not readily available.'

- a. Would it be appropriate in this case to attempt to find some variable, call it z, to serve as a proxy for $\log(P_2)$ within equation (2)? If not, why not?
- b. Suppose that there was some variable, X, and some constant, y, such that X^y appeared to be very highly correlated with $\log(P_2)$. Would it be appropriate in this case to substitute X^y into equation (2) as a proxy for $\log(P_2)$? If not, why not?
- c. If X^y as described in part b. were used instead of $\log(P_2)$ in equation (2). would the estimated value of b be biased? If so. please provide the precise mathematical formulation for the expected value of b expressed as a function of the true value of b?
- d. If X (not raised to the power y) as described in part b. were used instead of $\log(P_2)$ in equation (2), would the estimated value of b be biased? If so. please provide the precise mathematical formulation for the expected value of b expressed as a function of the true value of b?

RESPONSE:

a-d. Please see Dr. Kelejian's response to USPS/GCA-3 redirected to GCA witness Kelejian.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-58: In your response to USPS/GCA-T1-1(c), you say that witness Thress's own-price elasticity estimate is 'biased' because 'the Box-Cox specification ... dampens the true estimates.'

- a. Please confirm that it is possible for two unbiased estimates to have different values. Further, please confirm that if two estimates are different, this does not necessarily mean that either of the two estimates is 'biased' as you define that term in your response to USPS/GCA-T1-1(a).
- b. Why was the 'Box-Cox specification of the $\ln SF$ variable' used by witness Thress 'incorrect and unnecessary'?
- c. What is the specific bias which is introduced through witness Thress's use of the 'Box-Cox specification of the $\ln SP$ variable'? In your answer, please provide a precise mathematical formula for the expected value of the own-price elasticity from witness Thress's equation. If you are unable to provide such a formula, please explain how you can state with certainty that witness Thress's own-price elasticity is 'biased' as you define that term in your answer to USPS/GCA-T1-1(a).
- d. What is the basis for your assertion in your answer to USPS/GCA-T1-1(c) that "even if Box-Cox is correctly specified, its coefficients should be estimated along with the other coefficients using an appropriate econometric technique such as the maximum-likelihood estimation rather than least square technique. Otherwise, this could also be another source of bias."

RESPONSE:

- a. Confirmed for both.
- b. Please see my response to USPS/GCA-T1-56. Furthermore, there are plausible justifications for entering the $\ln SP$ variable in a linear form as I do in my VES model.
- c. Please see my response to USPS/GCA-T1-56 and the reference to Greene.
- d. Please see Dr. Kelejian's response to USPS/GCA-10, redirected to GCA witness Kelejian.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-59: In your response to USPS/GCA-T1-2, you state that "the definition of the U.S. payments market I adopt is based on that of the 2004 Federal Reserve Bank of Atlanta study."

- a. Please confirm that the "U.S. payments market" as defined in the 2004 Federal Reserve Bank of Atlanta study includes non-cash transactions made at the point of sale. For example, point-of-sale transactions are cited specifically on pages 4, 5, and 6 of this report.
- b. Please confirm that point-of-sale transactions would not have ever been sent through the mail. If you cannot confirm, please give an example of a point-of-sale transaction which **would** involve payment being sent through the mail.
- c. Please confirm that the greatest **increases** in non-cash payments identified in the Federal Reserve's **report** were for credit cards and debit cards.
- d. Please confirm that the vast majority of credit card and debit card payments represent point-of-sale transactions. If you cannot confirm, please provide the basis for your position.
- e. Since credit cards and debit **cards** are **used** primarily for point-of-sale transactions, and point-of-sale **transactions** would never have been sent through the mail, what would you expect the increase in the use of credit cards and debit cards to make point-of-sale transactions to be on the volume of First-class Mail? Please explain fully.

RESPONSE:

a. – e. You are missing the forest for the trees. The Postal Service has repeatedly underestimated the size of the U. S. Payments market in studies such as the annual Household Diary Study, with the result that its share of that market is made to look substantially larger than it actually is. **Ircredibly**, even the latest available 2005 Diary did not include debit cards as a bill payment method even though the 2004 Atlanta FED study indicates that debit card payments were nearly as large as credit card payments in 2003, 16 versus 19 billion respectively.

There is **no** explicit reference to "point of sale" transactions anywhere on pages 4-6 except page 5 with reference to consumer checks being converted into electronic payments. Unless you define point of sale transactions as those that would never have been sent through the mail, a reductio ad absurdum

proposition, then no, I do not confirm your query in b. Many of these transactions have involved the mail in some way in the past: older department store cards, for example, or layaway plans, that involved bills sent by mail and payments made by mail. as well as monthly bank statements sent by mail which included checks processed for various transactions and payments. **I do** confirm that debit cards were the fastest growing non-cash payment method in Exhibit 1 of the 2004 FED study but do not confirm that credit cards showed one of the two greatest increases. Credit cards were the second slowest growing means of non cash payments in that Exhibit 1.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-60: In your response to USPS/GCA-T1-3, you define 'pricing power' as "an economic term referring to the effect that a change in a firm's production price has on the quantity demanded of that product."

On page 4, line 1, of your testimony you make the following assertion. "The facts are the Postal Service has no remaining 'pricing power' in [the U.S. payments] market[], where its correctly measured market share is well under 50%."

- a. Do you believe that the Postal Service had a "correctly measured market share" greater than 50% in the U.S. payments market at one time? Please provide the basis for your answer.
- b. You state in your answer to USPS/GCA-T1-3 that "[p]ricing power relates to the 'Price Elasticity of Demand.' Do you believe that the 'Price Elasticity of Demand' has changed for First-class Mail within the U.S. payments market? Please provide all of the evidence upon which you base your answer.

RESPONSE:

- a. Yes. In addition to the payments instruments listed in the 2004 Atlanta FED study, please refer to annual Household Diary Study tables such as Table 4.12 in the 2005 study. In addition to 'Mail'. the other payments instruments listed are either relatively recent competitors to the mail, or insignificant. or both. Before automatic deduction, the Internet, the credit card, the ATM, etc., mail appears clearly to have been more dominant in the payments market than it is today.
- b. Yes. See Table 3 on page 20 of my testimony, and the requested revisions to that table provided to the Postal Service in my response to USPS/GCA-T1- 49.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-61: In your response to USPS/GCA-T1-44, you confirm that your First-class single-piece letters equation includes the volume of First-class single-piece letters lagged two quarters as an explanatory variable.

- a. In your answer to **USPS/GCA-T1-44(b)**, you say that witness Thress's "econometric program is incapable of dealing with the autocorrelation problems." What do you mean by this statement? Please provide all statistical evidence to suggest that witness Thress's econometric program has failed to adequately deal with autocorrelation in his equations.
- b. In your response to **USPS/GCA-T1-44(b)**, you say that 'Autocorrelation and partial autocorrelation that Mr. Thress has provided ... reveals that his econometric program is incapable of dealing with the autocorrelation problems.' In his testimony on page 321, at line 3, Mr. Thress says that "a 95 percent confidence level is used to test for the presence of autocorrelation." Please confirm that the **partial** autocorrelation values associated with First-class single-piece letters presented by witness Thress in his output file, **demandequations.txt**, in LR-L-64, are not significant at a 95 percent confidence level. If not confirmed, please explain fully.
- c. In your answer to **USPS/GCA-T1-44(b)**, you state that with respect to witness Thress's demand equations "in most cases the calculated Durbin Watson values are in the indeterminant range of critical values.' Please confirm that a Durbin Watson value 'in the indeterminant range" is not evidence of autocorrelation. If not confirmed, please explain fully.
- d. In the third edition of Econometric Analysis by William H. Greene (1997), on page 586, the author says, 'If the regression contains any lagged values of the dependent variable, least squares will no longer be unbiased or consistent.' In your response to **USPS/GCA-T1-47(a)** you confirm that your demand equation for First-class singlepiece letters presented in Table A-8 of your testimony includes a lagged value of the dependent variable. Please confirm that your elasticity estimates from this equation are therefore biased and inconsistent. If not confirmed, please explain fully.

RESPONSE:

a. Please see Dr. Kelejjan's response to USPS/GCA-11 redirected to GCA witness Kelejjan. In addition to Dr. Kelejjan's response, below in Table One, I have provided several examples of the final autocorrelation tables given in Thress' USPS-LR-L-64, file, **demandequations.txt**. It is evident from this table that, in each case, one to several lags have significant autocorrelation at less than a 10% significance level. For example, in the case of Single-Piece

equation, lags 1, 2, 8, and 9 are significant. In the case of Standard A Regular, lag 3 is significant. In the Worksharing equation lag 3 is significant at 5% level. In the case of Standard ECR, lag 3 is significant at less than 5% significance level and etc. In summary, in the majority of mail category equations in the Thress forecasting model, one to several autocorrelation lags are significant.

To illustrate the issue by way of examples, we used the Correlogram autocorrelation procedure in Eviews and applied it to the residuals for Single-Piece and Standard A Regular. These residuals are given in USPS-LR-L-64, file. demandequations.txt. The Q-statistics tests are presented in Table two. The tests confirm that Thress's autocorrelation procedure has not removed all the autocorrelation.

Table One

Single-Piece AUTOCORRELATION STRUCTURE OF FINAL RESIDUALS					
Lag	Auto- Correlation	Partial Auto- Correlation	Standard Error	T-Stat on Partial	
1	-0.192944	-0.197703	0.104828	-1.838267	
2	-0.142928	-0.189308	0.105409	-1.795835	
3	0.103217	0.037505	0.106000	0.353825	
4	-0.108569	-0.111740	0.106600	-1.048212	
5	-0.072175	-0.104853	0.107211	-0.978003	
6	0.009435	-0.072409	0.107833	-0.571494	
7	-0.088379	0.126214	0.108465	-1.183632	
8	-0.123707	-0.208976	0.109109	-1.915299	
9	-0.050280	-0.210224	0.109764	-1.915230	
=====					
Worksharing AUTOCORRELATION STRUCTURE OF FINAL RESIDUALS					
Lag	Auto- Correlation	Partial Auto- Correlation	Standard Error	T-Stat on Partial	
1	0.113749	0.112402	0.134840	0.833599	
2	-0.146698	-0.159241	0.136083	-1.170180	
3	-0.310930	-0.280148	0.137351	-2.039508	
4	-0.219804	-0.208538	0.138675	-1.503789	
5	0.099514	0.080071	0.140028	0.571821	
6	0.108953	-0.012803	0.141421	-0.090529	
7	0.152998	0.01755	0.142857	0.122816	
8	-0.164988	-0.162290	0.144338	-1.124378	
9	-0.057732	0.036171	0.145865	0.247978	
=====					
Standard Regular AUTOCORRELATION STRUCTURE OF FINAL RESIDUALS					
Lag	Auto- Correlation	Partial Auto- Correlation	Standard Error	T-Stat on Partial	
1	-0.047419	-0.048603	0.122169	-0.397835	
2	-0.081203	-0.085251	0.123091	-0.692584	
3	-0.066552	-0.075993	0.124035	-0.612676	
4	-0.188767	-0.209373	0.125000	-1.674984	
5	-0.031691	-0.075655	0.125988	-0.603492	
6	0.184208	0.141777	0.127000	1.116353	
7	0.346392	0.373034	0.128037	2.913486	
8	-0.375005	-0.383206	0.129099	-2.898302	
9	-0.110396	-0.176445	0.130189	-1.355299	
=====					
Standard ECR AUTOCORRELATION STRUCTURE OF FINAL RESIDUALS					
Lag	Auto- Correlation	Partial Auto- Correlation	Standard Error	T-Stat on Partial	
	-0.075358	-0.075453	0.120386	-0.626764	
	-0.079535	-0.085812	0.121268	-0.707621	
	-0.274600	-0.297865	0.122169	-2.438128	
	-0.055716	-0.116286	0.123091	-0.944708	
	0.095012	0.030596	0.124035	0.246672	
	-0.010124	-0.095924	0.125000	-0.767390	
7	-0.047040	-0.103388	0.125988	-0.820613	
8	-0.060207	-0.080472	0.127000	-0.633634	
9	0.188353	0.141571	0.128037	1.105702	

Source: R2006-1, LR-L-64, demandequestions.txt.

Table Two									
Correlogram									
Thress's Single-Piece Residuals					Thress's Standard Regular Residuals				
Lag	AC	PAC	Q-Stat	Prob	AC	PAC	Q-Stat	Prob	
1	-0.193	-0.193	3.525	0.060	-0.046	-0.046	0.152	0.697	
2	-0.142	-0.186	5.453	0.065	-0.079	-0.081	0.801	0.740	
3	0.102	0.037	6.468	0.091	-0.065	-0.073	0.907	0.824	
4	-0.107	-0.110	7.589	0.108	-0.182	-0.199	3.380	0.496	
5	-0.071	-0.102	8.090	0.151	-0.031	-0.070	3.451	0.631	
6	0.009	-0.072	8.098	0.231	0.172	0.132	5.721	0.455	
7	-0.085	-0.126	8.827	0.265	0.315	0.324	13.461	0.062	
8	-0.118	-0.201	10.258	0.247	-0.331	-0.348	22.134	0.005	
9	-0.048	-0.207	10.495	0.312	-0.096	-0.122	22.873	0.006	
10	0.126	-0.012	12.177	0.273	-0.128	-0.103	24.226	0.007	
11	-0.038	-0.097	12.331	0.339	-0.048	0.065	24.416	0.011	
12	-0.175	-0.302	15.634	0.209	0.169	0.046	26.849	0.008	
13	0.172	-0.090	18.887	0.127	0.066	-0.124	27.226	0.012	
14	0.111	0.005	20.252	0.122	0.077	0.038	27.743	0.015	
15	0.041	0.055	20.444	0.156	-0.303	-0.111	35.984	0.002	
16	-0.060	-0.166	20.849	0.184	-0.082	-0.105	36.606	0.002	
17	0.031	-0.075	20.957	0.228	0.015	0.008	36.628	0.004	
18	-0.066	-0.117	21.462	0.257	0.107	0.032	37.722	0.004	
19	0.053	-0.009	21.791	0.295	0.163	0.036	40.311	0.003	
20	0.010	-0.096	21.802	0.351	-0.164	-0.263	42.976	0.002	
21	-0.092	-0.132	22.830	0.353	0.098	0.162	43.955	0.002	
22	0.042	0.045	23.044	0.399	0.218	0.013	48.855	0.001	
23	0.005	-0.022	23.047	0.458	0.056	0.020	49.188	0.001	
24	-0.079	-0.183	23.838	0.471	0.122	-0.102	50.811	0.001	

b. Confirmed. First, arguably, using a 95% Confidence level is somewhat too restrictive. Second, in the four examples I have shown above in Table One, some lags are significant at less than 95% (lag3 in worksharing, lag7 & lag8 in standard regular and etc.), while others are significant at a little more than 95% confidence level (lag1, lag2, lag8 & lag9 in single-piece).

c. Confirmed. A Durbin Watson value "in the indeterminate range" is not evidence of autocorrelation. However, when this happens one needs to perform further testing. The Q-Statistics test given above is an example of such tests, which confirms the presence of autocorrelation in the Single-Piece and the Standard & Regular models.

d. The paragraph from Greene you quote is totally out of context in this section of his text book. You need to read the whole section including, in particular, the last paragraph. What this section says is that if one has a model with the lag dependent variable ($Y_t = Y_{t-1} + \varepsilon_t$) and its residuals are correlated ($\varepsilon_t = \rho \varepsilon_{t-1} + u_t$) then using OLS leads to inconsistent and biased results. Otherwise, if the error terms are not correlated, then, OLS is fine. The following table provides Q-statistics for my Single-Piece linear model obtained using the Correlogram procedure in the Eviews on the residuals.

g	AC	PAC	Q-Stat	Prob
1	0.094	0.094	0.847	0.358
2	-0.002	-0.011	0.847	0.655
3	0.211	0.214	5.156	0.161
4	-0.063	-0.110	5.543	0.236
5	-0.089	-0.068	6.331	0.275
6	-0.034	-0.071	6.450	0.375
7	-0.157	-0.121	8.949	0.256
8	-0.160	-0.116	11.590	0.170
9	-0.057	-0.031	11.927	0.217
10	0.088	0.151	12.736	0.239
11	-0.107	-0.110	13.961	0.235
12	-0.109	-0.119	15.256	0.228
13	0.082	0.014	15.990	0.250
14	-0.007	0.005	15.996	0.314
15	0.113	0.143	17.430	0.293
16	0.065	-0.032	17.918	0.329
17	0.172	0.220	21.321	0.212
18	0.081	-0.013	22.092	0.228
19	0.030	-0.006	22.198	0.275
20	-0.068	-0.205	22.748	0.301
21	-0.193	-0.165	27.288	0.162
22	-0.091	0.024	28.319	0.165
23	-0.046	0.020	28.581	0.195
24	-0.140	0.008	31.083	0.151

My linear Single-Piece model has a lag-dependent variable in it and as the above table shows, the residuals for it are **not** autocorrelated. Therefore, the OLS technique is appropriate for my model, but witness Tnress's program has not eliminated autocorrelation in his model.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-62: USPS/GCA-T1-15(c), asked the following: "If the percentage of checks which are mailed, as opposed to being used at the point of sale, has been increasing over time, could the number of checks which are mailed have increased even as the total number of checks has decreased?"

- a. If a variable, A, increases over time, and a variable, B, decreases over time, please confirm that the product of these two variables, AB, could increase or decrease over time, depending on the specific values of A and B. If not confirmed, please explain fully.
- b. Let A = the percentage of checks which are mailed, as opposed to being used at the point of sale. Let B = the total number of checks. Please confirm that the number of checks which are mailed would be equal to $A*B$. If not confirmed, please explain fully.
- c. Please confirm that, if A has been increasing over time and B has decreased, that the value of AB could have increased over time. If you cannot confirm, please reconcile your answer to your answer to part a.
- d. Please confirm that the answer to USPS/GCA-T1-15(c) is 'Yes.' If you cannot confirm, please reconcile your answer to your answer to parts a - c. above.

RESPONSE:

You are attempting to make a mathematical point, completely outside the actual factual context, that hypothetically, even if overall check volumes are in decline, checks sent through the mail could still be increasing. Yet, the Postal Service's own bill payment data from annual Household Diary studies contradicts your hypothetical! It shows bill payments made by mail per month have dropped from 8.6 in FY2002 to 8.0 in FY2005. Since bill payments made by mail almost always include a check, a decline in such mail means a decline in the number of checks that are mailed.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-63: In your response to USPS/GCA-T1-16, you quote Dennis Carlton and Jeffrey Perloff, 'All else the same, the larger a cross-elasticity of demand, the larger in absolute value is the direct elasticity of demand.'

- a. Please confirm that Carlton and Perloff are talking about true (i.e., not estimated) price elasticities under long-run equilibrium conditions in the quoted text. If not confirmed, please explain fully.
- b. Question USPSIGCA-T1-16 asked about your quote that "[a] direct estimate of that cross price elasticity, b_2 , would greatly sharpen the estimate for b , the own-price elasticity of demand for single piece payments mail." Please confirm that the relationship between the estimated values b and b_2 is a mathematical relationship, not an economic relationship. If not confirmed, please explain fully.
- c. Consider the following two equations:

$$(1) \quad V = a + bX_1 + u$$

$$(2) \quad V = a + b_1X_1 + b_2X_2 + u$$

Please express the OLS estimator of b in equation (1) as a function of the OLS estimator of b_1 in equation (2).

- d. Please confirm that the OLS estimator of b in equation (1) and the OLS estimator of b_1 in equation (2) in part c. of this question will be identical if sample correlation between X_1 and X_2 is zero. If not confirmed, please explain fully.
- e. On page 17, at line 20 through page 18, line 2, you claim that "[o]ther things being equal, a further property of the demand specification in equation (2) is that when the cross price elasticity b_2 is high, the absolute value of the own price elasticity, b , will also tend to be high." Please confirm that this statement is only true mathematically if the prices P and P_2 are correlated. If not confirmed, please explain fully.
- f. Please define the mathematical term 'correlation' as it is commonly used in the fields of statistics and econometrics.
- g. Please answer USPS/GCA-T1-17(d) using the definition of "correlation" in part f. above.

RESPONSE:

a. Not confirmed. Your assertion is totally contradicted by Carlton's and Perloff's discussion surrounding elasticities. For example, on page 647 they define "price correlations [as] a statistical measure of how closely prices move together among different products that are under consideration for inclusion in the same product market." Their entire discussion is about estimated elasticities in the real world,

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-64: Please refer to your response to USPSIGCA-TI-12. Part b. of the question asked what percentage of First-class Mail single piece letters consist of payments sent by households. Please indicate where in your response that percentage is identified, or please provide it now.

RESPONSE:

53.7%. as stated on the last line in the answer to USPSIGCA-TI-12.

for example "in court decisions", not about 'long run equilibrium' or 'true' concepts. The reference to Henderson and Quant in footnote 23 is to those authors' discussion early in their text in a chapter on consumer behavior about price and income elasticities of demand, yet nowhere in that discussion is it claimed that the demand conditions are **long** run or **short** run.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-65: In your response to **USPS/GCA-T1-22(a)**, you say that the BEA deflator in the GDP accounts for **computers** and peripheral prices "performed appreciably better" as a 'proxy for electronic substitutes' because "[t]he GDP deflator has a higher correlation with the single-piece volume compared to the BLS series." Why would you expect the correlation of a variable with respect to mail volume to measure **the** appropriateness of using such a variable as a proxy for the price of non-mail payment methods? Wouldn't a more appropriate test be to consider how well such a variable correlated with the volume of electronic substitutes? Please explain fully.

RESPONSE:

Not enough time series data on the volume of electronic substitutes was available to do the corresponding correlation

RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE

USPS/GCA-T1-67: In your response to USPS/GCA-T1-25, you say that you "have descriptive statistics for the payments market, which indicate own price elasticities for the payments market could be well above -1.0.*" Please provide all such statistics or provide an exact citation to where such statistics might be found in your testimony in this case.

RESPONSE:

Please see Table 3 from my testimony and the discussion surrounding it insofar as the relationship between high cross elasticities and high own price elasticities for the U. S. payments market.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-68: Interrogatory **USPS/GCA-T1-40(a)** asked, "What are the factors which you believe determine the real price of stamps?" You do not appear to have answered this question. Please do so now.

RESPONSE:

As indicated in my original answer the real price of stamps is largely set by USPS management since it can adjust its nominal proposed rate increases in light of its knowledge of inflation and inflationary expectations, including the Board of Governors' decision to accept or reject a rate case recommendation. If you are asking about the cost factors underlying USPS rate requests before the Commission, about 80% of total costs are driven by various collective bargaining agreements, which almost always end up in arbitration for a final decision. Most of these agreements contain substantial COLA's on top of nominal wage increases, and that appears to dictate a floor, but unfortunately not a ceiling. for real price changes in stamps. While I have not studied COLAs for many years, while trying to cap them for federal entitlements when I was Republican Staff Director of the House Budget Committee, I found there was a stable long term relationship for the indexation of wages, namely for all working age Americans, union and non-union combined, COLA's averaged 57% of the CPI, moving up and down around this long run equilibrium figure. That would, possibly, be a good goal for arbitration or legislation that would foster real price Competition against electronic substitutes for FCM.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-69: Interrogatory **USPS/GCA-T1-40(b)** asked, "If the Postal Service does not go to the Postal Rate Commission and seek an increase in the real price of stamps, is there any mechanism by which stamp prices will increase? Please explain." You do not appear to have answered this question. Please do so now.

RESPONSE:

Real stamp prices can increase through deflation, through new product offerings at a new fresh price which cannibalizes some existing product volumes, or through legislative changes such as the now defunct postal reform bill. which tied annual rate increases for a broad set of products on average to inflation.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-70: Interrogatory USPS/GCA-T1-40(c) asked, 'If mail volume declines as a result of an increasing 'presence of competing substitutes due to Internet diversion and electronic payments substitutes for the mail' when nominal stamp prices remain unchanged, what do you believe this indicates about the own-price elasticity for First- Class Mail? Please explain why you believe this.' You do not appear to have answered this question. Please do so now.

RESPONSE:

I would need more information to answer this question for a "real prices matter" decision model. Is inflation positive, negative or zero? If consumers are reacting to nominal prices and they remain unchanged, one cannot say anything about elasticity because one has to have sufficient variation in the independent variable to calculate an elasticity.

**RESPONSE OF IG CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPSIGCA-TI-72: In your response to **USPS/GCA-T1-28(c)**, you say that witness Thress's First-class single-piece letters demand equation does not represent "statistical data that would allow one to calculate an **own-price** elasticity for single piece mail when letters prices are cut' because you are 'talking about a cut in the nominal price of stamps."

- a. **Do** you believe that consumers respond to real prices or nominal prices?
- b. If you believe that consumers respond to real prices, please confirm that witness Thress's First-class **single-piece** letters demand equation represents "statistical data that would allow one to calculate an own-price elasticity for single piece mail when letters prices are cut'. If not confirmed, please explain fully
- c. If you believe that consumers respond to nominal prices. please explain why you did not include the nominal price of First-class single-piece letters in your estimated demand equations for First-class single-piece mail which you present in Appendix A of your testimony.
- d. If you believe that consumers respond to nominal prices, please provide citations in the economics literature which support your position.

RESPONSE:

- a. I do not know as I have not **conducted** a study' **or** seen any. It just strikes me as far-fetched that consumers in **particular** think about real stamp prices when making decisions. What a consumer generally, **and** a consumer of greeting cards in particular, will note about this case is that stamp prices have just gone up from 37 cents to 39 cents, and now – if USPS' proposals are **adopted**—**are** going up suddenly all over again with an increase from ~~39~~ to 42 cents.
- b. See my answer to a. above.
- c. The single piece demand equation is not just for consumers, but for business, government and other entities. Large businesses may well react to real changes. This would be one explanation of why consumers have greatly reduced bill payments by mail in favor of electronic substitutes in recent years (because their decisions are based on nominal stamp increases) while bills sent by large worksharing mailers have not so declined (because their decisions are based on roughly constant real prices).



d. See my answer to a. and c. above.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPSIGCA-TI-73: In your response to **USPS/GCA-T1-29(c)**, you say that 'Mr. Thress' R2006-1 internet variable does not reflect or even capture the price of competing substitutes to First-class single-piece mail.'

In your testimony on page 21, beginning at line 7, you state the following:

"While direct price data are hard to come by for each of these electronic substitutes, I tested both the BLS series for computer prices and the BEA deflator in the GDP accounts for computer and peripherals prices. The latter series performed appreciably better, and I adopt it as a proxy for the prices of electronic substitutes."

- a. Do you believe that "the BEA deflator in the GDP accounts for computer and peripherals prices" reflects or even captures the price of competing substitutes to First-class single-piece mail? If your answer is yes, please explain why you believe this GDP deflator better 'reflects or ... captures the price of competing substitutes' as compared to 'Mr. Thress' R2006-1 internet variable."
- b. Why do you believe that 'Mr. Thress' R2006-1 internet variable' is an inappropriate "proxy for the prices of electronic substitutes"?

RESPONSE:

a. I do not believe there is currently a good proxy available to represent the price of Internet use for mail substitutes. I used what was available, but the lack of an ideal numerical measure is obviously not at the heart of my critique of Thress and my proposed alternative, namely the use of a straightforward VES demand function which seems clearly better suited to identifying changing demand elasticities due to electronic or other substitutes, and therefore better suited to being an input for rate making by the Commission and rate proposals by the Postal Service.

b. Mr. Thress's R2006-1 variable measures the number of Internet subscribers, not the price of Internet use for mail substitutes.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPSIGCA-TI-74: In your response to **USPS/GCA-T1-34(a)**, you confirm "that the Internet variable(s) used by witness Thress were different in R2001-1, R2005-1, and R2006-1."

On page 33 of your testimony, starting at line 5, you make the following statement:

'In R2001-1, the estimated coefficient, lambda, for witness Thress' non-linear transformation of the Internet variable was 0.560; in R2005-1, it was 0.326; and in R2006-1, the value has fallen to 0.122. His non-linear transformation of the Internet variable is tending to a lambda of zero. In terms of mathematics, any variable to the power of zero equals one. This is the same as saying the Internet has no impact on the demand for single piece letters. This is an a priori absurd result which further points to the weakness of Mr. Thress' approach to the demand for single piece mail in the presence of strong competing substitutes."

In your response to **USPS/GCA-T1-34(b)**, you confirmed that "a coherent discussion of an alleged "trend" in the coefficient estimates of a variable requires the definition of the variable to be consistent for each coefficient estimate under discussion."

- a. Please confirm that, because the internet variables used by witness Thress were different in R2001-1, R2005-1, and R2006-1, it is not possible to have a coherent discussion of an alleged "trend" in the lambda coefficients associated with these variables. If not confirmed, please explain fully.
- b. Please confirm that your statement that witness Thress's 'non-linear transformation of the internet variable is tending to a lambda of zero"suffers from the same lack of coherence you acknowledged in response to USPS/GCA-T1-34. If not confirmed, please explain fully

RESPONSE:

a.-b. Not confirmed, These model variations are minor evolutionary changes of essentially the same basic model structure. As a practical matter, therefore, it is legitimate to compare them. The reductio ad absurdum definition of an 'improvement" in Thress' model case by case seems to be that improvement means the same low elasticity or an even lower elasticity, a strange definition of improvement when such a result flies in the face of obvious business facts, as it has case by case since the last litigated case in 2000.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-75: InterrogatoryUSPS/GCA-T1-35(a) asked for evidence "that Mr. Thress's choice criterion did, in fact, lead to an incorrect model" (emphasis added). Your response to this question identified several issues that "can affect the MSE value" (emphasis added). Please confirm that your answer to **USPS/GCA-T1-35(a)** confirms that you have no evidence that Mr. Thress's choice criterion did, in fact, lead to an incorrect model. If not confirmed, please explain fully.

RESPONSE:

Please see Dr. Kelejian's response to USPSIGCA-7 redirected to GCA witness Kelejian and my response to USPSIGCA-TI-56. It was shown that Mr. Thress's equation is mis-specified due to either incorrect Box-Cox transformation or incorrect reformulation of the Box-Cox transformation. Such a result is an example of a specific issue out of the "several issues" referenced in your question above which can lead, and in fact did lead, to an incorrect choice of the model, namely, a Box-Cox that was not a Box-Cox.

RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE

USPS/GCA-T1-76: Interrogatory USPSIGCA-TI-36 asked you to what you referred when you claimed in your testimony that 'Mr. Thress' model ... includes prolonged periods in the 1970s." Please confirm that Mr. Thress's First-class Mail models do not rely upon any data earlier than 1983. so that, in fact. Mr. Thress's model does not rely upon any data from the 1970s at all. If not confirmed, please explain fully.

RESPONSE:

It would be more precise to say that 'RCF models" produced by associates of that firm have involved data from the 1970s rather than "witness Thress' models" per se. RCF forecasting models for the Postal Service in rate cases have involved witnesses Tolley and Thress over the years.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-77: Please confirm that the 'experimental own-price elasticities' which you describe in your response to **USPS/GCA-T1-41** are calculated assuming that all factors remain unchanged during the period surrounding Postal rate changes except for the price of First-class single-piece letters. If not confirmed, please explain fully.

RESPONSE:

Confirmed.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-78: In your response to **USPS/GCA-T1-41**, you indicate that "the experimental own-price elasticities which you found necessary to 'bring the forecasted volume curve to the actual volume curve" had values which were greater than zero."

- a. Please provide the values for these 'experimental own-price elasticities' for each of the rate cases for which you calculated such elasticities.
- b. Would an "experimental own-price elasticity" greater than zero indicate that the negative impact of the change in First-class postage rates was less than the impact estimated by witness Thress for a particular rate case?
- c. If your answer to b. is **affirmative**, would an 'experimental own-price elasticity" greater than zero therefore suggest that witness Thress's own-price elasticity estimates for First-Class Mail in recent cases are **not too** low? **If** not, why not?
- d. On page 40 of your testimony, beginning at line 13. you say the following:

"Figures 4 and 5 indicate the general bias that appears to exist with respect to USPS-sponsored volume forecasts in rate cases that are based on, among other things, their **own** price demand elasticity parameters that are estimated in order to do the forecast."

 - (i) What is the direction of **this "general** bias"?
 - (ii) What is the source of this 'general bias"?

RESPONSE:

a. We used the forecasting model provided in the Docket No. R2000-1. The value of the single-piece own price elasticity was changed to see when the forecast volumes approached the actual volumes. An elasticity close to 3 made the forecast values approach the actual values.

Given that theoretically and statistically the own-price elasticity should be negative, what this could imply is that the estimated model is probably not correctly specified with respect to the reality of postal products and competing substitutes in relevant markets. Either certain relevant variables are omitted or irrelevant variables are included in the model and/or a wrong estimation technique is used. It could also be that the forecasted explanatory variables which are used to forecast the volume are not good forecasts themselves.

Another possible explanation for "over-forecasting" is that, a few quarters **after** the rate case is implemented the real prices begin to drop given the **quarterly** BLS data used to compute real prices. The consequence of this is that the forecasting is good for only a very short period, **possibly** a couple of quarters. depending on inflation for the following reason. Since the elasticity is negative. the drop in the real prices results in an increase in the forecast volume, making the gap between the forecast volume and the actual volume wider than before. However, using Thress's forecasting model and holding everything else constant. if the own-price elasticity is changed to positive, in the presence of the declining real prices, the forecasted volume declines, making the gap between actual and forecast smaller. As was stated in part a. an elasticity close to 3 made the forecast values approach the actual values. However, this approach does not make any economic sense as the elasticity is obviously not positive.

- b. See my answer to part b. above.

- c. (i) Over-forecasting.
(ii) See my response to part b. above.

RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE

USPS/GCA-T1-79: In your response to **USPS/GCA-T1-46(c)-(d)**, you state that you "did not investigate, and had no reason to investigate, the period between 1983 and 1990."

- a. Please confirm that the period between 1983 and 1990 was included within the sample period over which your own-price elasticity of -0.456 was estimated.
- b. Wouldn't the presence of this time period within your sample period provide a "reason to investigate the period between 1983 and 1990"?
- c. You state, in your response to **USPS/GCA-T1-46(c)-(d)** that your "focus was on the post-1995 period." Did you attempt to estimate a demand equation for First-class single-piece letters relying only on data since 1995? If so, please report the results of all such experiments. If not, why not?

RESPONSE:

a - c. You misunderstand my statement. I had no reason to break out of the overall period 1983-2005 a 1983 - 1990 period because the Internet was not really operationally widespread during this period. 1990-1995 is the earliest period for which it would have made sense to examine whether increased Internet penetration was affecting mail elasticities, and as my data showed, it did appear to impact elasticities for that period. The elasticities that I have given in Table A8 of my testimony are point elasticities which shows an upward trend starting in 1990.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-80: In your response to USPS/GCA-T1-47, you indicate that your source for "commercial checks" was the 2004 Federal Reserve Payments Study.

- a. Please confirm that the number of Commercial Checks presented in Table 2 on page 20 of your testimony is equal to 15,993 million in 2000 and **15,805** million in **2003**. If not confirmed, please explain fully.
- b. Please confirm that the number of Commercial Checks shown in Appendix A (page 11) of the 2004 Federal Reserve Payments Study were 41.4 billion in 2000 and 36.2 billion in 2003. If not confirmed, please explain fully.
- c. Please reconcile the difference between these numbers.

RESPONSE:

- a. - c. No reconciliation is needed. The source of the 41.9 billion figure for 2000 and other years is "checks paid by depository institutions, U. S. Treasury checks, and postal money orders." (See footnote 1, page 181, <http://www.federalreserve.gov/pubs/bulletin1200S/spring05payment.pdf>). The other figure, 16.993 billion is commercial checks collected through the Federal Reserve. (See <http://www.federalreserve.gov/paymentssystemsc/creckservices/commcheckcolannual.htm>)

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-81: In your response to USPS/GCA-T1-48, you make the following claim: "It seems you are calculating the change in volume for a percentage change in price" while "[t]he sum of the coefficients of single-piece price and its lag which I have estimated gives the change in volume for one unit change in price." Please confirm that for any specific change in price from P_1 to P_2 , this change could be expressed as either a 'percentage change in price', i.e., $(P_2/P_1) - 1$, or a "unit change in price", i.e., $P_2 - P_1$. If not confirmed, please explain fully.

RESPONSE:

Confirmed. However, $(P_2/P_1) - 1$ and $P_2 - P_1$ are not the same values.

Please note:

Thress's log-log Model is:

$$\ln(V_t) = a + b_1 \cdot \ln(X_{1t}) + b_2 \cdot \ln(X_{2t}) \dots + b_n \cdot \ln(X_{nt}) + \ln(\epsilon_t), \text{ where } b_i$$

coefficients are elasticities, showing the percentage change in volume for a percentage change in the variable.

My linear model is:

$V_t = a + b_1 \cdot X_{1t} + b_2 \cdot X_{2t} \dots + b_n \cdot X_{nt} + \epsilon_t$, where b_i coefficients are slopes showing a change in volume for a one unit change in the variable.

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USPS/GCA-T1-82: In your response to USPS/GCA-T1-48, you make the following claim: "It seems you are calculating the change in volume for a percentage change in price" while "[t]he sum of the coefficients of **single-piece** price and its lag which I have estimated gives the change in volume **for** one unit change in price." Please confirm that a change in **price** from \$0.410336 to \$0.451369 represents a unit change of \$0**041034**. Please further confirm that this unit change in price could be written mathematically as $(\$0.451369 - \$0.410336)$. If not confirmed, please explain fully.

RESPONSE:

Confirmed.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-83: In your response to USPS/GCA-T1-48, you claim that the interrogatory "calculat[es] the change in volume for a percentage change in price." USPS/GCA-T1-48(d) expresses the change in the First-class single-piece letters price as "(\$0.451369 - \$0.410336)." Please confirm that (\$0.451369 - \$0.410336) expresses the "unit change in price." If you cannot confirm, please identify the "unit change in price" which **would** result from an increase in the price of First-class single-piece letters from \$0.410336 to \$0.451369.

RESPONSE:

Confirmed.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-84: In your response to USPS/GCA-T1-48, you claim that the interrogatory "calculat[es] the change in volume for a percentage change in price." USPS/GCA-T1-48(g) expresses the change in the average First-class worksharing discount as "(\$0.113192 - \$0.072158)." Please confirm that (\$0.113192 - \$0.072158) expresses the "unit change in price." If you cannot confirm, please identify the "unit change in price" which would result from an increase in the average First-class worksharing discount from \$0.072158 to \$0.113192.

RESPONSE:

Confirmed. However, your hypothetical makes no sense in light of the history of worksharing discounts and single piece rate changes. [See my response to USPS/GCA-T1-87 below for actual historical ranges of changes in the two sets of rates.] You are increasing the Single-Piece price by 10% whereas the corresponding WS discount in your hypothetical is increased by 58%. That is, the unit change in the single-piece price (\$0.041034) you have given in USPS/GCA-T1-82 is for a 10% increase in the single piece price. The \$0.041034 increase in the WS discount you have given above is equivalent *to* a 58% (0.041034/0.072158) increase in the WS discount.

What underscores your original interrogatory #48 as well as this set of interrogatories, 81-95, bearing on my original response to #48, is a fundamental mis-perception that USPS witness Thress has about the relationship between single piece volumes and workshared volumes at a mature stage of worksharing as it has existed for several years. The two key differences between my demand equation and witness Thress' are: (1) a straightforward linear VES approach which does not require any **Box** Cox or arbitrary non-linear transformation versus Thress' highly problematic double log CES approach; (2) an endogenous approach to the worksharing coefficient based on business facts, versus witness Thress' a priori restrictions on the sign and value of that worksharing coefficient, which negative restriction on the sign of the worksharing discount variable turns out to be at complete odds with known business facts about the positive contemporary relationship between workshared and single piece volumes.

The negative sign restriction in Mr. Thress' worksharing variable in the single piece demand equation is an untested presumption on his part that there is still substantial "conversion" of single piece mail to presort, as there clearly was many years ago when presort discounts were first instituted. It is an incorrect presumption today and has been for several years. There is little if any remaining conversion letter mail. When I ran the Thress data endogenously rather than imposing a presumption of conversion through a negative sign restriction, the sign for the worksharing variable was positive for both Thress' R2005-1 and R2006-1 single piece demand equations. The answer as to why is known to almost every large mailer, and a credit card company example is one way to illustrate why that coefficient is positive.

There is now considerably more worksharing mail volume in First Class than single piece volume. Suppose a credit card company, incentivized by an increase in a worksharing discount, sends one or more advertising letters by First Class or Standard Mail asking a potential customer to sign up for its credit card. When a potential customer signs up, several things happen in the First Class mailstream volume. To begin with, a welcome letter and the new plastic card will be sent at First Class workshared rates. The cardholder then begins using the card and a monthly bill becomes generated and is also sent at First Class workshared rates. All of this extra volume in workshared mail is not the result of conversion from single piece, but the result of the propensity of businesses to want to grow their companies, aided in this example by a greater worksharing discount initially.

Consistent with my econometric analysis and the specification of my single piece demand equation, deepening worksharing discounts now generate greater single piece volume, not less as in witness Thress' demand equation. For each monthly credit card billing statement sent, a payment must be made and most of these will be made by single piece mail. The extra workshared bills generate more

single piece volume, not less in this cycle of growth in credit card customers. In this real world example which typifies a substantial amount of letter volume increases, there is no conversion of single-piece letter mail to workshared letter mail, and accordingly no negative sign associated with the worksharing coefficient in the single piece demand equation.

This statement of business fact is, I believe, why our endogenous runs on Thress' workshared variable yielded a positive sign, as one would expect if one knew the business facts. As to these business facts, see also the legal brief submitted by MMA in response to the Commission's request for comments on de-linking. (Docket No. R2006-1, August 17, 2006, Comments of Major Mailers Association in Response to Notice of Inquiry No. 3).

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-85: Your response to USPSIGCA-T1-48 failed to confirm part (d) of that question:

Please confirm that, given the functional form of your equation, the impact of a 10 percent increase in the price of First-class single-piece letters would be equal to the following:

$$\begin{aligned} \text{Change in volume (pieces per adult per day)} &= \\ (\$0.451369 - \$0.410336) * (-1.0552) &= -0.0433 \end{aligned}$$

Please provide the correct formulation for the impact of an increase in the price of First-class single-piece letters from \$0.410336 to \$0.451369 given the functional form of your equation. For the purposes of your answer, please interpret the change in the price of First-class single-piece letters as a 'unit change in price.'

RESPONSE:

Confirmed. \$0.0410336 rise in the singlepiece price results in 0.0433 units decline in the single-piece volume. holding all other **explanatory** variables constant. However, note that your example necessarily entails having to raise the price of workshared letters in order to keep the discount constant.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-86: Your response to USPS/GCA-T1-48 failed to confirm part (g) of that question:

Please confirm that, given the functional form of your equation, the impact of a change in the average worksharing discount from \$0.072158 to \$0.113192 would be equal to the following:

$$\begin{aligned} \text{Change in volume (pieces per adult per day)} &= \\ (\$0.113192 - \$0.072158) * (1.2683) &= +0.0520 \end{aligned}$$

Please provide the correct formulation for the impact of an increase in the average worksharing discount from \$0.072158 to \$0.113192 given the functional form of your equation. For the purposes of your answer, please interpret the change in the average worksharing discount as a "unit change in price."

RESPONSE:

Confirmed. A \$0.0410336 rise in the average worksharing discount results in 0.0520 units increase in the single-piece volume, holding all other explanatory variables constant. However, note that your example necessarily entails having to reduce the price of workshared letters or raise the price of single piece letters, or both, in order to vary the discount.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-87: Your response to USPS/GCA-T1-48 failed to confirm part (h) of that question:

Please confirm that, combining the impacts shown in d. and g. above, the total change in the volume of First-class single-piece letters (pieces per adult per day) predicted by your model, given a 10 percent increase in the price of First-class single-piece letters, holding the price of First-class workshared letters constant, will be equal to an increase of 0.0087 (minus 0.0433 plus 0.0520).

Please provide the correct value for "the total change in the volume of First-class single-piece letters (pieces per adult per day) predicted by your model, given a 10 percent increase in the price of First-Class single-piece letters, holding the price of First-class workshared letters constant" given your responses to USPSIGCA-T1-85 and USPSIGCA-T1-86 above.

RESPONSE:

Not confirmed.

Your hypothetical example states ~~that~~ you are increasing the SP price by 10% which also means the WS discount is ~~raised~~ by about 58%. Over the 1983-2005 period of investigation, there has never been a case in which the Postal Service has increased the SP rate by 10% and the WS discount by about 58%. The attached table gives the non-log values of the single-piece price and worksharing discount along with the level change and the percentage change in the values of these two variables as well as their relative values and the absolute difference between the change in the single-piece price and the change in the worksharing discount. The average values and the minimum and the maximum values are also reported in this table.

The key facts from this table are: (i) the maximum change for the 1983-2005 period in the level of the WS discount is \$0.01249 in 1996PQ4 compared to your hypothetical example of \$0.041034; (ii) the maximum ~~p~~ change in the WS discount is 22.2% compared to your number of 58% ; The

22.2% maximum increase in WS discount corresponds to a 0.42% decrease in the single-piece price in 1996PQ4;

(iii) The maximum increase in the single-piece price was 9.6% corresponding to a 2.6% increase in worksharing discount in 1988PQ3; (iv) the average difference between the change in the single-piece price and the worksharing discount over the sample period in absolute term has been about 0.43 cent. Furthermore, as the last column shows, at the times that Postal Services changed the rates the Single-Piece rate was increased by several cents more than the increase in the worksharing discount. For example, in 1988PQ3 the change in the single-piece price was 3.63 cents higher than the change in the worksharing discount; in 1991PQ2 and 1995PQ2 these differences were about 2.0; and in 2002GQ4 it was 2.2 cents. The average of those large differences which must correspond to Postal Service rate increases, is about 2.4 cents. This implies on the average the single-piece price increases have been 2.4 cents larger than the increases in the worksharing discount. By contrast, your hypothetical assumes equal increases in single piece rates and worksharing discounts. [The Thress model, unlike my model, also presumes the impact of the own price coefficient and the WS discount are both negative so the combined impact is always **negative** even though we know the sign of the WS discount coefficient in the single piece equation is not negative, as discussed in my answer to USPS/GCA-T1-84.]

Furthermore, , your hypothetical example implicitly assumes that, when the single-piece price rose, for example, by 1 cent, the worksharing discount must have risen by 1 cent. In fact , over this period the average change for the single-piece has been $-\$0.00038$ and for the worksharing discount has been $+\$0.00025$. If we run a simple linear regression between the worksharing discount as the dependent variable and the single-piece price as the explanatory variable, if the coefficient of the single-piece price is found to be statistically equal to 1 and significant, then this example make sense. Table

Two shows the regression output. This coefficient is found to be **-0.076** and is insignificant, implying not only it is not **statistically equal to 1**, but also that there is not even a linear relationship between the worksharing discount and the single piece price over the 1983-2005 sample period.

TIME	PX01SP	D1 3WS	Level Change		% Change		Relative Value SP Price In WS Discount	Absolute Value of Difference Between SP Price Level Change & WS Discount Level Change (B)-abscon(3)+4
			SP Price	WS Discount	SP Price	WS Discount		
			(3)	(4)	(5)	(6)		
1983PQ1	\$0.43995	\$0.04848					9.08	0.298
1983PQ2	\$0.43660	\$0.04811	-\$0.00335	-\$0.00037	-0.76%	-0.76%	9.08	0.417
1983PQ3	\$0.43191	\$0.04759	-\$0.00469	-\$0.00052	-1.07%	1.07%	9.08	0.481
1983PQ4	\$0.42851	\$0.04700	-\$0.00541	-\$0.00060	-1.25%	-1.25%	9.08	0.867
1984PQ1	\$0.42213	\$0.05130	-\$0.00437	\$0.00430	-1.02%	1.15%	8.23	0.352
1984PQ2	\$0.41866	\$0.05135	-\$0.00347	\$0.00005	-0.82%	0.10%	8.15	0.312
1984PQ3	\$0.41511	\$0.05092	-\$0.00358	-\$0.00044	-0.85%	-0.85%	8.15	0.398
1984PQ4	\$0.41171	\$0.05050	-\$0.00340	-\$0.00042	-0.82%	-0.82%	8.15	0.302
1985PQ1	\$0.40827	\$0.05008	-\$0.00344	-\$0.00042	-0.84%	-0.84%	8.15	0.832
1985PQ2	\$0.41538	\$0.05436	\$0.00711	\$0.00428	1.74%	8.55%	7.64	0.338
1985PQ3	\$0.43279	\$0.06345	\$0.01741	\$0.00908	4.19%	16.72%	6.82	0.404
1985PQ4	\$0.42882	\$0.06287	-\$0.00397	-\$0.00058	-0.92%	-0.92%	6.82	0.370
1986PQ1	\$0.42408	\$0.06217	-\$0.00474	-\$0.00089	-1.10%	-1.10%	6.82	0.024
1986PQ2	\$0.42091	\$0.06171	-\$0.00317	-\$0.00046	-0.75%	-0.75%	6.82	0.290
1986PQ3	\$0.42120	\$0.06175	\$0.00028	\$0.00004	0.07%	0.07%	6.82	0.369
1986PQ4	\$0.41758	\$0.06122	-\$0.00362	-\$0.00067	-0.89%	-0.89%	6.82	0.282
1987PQ1	\$0.41418	\$0.06072	-\$0.00340	-\$0.00050	-0.81%	-0.81%	6.82	0.321
1987PQ2	\$0.40938	\$0.06009	-\$0.00432	-\$0.00083	-1.04%	-1.04%	6.82	0.384
1987PQ3	\$0.40610	\$0.05964	-\$0.00377	-\$0.00056	-0.92%	-0.92%	6.82	0.407
1987PQ4	\$0.40159	\$0.05888	-\$0.00450	-\$0.00086	-1.11%	-1.11%	6.82	0.189
1988PQ1	\$0.39682	\$0.05818	-\$0.00477	-\$0.00070	-1.19%	-1.19%	6.82	0.329
1988PQ2	\$0.39461	\$0.05785	-\$0.00222	-\$0.00032	-0.56%	-0.56%	6.82	0.822
1988PQ3	\$0.43238	\$0.05934	\$0.03778	\$0.00148	8.57%	2.57%	7.29	0.486
1988PQ4	\$0.44046	\$0.05920	\$0.08007	-\$0.00014	1.87%	-0.24%	7.44	0.414
1989PQ1	\$0.43485	\$0.05844	-\$0.00561	-\$0.00075	-1.27%	-1.27%	7.44	0.502
1989PQ2	\$0.43007	\$0.05780	-\$0.00478	-\$0.00064	-1.10%	-1.10%	7.44	0.338
1989PQ3	\$0.42427	\$0.05702	-\$0.00580	-\$0.00078	-1.36%	-1.36%	7.44	0.380
1989PQ4	\$0.42035	\$0.05649	-\$0.00392	-\$0.00053	-0.92%	-0.92%	7.44	0.736
1990PQ1	\$0.41596	\$0.05590	-\$0.00439	-\$0.00058	-1.04%	-1.04%	7.44	0.840
1990PQ2	\$0.40745	\$0.05476	-\$0.00850	-\$0.00114	-2.04%	-2.04%	7.44	0.498
1990PQ3	\$0.40220	\$0.05405	-\$0.00526	-\$0.00071	-1.29%	-1.29%	7.44	0.205
1990PQ4	\$0.39711	\$0.05337	-\$0.00509	-\$0.00088	-1.27%	-1.27%	7.44	0.394
1991PQ1	\$0.39137	\$0.05260	-\$0.00573	-\$0.00077	-1.44%	-1.44%	7.44	0.302
1991PQ2	\$0.41365	\$0.05463	\$0.02228	\$0.00203	5.69%	3.86%	7.74	0.318
1991PQ3	\$0.44781	\$0.05784	\$0.03415	\$0.00321	8.29%	5.89%	7.74	0.271
1991PQ4	\$0.44433	\$0.05739	-\$0.00347	-\$0.00048	-0.78%	-0.78%	7.74	0.244
1992PQ1	\$0.44068	\$0.05692	-\$0.00365	-\$0.00040	-0.82%	-0.82%	7.74	0.285
1992PQ2	\$0.43756	\$0.05652	-\$0.00312	-\$0.00047	-0.71%	-0.71%	7.74	0.226
1992PQ3	\$0.43476	\$0.05616	-\$0.00290	-\$0.00038	-0.64%	-0.64%	7.74	0.159
1992PQ4	\$0.43172	\$0.05577	-\$0.00304	-\$0.00039	-0.70%	-0.70%	7.74	0.192
1993PQ1	\$0.42873	\$0.05543	-\$0.00299	-\$0.00034	-0.69%	-0.69%	7.74	0.121
1993PQ2	\$0.42668	\$0.05516	-\$0.00208	-\$0.00027	-0.48%	-0.48%	7.74	0.187
1993PQ3	\$0.42408	\$0.05482	-\$0.00259	-\$0.00034	-0.61%	-0.61%	7.74	0.260
1993PQ4	\$0.42226	\$0.05459	-\$0.00182	-\$0.00024	-0.43%	-0.43%	7.74	0.086
1994PQ1	\$0.42006	\$0.05430	-\$0.00221	-\$0.00026	-0.52%	-0.52%	7.74	0.017
1994PQ2	\$0.41667	\$0.05412	-\$0.00139	-\$0.00018	-0.33%	-0.33%	7.74	0.132
1994PQ3	\$0.41651	\$0.05385	-\$0.00215	-\$0.00026	-0.51%	-0.51%	7.74	0.086
1994PQ4	\$0.41303	\$0.05340	-\$0.00348	-\$0.00045	-0.84%	-0.84%	7.74	0.017
1995PQ1	\$0.41056	\$0.05308	-\$0.00247	-\$0.00032	-0.60%	-0.60%	7.74	0.303
1995PQ2	\$0.43431	\$0.05659	\$0.02374	\$0.00351	5.78%	8.81%	7.68	0.223
1995PQ3	\$0.44075	\$0.05757	\$0.00644	\$0.00088	1.48%	1.74%	7.68	0.548
1995PQ4	\$0.43863	\$0.05729	-\$0.00212	-\$0.00026	-0.48%	-0.48%	7.68	0.184
1996PQ1	\$0.43671	\$0.05704	-\$0.00193	-\$0.00025	-0.44%	-0.44%	7.68	0.168
1996PQ2	\$0.43456	\$0.05676	-\$0.00215	-\$0.00028	-0.49%	-0.49%	7.68	0.187
1996PQ3	\$0.43156	\$0.05637	-\$0.00299	-\$0.00039	-0.69%	-0.69%	7.68	0.260
1996PQ4	\$0.42977	\$0.05686	-\$0.00180	\$0.00149	-0.42%	22.16%	6.24	1.429
1997PQ1	\$0.42688	\$0.07430	-\$0.00286	\$0.00844	-0.67%	7.30%	5.75	0.831
1997PQ2	\$0.42493	\$0.07396	-\$0.00196	-\$0.00034	-0.46%	-0.46%	5.75	0.162
1997PQ3	\$0.42371	\$0.07375	-\$0.00122	-\$0.00021	-0.29%	-0.29%	5.75	0.101
1997PQ4	\$0.42117	\$0.07360	-\$0.00084	-\$0.00015	-0.20%	-0.20%	5.75	0.070
1998PQ1	\$0.42070	\$0.07332	-\$0.00047	-\$0.00030	-0.40%	-0.40%	5.75	0.140
1998PQ2	\$0.42025	\$0.07314	-\$0.00045	-\$0.00008	-0.11%	-0.11%	5.75	0.039
1998PQ3	\$0.41908	\$0.07294	-\$0.00117	-\$0.00020	-0.28%	-0.28%	5.75	0.037
1998PQ4	\$0.41748	\$0.07266	-\$0.00160	-\$0.00026	-0.38%	-0.38%	5.75	0.097
1999PQ1	\$0.42017	\$0.07450	\$0.00270	\$0.00184	0.65%	2.53%	5.64	0.132
1999PQ2	\$0.42117	\$0.07567	\$0.00100	\$0.00117	0.24%	1.57%	5.64	0.086
1999PQ3	\$0.41871	\$0.07523	-\$0.00246	-\$0.00044	-0.58%	-0.58%	5.57	0.017
2000GQ1	\$0.41527	\$0.07461	-\$0.00344	-\$0.00062	-0.82%	-0.82%	5.57	0.282
2000GQ2	\$0.41167	\$0.07396	-\$0.00360	-\$0.00065	-0.87%	-0.87%	5.57	0.295
2000GQ3	\$0.40968	\$0.07360	-\$0.00200	-\$0.00036	-0.49%	-0.49%	5.57	0.164
2000GQ4	\$0.40778	\$0.07326	-\$0.00189	-\$0.00034	-0.46%	-0.46%	5.57	0.155
2001GQ1	\$0.40597	\$0.07294	-\$0.00182	-\$0.00033	-0.45%	-0.45%	5.57	0.149
2001GQ2	\$0.40895	\$0.07412	\$0.00299	\$0.00118	0.74%	1.62%	5.52	0.181
2001GQ3	\$0.40682	\$0.07377	-\$0.00213	-\$0.00034	-0.52%	-0.46%	5.51	0.178
2001GQ4	\$0.41278	\$0.07171	\$0.00696	-\$0.00206	1.47%	-2.79%	5.78	0.802
2002GQ1	\$0.41220	\$0.07161	-\$0.00059	-\$0.00010	-0.14%	-0.14%	5.76	0.048
2002GQ2	\$0.41125	\$0.07145	-\$0.00095	-\$0.00016	-0.23%	-0.23%	5.76	0.078
2002GQ3	\$0.40875	\$0.07102	-\$0.00250	-\$0.00042	-0.61%	-0.58%	5.76	0.208
2002GQ4	\$0.43854	\$0.07677	\$0.02779	\$0.00574	6.80%	6.09%	5.69	2.205
2003PQ1	\$0.43476	\$0.07645	-\$0.00178	-\$0.00031	-0.41%	-0.41%	5.69	0.147
2003PQ2	\$0.43152	\$0.07598	-\$0.00324	-\$0.00057	-0.75%	-0.75%	5.69	0.267
2003PQ3	\$0.43082	\$0.07576	-\$0.00069	-\$0.00012	-0.16%	-0.16%	5.68	0.057
2003GQ4	\$0.42874	\$0.07539	-\$0.00208	-\$0.00037	-0.48%	-0.48%	5.69	0.172
2004GQ1	\$0.42735	\$0.07515	-\$0.00138	-\$0.00024	-0.32%	-0.32%	5.68	0.114
2004GQ2	\$0.42334	\$0.07445	-\$0.00402	-\$0.00071	-0.94%	-0.94%	5.68	0.331
2004GQ3	\$0.41941	\$0.07375	-\$0.00393	-\$0.00069	-0.93%	-0.93%	5.68	0.324
2004GQ4	\$0.41788	\$0.07348	-\$0.00153	-\$0.00027	-0.36%	-0.36%	5.69	0.126
2005GQ1	\$0.41466	\$0.07292	-\$0.00322	-\$0.00057	-0.77%	-0.77%	5.69	0.265
2005GQ2	\$0.41236	\$0.07251	-\$0.00230	-\$0.00040	-0.55%	-0.55%	5.69	0.190
2005GQ3	\$0.40902	\$0.07193	-\$0.00334	-\$0.00059	-0.81%	-0.81%	5.69	0.275
2005GQ4	\$0.40642	\$0.07129	-\$0.00360	-\$0.00083	-0.88%	-0.88%	5.69	0.297
Average 1983-2005	\$0.42096	\$0.06300	-\$0.00336	-\$0.00025	-0.79%	0.49%	6.81	0.427
Minimum 1983-2005	\$0.39137	\$0.04700	-\$0.00850	-\$0.00206	-2.14%	-2.79%	5.51	
Maximum 1983-2005	\$0.44781	\$0.07677	\$0.03778	\$0.01249	9.57%	22.16%	9.08	
Average 2005	\$0.41037	\$0.07216						
Hypothetical Example								
10% Increase in SP Price								
Holding WS Price Constant	\$0.46140	\$0.11320	\$0.04104	\$0.04104	10.12%	58%	3.99	

Table Two
Simple Linear Regression Between Worksharing Discount
8 Single-Piece Price Over 1983-2005 Period

Dependent Variable: Worksharing Discount

<i>Regression Statistics</i>						
Multiple R						0.097192
R Square						0.009446
Adjusted R Square						-0.00156
Standard Error						0.009299
Observations						92

<i>ANOVA</i>						
	<i>df</i>	<i>SS</i>	<i>MS</i>	<i>F</i>	<i>Significance F</i>	
Regression	1	7.42E-05	7.42E-05	0.858273	0.3567	
Residual	90	0.007783	8.65E-05			
Total	91	0.007857				

	<i>Coefficients</i>	<i>Standard Error</i>	<i>t Stat</i>	<i>P-value</i>	<i>Lower 95%</i>	<i>Upper 95%</i>
Intercept	0.094857	0.034405	2.757066	0.007062	0.026505	0.163208793
SP Price	-0.075686	0.081697	-0.92643	0.3567	-0.237991	0.086618514

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-88: Please answer USPS/GCA-T1-48(i) with respect to the answer which you provide in your response to USPS/GCA-T1-87.

RESPONSE:

Please see my responses to USPS/GCA-T1-84 and USPS/GCA-T1-87.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-89: USPS/GCA-T1-48(k) asked the following:

Please confirm that your model would predict that a reduction in the price of First-class single-piece letters, coupled with an equal reduction in the average First-class worksharing discount, would predict a reduction in the volume of First-class single-piece **letters**. If you cannot **confirm**, please explain fully.

You do not appear to have answered **this question**. Please do so now. For the purposes of your answer, please **interpret** the word "reduction" to refer to a "unit change in price."

RESPONSE:

Confirmed. However, please see **my** responses to USPSIGCA-T1-84 and USPS/GCA-T1-87.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPSIGCA-TI-90: In your response to USPS/GCA-T1-48, you relied upon average own-price and discount elasticities over the period from 1983 – 2005, based upon your equation in Table A-8 of your testimony. For example, you calculated the discount elasticity based upon an average First-class worksharing discount of "0.0610."

The example in USPS/GCA-T1-48 refers explicitly to prices in 'GFY 2005.' For example, the average First-class worksharing discount used in steps (v) - (viii) of your response to USPS/GCA-T1-48 is equal to '\$0.072158.'

Please confirm that the average First-class worksharing discount which is used to calculate the discount elasticity should be equal to the average First-class worksharing discount identified in steps (v) – (viii) of your response to USPS/GCA-T1-48 in order for your answer to be correct mathematically. If not confirmed, please explain fully.

RESPONSE:

Confirmed.

RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE

USPSIGCA-TI-91: In your response to USPSIGCA-T1-48, you relied upon average own-price and discount elasticities over the period from 1983 – 2005, based upon your equation in Table A-8 of your testimony. The example in USPS/GCA-T1-48 refers explicitly to prices in 'GFY 2005.'

Please repeat the calculations which you provide in response to USPS/GCA-T1-48 using own-price and discount elasticities for GFY 2005.

RESPONSE:

Using the average values for the year 2005, the single-piece price elasticity is -0.622 and the worksharing discount elasticity is +0.133. Following those steps (v) – (viii) in USPSIGCA-T1-48, we obtain a 0.00075 unit increase in the single-piece volume due to simultaneously increasing the single-piece price and the worksharing discount by an amount of \$0.041034 corresponding to a 10% increase in the single-piece price and a 58% increase in the worksharing discount. However, please see my response to USPSIGCA-T1-84 for a conceptual and factual explanation of such a result. Furthermore, see my response to USPS-GCA-T1-87, showing why equal amount of simultaneous increase or decrease in the single-piece price and the worksharing discount does not make any historical and statistical sense.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-92: In your response to USPS/GCA-T1-48, you indicate that "the impact of a change in the average worksharing discount from \$0.072158 to \$0.113192 would be" to increase volume by "3.64%." Why do you believe that a change in the relative prices of First-class single-piece and workshared letters that would make First-class single-piece letters more expensive relative to First-Class workshared letters would lead to an increase in First-class single-piece letters volume?

RESPONSE:

Please see my response to USPSIGCA-T1-84.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-93: In your response to USPS/GCA-T1-48, you indicate that "the impact of a change in the average worksharing discount from \$0.072158 to \$0.113192 would be" to increase volume by "3.64%." What do you believe would be the source of this 3.64 percent increase in First-class single-piece letters volume resulting from this increase in the average First-class worksharing discount? That is, would this represent mail that was not previously sent through the Postal Service or would it represent mail that was previously sent as some other category of mail? If you believe that this would represent mail that was not previously sent through the Postal Service, to what incentives would such mail be responding in this case, in light of a 10 percent increase in the price of First-Class single-piece letters. If you believe that this would represent mail that was previously sent as some other mail category, what mail category do you believe this mail would have previously been sent as, and what precisely do you believe would be the incentives which would prompt such mail to shift to First-class single-piece letters?

RESPONSE:

Please see my response to USPS/GCA-T1-84.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-94: In your response to USPS/GCA-T1-48, you indicate that "the impact of a change in the average worksharing discount from \$0.072158 to \$0.113192 would be" to increase volume by "3.64%." In your opinion, would you expect an increase in the average First-class worksharing discount to lead to an increase or a decrease in *the* volume of First-class workshared letters? If your expectation is that an increase in the average First-class worksharing discount would lead to an increase in the volume of First-class workshared letters, please explain how this expectation is consistent with your response to USPS/GCA-T1-48 as quoted in this question. If your expectation is *that* an increase in the average First-class worksharing discount would lead to a decrease in the volume of First-class workshared letters, please explain your answer fully and provide all evidence in support of your *position*.

RESPONSE:

Please see my response to USPS/GCA-T1-84.

**RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO
INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE**

USPS/GCA-T1-95: In your response to USPS/GCA-T1-48, you claim that "[t]he sum of the coefficients of single-piece price and its lag which I have estimated gives the change in volume for one unit change in price.' Based on your model, what would be the impact on First-class singlepiece letters volume of a one-cent decrease in the price of First-class ~~single-piece~~ letters, holding the price of First-Class worksharing letters constant? ~~That s~~, based on your model, what would be the impact on First-class single-piece letters volume of a one-cent decrease in the price of First-class single-piece letters and a corresponding one-cent decrease in the average First-class worksharing discount?

RESPONSE:

The combined impact of a one-cent simultaneous decrease in the single-piece price and the worksharing discount is a **decline** in the single-piece volume. However, please see my response to USPS/GCA-T1-84 for a conceptual and factual explanation of such a result, **Furthermore**, see my response to USPS-GCA-TI-87, showing why an equal amount of simultaneous increase or decrease in the single-piece price and the worksharing discount does not make any historical and statistical sense.

1 MR. ACKERLY: Mr. Cha man, if I may? T dd
2 Ackerly representing TMA. I have additional
3 designations for the record if this would be an
4 appropriate time to present them.

5 CHAIRMAN OMAS: Yes, sir. Please continue.
6 (The documents referred to
7 was marked for identification
8 as Exhibit Nos. 10, 11 and
9 12.)

10 DIRECT EXAMINATION

11 BY MR. ACKERLY:

12 Q Dr. Clifton, I am showing you documents
13 containing your answers just recently filed DMA
14 Interrogatories Nos. 10, 11 ana 12. Would you check
15 them, please, to be sure that they are accurate and
16 state for the record whether or not the -- your
17 answers would be the same?

18 A Yes, they would, Mr. Ackerly.

19 MR. ACKERLY: Mr. Chairman, I'm handing two
20 copies of this document package to the reporter --
21 transcribed into the record --.

22 CHAIRMAN OMAS: Without objection so
23 ordered.

24 //

25 //

1 (The documents referred to,
2 previously identified as
3 Exhibit Nos. 10, 11 and 12,
4 were received in evidence.)

5 CHAIRMAN OMAS: Thank you, Mr. Todd.

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RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO INTERROGATORIES OF THE DIRECT MARKETING ASSOCIATION

DMA/GCA-T1-10. Please refer to your response to DMA/GCA-T1-3(b), where you state that "From the latest publicly available reliable data I have seen, a majority of the banking industry's mail volume in First Class continues to be mailed at the full single piece rate."

- a) Please produce the "latest publicly available reliable data" to which you refer.
- b) Please explain how you verified that the data are reliable

RESPONSE:

- a. Please see the attached pie chart from ~~the~~ 2000 ABA postal survey, the latest available at the time I answered DMA/GCA-T1-3(b).
- b. I did not attempt to further verify the above-referenced pie chart for a couple reasons. First, the pie chart was unambiguous in what it stated about the relative volumes of single piece full rate FCM postage sent by banks, namely 66% of total FCM bank volume. Second, there was no reference on the pie chart as to how the percentage was calculated and/or from what if any detailed data tables in the 2000 survey the 66% was taken from or calculated from. As a result, I did not at the time dig deeper into the issue. In researching to provide answers to DMNGCA-T1-1-3, I obtained the publicly available ABA 2000 Postal Survey.. and also produced the pie chart attached here in a response to a USPS interrogatory(USPS/GCA-T1-52).

ABA POSTAL OPERATIONS SURVEY REPORT

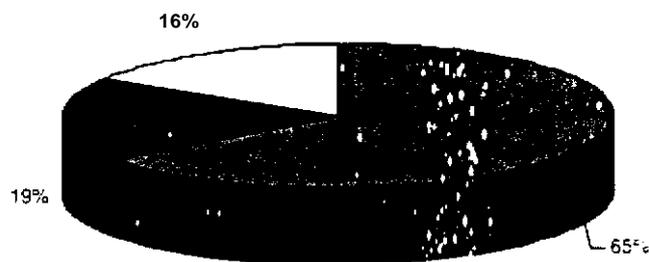
FIGURE 5: BANKING INDUSTRY'S OUTGOING FIRST CLASS MAIL VOLUME 1999

By Program Type



■ Full Postage ■ Delivery Pan: Bar Code □ Nonautomation Retail Presort

By Weight



■ Up to 1 Ounce ■ to 2 ounces □ More than 2 Ounces

RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO INTERROGATORIES OF THE DIRECT MARKETING ASSOCIATION

DMA/GCA-T1-11. Please refer to your response to **DMA/GCA-T1-3(b)**, where you state that “This probably reflects the fact that banks outside of urban and suburban areas do not necessarily have access to a presort bureau and do not have enough mail volume to warrant leasing or purchasing automation machinery.”

- a) Please define what you mean by the phrase ‘have access to a presort bureau.’
- b) What is the maximum distance **between** a bank and the nearest presort bureau for use of a presort bureau to be practical and cost effective?
- c) What percentage of First-class Mail **entered** by banks is generated within 25 miles of a presort bureau? Within 50 miles? Within 100 miles? Within any other distance **for** which you have data?
- d) What is the minimum size of a local market needed to support a presort bureau?
- e) What percentage of First-Class mail entered by banks is generated in communities equaling or **exceeding** the size identified in response to part (d)?
- f) What is the minimum mail volume **generated** by a bank to warrant leasing or purchasing its own automation machinery?
- g) What percentage of First-Class mail entered by banks is generated by banks with a mail volume equaling or exceeding the minimum identified in response to part (f)?
- h) Please produce all data, studies and analyses that support your answers to the previous parts of this **interrogatory**.
- i) Please produce any other data, studies and analyses indicating that banks outside of urban and suburban areas lack access to a presort bureau.

RESPONSE:

11. a-i. In addition to my general working knowledge from previous engagements with NAPM including knowledge of where their members are based, the basis for my statement quoted above **via**s information obtained from the USPS website containing the “RIBBS lists” for presort bureaus operating automation equipment as well as major mailers such as large banks operating

their own automation equipment. It is clear from these lists that presort bureaus do not locate and operate in rural areas **but** mainly in large metropolitan areas or their suburbs as well as other cities. I have not kept downloads of any of this information. Please also see an interesting **article** in the October 23rd Business Mailers Review, "Case Study: Bank Moves to **Neopost** Automation". This article does not mean the move to automation mail rates from presorting by Lebanon Citizens National Bank, but to the fact that efficiencies gained by Neopost's newly acquired mail room equipment saves **on** bank employee costs. "The 20-branch Ohio bank was manually folding, **stuffing** and attaching postage to 50,000 statements each month—a job that involved a full-time staffer and four part time employees who came in three days a week **solely for** that purpose."

RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO INTERROGATORIES OF THE DIRECT MARKETING ASSOCIATION

DMA/GCA-T1-12. Please refer to your response to **DMA/GCA-T1-3(b)**, where you state that "Less than 6% of the bank industry's volume of mail and cost of mail is posted at Standard A Regular Rates according to the public available reliable data I have seen."

- a) Please produce the "publicly available reliable data" to which you refer.
- b) Please explain how you verified that the data are reliable.

RESPONSE:

12. a. and b. My response to **DMA/GCA-T1-3(b)** (which asked about my "belief") was based upon the 2000 ABA postal survey that was available at the time I answered **DMA/GCA-T1-3(b)**. See also the response to **DMNGCA-T1-10**.

I would further note that whether the banking industry benefits or does not benefit from GCA's proposal to cut the single piece rate by one cent does not depend on whether the percentage of single piece fully paid postage is 66% or even a majority of the FCM volume sent by the industry. So long as the volume of single piece fully paid FCM exceeds the volume of Standard A regular mail sent by the industry, but even under weaker conditions than this as well, the banking industry benefits from the GCA proposal. The one cent cut is spread over approximately 39 billion pieces of single piece FCLM, and that revenue loss is spread over approximately 51 billion pieces of Standard A Regular letter mail. As a result, the per piece increase in the Standard A Regular rate on average is less than a cent because the institutional cost shift is spread across a much larger volume of mail compared to single piece FCM. If some individual banks sending more Standard A Regular mail have increased costs under the GCA proposal, they can under the standard compensation principle from welfare economics be made as well off as before from those banks benefiting from the cut in the single piece rate. The industry benefits.

The statistics from the ABA survey as I have now further investigated are based on the data from Appendix Tables 2 and 9 for a reconsideration of their 66% pie chart percentage for fully paid postage and utilize statistics on the volume of

Standard Mail found at the top of page 2. The latter indicates that "standard third class mail volume" totaled '426.2 million pieces in 1999" and 'accounted for 5.4% of industry outgoing mail volume." From Tables 2 and 9, it appears clear ABA made a serious error in its own pie chart in showing that 66% of FCM mail volume in 1999 was single piece fully paid postage. My own calculated percentage is 22.1%. Multiplying this percentage by the total FCM volume of 7.5 billion pieces reported on page 1 of the ABA survey, the volume of fully paid single piece mail sent by the banking industry in 1999 approximated 1.7 billion pieces, or 4 times the volume of Standard Mail sent by the banking industry.

Cutting one cent on 1.7 billion pieces of fully paid single piece bank mail, and raising the rate on 426 million pieces of Standard A Regular bank mail by less than one cent, the impact of the GCA proposal on the banking industry, is obviously, and irrefutably, a net gain for the banking industry. Thus, my conclusion about the impact of the GCA proposal on the banking industry does not and did not hinge on the 66% figure, and is equally valid after correcting ABAs own survey errors in their pie chart.

Subsequent to my answering **DMA/GCA-T1-3(b)**, ABA made available on its website a new 2006 study. Because of the 66% vs. 22.1% error in the 2000 survey, I have no confidence in the newly released (2006) study and would need to discuss the data used, and presentation in that study, with ABAs statistician before I could form an opinion about it.

1 MR. KOETTING: Mr. Chairman, have
2 additional designations as well.

3 CHAIRMAN OMAS: Mr. Koetting?
4 (The documents referred to
5 were marked for
6 identification as Exhibit
7 Nos. USPS-GCA-T-1-66 and
8 USPS-GCA-T-1-71.)

9 DIRECT EXAMINATION

10 BY MR. KOETTING:

11 Q Dr. Clifton, I'm handing you a copy of two
12 interrogatories that were recently filed in response
13 to USPS-GCA-T-1-66 and USPS-GCA-T-1-71. Would you
14 confirm those are the answers that you previously
15 provided in writing?

16 A That one is. Okay. All right.

17 Q If you were asked those questions orally
18 today those answers would be the same?

19 A Yes, they would.

20 MR. KOETTING: With that, Mr. Chairman, the
21 Postal Service moves that the responses of Dr. Clifton
22 to USPS-GCA-T-1-66 and USPS-GCA-T-1-71 be admitted in
23 evidence.

24 CHAIRMAN OMAS: Without objection so
25 ordered.

2 (The documents referred to,
3 previously identified as
4 Exhibit Nos. USPS-GCA-T-1-66
5 and USPS-GCA-T-1-71, were
6 received in evidence.)

7 CHAIRMAN OMAS: Are there any other matters
8 at this point?

9 (No response.)

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RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE

USPS/GCA-T1-66. USPS/GCA-T1-24 asked about your equation which models commercial check volume as a function of the First-class additional ounce rate. In your response, you described this work as 'descriptive' and said that 'no other explanatory variable was included.'

(a) Is it possible for two variables to exhibit a high mathematical correlation over a 10-year period while having no true causal relationship with one another? Please explain any answer other than 'Yes.'

(b) You state in your response to USPS/GCA-T1-24, "Clearly, other factors have been impacting check volumes, but data was not readily available to investigate their relative importance." Could these other factors account for all of the change observed in check volumes over the time period which you investigated? If your answer is **No**, please explain how you could make such a determination, given that you did not "investigate their relative importance"?

(c) In your response to USPS/GCA-T1-24, you state, 'In periods of low inflation such as the limited period examined here, business and consumer decision making may reflect nominal rates as much or more than it reflects real rates.'

(i) Please confirm that the implicit price deflator for personal consumption expenditures, as presented by witness Thress in LR-L-63 in this case, increased by 18.9% from 199501 to 200404. If not confirmed, please explain **fully**.

(ii) Do you believe that consumers will respond to an 18.9% price change?

(iii) If your answer to (ii) is yes, please explain why you did not consider the effect of inflation on check volumes.

(iv) If your answer to (iii) is no, please reconcile this with your results here in which you assert that check volumes were affected by changes in First-class additional ounce rates of less than 10%.

RESPONSE:

- a. Yes it is possible if your sample is not a representative of the population. Either your sample is too small relative to the population size or it is not a random sample of the underlying population.
- b. As is clear from Figure 1 at page 25 of my testimony, commercial checks cleared exhibited modest growth or stability from 1995 through 2001. The rapid drop off in that variable following the hike in the extra ounce rate is clear. "Ceteris paribus" conditions tend to hold in the short run, and we are

speaking here of only a 1, 2 and 3 year effect, not e.g. the 1983-2005 data series witness Thress employs and for which one ~~cannot~~ assume ceteris paribus but must explicitly correct for other ~~factors~~. Other factors have been operating over the entire 1995-2004 period, and these can be summarized as a variety of gradual and evolutionary ~~technological~~ improvements in sundry electronic payments systems which reduced their costs or improved their convenience of use. I am not aware of any particular change in the 2002-2004 period which would have led to a rapid drop off in commercial checks cleared other than the extra ounce rate hike.

- c. i. Confirmed.
- ii. Consumers and small businesses are unlikely to respond to an 18.9% change over so long a time period. If that 18.9% increase (nominal or real) were concentrated in one ~~case, consumers~~ and small businesses would ~~be~~ more likely to react.
- iii. and iv. The time period was too ~~short,-- 3 years and one rate hike--~~ and as explained I believe small business and ~~consumers~~ react to nominal changes, especially in low inflation environments. While you indicate the rate change was less than 10%, expectations may have played a role here as well. Since the extra ounce rate is not ~~related~~ to cost in any close way, but produces revenue well in excess of ~~costs~~, it may have been expected that after two reductions in the extra ounce rates, there would be more. When, instead, USPS raised that rate again, expectations were dashed, and competing substitutes began to be emphasized again.

RESPONSE OF GREETING CARD ASSOCIATION WITNESS CLIFTON TO INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE

USPSIGCA-TI-71. In your response to USPS/GCA-T1-27 you indicate the "firm" to whom you refer in your testimony on page 28 at line 23 is "[a]n oligopolist as defined in the theory of the firm in microeconomics." The full context here in your testimony is the following paragraph, which begins on page 28 at line 22 of your testimony:

"It has long been recognized in the literature of pricing under oligopolistic conditions that the response to a market price increase by a firm is not necessarily the same as the response to a market price decrease, and that therefore the price elasticities may not be the same for the two situations."

- a. Please confirm that the "response to a market price" which is discussed in the literature of pricing under oligopolistic conditions" refers to the pricing strategy of firms which are in competition with the "oligopolist as defined in the theory of the firm in microeconomics". If not confirmed, please explain fully.
- b. Please confirm that the own-price elasticity of demand for a product is determined by the behavior of consumers of a product in response to changes in prices. If not confirmed, please explain fully.
- c. Please confirm that the "consumers of a product" in part b. of this question are not the "firms which are in competition with the oligopolist" as defined in part a. of this question. If not confirmed, please explain fully.
- d. Please confirm that the textbook definition of "own price elasticity", which measures the degree of demand changes as a response to changes in own price, assumes that all other market conditions be constant. If not confirmed, please explain fully.
- e. Do you agree that "under oligopolistic conditions" a market price decrease by a firm would be followed by a market price decrease by its competitors while a market price increase by a firm would not be followed by a market price increase by its competitors? If not, why not?
- f. If the quantity demanded of a good decreases due to decreases in the competitor's price, which in turn is triggered by the decrease in own price, should this effect be measured by "own price elasticity"? If it is to be measured by own price elasticity, would the result of a positive own price elasticity be self-contradicting? Please explain fully.
- g. "Under oligopolistic conditions" should there be any difference in own price elasticity when a firm increases price and when a firm decreases price if the effect of its competitor's price changes is properly controlled for? If there is any difference, what is the source of this difference? Please explain fully.

RESPONSE:

- a. Not confirmed. I was referring to the issue discussed in my testimony that we really do not know how purchasers of stamps would react to a nominal rate

decrease because it has never been tried, but that the literature on oligopolistic behavior indicates that the reaction to a price decrease may not be the same as that to a price increase.

- b. Confirmed.
- c. – g. The issue under conditions of oligopoly is far more complicated than you make it out to be, and you are making an artificial separation in what can often be a complex pattern of repeated interactions among oligopolists that precedes but influences those consumers. and is influenced by those consumers. **In** essence your question implicitly assumes that competition **is** a static, one shot simultaneous event. Even **so**, ~~consider~~ statical Bertrand competition, in which USPS could face just one competitor and nonetheless emerge with perfectly competitive prices with a very high elasticity of demand indeed. For a textbook summary of dynamic or repeated interaction models of oligopoly, see, e.g., A. Mas-Colell, **M.** Whinston, and **J.** Green, Microeconomic Theory, (1995), Chapter 12. For repeated interaction models, including but not limited to the repeated Bertrand model, a useful observation is the so-called folk theorem: “Although infinitely repeated games allow for cooperative behavior, they also allow for an extremely wide range of possible behavior.” (A. Mas-Colell, et. al. 1995, page **404**)

CHAIRMAN OMAS: The being none this brings
2 us to oral cross-examination. Two parties have
3 requested oral cross-examination of Witness Clifton,
4 the Alliance of Nonprofit Mailers, the National
5 Association of Presort Mailers and the National Postal
6 Policy Council.

7 Mr. Levy, would you introduce yourself for
8 the record?

9 MR. LEVY: Thank you, Mr. Chairman.

10 CROSS-EXAMINATION

11 BY MR. LEVY:

12 Q Dr. Clifton, I'll be asking questions for
13 the Alliance of Nonprofit Mailers by the National
14 Association of Presort Mailers and the National Postal
15 Policy Council. Will you turn to page 11 of your
16 testimony?

17 MR. LEVY: Mr. Chairman, if you'd let me know
18 if I'm too close to the mic?

19 BY MR. LEVY:

20 Q Beginning on page 11. is the beginning of
21 Section 4 of your testimony, correct?

22 A Uh-huh.

23 Q In Sections 4 and 5 of your testimony you
24 discuss the competition that you believe the Postal
25 Service faces for bill payments. Is that correct?

1 A Uh-huh.

2 Q Bill payments are a subset of single piece
3 first-class mail, that is bill payments sent by mail?

4 A Yes.

5 Q But bill payments are not the only kind of
6 single piece first-class mail, are they?

7 A No, they're not, but I believe that they are
8 a distinct, you would call it a submarket or market.

9 Q Bill payments are a submarket of single
10 piece first-class mail --

11 A Well, what I'm saying is bill payments
12 compete in a market that I would classify and discuss
13 in my testimony as being the U.S. payments market.

14 Q My question is focusing not on the market,
15 but on the mail. Single piece first-class mail
16 includes matter other than bill payments, doesn't it?

17 A Yes, it does.

18 Q One kind of matter that single piece first-
19 class mail also carries is correspondence, correct?

20 A Correct.

21 Q In the year 2005 households sent and
22 received approximately six billion pieces of personal
23 correspondence, correct?

24 A Subject to check, yes.

25 Q Most of that was by single piece first-class

mail?

2 A One would presume so.

3 Q Now, your testimony doesn't analyze the
4 competition that the Postal Service faces for single
5 piece first-class correspondence mail, does it?

6 A No, it does not.

7 Q Likewise your testimony doesn't estimate
8 elasticities of demand for single piece first-class
9 mail used for personal correspondence, correct?

10 A That would not be correct. The overall
11 elasticity that I estimate for single piece mail would
12 include correspondence.

13 Q But you don't disaggregate your elasticity
14 for correspondence mail?

15 A No, I do not.

16 Q Your client, the Greeting Cards Association,
17 represents the manufacturers of greeting cards. Is
18 that correct?

19 A Correct.

20 Q The majority of personal correspondence that
21 is mailed to and from households consists of greeting
22 cards. Isn't that correct?

23 A Subject to check, yes.

24 Q Your testimony doesn't analyze the
25 competition that the Postal Service faces for the

1 delivery of greeting cards, does it?

2 A No, it doesn't.

3 Q Likewise your testimony doesn't separately
4 estimate the elasticity or demand for first-class mail
5 used to send greeting cards. Is that correct?

6 A That is correct. My testimony analyzes
7 those areas which the Postal Service itself and others
8 believe represent the areas facing the greatest
9 competition as witnessed by the fact that these are
10 areas where volume is substantially declining.

11 Q Now, the demand for mail delivery of
12 greeting cards is quite inelastic, isn't it?

13 A It would be inelastic just like my aggregate
14 inelasticity. Yes. It's inelastic. Yes.

15 Q Greeting cards mailed has a high value to
16 the sender, doesn't it?

17 A It has a high value to the sender, and let
18 me modify my previous answer, Mr. Levy. I think
19 during periods of holidays evidence that I had many
20 years ago from Pal Mar Corporation indicated a much
21 higher elasticity during periods where consumers were
22 buying a lot of stamps than lets say today.

23 Q Overall the elasticity of demand for
24 greeting card postage is inelastic?

25 A I'm not sure. I'd have to look at the

quantities sent during the holiday period as a
2 percentage of the total quantities.

3 Q Greeting cards have a high value to the
4 recipient as well?

5 A I assume they do.

6 Q Now, postage is a relatively small part of
7 the total cost of sending a greeting card, isn't it?

8 A Many greeting cards. I bought some cheap
9 ones out in Arizona last week that I sent back to my
10 kids.

11 Q Well, the typical price of a greeting card
12 is about \$2 to \$4, isn't it?

13 A I don't know what the typical price of a
14 greeting card is, Mr. Levy.

15 (The document referred to was
16 marked for identification as
17 Exhibit No. ANM-X-1.)

18 **BY MR. LEVY:**

19 Q I would like to have marked as cross-
20 examination Exhibit No. ANM-X-1 a document that I will
21 describe as it's being passed around. Exhibit No.
22 ANM-X-1 I will represent is a two page document that I
23 downloaded from the GCA website on Saturday and it
24 bears the heading general facts.

25 I want to refer your attention, Dr. Clifton,

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1 to the fourth bullet on the first page which reads
2 greeting cards range in price from 50 cents to \$10,
3 although counter cards typically cost between \$2 and
4 \$4. Do you see that sentence?

5 A Yes. Uh-huh.

6 Q Do you have any reason to dispute the
7 accuracy of that statement?

8 A No.

9 Q Now, assuming that a greeting card costs the
10 bottom of that range, \$2, then a one penny decrease in
11 the price of a postage stamp would be a percentage
12 saving of the delivered costs of the card of what
13 percent?

14 A Well, one could calculate it. I don't have
15 my calculator, but it would not be much.

16 Q Well, one cent out of \$2.40 would be
17 approximately four-tenths of one cent, right?

18 A Uh-huh.

19 Q If the price of the card were \$4 rather than
20 \$2 then the percentage saving in delivered costs would
21 be a smaller fraction of one percent?

22 A When you're talking about buying a single
23 card like for my son's birthday coming up in January
24 that's true, but note on this that it says seasonal
25 and every day. Seasonal would be greeting cards

1 bought in bulk. I think a penny matter a lot during
2 the seasonal period and that's about a 50/50 split
3 here, so that answers our question from a few moments
4 ago.

5 So for half of the cards purchased whether
6 purchased in quantities of 75, 100, whatever, during
7 the Christmas, Hanukkah, et cetera, season it's not
8 one penny that you're worried about, it's a penny
9 times whatever volume you buy.

10 Q Well, for each volume that you buy you also
11 have to multiply it by the price of the card, correct?

12 A Correct. When you buy cards in bulk they're
13 usually quite a bit cheaper than what you're noting
14 here.

15 Q What's the average cost of a seasonal card?

16 A I do not know, but I do know from 59 --
17 well, when did I start buying greeting cards? When I
18 was an adult I suppose. I know from my own experience
19 that they're a lot less than if you buy them one by
20 one at CVS, but I can't give you a magnitude.

21 Q Okay. Well, let's say that the price of a
22 seasonal card is \$1 and a one penny reduction in
23 postage would be a one percent reduction approximately
24 in the delivered cost of the card, right?

25 A On your example, yes.

1 Q Now, the Postal Rate Commission obviously
2 doesn't regulate the price charged by greeting card
3 manufacturers, does it?

4 A The Postal Service are you saying?

5 Q Postal Rate Commission.

6 A Postal Rate Commission. No.

7 Q So if card manufacturers raise the price of
8 a card by an amount to offset the decrease in postage
9 the consumer wouldn't see any saving at all?

10 A Correct.

11 Q Now. if the Commission at the end of the day
12 is persuaded by your testimony about the elasticity of
13 demand for bill payment mail, hut were to find that
14 the demand elasticity for personal correspondence were
15 much more inelastic then one way to differentiate
16 between the two kinds of single piece mail would be to
17 charge a relatively high mark up for single piece mail
18 generally but to offer a discount for say courtesy
19 reply mail?

20 A That is certainly an option.

21 Q Would you go to page 37 of ycur testimony?
22 I ask you to look at the footnote 25 at the bottom.

23 A Uh-huh.

24 Q That footnote runs to page 38, doesn't it?

25 A Yes, it does.

Q In the footnote to paraphrase you're saying
2 among other things that the Postal Service's
3 hypothesist that the demand for single piece first-
4 class mail is becoming more elastic is --

5 A You mean more inelastic?

6 Q I'm sorry. You are absolutely right. More
7 inelastic is inconsistent with the observation that
8 the real price of postage over time has been roughly
9 constant. Is that a correct paraphrase of at least
10 one point you made in that footnote?

11 A Yes.

12 Q Now, there's another possible explanation
13 for the fact that the real price of single piece
14 postage had remained relatively constant after
15 inflation, namely that the Postal Rate Commission
16 regulates the rates, doesn't it?

17 A The Postal Rate Commission does regulate the
18 rates, but I wouldn't say it follows that that's why
19 the real price has remained relatively constant over
20 time. The Postal Service begins by proposing rates.
21 The Commission disposes of those rates. Furthermore
22 that empirical phenomenon that you mention has not
23 held true through all periods and I think it's
24 actually breaking down now.

25 I think the Postal Service is beginning to

1 raise nominal prices above real rates.

2 Q Let me ask you to clarify the last few
3 words. You're saying that the Postal Service is
4 raising nominal rates to the point that the real rates
5 are going up?

6 A My sense is that's where we're headed, yes,
7 and that would suggest, under the logic of footnote
8 25, that the Postal Service believes that the demand
9 for single-piece mail is becoming more inelastic. It
10 would be consistent with what Witness Thress says. It
11 would be a mistake, but it would be consistent with
12 their witness.

13 Q Let me turn back to the footnote, though.
14 You couldn't draw any inference about the extent of
15 the elasticity trends for single-piece, first-class
16 mail if the rates actually charged by the Postal
17 Service were constrained by the regulator. Isn't that
18 true?

19 A I think you would have to give me many more
20 details before I could answer the question, Mr. Levy.

21 Q Thank you. Now, let's go to page 59, if you
22 would. Now, to summarize, you're proposing that the
23 Commission set the single-piece, first-class rate at
24 41 cents per piece.

25 A In this case, yes.

1 Q And that on penn~~y~~ less than the Postal
2 Service is proposing. Correct?

3 A Correct.

4 Q And you've estimated that the revenue
5 shortfall from that one penny reduction would be
6 approximately \$340 million, making due allowances for
7 elasticity effects.

8 A I have two estimates, really. one under the
9 assumption of linking and one under the assumption of
10 delinking. About 340 with delinking.

11 Q We'll get to linking ~~in~~ a minute.

12 A Okay. All right.

13 Q Now, you propose that the Postal Rate
14 Commission make up the shortfall by raising rates for
15 standard mail.

16 A For Standard A, regular letters.

17 Q What is "Standard A"?

18 A What is "Standard A"?

19 Q Yes.

20 A It is largely made up of marketing mail.

21 Q Is there still a classification for Standard
22 A?

23 A Well, I believe there is a classification
24 called "Standard A Regular."

25 Q Now, let's go to the delinking part that you

1 alluded to. A few days ago, you changed your
2 testimony by adding the sentence that now appears at
3 the bottom of 59 and continues to the top of 60. Is
4 that correct?

5 A I don't think it was a few days ago. I
6 answered a DMA interrogatory and felt it necessary to
7 give two calculations, and I do not even know if I can
8 explain why I did that.

9 Q Well, let's get the date certain. The
10 notice of change of the testimony -- will you accept,
11 subject to check? -- was filed on November 2nd.

12 A Yes.

13 Q And it was prompted by an answer to a DMA
14 interrogatory.

15 A Correct.

16 Q And your original answer to the DMA
17 interrogatory was filed on October 11th

18 A Subject to check. I don't know if you mean
19 the answer to DMA-1, where I did not do these
20 calculations. They asked me to do them, and in a
21 follow-up interrogatory, I did, but I don't remember
22 the date.

23 Q Subject to check is fine.

24 A Okay.

25 Q Now, you've estimated that -- let's make

1 clear for the record, what you mean by a "linked
2 proposal" is you were proposing to apply the one-
3 percent reduction from the Postal Service proposal not
4 only to single-piece, first-class mail but also to
5 presort, first-class mail. Is that what you're
6 talking about?

7 A Not one percent, Mr. Levy. One cent.

8 Q Thank you. I misspoke. You're right.

9 A Yes. The intent of the testimony throughout
10 this process has been to be neutral with respect to
11 the first-class-letter subclass. If the Commission
12 does not adopt the delinking proposal, then we're back
13 in a world where you **have** to estimate discounts from
14 single piece rather than from mixed AADC, and, in that
15 case, I would not propose to change the Postal
16 Service's discounts from single piece. Therefore, if
17 I reduce single piece by one cent, I reduce all of the
18 work-sharing rates by one cent.

19 Q Now, for the linked, or more expanded
20 version of your proposal, you estimate that the
21 reduction in Postal Service revenue would be
22 approximately \$519 million a year.

23 A Correct.

24 Q Now, there are about close to a billion
25 pieces of first-class mail. Is that correct?

1 A One billion?

2 Q One billion, 980 million -- I'm sorry -- 98
3 billion, "B" as in "baby."

4 A I believe that includes all first-class
5 letter mail, not just single piece.

6 Q Why is the revenue shortfall that you
7 estimate for your linked or expanded proposal \$519
8 million rather than something in the range of \$980
9 million? What first-class mail are you not proposing
10 to apply your linked or expanded proposal to?

11 A I'll have to give you a written answer to
12 that, but that is what comes out of the models, but I
13 would be happy to give you a written answer.

14 Q Let me see, without getting into the math,
15 is there any kind of first-class mail to which you do
16 not propose to apply the one-cent discount under your
17 linked proposal?

18 A It's being applied to first-class, single-
19 piece, letter mail and to first-class, workshared,
20 letter mail.

21 Q But not to flats or parcels.

22 A Well, I will have to go back and examine
23 what the actual numbers, whether they are using data
24 that is letter only or data which includes letters,
25 parcels, and flats.

1 Q Is it your intention to ~~pp1~~ the broader
2 version of your proposal to parcels and flats as well?

3 A It's not my intention to do that.

4 Q And is it your intention to apply the
5 broader version of your proposal to current first-
6 class cards?

7 A No.

8 Q Now, if you don't apply the one-cent
9 reduction to flats or parcels, then you are reducing
10 the shape-based differentiation that the Postal
11 Service has proposed in this case, aren't you?

12 A Yes.

13 Q Have you discussed that effect in your
14 testimony?

15 A No, I have not.

16 Q Could you go to line 6 of page 59? On lines
17 8 to 12, you urge the Commission to disregard the
18 elasticity data offered by Postal Service Witness
19 Thress in this case. Is that correct?

20 A I don't think I talk about Witness Thress by
21 name in here, but, yes, I'm referring to his work.

22 Q In fact, much of your testimony, though, is
23 an extended explanation for why you will be the
24 Commission should disregard those elasticity
25 estimates. Correct?

1 A Much of my testimony is a critique of
2 Witness Thress's procedures, yes.

3 Q The point of the critique, or the punchline
4 of the critique, is that his elasticity estimate
5 should be disregarded. Correct?

6 A They should be disregarded for single-piece
7 mail.

8 CHAIRMAN OMAS: Mr. Levy, would you speak a
9 little louder, please?

10 MR. LEVY: Yes, sir.

11 CHAIRMAN OMAS: Thank you.

12 BY MR. LEVY:

13 Q Now, you do believe that the Commission
14 should consider your elasticity estimates in setting
15 first-class rates. Correct?

16 A Yes, but not in a mechanical sense.

17 Q Your own price elasticity for single-piece,
18 first-class, letter mail is negative 0.456. Is that
19 correct?

20 A Correct.

21 Q In plain terms, that means that if there is
22 a small increase in the price of single-piece mail,
23 volume will go down less than half as much as the
24 price goes up.

25 A That's the definition of an inelastic demand

1 curve, y

2 Q So all of the things being equal, the Postal
3 Service will get more revenue from a 42-cent, single-
4 piece stamp than from a 41-cent, single-piece stamp.

5 A And that holds true for all Standard A,
6 regular mail rates also. They are also very price
7 inelastic.

8 Q Now, in your testimony, you referred to a
9 death spiral.

10 A I used the terminology that some other
11 economists have used in papers, yes

12 Q You're not contending that, during the life
13 expectancy of the rates proposed here, a death spiral
14 would result from a 42-cent, first-class stamp, are
15 you?

16 A I'm not saying that this one rate increase
17 will do it, but I have made estimates in a footnote to
18 the effect that if the Postal Service continues to
19 mainly focus on raising rates by raising first-class
20 rates in general and single-piece rates, if you plot
21 out the current dynamics, you are left with many, many
22 billions less in volume within a relatively short
23 period of time.

24 Q Even under your view of competition and
25 elasticity, that period of time would be longer than

1 the expected life of these rates. Correct?

2 A Yes, but one never knows, Mr. Levy, because
3 an important point of my testimony is that, unlike the
4 known competitive substitutes for standard mail,
5 Standard A, regular mail, which are well known -- the
6 pricing is well known, and how it impacts postal rates
7 when postal volumes and postal rates go up -- there is
8 a lot of data on that, and it's very well known.

9 What is very risky in this environment is
10 that one does not really know what is going to happen
11 with this Internet and electronic payments
12 competition. I'm concerned you could have another
13 wave of volume losses in first class like you did in
14 the earlier part of this decade as you go through this
15 S-shaped growth curve of broadband.

16 So you could see, within this rate cycle, a
17 fairly substantial drop-off again, and raising rates
18 on single-piece mail sure is not going to help that.

19 Q Well, based on the data we have before us,
20 you predicted an elasticity that implies the Postal
21 Service will make more money over the life cycle from
22 a 42-cent stamp.

23 A I do, but, Mr. Levy, please read all of the
24 testimony. I also stated that, at the margin, the
25 overall aggregate, own price elasticity, as of 2005,

1 may be as much as .765, whereas over the entire period
2 that Mr. Thress examines his long run on price
3 elasticities, 1983 through, I guess, all of the
4 quarters of 2005, .456, but it appears to me, with the
5 very basic kind of demand curve I use, which allows
6 one to vary elasticities, at the margin of time, we're
7 trending towards an elasticity of one, in which case
8 it makes no sense to raise postal revenues. You don't
9 raise postal rates. You don't get more revenue; you
10 don't get less and may be trending above one.

11 Q With an inelasticity of negative 0.7, the
12 Postal Service would still make more money with a 42-
13 cent stamp than with a 41-cent stamp.

14 A Well, not necessarily, because the
15 implementation would be January of 2007. Is that
16 correct? And if that number is trending to .765 in
17 2006, right now, and that .765 is 2005 data, you could
18 well have a unitary elasticity on your hands by 2007.

19 Q Have you submitted any calculations on the
20 record showing that the elasticity will be unitary or
21 higher before the end of 2007?

22 A No, I haven't, but I have submitted evidence
23 in this testimony that in certain markets, which are
24 the markets of concern, like the U.S. bill payments
25 market, one can infer from very high cross-

1 e elasticities that, at least for initial payments, you re
2 probably already in the elastic region, and that's not
3 healthy for the Postal Service, to be losing more bill
4 payments mail by raising rates.

5 Q And that situation could be mitigated by
6 offering a courtesy reply mail discount.

7 A Yes. As I discuss in a footnote to my
8 conclusion, it could be mitigated by any number of
9 things, including my rate proposal: a P stamp
10 proposal; a value-added rebate on fully paid postage,
11 which, I think, would incentivize the private sector
12 to sort more mail upstream. There is no one way to
13 lick this problem, but the Commission can only deal
14 with rates. If I cannot deal with some of these other
15 proposals.

16 Q You have seen no evidence to indicate that
17 the elasticity of demand for correspondence mail is
18 close to unitary, have you?

19 A No, I have not.

20 Q Would you to your response to Interrogatory
21 DMA, Question 6(e)?

22 A It will take me a moment to find it, but
23 bear with me, please. Mr. Levy, I'm sorry. Six --

24 Q Subpart (e).

25 A Subpart (e). Okay.

1 **Q** You see there is a discussion of Ramsey
2 pricing. Just to clarify, you're not proposing that
3 the Commission set rates in this proceeding based on
4 Ramsey pricing, are you?

5 **A** No. I'm not suggesting that.

6 **Q** Are you suggesting that the Commission
7 should base any weight on relative elasticities in
8 setting coverage ratios?

9 **A** I am suggesting that they need to look at
10 those and look at our elasticity estimates for single
11 piece and Standard **A** regular, in particular, because
12 they are inverted. It appears quite clear to me that
13 the own price elasticity of demand for single-piece
14 mail on the face of this Internet competition is
15 somewhat more elastic than the elasticity for Standard
16 **A**, regular mail. That does have implications for cost
17 coverages, the shifting of institutional costs, and
18 markups, but I'm not suggesting that that's the only
19 factor that should be considered in the setting of
20 rates.

21 **Q** Are you testifying that a factor the
22 Commission should consider is that higher markups
23 should go to classes with more inelastic demand?

24 **A** Well, let me be specific. I'm suggest that,
25 in light of the fact that Standard **A**, regular mail

1 do s n t experience falling volumes, like single
2 piece, it can much more easily afford a higher rate
3 increase in this case than that proposed by the Postal
4 Service. So the answer to your question is yes, but
5 with regard to the specific recommendations I'm
6 making, not your general question.

7 Q So there are other classes of mail where you
8 would give no weight to relative elasticities in
9 setting current ratios, or you just have no position.

10 A The proposal that I have and the analysis I
11 did was pretty deliberate in believing that this is
12 the best place to get the extra revenue from to
13 support the GCA proposal.

14 Q I'm sorry, Dr. Clifton. Maybe my question
1.5 is unclear. I'm asking for your opinion on a rate-
16 making principle. The principle is that a factor that
17 should be considered in allocating institutional costs
18 is that the more inelastic the demand, the larger the
19 share of institutional costs should be allocated to
20 that class or subclass.

21 Before you say whether or not you disagree
22 with that proposition, do you understand that
23 proposition?

24 A I believe I understand that proposition.
25 You're sort of stating the same question that you

1 stated about Ramsey pricing. My answer is the same:
2 I'm not recommending Ramsey pricing. But I will say
3 that these demand elasticities convey a lot of
4 information about the market, and in one interrogatory
5 response, Witness O'Hara made it very clear himself
6 that he would not have recommended the rates that he
7 recommended if he knew the elasticities of any of
8 these major rate categories were different than what
9 was supplied to him by Witness Thress. We now know
10 that those elasticities are not correct, and the
11 Postal Service's own pricing witness probably could
12 not support those same rates today.

13 So the elasticities aren't the only
14 important thing, but I think they are a very important
15 thing, and I think they are especially important in
16 the climate that we face of falling volumes of the,
17 you know, goose that laid the golden egg. What kind
18 of business would be raising rates in its product
19 areas where they are having competitive problems?

20 Q Is that a yes?

21 A It's a qualified yes, Mr. Levy.

22 Q Now, you're not a lawyer, Dr. Clifton, are
23 you?

24 A Probably just a wanna-be lawyer.

25 Q We all either want to be lawyers or want to

1 be economists.

2 A We've had that discussion before many times.

3 Q But you are aware, as an experienced Postal
4 Rate Commission witness, that Section 3622(b) of the
5 act requires the Commission to consider a bunch of
6 factors in allocating institutional costs.

7 A Yes, I am.

8 Q What follows is not going to be a quiz but a
9 series of road marks. One of the factors is the value
10 of service to the sender. Correct?

11 A Correct.

12 Q You agree that single-piece, first-class
13 mail has a greater value of service than standard
14 mail.

15 A Yes, but I will state, as a result of my
16 analyses, that Standard A, regular mail has higher
17 value added of service than I previously believed
18 because it's more inelastic.

19 Q My question is value to the sender. Single-
20 piece, first-class mail has a higher value to the
21 sender than standard mail does.

22 A Uh-huh.

23 Q Single-piece, first-class mail has higher
24 value to the recipient than standard mail, doesn't it?

25 A One would think so, but not for my wife. My

1 wife is Brazilian and does receive advertising
2 now. She learns a great deal about this country that
3 way.

4 Q Another factor that the Commission must
5 consider is the fairness and equity of the rates.

6 A Yes, sir.

7 Q And that sometimes has been described as
8 a fairness in terms of exploiting monopoly power.

9 A Yes.

10 Q Now, your testimony is that the Postal
11 Service has little or no monopoly power over **single-**
12 **piece**, first-class mail.

13 A Not in the aggregate. What I stated in the
14 test finding was it appears to me that the Postal
15 Service almost has to act like a price taker in the
16 U.S. payments market. I believe its market share has
17 fallen so far under 50 percent that it can't make
18 prices anymore. I mean, it pretends to, and then it
19 loses all of its volume.

20 So, in the U.S. payments market, if not in
21 the aggregate in the single-piece world, I believe the
22 Postal Service does not have any remaining market
23 power.

24 Q Another factor under the act is educational,
25 cultural, scientific, and information value to the

1 recipient.

2 A Yes.

3 Q And that's commonly known as -- I never
4 pronounce this right -- the "XC factor."

5 A I call it "XE," but you're probably right.

6 Q Your written testimony, in any event,
7 doesn't discuss the relative XC value of single-piece,
8 payment mail versus standard mail, does it?

9 A No, it doesn't.

10 Q Now, another factor is the effect of rate
11 increases on the general public. Correct?

12 A Correct,

13 Q Now, your testimony doesn't estimate how
14 much your proposal would save the average consumer in
15 first-class postage.

16 A I haven't made that estimate, no.

17 Q And your testimony also doesn't consider how
18 much the consumer would pay indirectly for higher-
19 standard postage paid by its vendors or advertisers.

20 A I have not made that calculation.

21 Q Now, one final line of questioning. Both
22 you and Dr. Colejian have testified about the need for
23 econometric models to have sound theoretical
24 underpinnings.

25 A Correct.

1 Q And you on rast that with cook book
2 econometrics.

3 A Yes.

4 Q Another way of saying that is it's not
5 enough to stumble on equations that produce low error
6 terms by trial and error. The equations and the
7 results need to make good economic sense.

8 A We're talking art, not science. But it is
9 better to proceed from sound, theoretical principles
10 and do a lot of the work up front before you begin
11 playing with estimations.

12 Scientific econometrics does not mean that
13 you don't, you know, explore different estimation
14 techniques, but you don't import the theory from the
15 rear end after you simply hit a high R square. You
16 don't then, ex post, fill it in with a theoretical
17 principle.

18 Q There is a certain amount of judgment
19 involved. It's not just a mechanical exercise.

20 A No. I mean, it has a lot of equations, it
21 has a lot of numbers, but the fact is, there is a lot
22 of judgment.

23 Q Now, another factor that the Commission
24 needs to consider in allocating institutional costs is
25 the effect of rate increases on business mail users.

1 Isn't that right?

2 A That's correct.

3 Q And one of the class of business mailers
4 that use both first-class and standard mail is the
5 banking industry. Is that correct?

6 A That use both, yes. uh-huh.

7 Q And you answered several interrogatories
8 about the effect of your proposals on the banking
9 industry that were filed by the Postal Service in DMA?

10 A I'm not sure how many were filed by the
11 Postal Service, but certainly DMA filed a set of them.

12 Q Postal Service Question 52. This is not a
13 quiz; this is just --

14 A Okay. Subject to check, fine.

15 Q Now, would you go to your response to DMA
16 Interrogatory No. 3?

17 A I have it.

18 Q There, you responded that the banking
19 industry should be pleased with your initial proposal.
20 Is that correct? Is it correct that you said that?

21 A Yes.

22 Q Because, in your view, the average or
23 typical bank would save enough on single-piece, first-
24 class postage to outweigh the increase in standard
25 postage .

1 A That's not at all what I said.

2 Q The industry, as a whole, would save enough
3 on single-piece, first-class postage to outweigh the
4 increase in standard postage.

5 A Based on the data that I had, the caveat
6 that you have to make in this is, and I am speaking as
7 a professional economist here -- the caveat that you
8 have to make in a welfare economics judgment like this
9 is called the "compensation principle" in welfare
10 economics. The GCA proposal would save a penny for
11 every piece of single-piece mail sent by banks, and
12 based on the data that I had available when I did all
13 of this work, all of these estimations, that outweighs
14 the additional costs that some banks would have
15 because they do a lot of Standard A, regular marketing
16 mail.

17 In other words, the winners can compensate
18 the losers and make them at least as well off, or
19 better off, while being better off themselves. So,
20 unambiguously, the industry is better off.

21 Q Let me ask a clarification question before I
22 go into the main part of this compensation principle
23 you talked about. You're not suggesting that the
24 Commission has the authority to order the winning
25 banks to compensate losing banks, are you?

1 A Well, they might be able to do that in some
2 way without too much difficulty, actually, but I
3 haven't recommended a procedure for them to do that.

4 Q How would they do that? How would the
5 Commission order the banks that did well under the
6 proposal to compensate the banks that did poorly?

7 A I haven't thought about it, but it doesn't
8 change my statement about what benefits the industry.
9 I mean, the notion of an industry itself is a bit
10 abstract, but the answer I've given is quite clear cut
11 and, I think, irrefutable.

12 Q What you're really proposing is sort of a
13 parietal thought experiment that if the winner is
14 compensated, the loser, the industry, as a whole,
15 would be better off.

16 A Well, parietion -- you parietal optimality,
17 you don't have to go that far. The compensation
18 principle doesn't require this at all. We're not
19 talking about any parietal optimal position; we're
20 just talking about a straightforward principle in
21 welfare economics called the compensation principle.

22 Q Now, the compensation principle, though,
23 does require that the dollars won by the winners
24 exceed the dollars lost by the losers, doesn't it?

25 A Correct.

1 Q And so a premise of your compensation
2 argument is that for the banking industry as a whole,
3 the dollars won by the winners would exceed the
4 losses, dollars lost, by the losers. Right?

5 A Right, and that follows from the volume of
6 single-piece mail sent by banks being about four times
7 the volume of standard mail sent by banks and by the
8 fact that the one-cent decline in single-piece mail is
9 spread over 39 billion single-piece mail pieces and is
10 made up by approximately 51 billion Standard A,
11 regular pieces. So the one-cent decline in the single
12 piece would result in a less-than-one-cent increase in
13 that larger volume of Standard A regular.

14 Q Now, in your response to DMA No. 3, Part B,
15 you estimated that a majority of the banking
16 industry's first-class mail volume is single piece.

17 A Based on my belief when I wrote this, that
18 was what I understood.

19 Q That's *not* your belief now, is it?

20 A No, it's not.

21 Q And you also estimated that only six percent
22 of the banks' mail was Standard A.

23 A A little less than six percent.

24 Q Is that still your belief?

25 A Yes. That is my belief, based on the data

1 that I had available to me.

2 Q And the data that you had available to you
3 were a 2000 American Bankers Association survey
4 report.

5 A A publicly available survey report, yes.

6 Q And that report was based on data for 1999.

7 A Correct.

8 Q Dr. Clifton, before you answered that
9 interrogatory, did you look for any more recent data
10 than data from 2000 or 1997

11 A Did I look for any more recent data?

12 Q Yes.

13 A No, I did not.

14 Q Now, in your testimony, you mention the
15 household diary study several times, don't you?

16 A Yes.

17 Q Subject to check, you mention it 12 times in
18 your testimony.

19 A You've gone over it more carefully than I
20 have, Mr. Levy.

21 Q Well, it was late at night, so you had
22 better check. And you cite the 2005 household diary
23 study two times, don't you, on page 9 of your
24 testimony and page 12?

25 A Yes. I see the reference to 2005 there.

1 Q A d somewhere in your office, you have a
2 copy of the 2005 household diary study.

3 A I may or may not have the entire household
4 diary study. I'm very focused. I tend to download
5 only the pages I need because I don't like paying for
6 more --

7 Q -- paper?

8 A -- cartridges than I need to.

9 MR. LEVY: We won't ask the price elasticity
10 of that.

11 I'm going to mark as **ANM** Cross-examination 2
12 some other pages from the **2005** household diary.

13 (The document referred to was
14 marked for identification as
15 Exhibit No. ANM-X-2.)

16 MR. LEVY: I will represent for the record
17 that **ANM** Cross-examination Exhibit 2 includes pages
18 20, 32, 39, and Appendix Table A-2-20 of the 2005
19 household diary study, and I have the entire thing
20 here, if counsel or the witness want to refer to it.

21 BY MR. LEVY:

22 Q Dr. Clifton, would you look at the last page
23 of Exhibit 2, which is Table A-2-20?

24 A Okay.

25 Q Now, the caption of the table is "Total

1 Percent of Industry's First-class Mail Received by
2 Households Which Is Sent Presort" for three different
3 fiscal years. Do you see that?

4 A Uh-huh.

5 Q And do you see the second line is "credit
6 card"?

7 A Yes.

8 Q And for 2005, the percent is 97.1 percent.
9 Do you see that?

10 A **Uh-huh.**

11 Q And the line below there, "bank"; do you see
12 that?

13 A Yes.

14 Q And the value is **83.9.**

15 A Yes.

16 Q And "total financial," which is about five
17 lines down, the value is **86.4.** Do you see that?

18 A Uh-huh.

19 Q Have you ever seen this page before?

20 A I'm not sure if I have seen it until very
21 recently. I forget where I have seen it recently, but
22 it may have been in response to some interrogatories
23 floating around.

24 Q Now, at some point, you came to believe that
25 the percentage of first-class mail sent by banks that

1 was single piece, according to the 2000 ABA study. was
2 22 percent rather than 66 percent. Is that correct?

3 A 22.1 percent, yes.

4 Q And that number was based on the data in the
5 ABA report as opposed to the pie graph.

6 A Right. The pie graph didn't have any
7 sourcing with it. It was unambiguously clear, and I
8 had relied on that. There did not go much beyond that
9 in my testimony because it was my mistaken belief at
10 the time, from something that was said to me, that the
11 survey was private and Confidential, so I knew I
12 couldn't use it in any direct way in my testimony.

13 Q Excuse me. Let me interrupt you just to
14 clarify it for the record. I'm not representing the
15 ABA, and so I don't have any authority to ask you
16 anything about anything confidential that you may have
17 discussed with them. If I ask anything that's -- let
18 me know.

19 A Okay. I'll try to be responsive, but I also
20 do not want to -- this is an awkward position here,
21 but sure.

22 Q Would you go to DMA Interrogatory 12 to you?
23 And in that interrogatory, you calculate that, even if
24 only 22 percent of banks' first-class mail is single
25 piece, they would still come out ahead under your

1 proposal, under your narrower, delinked proposal.

2 A Well, I don't think it has anything to do
3 with linked or delinked, per se. The driving factors
4 here are in this **ABA** survey. The volume of Standard
5 **A**, regular mail sent by banks is only one-quarter of
6 the single-piece mail sent by banks by first-class
7 single piece.

8 Q **And** the value of standard mail to which you
9 refer is **426.2** million pieces.

10 A That's the number that was in the **ABA**
11 survey, yes.

12 Q And that number was for **1999**.

13 A Right.

14 Q And you believe that's still a reasonable
15 estimate for the year **2005** or **2006**.

16 A I have no idea, Mr. Levy. I based what I
17 said in my testimony in response to these
18 interrogatories on an **ABA** survey, which at least
19 covers the waterfront, which your table does not.
20 Your table only says "first-class mail received by
21 households." There is a lot of other mail out there
22 that banks send to nonhouseholds. My corporation, I
23 would estimate I get 10 corporate pieces from banks
24 for every piece my household gets from a bank.

25 That's the limitation of these percentages,

1 and as we're going t rough here, I think, in response
2 to some of the DMA interrogatories, I dug **down** and did
3 find this data, and I had to reject it out of hand as
4 being very useful because this is just mail received
5 by households. **A** lot more mail **is** sent by banks than
6 just mail that banks send to households, so I don't
7 know if these percentages have much meaning.

8 Q About three-quarters of all mail sent in the
9 United States is sent to households.

10 A I can't confirm for you what the statistics
11 are, but we're not talking about overall mail; we're
12 talking about bank mail.

13 Q Would you be surprised if there were an
14 answer to that question in the household survey diary?

15 A I have no emotional reaction to it at all.

16 Q The **426** million figure; let's do a reality
17 check for that. This is **426** million pieces of
18 standard mail sent in the United States. There are
19 approximately **220** million Americans above the age of
20 **18**. Would you accept that, subject to check?

21 A Sure.

22 Q So **426** million pieces translates **into** two
23 pieces per adult per year approximately.

24 A Sent by a bank?

25 Q Yes, standard mail sent by a bank.

1 A I assum th math follows?

2 Q Do you get two pieces of standard mail from
3 a bank in a year?

4 A I have no idea.

5 Q Do you think the average resident in a
6 middle- or upper-middle-class neighborhood gets only
7 two pieces of standard mail from a bank in an entire
8 year?

9 A I have no idea. I know I get a lot of -- I
10 can't quantify it for you -- I know I get a lot of
11 first-class, advertising mail from banks.

12 Q Would you take a look at **ANM** X-2 again?
13 This time, look at the third page, which is page 39 in
14 the original document. Do you see the bar chart at
15 the bottom that's labeled Figure 5.2?

16 A Yes.

17 Q Do you see the two bars that are very dark?

18 A Yes.

19 Q **And** the one on the right is labeled "19.4." Do
20 you see that?

21 A It's a little fuzzy, but I **see** it, **yes**. I
22 think I see where the decimal point is.

23 Q And that indicates that, in 2005, households
24 received 19.4 billion pieces of standard mail,
25 advertising mail, from the financial industry.

1 A Yes, but financial industry goes way, way,
2 way beyond banks, Mr. Levy --

3 Q Okay.

4 A -- from other tables in the survey.

5 Q Like, for example, let's turn to the second
6 page of the exhibit, which was page 32 of the original
7 document. Do you see the top third of the chart has
8 some numbers for the financial industry?

9 A Yes.

10 Q And this is bill and statement volume.
11 Right?

12 A Yes.

13 Q And just eyeballing, it appears that banks,
14 S&Ls, credit unions, and credit card issuers send
15 slightly more than half of all billing and statement
16 mail sent by the financial industry.

17 A Well, banks don't send a very high
18 percentage of that 7.89 billion, do they? They send
19 1.26 billion out of the 7.89 billion.

20 Q I repeat my question: Banks, S&Ls, credit
21 unions, and credit cards collectively account for
22 slightly more than half of the bills and statements
23 sent by the financial services industry.

24 A The answer to your question is yes, but I
25 was not examining all of these; I was examining banks

1 in response to the MA interrogatories.

2 Q Now, you, in your testimony, refer several
3 times to -- I'm sorry -- I'm mischaracterizing. You
4 refer at least one time to negotiated service
5 agreements.

6 A I believe I refer to them once, yes.

7 Q And you also refer to -- you are familiar
8 with what a negotiated service agreement is.

9 A Roughly. I haven't worked on it yet. I
10 hope to work on some in the future.

11 Q You and I were at a conference with about
12 200 people on letter mail shortly after the filing of
13 the rate case.

14 A I was there.

15 Q Do you recall a discussion of the mail
16 volumes of NSA banks?

17 A No.

18 Q Do you recall whether the Postal Service
19 files any data on the volume of standard mail entered
20 by NSA banks?

21 A I don't believe I've ever seen any **Postal**
22 Service data on that. It doesn't mean it doesn't
23 exist. I haven't looked at it.

24 MR. LEVY: Let me see if I can refresh your
25 recollection, and I'm going to mark this as ANM-X-3, a

1 two-page excerpt from a February 6, 006, report by
2 the Postal Service on its NSA with Capital One in
3 Docket MC2002-2 that I downloaded from the
4 Commission's Web site last night.

5 (The document referred to was
6 marked for identification as
7 Exhibit No. ANM-X-3.)

8 BY MR. LEVY:

9 Q Will you look at the second page, which is
10 page 16 of the original?

11 A Uh-huh.

12 Q Do you see, this page deals with standard
13 mail solicitations?

14 A Okay.

15 Q Do you see the total volume number for mail
16 category that begins with a one?

17 A Midway, total volume, yes.

18 Q It's slightly over a billion pieces of
19 standard mail.

20 A Okay.

21 Q This is for one bank. You've seen that
22 before?

23 A I don't believe I have.

24 Q Dr. Clifton, the ..

25 A Can I just ask a question? This says

1 "October 2005 through September 2005." Is that --

2 Q Yes. If you look at the first page of the
3 document, in the narrative, it says "October 2004 to
4 September 2005."

5 A Oh, I see. Okay.

6 Q You're right. The heading on the second
7 page appears to be a typo.

8 Would you accept, subject to check, that the
9 figures for Bank One and Discover were about 450
10 million pieces?

11 A Over the same time period?

12 Q Over a one-year period.

13 A The same one-year period?

14 Q Not the same months, but a one-year period.
15 I have them, if you want to see them.

16 A Subject to check, sure.

17 Q If you were aware of these numbers, would
18 you have suggested that the standard mail volume of
19 the industry was approximately 450 million pieces?

20 A The standard mail volume of what industry?

21 Q The banking industry.

22 A Again, I would have to define "bank" because
23 I'm not talking about banks that are really just
24 credit card companies and all the rest. My testimony
25 referred to banks.

1 MR. LEVY: Th nk you, and that's all I have.

2 Mr. Chairman, is now or at the end of the
3 other cross the time to move in the exhibits?

4 CHAIRMAN O W : I would do it right now.

5 MR. LEVY: Then **let** me do that right now, if
6 I may. I move that they be admitted.

7 CHAIRMAN O W : You mean your --

8 MR. LEVY: ANM-X-1 through X-3.

9 CHAIRMAN OMAS: All right. That's what I
10 needed to hear. You want to move them into evidence.

11 MR. LEVY: Yes, sir.

12 CHAIRMAN OMAS: Without objection, so
13 ordered.

14 //

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1 (The documents referred to,
2 previously identified as
3 Exhibit Nos. ANM-X-1 through
4 ANM-X-3, were received in
5 evidence.)

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ANM-X-1



- The Greeting Card
- Connecting with Greeting Cards
- The Greeting Card Association
- Business Resources & Contacts
- It's in the Cards
- Membership Information
- LOUIE Awards
- Heroes in our Midst
- Media Center
- Members Only

The Greeting Card

General Facts

- U.S. consumers purchase approximately 7 billion greeting cards each year, generating nearly \$7.5 billion in retail sales.
- More than 90 percent of all U.S. households buy greeting cards, with the average household purchasing 30 individual cards in a year.
- The average person receives more than 20 cards per year, about one-third of which are birthday cards.
- Greeting cards range in price from 50 cents to \$10, although counter cards typically cost between \$2 and \$4. Cards featuring special techniques, intricate designs and new technologies are at the top of the price scale.
- The exchange of greeting cards is one of the most widely accepted customs in the U.S. There are cards for virtually any occasion or relationship, and they are widely available. Approximately 100,000 retail outlets around the country carry greeting cards.
- Women purchase more than 80 percent of all greeting cards. Although women are more likely than men to buy several cards at once, men generally spend more on a single card than women.
- There are two categories of greeting cards -- Seasonal and Everyday. Total card sales are split approximately 50-50 between the two types.



*celebrating, promoting and protecting
the tradition and cultural values of
exchanging greeting cards.*

The most popular Everyday cards are Birthday (60%), Anniversary (8%), Get Well (7%), Friendship (6%), and Sympathy cards (6%).

The most popular Seasonal cards are Christmas (60%), Valentine's Day (25%), Mother's Day (4%), Easter (3%), and Father's Day (3%) cards.

- There are an estimated 3,000 greeting card publishers in the U.S., ranging from small family-run organizations to major corporations. GCA-member publisher companies account for approximately 95 percent of industry sales.
- Nine out of 10 Americans say they look forward to receiving personal letters and greeting cards because cards allow them to keep in touch with friends and family and make them feel they are important to someone else.
- Although e-mail, text messaging and phone calls are valued by Americans for helping them communicate with family and friends, the majority of Americans say they prefer the old-fashioned handwritten card or letter to make someone feel truly special.

[The Greeting Card](#) | [Connecting with Greeting Cards](#) | [The Greeting Card Association](#) | [Business Resources & Contacts](#)
[It's In the Cards](#) | [Membership Information](#) | [LOUIE Awards](#) | [Media Center](#) | [Members Only](#)

[Home](#) | [Contact GCA](#)

college degree) than households without (11% have a college degree). In fact, these correlations could be a warning sign for mail, since more volume goes to households that are vulnerable to diversion. Table 3.11 shows that, although the number of mail pieces sent by households with Broadband is higher than for household without access, it is also lower than the number for Dial-up users. This may indicate that diversion increases as households upgrade to faster technologies.

Table 3.11:
Correspondence Mail Sent by Type of Internet Access
(Pieces per Household per Week)

Internet Access	Pieces per Household per Week
Broadband	1.3
Dial-up	1.5
None	1.0
Total	1.3

Table 3.10
Correspondence Mail Received by Type of Internet Access
(Pieces per Household per Week)

Internet Access	Pieces per Household per Week
Broadband	2.7
Dial-up	2.7
None	1.7
Total	2.5

Source: Household Diary Study, FY 2005.

Table 3.12: Personal Correspondence Sent and Received

Correspondence Type	Volume (Million Pieces)			Change 2003-2005
	2003	2004	2005	
Personal Letters	1,468	1,385	1,227	-16.4%
Holiday Greeting Cards	2,417	2,417	1,169	-1.1%
Non-Holiday Greeting Cards	1,620	1,597	1,418	-12.5%
Invitations	665	728	657	1.2%
Announcements	183	136	124	-32.3%
Other Personal	326	298	275	-15.5%
Total	6,458	6,561	5,870	9.1%
Internet Cards	1,541	1,654	1,399	-9.2%
Correspondence Type	Pieces per Household per Week			Share of 2005 Total
	2003	2004	2005	
Personal Letters	.3	.2	.2	17%
Holiday Greeting Cards	.4	.4	.4	30%
Non-Holiday Greeting Cards	.3	.3	.2	20%
Invitations	.1	.1	.1	9%
Announcements	.0	.0	.0	2%
Other Personal	.1	.1	.0	4%
Total	1.1	1.1	1.0	81%
Internet Cards	.3	.3	.2	19%

Source: Household Diary Study, FY 2003, 2004 and 2005. Note: Totals may not sum due to rounding.

Tabk4.14
Bill and Statement Volumes by Industry

Industry	Volume	
	Bill Volume	Statement Volume
Financial		
Bank, S&L, Credit Union	1,263	1,676
Credit Card	3,981	25
Insurance Company	2,146	497
Real Estate/Mortgage	363	136
Other Financial	139	1,547
Total Financial	7,892	5,881
Merchants		
Department Store	617	20
Publisher	541	11
Mail Order Company	158	1
Other Merchants	425	18
Total Merchants	1,761	50
Service		
Telephone Company	2,117	20
Medical and Other Professional	1,914	165
Cable TV	912	9
Other Service	577	45
Total Service	8,308	253
Manufacturers	58	23
Government	577	295
Social/Nonprofit	8	1
Other/Don't Know/Refused	52	92
Total - All Industries	18,656	6,594

Source: Household Diary Study, FY 2005

Internet Access

Finally, Table 5.8 shows the relationship between advertising mail received and Internet access. Despite all the attention paid to online and e-mail advertising, households with Internet access receive more advertising mail than those without access.

To a large degree, this reflects other characteristics of the household; Internet access is closely tied to income and education. However, it shows that advertising mail continues to be sent even when new advertising media become available. In addition, Table 5.8 may demonstrate the use of Internet information to target potential customers through direct mail advertising.

Table 5.8:
Ad Mail Received by Internet Access
(Pieces per Household per Week)

Broadband	20.7
Dial-up	18.0
None	12.6
Total	17.3

Source: Household Diary Study, FY 2005.

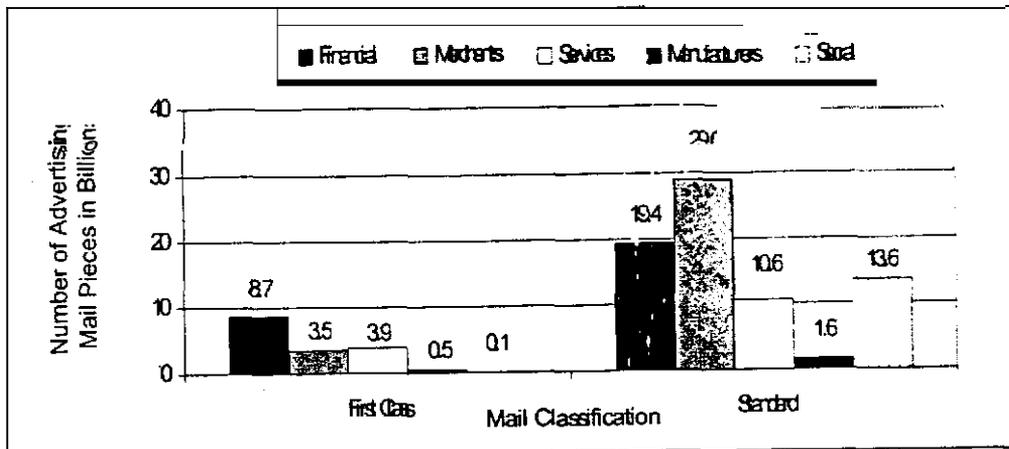
Senders of Advertising Mail

Figure 5.2 provides data on the senders of advertising mail to households. Merchants continue to be the largest senders; in 2005, they sent nearly 40 percent of Standard advertising mail and 21 percent of First-class advertising mail. Financial firms are the second largest sender and the largest sender of First-Class advertising (52 percent). Many bills and statements, especially those for credit cards, include advertising.

Attitudes toward Advertising

With \$276 billion spent in the United States on advertising, it is not surprising that few households wish they received more. Yet many households find some advertising interesting. Figure 5.3 shows about 38 percent of households find some direct mail pieces interesting, a figure that is about the same as for television and radio advertising and significantly less than for newspapers.

Figure 5.2
Advertising Volumes for First-Class and Standard Mail Advertising by Sender Type



Source: Household Diary Study, FY 2005.

Note: First-Class and Standard Advertising Mail Pieces excluding Unsolicited Samples and pieces for which no industry of sender was given

Table A2-20
Total Percentage of Industry's First-Class Mail Received by
Households Which is Sent Presort
Postal Fiscal Years 1987, 2004 and 2005
(Diary Data)

Industry	Percent Sent Presort		
	1987	2004	2005
Financial:			
Credit Card	76.9	96.5	97.1
Bank	59.1	83.2	83.9
Securities	37.6	79.6	80.3
Money Market ①	52.4	82.6	83.6
Insurance	62.2	83.1	85.5
Mortgage	19.0	56.2	57.5
Total Financial	58.9	84.9	86.4
Merchants:			
Supermarkets	N/A	76.0	81.2
Department Store	73.5	91.5	92.1
Mail Order	50.0	80.1	79.6
Other Store	33.1	72.0	76.2
Publisher	58.9	86.8	85.8
Land Promotion ①	61.9	61.8	66.9
Restaurant ①	50.0	48.8	41.4
Consumer packaged goods	30.3	72.6	74.5
Auto dealers ①	45.5	71.9	72.1
Service stations ①	14.3	72.6	75.9
Total Merchants	55.0	76.5	77.9
Services:			
Telephone	84.4	67.0	62.6
Other utility	81.2	84.6	84.9
Medical	35.9	61.2	63.4
Other professional	7.3	44.7	42.3
Leisure service	31.1	64.6	67.6
Cable TV	57.2	65.0	61.0
Computer ①	15.4	80.5	83.1
Craftsman ①	22.2	28.3	28.2
Total Services	56.7	68.4	67.8
Federal government	N/A	74.3	80.4
Nonfederal government	54.0	70.1	67.6
Social/Charitable/Political/Nonprofit	16.5	38.2	39.6
Total Nonhousehold Mail Received by households	53.9	67.2	69.1
Pieces per household per week	3.7	6.5	6.8

ANM-X-3

LEGAL POLICY & RATEMAKING LAW SECTION
LAW DEPARTMENT

Postal Rate Commission
Submitted 2/7/2006 3:35 pm
Filing ID: 47790
Accepted 2/7/2006



February 7, 2006

Hon. Steven W. Williams, Secretary
Postal Rate Commission
901 New York Avenue, NW
Suite 200
Washington, DC 20268-0001

RE: Docket No. MC2002-2

Dear Mr. Williams:

In accordance with the Commission's Opinion and Recommended Decision in Docket No. MC2002-2, Experimental Rate and Service Changes to Implement Negotiated Service Agreement with Capital One, attached is the Postal Service's second Data Collection Report for the time period October 1, 2004 to September 30, 2005. I have also attached the Excel spreadsheet showing the contribution analysis.

The report was due January 30, 2006, and we apologize for the delay.

Sincerely,

Nan K. McKenzie
Attorney

Attachments

475 L'ENFANT PLAZA SW
WASHINGTON DC 20260-1137
202-268-3089
FAX: 202-268-5204

**MC 2002-2 Data Collection Report
Capital One NSA
October 2005 – September 2005**

12. Data Collection Requirement Number 12

Volume of Standard Mail solicitations by rate category in eligible Capital One permit accounts.

Mail Category	Volume
Mixed AADC Auto	7,172,808
AADC Auto	50,138,148
3-Digit Auto	500,818,749
5-Digit Auto	409,097,722
Basic Nonauto	27,445,918
3/5 Digit Nonauto	70,223,895
Total Volume	1,064,897,239
ECR Revenue per piece	
Mail Category	Volume
Basic Nonauto Letters	
Basic Auto Letters	19,776,105
Saturation Letters	-
Total Volume	19.776.105

1 CHAIRMAN **OMAS**: Mr. Koetting?

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

3 CROSS-EXAMINATION

4 BY MR. KOETTING:

5 Q Good afternoon, Dr. Clifton.

6 A Good afternoon.

7 Q I would like to start with your direct
8 testimony, page 16, lines 3 through 6.

9 A Page 16, Mr Koetting?

10 Q That is correct.

11 A Okay.

12 Q And on those lines, you say, "The Atlanta
13 Fed payments data are a strong indication that the
14 Postal Service has little remaining market power or
15 none at all, in the U.S. payment system, whether the
16 comparison is made using the number of checks or the
17 number of bills and bill payments made by mail. **Is**
18 that correct?

19 A Correct.

20 Q And by "Atlanta Fed payments data," you are
21 referring to the data reproduced on the previous page
22 of your testimony, page 15 and Table 2. Is that
23 correct?

24 A Yes.

25 Q Okay. I would like to make the comparison

1 you referred to in the quote I just read from page 16,
2 but of the two options you offer, I want to use the
3 number of bills and bill payments made by mail, and,
4 looking at Table 2, I see data on number of checks,
5 but I do not see anything on bills or bill payments
6 made by mail. Is that correct?

7 A That is correct, but you can also see from
8 other parts of my testimony the inference I made that
9 that's a pretty good proxy: Bill payments made by
10 mail. How else would they be made other than by
11 checks? They are made by checks. There may be a few
12 postal money orders in there, but they are
13 overwhelmingly made by checks.

14 Q You admit, on page 14, lines 14 through 15,
15 that the Fed study does not directly report payments
16 by mail. Correct?

17 A Right, and I follow and say, "However, it
18 does report payments made by check and online cash
19 payments. Payments made by check are an excellent
20 proxy for payments made by mail because, at the point
21 of sale, checks are rarely used anymore.

22 Q So your statement on page 16, lines 3
23 through 6, is wrong to the extent that it claims that,
24 in addition to comparisons based on the number of
25 checks, the Atlanta Fed data allows me to make

1 comparisons based on number of bills and bill payments
2 by mail. Isn't that true?

3 A I don't really understand your question, Mr.
4 Koetting.

5 Q Well, your statement on page 16 says that
6 whether I want to compare using the number of checks
7 or the number of bills and bill payments made by mail,
8 the Atlanta Fed payment data is a strong indication
9 the Postal Service has little remaining market power.

10 You're saying there's two ways I can look at
11 that Atlanta Fed data and draw that conclusion, or a
12 strong indication of that conclusion. I'm saying,
13 when I go to the Atlanta Fed data, I see the checks.
14 I don't see anything about bills and bill payments
15 made by mail.

16 A Mr. Koetting, that's because I haven't
17 measured the payments market in that fashion. I've
18 measured the payments market using the Fed data base,
19 and the reason I ended up measuring the U.S. payments
20 market that way is that the Postal Service's measure
21 of how important bill payments are by mail as a
22 percent of the total U.S. payments market, that
23 household diary study has a fundamental -- really, an
24 incredulous flaw, which this Fed study does not.

25 It does not include debit card transactions

1 as part of the U.S. payments market, and yet debit
2 cards are almost as large as credit cards as a form of
3 payment, 16 versus 19 billion. Furthermore, debit
4 cards are the fastest-growing means of payment.

5 SO a reasonable inference is the reason
6 we're seeing a decline in U.S. payments mail through
7 the Postal Service is **that** people are using debit
8 cards instead of making payments through the mail.

9 I will tell you that future household diary
10 studies, based on our discussion with your vendor, are
11 going to include debit cards, but it is just a real
12 serious misimpression **that** the household diary study
13 leaves because it doesn't include debit cards **as** to
14 what the relative market position of the Postal
15 Service is in the U.S. payments market. When you
16 include debit cards, it ends up being substantially
17 smaller.

18 In this system here, in this table -- may I
19 please finish? -- the advantage is that it includes
20 debit cards, and we make the presumption here, given
21 this database, we're not trying to corrupt this
22 database. We're trying to deal with a database that
23 is internally consistent, and we, therefore, make the
24 assumption that the check totals listed here, you
25 know, are a good proxy for payments mail.

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1 Q And that's what you say in the first part of
2 the sentence on page 16 -- correct? -- that you can
3 look at the number of checks, and the Fed data tells
4 you something about that. Correct?

5 A Right.

6 Q And what I'm asking about is the second part
7 of your statement, on page 16, where you suggest that
8 the Fed data tells me something about bills and bill
9 payments by mail, and I'm saying, I don't see that in
10 Table 2, and, therefore, the second part of your
11 statement on page 16 is incorrect.

12 A Not given the assumption that I made.

13 Q The assumption you made is that checks are
14 an appropriate proxy. Correct?

15 A For bill payments.

16 Q **And** that's the first part of your statement,
17 but you've suggested that, in addition to checks, if I
18 want to look at it some way other than checks, you
19 suggest, whether the comparison is made using the
20 number of checks or the number of bills and bill
21 payments, and I'm simply saying that the second part
22 of that is not true. It is **true** with respect to
23 checks, if you want to consider them a proxy, but it
24 is not true with respect to number of bills and bill
25 payments made by mail.

1 A I disagree with that. I disagree with your
2 position.

3 Q Can you show me where on Table 2 you allow
4 me to make a comparison that talks directly about
5 bills and bill payments?

6 A I have a discussion, which I believe to be
7 empirically true, that these checks in this table are
8 a good proxy for payments sent through the mail
9 because that is my belief as to what most checks end
10 up being written for. I don't go to the department
11 store and buy my kid a gift and give them a check
12 anymore. I use a credit or a debit card. But where I
13 do use checks, and about the only place I use checks,
14 are for my monthly bill payments. I'm old fashioned.
15 I support the mail. I still use it. I don't go
16 online.

17 Q Well, let's talk a little bit about the
18 number of checks. In Table 2 on page 15, I take it,
19 you are suggesting that we compare the number of
20 checks in 2003 versus the lower number of checks in
21 2000. Is that correct?

22 A That's the only data that was available.

23 Q The decline in total checks over that
24 period, from 41.9 billion to 36.7 billion, for an
25 annual decline of 4.3 percent; that's the comparison

1 you're suggesting we make. Correct?

2 A Uh-huh.

3 Q Now, going back to page 14, lines 16 through
4 18, and I think you actually restated this before, you
5 say, "Payments made by check are an excellent proxy
6 for payments made by mail because, at the point of
7 sale, checks are rarely used anymore, having been
8 displaced by credit and debit cards." That's what you
9 say. Correct?

10 A Correct.

11 Q All right. Let's talk about that a little.

12 First of all, am I correct with respect to
13 your statement that checks are rarely used at the
14 point of sale, that that is based on your personal
15 observation of what people do rather than on any
16 statistical data?

17 A That's correct.

18 Q So, without trying to get too personal here,
19 do you do your weekly grocery shopping?

20 A No. I do the daily fill-ins.

21 Q So if I go to the grocery store every week,
22 which I do, and virtually every time three or four
23 people are ahead of me in line, if I were to typically
24 see one of them pay by check, which is what I see,
25 then I can only conclude that my personal observations

1 are different from yours. Is that true?

2 A No. I don't think you could conclude that,
3 Mr. Koetting, because that's only, you know, one store
4 that people visit in a week, and I would concur with
5 your observation about grocery stores, incidentally.
6 I see people in line use checks. I can usually never
7 find my checkbook, but I have my wallet, and my credit
8 and debit cards are there, so that's what I use.

9 But I go to many, many more stores each week
10 than just the grocery store, and I don't see, in most
11 of those other stores -- in fact, none other come to
12 mind other than grocery stores -- where people are
13 writing personal checks anymore.

14 Q Okay. But I think we can agree that some
15 checks have been replaced by credit and debit cards at
16 the point of sale along the lines you state on page
17 14. Correct?

18 A I would concede that.

19 Q So, going back to Table 2, the decline in
20 checks from 2000 to 2003; could some of that have been
21 customers at grocery stores paying by check in 2000
22 and then, by 2003, switching to a credit or debit
23 card?

24 A Possibly.

25 Q That would be an example of the type of

1 displacement you're talking about at the bottom of
2 page 14. Correct?

3 A Could be.

4 Q Would you agree that, to the extent that the
5 decline in checks between 2000 and 2003 shown in your
6 Table 2 was the result of customers at point-of-sale
7 transactions, such as grocery stores, switching from
8 checks to debit or credit cards, those particular
9 changes in consumer behavior would not likely result
10 in any material reduction in single-piece, first-class
11 mail volume?

12 A I couldn't conclude that. I would have to
13 do an analysis to answer your question, Mr. Koetting,
14 and I'm not sure that the data would be available.

15 Q Well, can you explain the logic to me by
16 which it would likely result in a material reduction
17 in first-class mail?

18 A Excuse me.

19 Q Can you explain to me, if we focus our
20 analysis on customers, consumers, who, between 2000
21 and 2003, switched their method of paying for their
22 groceries from checks to debit or credit cards, could
23 you explain to me how that phenomenon, that shift,
24 would likely result in any material reduction in
25 single-piece, first-class mail volume?

1 A That specific example that you gave would
2 not result in that, but if you look at that compound
3 annual rate of decline minus 4.3 percent, and you look
4 at that time period, and then you look at declines in
5 payments mail by single piece, there is a really good
6 correlation there, and I don't think it can be
7 explained by, in general, the phenomenon you're
8 looking at.

9 Q Well, would you agree that payments made
10 during the type of point-of-sale transactions that
11 never generated a bill and, historically, were paid by
12 cash or check but now are frequently paid by debit or
13 credit cards, those **are** outside of the market relative
14 to the Postal Service?

15 A No. Those would not be outside of the
16 market.

17 Q Why would they be relevant to the market
18 served by the Postal Service?

19 A Well, I think what you're talking about are
20 extremely minor phenomena, but I would define them as
21 part of the U.S. payments market. I would include as
22 part of the U.S. payments market the pensioner, the
23 little old lady, maybe even Aunt Minnie here, you
24 know, going to the bank window to pay a bill rather
25 than using the Postal Service.

1 Q Isn't it the propensity of a payment to be
2 made in response to a bill rather than at the point of
3 sale that puts it into the market relevant to the
4 Postal Service?

5 A Not necessarily.

6 Q Why isn't the relevant market the bill-
7 payment market rather than the broader payment market?

8 A Well, I think that the relevant market is
9 something called the U.S. payments market. I don't
10 claim to have a perfect definition of that market, but
11 the best estimate I **was** able to come up with in my
12 research is this, you know, consulting study done
13 through the Atlanta Fed.

14 Q And you call that the payment market --
15 correct? -- in general, generically.

16 A Do I call it the payment market? It's how
17 the Federal Reserve System is defining it, and I
18 adopted that for purposes of my investigation.

19 Q My point is, it's not really the total
20 payment market; it's the noncash-payment market.
21 Correct?

22 A It does not include cash. That's right.

23 Q Why would you exclude cash from the relevant
24 payment market that we're talking about, if you think
25 that the relevant market is payments? Are cash

1 payments payments?

2 A Well, now I'll do a flip on you because I
3 don't think that cash is something that the Postal
4 Service is ever likely to compete with in terms of a
5 payment. I pay workmen around my house in cash. I
6 don't think the mail system is ever going to, you
7 know, compete for that business, and I don't think,
8 you know, my credit card companies or my debit card
9 companies are going to compete for that business
10 either.

11 Q If somebody previously paid for their
12 groceries by cash but more recently switched to a
13 credit or debit card, previously they were not in the
14 market you believe to be relevant, but now they are in
15 the market you believe to be relevant. Correct?

16 A All of this logic chopping. If they paid by
17 cash, but they are now paying by credit card, that's
18 right, That's no like economic examples of a
19 housewife's services are not included in the GDP, even
20 though a woman may work 20 hours a day, and suddenly
21 she goes to work doing less work but is paid for it,
22 and now it's part of the GDP, same thing you're
23 saying.

24 Q Well, when they switch from cash to credit
25 card to pay for their groceries, you would interpret

1 that as a loss in the Postal Service's market share of
2 the relevant market. Correct?

3 A No, because I don't think there is any issue
4 of declining check volume involved in your example.

5 Q Well, when they paid cash, they were not in
6 the market, but when they switched to the card, they
7 are in the market. So that increases the denominator
8 of the Postal Service's market share. Correct?

9 A Uh-huh.

10 Q But, as you say, it's not a check, so there
11 is no increase in the numerator, so we have a
12 situation where the denominator has gone up, the
13 numerator is constant, and the Postal Service's market
14 share, as you define it, has gone down. Correct?

15 A In this logic-chopping exercise, you're
16 right, but I think this just has no practical bearing
17 at all on data between 2000 and 2003. How many people
18 converted from cash to credit cards in a grocery
19 store, and what bearing can that possibly have on what
20 I'm saying here?

21 What I'm saying in my testimony, Mr.
22 Koetting, again, to make it absolutely clear what
23 we're talking about, it is the Postal Service which
24 has greatly exaggerated, in the household diary study,
25 its presence in the U.S. payments market, however

1 defined, because it hasn't included debit cards. In
2 answers to some interrogatories that you asked of me,
3 you seem to think that debit cards and credit cards
4 are at the low end of the payment stream, where, in
5 fact, debit cards totaled \$6.2 billion in the most
6 recent data I have, and yet they are not included as
7 part of the payments market.

8 So that makes your statistics in the
9 household diary study on bill payments look as if the
10 Postal Service has a far greater presence in the U.S.
11 payments market, however defined, than, in fact, it
12 does, and that's the point of the testimony.

13 Q For the purposes of evaluating impact on the
14 mail, isn't focusing on the Postal Service's share of
15 the bill-payment market, as **shown** in your Table 1 on
16 page 12, likely to be more useful than focusing on the
17 broader payment market, as you do in Table 2 on page
18 15?

19 A Absolutely not.

20 Q Well, aren't the trends on page 15, as we
21 just discussed, going to be influenced by point-of-
22 sale payments that largely have nothing to do with the
23 Postal Service?

24 A Table 1 doesn't include debit cards, and,
25 you know, when you, therefore, talk about bill

1 payments as a percent of the household diary studies'
2 definition of the payments market, you have something
3 like 2005 data; average number of bills paid per
4 month, eight; total, including all of these electronic
5 alternatives, 12. That implies that the Postal
6 Service has a two-thirds market. share in the U.S.
7 payments market. That's absurd.

8 Q Two-thirds market share in the bill-payments
9 market. Correct?

10 A In the bill-payments market, yes.

11 Q And on what basis do you believe that to be
12 absurd?

13 A It doesn't include debit cards, debit card
14 payments.

15 Q The section heading on page 11, lines 11 to
16 12, you allege that debit card transactions are the
17 fastest-growing means of bill payments. Correct?

18 A Correct.

19 Q The only place that I see you back that up
20 in the text is page 13, lines 10 through 11. You cite
21 a source for the proposition that debit cards are the
22 fastest-growing means of payment. Is that correct?

23 A I do, and the source for that is in an
24 answer to one of your interrogatories, Mr. Koetting.

25 Q Those are two different statements, aren't

1 they, the statement on page 11 regarding debit cards
2 and bill payments versus the one on page 13 regarding
3 debit cards and payments? Isn't it true that those
4 are two different statements?

5 A What is your latter source, Mr. Koetting?
6 What is the latter page? You talk about page 11. I
7 have that one.

8 Q Page 13, lines 10 through 11.

9 A I don't see any difference in the
10 statements.

11 Q You don't see the difference between a
12 statement that says, "Debit cards are the fastest-
13 growing means of bill payment," versus a statement
14 that says, "Debit cards are the fastest-growing means
15 of payments generically"?

16 A No. I'm talking about bill payments. If
17 you mean a bill as, by definition, something that
18 comes through the mail, they are the fastest-growing
19 mechanism of payments.

20 Q And what is your support for that
21 proposition, that debit cards are the fastest-growing
22 means of payments for bills?

23 A That should read "payments." It would be
24 more accurate to label that as payments than bill
25 payments.

1 Q So what you're saying is there is no support
2 for the statement on page 11 unless you omit the word
3 "bill."

4 A No. I wouldn't say that there is no source,
5 but I would have to investigate it. I would say that
6 what I'm referring to, in terms of the growth of debit
7 cards, is that they are the fastest-growing means of
8 payment in the U.S. payments market.

9 Q So let's talk a little bit about debit cards
10 and bill payments. How do you pay a bill with a debit
11 card?

12 A Mr. Koetting, I have already conceded the
13 point. We don't need to go further with this.

14 Q No. I'm talking about your earlier point
15 that you were saying that the household diary has this
16 glaring omission because it doesn't include data on
17 bill payments by debit cards, and I'm inquiring as to
18 how it is one would pay a bill with a debit card.

19 A Well, I do pay bills with debit cards, but I
20 don't have data on it. I pay for transactions with
21 debit cards, as well as credit cards, the only
22 different being that the debit card is paid
23 immediately, and the credit card appears on a monthly
24 statement. Your balance in your account doesn't
25 automatically go down.

1 I am personally not great at paying bills on
2 time, and I will often, **so** that my Internet doesn't
3 get cut off, call the company from whom I get the bill
4 and pay with a debit card.

5 Q On the telephone?

6 A Yeah, all the time.

7 Q And so if we look at Table 1, which shows
8 the household diary bill-payment method, there is a
9 line in there for telephone, isn't there?

10 A There is a line for telephone, but in
11 discussing these issues with the people who produced
12 the household diary study, they told us that that was
13 a significant omission in the table but that they were
14 going to start to include debit cards in the next
15 household diary study. So the experts have conceded
16 the point.

17 Q Do you have any documentation of that?

18 A I'm a sworn witness, and that's my
19 documentation. We called them, and that was their
20 answer.

21 Q Once more, can you explain to me how it is
22 one pays a bill with a debit card in a manner that
23 does not involve the Internet or in person or a
24 telephone transaction?

25 A It involves those, but it's obvious, in our

1 discussion with them, that they are not picking up
2 payments by debit card. Why would they have told us
3 that they are going to include it in the future and
4 haven't in the past? I mean, I don't have the survey
5 questions that are asked.

6 CHAIRMAN OMAS: Mr. Koetting?

7 MR. KOETTING: Yes.

8 CHAIRMAN OMAS: I think we can sort of take
9 an afternoon break. Why don't we take about a 10-
10 minute break and sort of see where we are when we come
11 back? Thank you.

12 (Whereupon, a short recess was taken.)

13 CHAIRMAN OMAS: Mr. Koetting.

14 MR. KOETTING: Thank you. Mr. Chairman.

15 BY MR. KOETTING:

16 Q Dr. Clifton, I'm going to try to step back a
17 little bit, stay on the same topic but get a slightly
18 bigger picture of you of what we've been discussing.
19 Basically, we've been discussing the difference
20 between the bill-payments market, which is the subject
21 of your Table 1, and the broader payments market,
22 which is the subject of your Table 2. Correct?

23 A We've been talking about that, yes.

24 Q And at the bottom of page 15, you seem to be
25 suggesting that there is a material distinction

1 between the conclusions likely to be drawn from Table
2 1, which is the bill-payments market, versus --

3 A I wouldn't call that a market, Mr. Koetting.
4 I would say there is a U.S. payments market, and part
5 of that market, and forgive me for interrupting, part
6 of that market is paying bills, and part of it is
7 transactions. Transactions seems to be the broader
8 category.

9 Q So you're suggesting that what I'm calling
10 the "bill-payment market" is, in fact, a submarket of
11 the payments market.

12 A It's certainly a submarket in your own
13 studies of what are called "transactions." Bill
14 payments would properly be considered part of the
15 payments market. I would say that would be an
16 accurate characterization, yeah.

17 Q And the difference is that payment of a bill
18 requires something to be delivered, whereas a generic
19 payment may or may not. would you agree with that?
20 It's the method of delivery --

21 A Well, no, no, no. If you're identifying the
22 bill-payment submarket as being the mail, no, I
23 wouldn't equate those two. You don't have to deliver
24 something to pay a bill anymore. That's part of the
25 problem. You don't have to have a mail delivery.

1 Q Not a mail delivery, but some type of
2 delivery, perhaps electronic.

3 A Sure, yeah, and the same is true for, you
4 know, any payment.

5 Q Well, no. There is no delivery if I hand
6 the clerk at the grocery store my cash or my check.
7 Right? There is no intervening agent between me --

8 A There might not be there, but if you do a
9 credit card, there is a delivery to the credit card
10 company, and the same with debit cards.

11 Q Okay. Again, I'm referring specifically to
12 the bottom of page 15 and this distinction you're
13 trying to draw between the conclusions you would draw
14 looking at these various markets, or submarkets, if
15 you prefer, for bill payments.

16 To your knowledge, **is** anybody suggesting, on
17 the basis of Table 1 and the household diary study.
18 information there, anything other than that the Postal
19 Service's market share is moving down and is likely to
20 decline?

21 A People are saying that, but they are also
22 saying something else, and I don't think it's a very
23 subliminal, incidentally. What they are saying is,
24 yeah, you have the Internet, and, yes, it's eroding
25 the Postal Service's market share a little bit, but

1 it's so small a part of the total, it's not a very
2 important problem, and I think that's the
3 institutional attitude, and I think it's dead wrong

4 I think the Postal Service and the
5 Commission, if not being in a near panic about the
6 situation, should recognize that, you know, in the
7 payments market, and I'm talking about as defined by
8 the Fed, and with the assumptions I make about checks
9 and bill payments, that most bill payments in the mail
10 are done with checks. The Postal Service's market
11 share has gone down from -- in 2000, the market share
12 was 58 percent, and, in 2003, it's gone down to 45
13 percent.

14 I think that's a more accurate
15 characterization of why bill-payments mail is falling
16 as dramatically as it has fallen in some years since
17 the year 2000. There is a great erosion going on, and
18 yet you're proposing to raise the price for the second
19 time in a couple of years on all single-piece mail.
20 We're facing market conditions in an important part of
21 that single-piece-mail segment, namely, the bill-
22 payments market, where, arguably, you have price
23 elasticity in that submarket approaching one, and
24 maybe even greater than one, at the point that this
25 Commission's decision will be implemented. I think

1 it's a mistake.

2 Q Focusing on page 15 of your testimony,
3 again, you're comparing a view of the market share,
4 Table 1; view of the market share, Table 2. Is the
5 key distinction the issue you raised on lines 5
6 through 6 of page 15, that the Table 2 market share,
7 the broader payment market, is now well under 50
8 percent?

9 A I'm referring to Table 2 (DOES NOT FLOW)

10 A Mr. Koetting, I get the sense that we're not
11 connecting in this whole line of inquiry. And I think
12 perhaps the reason why is because Table 1 is how you
13 present the situation, okay, and you present the
14 situation in terms of bill payments and you look at
15 these alternative modes of bill payments. You, in
16 fact -- I checked with my colleague, who actually made
17 the call to the people at your household, IRA Study.
18 In fact, their survey does not include a question
19 about debit cards. So, that should be an answer to
20 that one, but it will and it should.

21 Q Well, like I say, it doesn't include it, but
22 --

23 A But in terms of this -- I'm not trying to
24 compare Table 1 with Table 2 and that's the direction
25 that you're going. I'm saying that Table 1 is sort of

1 the received doctrine, in terms of what I believe
2 people perceive the Internet as a problem; but, you
3 know, ho hum, evolutionary problem, slow decline, and
4 we still are dominant in the relevant market. And I
5 think the relevant market is not the bill payments
6 market, but the payments market. And in that market,
7 the share of mail is greatly declining and it's level.
8 You know, it's well under 50 percent now. And I think
9 it's a significant problem for the Postal Service.
10 You can raise prices in portions of -- for single
11 piece mail that are highly priced and elastic, you
12 face no problem. But, in the areas in which you're
13 losing volume, you raise prices on those and, you
14 know, you're losing more revenue than you gain.

15 Q Well, I would like to talk about the market
16 share. And, again, my question, which I'm not sure
17 you really addressed directly was, is the key
18 distinction issue you raise on lines five through six
19 at the Table 2 market share is now well under 50
20 percent.

21 A Yes, I'm talking about Table 2 there.

22 Q And is there any magic to 50 percent, in
23 terms of market power?

24 A I mean, I haven't taken a look at the
25 Antitrust Division's, you know, the way this

1 definition --

2 Q Well, if we --

3 A Under 50 percent means what it means.

4 Q If we were to look at the payments market,
5 but not limit it to non-cash payments and simply look
6 at the payments market in total, including cash
7 payments, have checks ever been over 50 percent of
8 that market?

9 A I responded in an interrogatory, Mr.
10 Koetting, that I don't know for sure. But, I would
11 suspect that they have been and ■ -- as you know from
12 your previous questioning before the break, I don't
13 agree that, in general, it makes sense to include
14 cash.

15 Q So, your bottom line is, we don't want to
16 just look at Table 1 bill payments, because that's too
17 narrow, and we don't want to look at total payment
18 markets, including cash, because that's too broad, but
19 we want to look at the total non-cash payments market
20 and what is important about that non-cash payments
21 market is that the share of checks, whether or not we
22 know whether the checks were sent through the mail
23 before or whether they're being sent in the mail
24 today, has now fallen below 50 percent. Is that a
25 fair summary of your bottom line?

1 A No, because I'm not comparing Table 1 and
2 Table 2 in the way that you are trying to get me to
3 compare them. I'm simply saying, here's Table 1,
4 here's how the Postal Service goes about measuring the
5 extent of the Internet problem, or electronic payments
6 problem. Here's how they assess it. It looks like
7 it's not a big problem. And when you look at the
8 payments market, as defined by the Fed, it's not my
9 definition, but it's the only ~~other~~ data that I was
10 able to come up with, and even there, just for two
11 years. But, those are an interesting two years,
12 because they -- you have a couple of rate increases
13 going on in those years; you get a different answer.

14 And in the context of all the other work
15 that we did, in connection with this testimony, I
16 think this is a truer estimate of the problem that the
17 Postal Service faces with bill payments mail. And
18 you're getting declining volumes. At the same time,
19 you're raising rates. And that is what I meant by the
20 death spiral. I don't think the Postal Service is in
21 danger of death, but you've got a death spiral in some
22 really important market segments that support the rest
23 of the first-class mail stream and where the high
24 institutional costs also support other parts of the
25 mail stream.

1 Q Could you turn, please, to your response to
2 our interrogatory 67?

3 A It takes me a while to search through these
4 300-400 questions, but I will eventually find it.

5 (Pause)

6 THE WITNESS: Okay, 67, right?

7 MR. KOETTING: Sixty-seven.

8 THE WITNESS: Okay.

9 BY MR. KOETTING:

10 Q In that response, you refer to Table 3 from
11 your testimony and discussions surrounding it as the
12 source of descriptive statistics for the payment
13 market, which indicate own price elasticities for the
14 payment market could be well over -1.0; correct?

15 A That quote is in your question.

16 Q Right. That's what we ask about and you
17 say, look at my Table 3 and the discussions
18 surrounding it. And Table 3 is on page 20 of your
19 testimony, correct?

20 A Around there.

21 Q What specific numbers are you referring to
22 as indicative of the own price elasticity for the
23 payments market, as you have defined it?

24 A You simply have to go through the following
25 logical reasoning. There are a bunch of cross

1 elasticities in that table that are -- whose absolute
2 values are well over one. And as Pearlton & Karloff
3 state in their textbook, one can infer from high cross
4 price elasticities high own price elasticities. Now.
5 I would like to have been able to do that experiment
6 directly where the dependent variable was Postal
7 volumes. But, I couldn't, because I don't have direct
8 prices for the competing substitute; i.e., Internet
9 electronic payments, et cetera, et cetera. But, what
10 I do have is quantity data, in terms of electronic
11 payments. So, I have enough variation to do, you
12 know, some calculations there and I have variations in
13 Postal prices. And that's the logic that I followed
14 through.

15 And you then go from that to recognizing
16 that you're likely to have symmetries in market
17 conditions. So, you can infer from these high price
18 elasticities a high own price elasticity in the
19 electronic payments market. And you can infer
20 symmetry of conditions, which means you likely have
21 high cross price elasticities in the Postal market for
22 that competing substitute. **And** from the high cross
23 price elasticities in the Postal market, you can infer
24 that the own price elasticity for single piece mail is
25 probably well above one.

1 You'll also note in my discussion that I
2 think this is the best way I'm able to measure with
3 available data, but I don't -- I wouldn't want to put
4 more weight on it than I have in my testimony. But,
5 that's hard drawing that conclusion. You're seeing
6 absolute elasticities above one.

7 Q These are ..

8 A You don't have -- may I just finish?
9 There's just one additional point. You don't have a
10 whole set of competing substitutes. You basically
11 have very few. And, therefore, the high price
12 elasticity, you can draw a reasonable inference that
13 you have a high own price elasticity.

14 Q Well, these are -- ~~the~~ numbers you're
15 pointing to are for individual competitors within the
16 payments market, correct?

17 A Well, let me turn to the tabla. These are -
18 - I don't know what you mean by 'individual
19 competitors.' I wouldn't characterize it as
20 individual competitors. These are simply products for
21 which we have volume data. That's how I would
22 characterize it.

23 Q Well, we're looking at 67 and 61 was a
24 follow-up to question 25; correct?

25 A That's what it states, yes.

1 Q And question 25, we were asking about the
2 quote in your testimony: 'in general, one expects
3 that the own price elasticity of demand curve for a
4 market is less elastic than the own price elasticity
5 faced by an individual competitor.' That's the
6 original -- that's where we started this whole line,
7 correct?

8 A Yes.

9 Q And what I was asking you about is your
10 statement that you're talking about the demand curve
11 for the whole market could well be above -1.0. And
12 I'm --

13 A No, not the whole market, just the payments.

14 Q Well, okay, for the entire payments market,
15 though.

16 A Based on the data that I have, that
17 approximates that, yes.

18 Q And the data that you have are for what, in
19 the language from your testimony, are data about the
20 individual competitors, rather than for the market as
21 a whole; correct?

22 A Well, no. As you look at all of these, as
23 you add them up, they, I think, are not identical to
24 the Fed definition, but they include credit cards,
25 they include debit cards of two varieties, credit

1 cards of two varieties. So, I think they somewhat
2 capture the market --

3 Q And you think that that ..

4 A -- as best we could.

5 Q And you think that the information in that
6 table is indicative that the elasticity for the
7 payments market as a whole could be well above -1.0?

8 A Yes, because the key cells -- the key cells
9 here to look at are the figures in the cross price
10 elasticities 2000-2003, 2001-2003, 2002-2003. And
11 what you see in there are a set of numbers that are
12 hugely above one. Now, cross price elasticities tend
13 to be positive. But, these numbers are consistently
14 hugely above one. **And** you made some valuable
15 contributions to refining this table in some of your
16 interrogatories and we provided you in an
17 interrogatory answer, you know, some corrected data,
18 in terms of making physical years consistent with
19 annual numbers. But when we did those runs, in
20 response to your interrogatory concerns, you know, you
21 came to the same general conclusion. And those high
22 cross price elasticities are indicative of high own
23 price elasticities within the payments market. And
24 through symmetry, you can begin to infer what's going
25 on, in terms of Postal prices and Postal cross price

1 elasticities.

2 Q What --

3 A Maybe, it would have been better to just
4 present those numbers, rather than all the other
5 numbers, because that's the key point from the table.

6 Q What did you mean **in** your testimony on page
7 **27**, which is, we address in our interrogatory 25,
8 where you were talking about, 'in general, one expects
9 that the **own** price elasticity of a demand curve for a
10 market is less elastic than the **own** price elasticity
11 faced by an individual competitor. The reverse
12 appears to be the case here.' Could you try to
13 explain somewhat more what you meant by the last
14 statement, 'the reverse appears to be the case here?'

15 A Yes. I'm going between the answer to
16 interrogatory **25** and trying to -- which page again was
17 it in my testimony?

18 Q It's page 27 in the testimony.

19 A Page 27 of the testimony, okay.

20 (Pause.)

21 THE WITNESS: Okay. **The** easiest way to
22 understand that statement is to look at the table
23 above. My impression is, notwithstanding my re-
24 estimation of the Witness Tress's elasticities, my
25 belief is that the way the Postal Service is competing

1 against these electronic forms of payments, if at all,
2 is just with non-price competition. It isn't really
3 trying to compete on price, whereas the general market
4 is faced by enormous price competition. And that's
5 why the Postal Service is losing **out** in the battle for
6 market share in this market. Electronic payment
7 systems have costs and prices coming down. And the
8 competition is not just non-price factors, it's very
9 much price competition. I think the best that the
10 Postal Service has been marshaling in this submarket.
11 you know, is maybe things like adhesive stamps and
12 other conveniences, non-price **forms** of competition. **as**
13 reflected in the elasticity. So, while you would
14 normally expect from principals of economics what I
15 say about market versus individual firm elasticities
16 here, that's what you would expect from Econ 101.

17 In this case, you find the opposite. The
18 elasticity of demand for the market, price elasticity
19 of demand is greater than it is for one of the
20 competitors in this market, the Postal Service,
21 because for whatever reason, for whatever
22 institutional reason, the Postal Service is really not
23 competing on price. It ought to be, but it's not.
24 So, it has an individual demand curve that is more --
25 that is different than what you would expect from

1 principals relative to the market demand curve.

2 BY MR. KOETTING:

3 Q Could we turn to your response to
4 interrogatory 54?

5 (Pause.)

6 THE WITNESS: I have it now.

7 BY MR. KOETTING:

8 Q And in subpart C, you say, 'people have to
9 pay most recurrent bills at the same volume, even if
10 they are cutting back on their overall level of
11 expenditure. For example, during a recession or
12 during a personal period of unemployment, a household
13 may have a much smaller credit card bill to pay each
14 month. However, they still have a bill to pay, which
15 can be paid on line or through the mail.' Doesn't
16 your response there suggest that if the price of
17 paying bills went up across the board, that is the
18 market price of bill payment went up, by the logic
19 that you are suggesting in your response to 54(c),
20 that people would still have to pay their bills and,
21 therefore, total bill payments would stay the same or
22 approximately the same; correct?

23 A The volume?

24 Q Yes, the volume.

25 A I believe that's what I said there.

1 Q So, wouldn't that suggest that the market
2 price elasticity for bill payments is not unitary, but
3 is, in fact, zero or near zero?

4 A That isn't the market. The market that we,
5 I think, settled on several minutes ago is the
6 payments market and those cross elasticities speak for
7 themselves in Table 3. So --

8 Q What's the alternative to paying the bill?

9 A You don't have to pay it through the mail.
10 That's --

11 Q Right. But, we're talking about the total
12 market for bill payments.

13 A Yes.

14 Q And what I'm trying to understand is how **you**
15 can say that the market elasticity is greater than -
16 1.0 and, at the same time, say that if the market
17 price goes up, volume is virtually unaffected.

18 A We're having a disconnect here. I mean,
19 despite recession, despite unemployment, you know,
20 people still have to pay their bills. If the nature
21 of this market is characterized by a lot of price
22 competition in the general market, but not price
23 competition by the Postal Service, they may still, in
24 these periods, switch from paying by Postal Service to
25 the competing alternatives.

1 Q But that doesn't affect the market
2 elasticity for bill payments, does it?

3 A When people switch from one mode of payment
4 to another, I think it impacts the demand curves.
5 But, my point is that you're facing a market
6 condition, in which the Postal Service does not
7 compete on price, but the market does. So --

8 Q I would like to look at page four of your
9 Appendix B.

10 A Is it a page or a table number?

11 Q Page four.

12 A Page four.

13 Q It's a page of text.

14 A Okay.

15 Q And there are no line numbers, but near the
16 bottom of the top paragraph, you say, 'consumers, who
17 bank on line, report convenience in saving time as the
18 top two -- of several reasons, but also report lower
19 costs (saves money) as among the top seven reasons;'
20 correct?

21 A Uh-huh.

22 Q And moving to the top of the next paragraph,
23 you say, 'such surveys confirm that Internet
24 technology competes on Postal services on both price
25 and non-price grounds;' correct?

1 A Uh-huh.

2 Q Now, in that last sentence, when you talk
3 about the price grounds, would it be correct that
4 you're referring in the previous paragraph to the
5 portion where they talk about lower cost saves money?
6 Is that the price grounds you were referring to?

7 A Yes.

8 Q And how does a consumer save money from on-
9 line banking?

10 A It's the most extreme aggressive form of
11 price competition that you could ever have. It's zero
12 and, obviously, subsidized, but it will have a price
13 attached to it **some** day.

14 Q What activities is it that they do at that
15 price of zero?

16 A What activities do they do? They pay bills
17 on line instead of sticking a postage stamp on an
18 envelope.

19 Q So, you're saying that the price is
20 effectively zero for paying bills on line; correct?

21 A Well, the cost isn't *zero*; but to attract
22 customers, I think most banks offer at a zero price
23 and it creates, I might add, a real problem in these
24 surveys, because when people think about alternatives,
25 you know, paying by postage or paying on line, if it's

1 offered for free, you don't think about price **as** a
2 factor. If you would correctly do that survey, price
3 would explode as being far more important than non-
4 price, in terms of why people do on line versus by
5 mail. I believe those would be the results.

6 Q Well, if the cost of using those on-line
7 services to consumers is effectively zero, then
8 consumers, who are currently still paying 39 cents to
9 pay their bills, must have some other reasons that
10 they find compelling why they haven't already switched
11 to that on-line bill service at zero cost; correct?

12 A You mean they may have non-price reasons?

13 Q They must have some reasons, correct? They
14 must be non-price reasons, yes.

15 A Yes. They must have some reasons, sure.

16 Q And aren't there likely to be very few
17 consumers, who would be motivated to switch from mail
18 to on-line services simply by a one cent shift in the
19 price of a single piece stamp, as you were proposing?

20 A I don't know, because if you're operating at
21 margins, you don't know in terms of behavior decision-
22 making what motivates people to switch. But, if you
23 get two rate increases in two years, it might motivate
24 people to switch. But --

25 Q why would a consumer, who already could use

1 on-line services at effectively zero marginal costs,
2 but who was passing up that opportunity, be motivated
3 to switch at a stamp rate of 42 cents, but not
4 motivated to switch at a stamp rate of 41 cents?

5 A I can't go into the minds of what consumers
6 would look like. A two cent reduction would be
7 better. A four cent reduction would be even better.

8 Q Well, let's go to question 79, please,
9 Postal Service interrogatory. In subpart C, we asked
10 you, 'did you attempt to estimate a demand equation
11 for first-class single piece letters relying only on
12 data since 1995?' And I am not sure that you answered
13 that question directly.

14 A Well, let me read your question again and
15 let me read my answer.

16 (Pause.)

17 THE WITNESS: Well, I believe I was
18 responsive to your question, Mr. Koetting. I referred
19 you to Table 8, which does show some point
20 elasticities in the time frame that you ask about in
21 that question.

22 BY MR. KOETTING:

23 Q Did you estimate any other demand equations
24 for first-class single piece letters relying on data
25 only since 1995?

1 A What we did was to use Witness Tress's, you
2 know, entire period 1983 to 1995. But, we broke that
3 out into periods, discrete periods, within which we
4 thought in the first period, there really is no
5 Internet competition -- it's not a material factor; a
6 transition period, where we believe Internet
7 technology was beginning to impact Postal; and then
8 the most recent period, probably post-1995 and even a
9 few data points after that. I know we had one data
10 point for 2005, one point estimate. But, we really
11 broke it down into three periods: a pre-Internet
12 period; a transitional period; and then the most
13 recent period, including, you know, broadband
14 deepening for consumers.

15 MR. KOETTING: Well, Dr. Clifton, let me cut
16 right to the chase here, although, Mr. Chairman, we
17 may have some issues, because what I would like to use
18 to refresh Dr. Clifton's recollection is a study that
19 was provided by **GCA** to counsel for the Alliance for
20 Non-Profit Mailers, which was then the subject of
21 protective -- motion for protected conditions. And
22 that status of this, at the moment, is not entirely
23 clear, because of the way it's been circulated.
24 However, I am hopeful that I can craft my questions in
25 such a way that Dr. Clifton can respond without

1 revealing any of the material that he has indicated he
2 believes would be prejudicial to him, if it was
3 disclosed. So, I'm going to proceed very cautiously
4 to avoid -- to attempt to avoid that.

5 BY MR. KOETTING:

6 Q But, specifically, do you recall any
7 analyses that were reported in this study, the
8 elasticity of first-class mail and the presence of
9 competing substitutes, dated March 31, 2006, that
10 focus on the 1994 -- the post-1995 period?

11 A Very vaguely. I haven't looked at that
12 March 31st study in months. We actually were going to
13 produce it as a library reference, but we decided that
14 it would be better to write testimony and simply
15 extract from that elasticity study what was most
16 appropriate for testimony. So the short answer is no.

17 MR. KOETTING: What I would like to do,
18 propose to do, Mr. Chairman, is to share with the
19 witness and his counsel the portions of this that I
20 would like to refer to and see if they can agree that
21 these don't include any of the cross elasticity
22 materials that Dr. Clifton had suggested he believed
23 would be prejudicial if disclosed, if that's an
24 acceptable procedure.

25 CHAIRMAN OMAS: You know, I think you can go

1 along, so long as your questions do not require an
2 answer from the protected material. You think you can
3 do that?

4 MR. KOETTING: I would like to introduce
5 into the record relevant portions of this study that I
6 believe don't fall within the scope of what Dr.
7 Clifton has argued would be prejudicial if disclosed
8 and are directly relevant to following up to this
9 interrogatory response, in terms of analyses he did in
10 the post-1995 period.

11 CHAIRMAN OMAS: So what are you saying?

12 MR. KOETTING: Well, I would like to show
13 the material to the witness and his counsel and see if
14 we can agree that this is material that is not --
15 doesn't contain any of the --

16 CHAIRMAN O M: You would like to take a
17 break to consult with counsel or --

18 MR. KOETTING: I'm not sure. It's all on
19 one page. So, if we want to take a couple of minutes
20 or I can just -- I think we can do it --

21 CHAIRMAN Oms: Why don't we just go off the
22 record while you do that for a second.

23 (Whereupon, a brief recess was taken.)

24 BY MR. KOETTING:

25 Q Dr. Clifton, would you agree that in the

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1 March 31st elasticity study that I referred to earlier,
2 you did a series of investigations and one of those
3 included a Granger positive analysis and you've looked
4 at three different periods, the period 19970 to 2005,
5 period 1983 through 1994, and the period 1995 to 2005?

6 (Interference)

7 Q I would like to read the conclusion that you
8 drew with respect to the 1995 to 2005 analysis, which
9 appears in the bottom paragraph on page 28 of that
10 report. And that reads, 'in the period most strongly
11 associated with intensifying competition for first-
12 class mail products 1995 to 2005, a remarkable result
13 is that unlike normal demand function relationships
14 observed in the other two periods between price and
15 volume, price ceases to be a Granger causative
16 variable in the volume demand equation and only
17 Internet services remain Grange?:causative. This is
18 just the reverse finding over that for the entire
19 sample period 1970 to 2005, where only price was
20 Granger causative and Internet expenditures was not.
21 These tests of Granger causality are perhaps the most
22 powerful econometric expression possible that non-
23 price competition form effective substitutes for
24 Postal services in first-class mail have 'taken over'
25 from Postal prices in explaining most of the volume

1 variations in first-class mail.' Is that the
2 conclusion you drew from the analysis as presented on
3 page 28 of your March 31st study?

4 A That is the conclusion I drew and one of the
5 reasons we hired Professor Collegian, a noted national
6 -- internationally noted econometrician, was to go
7 over that draft, in terms of what was good and bad
8 about it. And he told me, you cannot do Granger
9 causality in this arena. Granger causality has to do
10 with finance, not demand elasticities. And as a
11 result of the recommendation, we threw it out. It
12 does not appear in the testimony, because it was
13 turned out to be a wrong headed approach in the eyes
14 of Dr. Collegian.

15 Q I will need my copy of page 27 back. But
16 other than that, I think we're done with that. But,
17 I'll get that at the end. I would like to turn to
18 your response to our question 56, and specifically
19 page four of that response is where I would like to
20 start.

21 A Okay.

22 Q And at the top of that page, you make
23 several observations based on a comparison of results
24 you obtained after making some adjustments to the
25 model estimated by Witness Tress, opposed to the

1 results Mr. Tress, himself, obtained; correct?

2 A Yes, but these are within the Tress model,
3 understood, not within our model.

4 Q Right.

5 A Okay.

6 Q And those observations appear in the four
7 numbered paragraphs, I through iv; correct?

8 A Uh-huh.

9 Q Okay. So, we will be getting back to those;
10 but for now, I would like to go to page two of that
11 response. Now, on page two, I am interested in the
12 second equation, where you have attempted to
13 reformulate a correct Box **Cox** specification. **And** so,
14 that's the equation right below the line, 'let's
15 reformulate this specification and regroup relevant
16 terms.' Do you understand the equation in which I am
17 referring?

18 A Yes.

19 Q And within that equation, there are three
20 sets of brackets separated by two plus signs; correct?

21 A Uh-huh.

22 Q Within the second set of brackets, would you
23 agree that the coefficient on the interact on between
24 T1 and ISP to the power of lambda is equal to β_1 over
25 lambda?

1 A I would -- I would need to derive it.

2 Q Well, I mean, I suppose if you want to call
3 that what I'm asking you to do, then that's what I'm
4 asking you to do.

5 A Mr. Koetting, this question -- the question,
6 alone, was six pages long, consisting of numerous
7 equations and extremely detailed excruciating efforts
8 to show that Witness Tress's **Box** Cox transformation or
9 his reformulated transformation, you know, somehow
10 were correct. We don't agree with that for the
11 reasons put in here. He excludes two very significant
12 time trend variables in his 2006 formulation. Dr.
13 Collegian has replied that for different reasons
14 Witness Tress's Box **Cox** transformation, which is how -
15 - for the benefit of the Commission, which is how
16 Witness Tress models the impact of competing
17 substitutes, electronic payments systems, Internet
18 competition, and so forth -- we went to extraordinary
19 length to answer these things. **And** I think if we're
20 going to get involved in further answers here, we
21 would be delighted to respond to you, but we would
22 respectfully request that we respond to your questions
23 in writing. This is extremely technically difficult
24 stuff.

25 Q All I'm asking you to do now is to look at

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1 that equation and tell me what the coefficient is on
2 the interaction of two terms. It's your equation. I
3 don't see what is so difficult **about** that. I don't
4 see why we can't move forward with oral cross-
5 examination on your written answer.

6 A Witness Tress, I have a firm and there are
7 various specialties in my firm. And these answers are
8 constructed under my supervision, but not -- they
9 don't always involve me directly. And the answer to
10 this question 56 was prepared under my supervision.
11 It was not prepared by me directly. I am the witness.
12 I would be delighted to give you an answer. But, I
13 would respectfully request that the staff, who worked
14 on this, be allowed to answer it. And we would be
15 happy to answer as many questions as you have.

16 MR. KOETTING: Mr. Chairman, I would --

17 CHAIRMAN **OMAS**: Mr. Koetting, you know,
18 complicated calculations are not part of themselves,
19 to oral cross-examination. Please move on.

20 MR. KOETTING: Mr. Chairman, then let me
21 just simply note for the record that we offered to
22 allow this witness to explain some relationships that
23 are revealed through looking at his answer and he is
24 apparently unwilling to be cross-examined on those
25 orally. **And** if that's the case, that certainly is his

1 choice. But, we certainly tried to give him the
2 opportunity to respond to points that can be made
3 about these analyses.

4 THE WITNESS: Well, Mr. Chairman, that's his
5 reply.

6 CHAIRMAN OMAS: Well --

7 THE WITNESS: We have offered to answer
8 them.

9 CHAIRMAN OMAS: Please, **just** a minute. The
10 witness has said that he would provide those answers
11 to you in writing. Why can't you accept those answers
12 in writing?

13 MR. KOETTING: Because the witness is here
14 today to be orally cross-examination and I don't know
15 how I could orally ~~cross-examine~~ him on written
16 answers that come later. And he's not even willing to
17 attempt to approach the analysis

18 CHAIRMAN OMAS: Well, I think you should
19 try, to the best of your ability, to answer the
20 questions that Mr. Koetting has posed to you right
21 now. Can we go on? I don't want to see a log head
22 here, where we can't move on. I mean, this is
23 ridiculous. And you did present it as part of your
24 testimony. You did respond in an interrogatory. SO,
25 therefore, you should be prepared to answer the

1 questions under oral cross-examination.

2 MR. HORWOOD: Mr. Chairman, if I might
3 suggest that if the witness does -- is not able to
4 answer orally and needs to answer in writing, he can
5 always be recalled for further oral cross-examination,
6 if it were to get to that point.

7 MR. KOETTING: The problem I have with that,
8 Mr. Chairman, is, is that we have rebuttal testimony
9 due in a very short period of time. Dr. Clifton's
10 responses have been consistently filed late in this
11 proceeding. This entire topic of the Box Cox
12 transformation was delayed by virtue of the GCA's
13 choice to attempt to present the declaration of Dr.
14 Collegian, as an exhibit to this witness's testimony,
15 rather than separate testimony on September 6th that we
16 could have got to the bottom of immediately. Again, I
17 mean, I'm willing to move forward, if the witness is
18 having difficulty answering the questions and would
19 prefer not to respond. Then, I will be content to
20 leave the record where it stands and we can proceed
21 through rebuttal testimony.

22 THE WITNESS: You have another day of oral
23 cross here, November 9th. I would be happy to sit down
24 with my staff and answer questions you have on this
25 six-page length question and present them again

1 orally, under oath, on November 9th or whatever the
2 last day is of this week. But, what I am saying is
3 just a practical matter. Yes, these are my answers,
4 Mr. Chairman, but they are prepared by my firm, under
5 my supervision, by other staff. And this is an
6 extraordinarily complex line of investigation. And
7 rather than make errors in my own answers, I would
8 prefer to consult with staff and answer in an
9 expeditious manner, either orally or written or both.
10 **And** it shouldn't take over 24 hours.

11 CHAIRMAN OMAS: Mr. Koetting, you could have
12 submitted in advance of oral cross-examinations of
13 these questions, these technical questions. And as
14 the witness said, we can recall him, if that's what
15 you want. And he said he can respond to us in 24
16 hours. So, that means we can bring him back.

17 MR. KOETTING: Mr. Chairman, we'll just
18 leave the record, the state of the record where it is
19 right now and move forward with our own rebuttal case.
20 Thank you, Dr. Clifton. We have no further questions.

21 THE WITNESS: Thank you.

22 CHAIRMAN OMAS: Is there any follow-up
23 cross-examination for Witness Clifton? Mr. Ackerly?

24 MR. ACKERLY: Mr. Chairman, I do have just a
25 couple of questions that are based on the witness's

1 responses to cross-examination earlier today.

2 CHAIRMAN OMAS: would you identify yourself,
3 please?

4 MR. ACKERLY: My name is Todd Ackerly. I'm
5 counsel for Direct Market Association.

6 **CROSS-EXAMINATION**

7 BY MR. ACKERLY:

8 Q Do you recall in your response to a question
9 by Mr. Levy earlier today that you used the phrase
10 'kill the goose that laid the golden egg?'

11 A Uh-huh.

12 Q And if I remember correctly, you used it in
13 reference, in a way that you were asking the
14 Commission to price first-class single piece mail in a
15 way that would increase the volume of that mail. Is
16 that not a correct interpretation of what you were
17 saying at that point?

18 A Asking him at a price of first-class single
19 piece mail and do other things, which are in the
20 conclusion, to try to recover the markets for this,
21 yes.

22 Q Dr. Clifton, I don't know if you know this,
23 but it is a matter of public record that I, myself,
24 have used the phrase to the Commission, 'please don't
25 kill the goose that laid the golden egg,' in past

1 proceedings, only I was doing it in reference to
2 standard mail. And the reason that I used that phrase
3 was that I was asking the Commission to moderate the
4 price increases that were being proposed for standard
5 mail on the basis of testimony that showed a direct
6 causal connection between price increases and the
7 volume of standard mail, because of the testimony that
8 had been put in those cases with respect to the way in
9 which standard mailers go through their calculations,
10 calculate the cost for response and how they make
11 their decisions with respect to pricing mail and make
12 their decisions with respect to the volume of mail
13 that they put into the mail stream. In any event,
14 that's background for the question that I'm going to
15 ask you, because it did ring a certain bell with me,
16 when you used that phrase.

17 You're familiar with the term, I assume,
18 'multi cularity?'

19 A Uh-huh.

20 Q Could you describe for the record what that
21 term means to you?

22 A Just a cularity between different
23 variables.

24 Q So the variables could be moving in similar
25 directions, but there might not be a causal connection

1 between the two; is that correct?

2 A That's possible.

3 Q Okay. With respect to the own price
4 elasticity of single piece first-class mail today and
5 the large amount of testimony that there has been with
6 respect to the declining volume of first-class single
7 piece mail and the increases in prices of first-class
8 single piece mail, is it possible, in your view, that
9 that is a function not of a causal connection that's
10 related to payments by electronic media, but that, in
11 fact, is a phenomenon that one would describe as multi
12 colinearity?

13 A To the degree we have investigated the
14 issue, which the issue being a correct estimate of own
15 price elasticities, we believe the dynamics in those
16 are what is causing the phenomenon, not other
17 variables. I'm not going to say that non-price
18 competition within these other medium that you
19 mentioned are not important. But the tenancy is,
20 within these circles, as Mr. Koetting's effort to talk
21 about the Granger thing, that, gosh, it's just non-
22 price competition that's leading to these volume
23 declines. And the single most important outcome of
24 the study is to suggest that's not true. Postal
25 prices do matter, not just these non-price attributes.

1 And that's our conclusion and that's the basis of our
2 rate recommendation.

3 Q So the proposition that you're making, from
4 a commonsense point of view, is take any old
5 individual, take somebody like myself, and I need to
6 make a decision as to whether or not to pay my bills
7 by writing checks and putting them in the mail or to
8 go on line and set myself up and to pay on line. That
9 is the decision that I need to make, in order to have
10 an impact, one way or another, on Postal volume?

11 A Not just on line. I suppose you can pay
12 them over the telephone.

13 Q Some other way, some other way, but not
14 using the mail. And your proposition is that if the
15 price of a stamp were to change from 42 to 42 or 42 to
16 40, that that is going to make a significant
17 difference in the decision that I make with respect to
18 whether or not I use checks or some other payment
19 medium? That's the fundamental core of what you're
20 saying, isn't it?

21 A Well, you're personalizing it down to the
22 individual. I'm constrained in what I recommend to
23 this Commission by (a) what the Postal Service
24 proposes its rate. **And** as a practical matter, the
25 larger the price cut you could make for -- in a single

1 piece make, the more impact you would have. But, you
2 need to begin to start -- and the Commission need and
3 the Postal Service needs to begin starting somewhere
4 to reverse these price increases, if it wants to
5 effectively compete against these alternative payment
6 forms that you make. But, I can't tell you today how
7 much of an impact a one or two cent rate decrease
8 relative to what is proposed. I haven't made an
9 estimate of what kind of impact it would have on
10 consumers, other than what I've shown in elasticities.
11 But. what I have shown in elasticities is that in the
12 payments market, the statistics we've done suggests it
13 may, in fact, be absolutely price elastic.

14 Q And so your proposition is that the
15 Commission --

16 A My statistics more than my proposition, Mr.
17 Ackerly.

18 Q Proposition based upon your statistics and
19 your testimony and your judgment and everything else
20 you bring to the table is that the Commission should
21 help the Postal Service compete aggressively on **price**
22 to retain the payments mail stream that it is in the
23 process of losing? That's basically it, isn't it?

24 A Well, I mean, there are additional
25 submarkets, as well, transactions mail, in general.

1 Q So the answer is yes?

2 A The answer is yes.

3 MR. ACKERLY: That's all I have, Mr.
4 Chairman.

5 CHAIRMAN OMAS: Thank you, Mr. Ackerly. Is
6 there anyone else, who wishes to cross-examination
7 Witness Clifton?

8 MR. KOETTING: Mr. Chairman?

9 CHAIRMAN OMAS: Yes.

10 MR. KOETTING: If I could just follow-up on
11 that?

12 CHAIRMAN OMAS: Certainly.

13 **CROSS-EXAMINATION**

14 BY MR. KOETTING:

15 Q When you talk about the Granger causal
16 analysis, that wasn't anything I suggested, other than
17 simply by quoting to you a report that was prepared
18 under your supervision; correct? That wasn't the
19 Postal Service analysis, was it?

20 A That's correct. And I didn't mean to
21 suggest that you had a view. I am just saying that it
22 is pretty common knowledge within the institution of
23 Postal rate making and Postal management viewpoints
24 that the whole ball game is non-price competition.
25 And what I'm strongly suggesting is that it ought to

1 be, should be, and, in fact, is price competition.
2 Whether the Postal Service and the Commission want to
3 get in the ball game and compete, that's up to the
4 Commission and up to the Postal Service. But, if you
5 don't, you run the risk, I believe, of seeing another
6 round of strong declines in volume in single piece
7 mail. That was my point and I don't think that's good
8 for anybody. I don't think that's good for standard
9 mailers. I don't think it's good for first-class, you
10 know, work sharing mailers.

11 In response to Mr. Ackerly, when I talk
12 about the goose that laid the golden egg, I was
13 referring to high unit cost contribution price, **just**
14 so that you know what I'm referring to. And those are
15 in first class and we don't want to **lose** those.

16 Q But just to the record is clear, the Granger
17 causal analysis was your analysis, correct, not the
18 Postal Service's?

19 A It was. But the conclusions that it points
20 to, that it's all --

21 Q That's --

22 A -- non-price competition --

23 Q You've answered my question.

24 A Okay.

25 MR. KOETTING: Thank you. If counsel wants

1 to go further, that's fine, but you've answered by
2 question.

3 CHAIRMAN OMAS: Is there anyone else, who
4 wishes to cross-examine Witness Clifton?

5 (No response.)

6 CHAIRMAN OMAS: Mr. Horwood, would you like
7 some time with your witness?

8 MR. HORWOOD: Yes, just a few minutes.

9 CHAIRMAN OMAS: All right. Why don't we say
10 five minutes.

11 MR. HORWOOD: That will be fine.

12 (Whereupon, a brief recess was taken.)

13 MR. HORWOOD: **Yes**, Mr. Chairman, we have no
14 redirect of Dr. Clifton.

15 CHAIRMAN OMAS: Thank you. very much. Mr.
16 Clifton, that concludes your testimony here today. We
17 appreciate your appearance and we thank you. You are
18 now excused.

19 (Witness excused.)

20 CHAIRMAN OMAS: This concludes today's
21 hearings. We will reconvene tomorrow morning at **9:30**,
22 when we will receive testimony from witnesses Bach,
23 Cohen, Click, White, and Cabner. Thank you and have a
24 good evening.

25 //

1 (Whereupon, at 4:29 p.m., the hearing was
2 recessed, to reconvene at 9:30 a.m., Tuesday, November
3 7, 2006.)

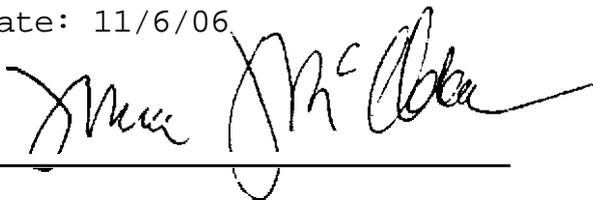
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REPORTER'S CERTIFICATE

DOCKET NO.: R2006-1
CASE TITLE: Postal Rate and Fee Changes
HEARING DATE: November 6, 2006
LOCATION: Washington, D.C.

I hereby certify that the proceedings and evidence are contained fully and accurately on the tapes and notes reported by me at the hearing in the above case before the United States Postal Service Commission.

Date: 11/6/06



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