

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

POSTAL RATE AND FEE CHANGES

Docket No. R2006-1

REVISED REPLY OF THE UNITED STATES POSTAL SERVICE
TO THE INITIAL COMMENTS OF THE PARTIES
ON RESUBMISSION [ERRATA]

The United States Postal Service hereby submits this reply to the comments of two parties filed on April 12, 2007, regarding resubmission of issues to the Postal Regulatory Commission in Docket No. R2006-1: the Initial Comments of the Greeting Card Association on Resubmission; and the Comments of Pitney-Bowes, Inc., in Response to the Notice of Request for Reconsideration.

Reply to GCA Regarding First-Class Mail Nonmachinable Surcharge

In its Initial Comments, GCA takes issue with the Postal Service's March 28, 2007, Initial Statement On Reconsideration, as it relates to the First-Class Mail nonmachinable surcharge recommended by the Postal Regulatory Commission in its Docket No. R2006-1 Opinion and Recommended Decision. At pages 2-4 of its Initial Comments, GCA asserts that history supports the Commission's Docket No. R2006-1 recommendation to continue to restrict the application of the First-Class Mail nonmachinable surcharge to one-ounce letters only. GCA's contention, however, overlooks the consequences of a shift to the newly recommended shape-based First-Class Mail rate design.

Historically, in order to compensate for the nonmachinability of First-Class Mail pieces weighing one ounce or less, a specific surcharge in addition to the basic initial-ounce rate has been assessed. For First-Class Mail pieces weighing more than one ounce, the additional-ounce rate was designed to compensate for the additional costs associated with additional weight, shape differences, as well as any nonmachinability of heavier weight pieces (whether letters, flats or parcels). Thus, the cost impact of nonmachinability was accounted for, either as a separate surcharge on one-ounce pieces, or as one part of the justification for substantial additional-ounce rates imposed on heavier pieces.

When the first surcharge of seven cents was implemented in July 1979, as a result of Docket No. R78-1, the initial-ounce First-Class Mail rate was 15 cents. At the same time, the additional-ounce rate was 13 cents, nearly 87 percent of the initial-ounce rate. The table below shows the initial-ounce and additional-ounce rates in effect since then.

	First- Ounce Rate (cents)	Additional Oz. Rate (cents)	Additional Oz. Rate as a % of 1st
July 15, 1979	15	13	86.7%
March 22, 1981	18	17	94.4%
November 1, 1981	20	17	85.0%
October 9, 1983	20	17	85.0%
February 17, 1985	22	17	77.3%
April 3, 1988	25	20	80.0%
February 3, 1991	29	23	79.3%
September 20, 1992	29	23	79.3%
January 1, 1995	32	23	71.9%
July 1, 1996	32	23	71.9%
January 10, 1999	33	22	66.7%
January 7, 2001	34	21	61.8%
July 1, 2001	34	23	67.6%

June 30, 2002	37	23	62.2%
January 8, 2006	39	24	61.5%
R2006-1	42	20	47.6%
Requested			
R2006-1	41	17	41.5%
Recommended			

In Docket No. R2006-1, the Postal Service's request and the Commission's recommended decision, for the first time, took into account shape-based cost differences and developed separate initial-ounce rates for First-Class Mail letters, flats and parcels. The rate design requested by the Postal Service sought recovery of the additional costs long-associated with nonmachinability of letters in two forms. First, in lieu of having to add a specific nonmachinable surcharge to the basic rate for one-ounce nonmachinable letters, the Postal Service proposed that such letters be charged the rate for one-ounce flats. Second, the request acknowledged that charging separate rates for flats reduced the need for the additional-ounce rate to act as a proxy for the cost effects of nonmachinability, shape, etc. It did not attempt to quantify the reduction, but did reduce the additional-ounce rate.

Since the additional-ounce rate historically has served as a proxy for the combined impact of shape, weight, and nonmachinability for multi-ounce pieces, it was to be expected that a request for shape-based initial-ounce rates would be accompanied by a request for reductions in existing additional-ounce rates. As recommended by the Commission, the new Docket No. R2006-1 rate structure results in a reduction of the current Docket No. R2005-1 additional-ounce rate -- 24 cents -- by almost 30 percent -- to 17 cents.

As GCA acknowledges at page 5 of its Initial Comments, “[h]istorically, the absence of a nonmachinable surcharge in the higher weight increments has been compensated for by the extra-ounce charge.” However, it also is important to observe that the First-Class Mail rate structure has historically reflected higher rates for nonmachinable two-ounce letters than for nonmachinable one-ounce letters. Accordingly, the current Docket No. R2005-1 rate design reflects the following:

<u>1-oz nonmachinable letter</u>	<u>2-oz nonmachinable letter</u>
52¢ (39¢ + 13¢ surcharge)	63¢ (39¢ cents + 24-¢ add. oz. rate)

As requested by the Postal Service in Docket No. R2006-1, the Commission recommended initial-ounce rates that reflect cost differences for First-Class Mail pieces based on shape (letter, flat, parcel).¹ The First-Class Mail letter rate design recommended in Docket No. R2006-1 continues to recognize the costs associated with additional weight through (albeit, significantly reduced) additional-ounce rates, but it calls into question whether, to borrow GCA’s

¹ However, the Commission recommended retention of a distinct surcharge for nonmachinable one-ounce First-Class Mail letters, as opposed to imposing the initial-ounce flat rate on such letters, as requested by the Postal Service. The Postal Service is not seeking review of the Commission’s recommendation to continue the practice of imposing higher rates for nonmachinable one-ounce letters through a specific surcharge, or the amount of the recommended surcharge. At page four of its Initial Comments, GCA characterizes the Postal Service’s Docket No. R2006-1 proposal to charge nonmachinable one-ounce letters the rate for one-ounce flats as a failure to recognize “the well-founded distinction between shape and (non) machinability.” The Postal Service is fully cognizant of the operational reality that, within each shape category (letters, flats and parcels), there are machinable and nonmachinable pieces, with different cost characteristics. Contrary to the GCA’s assertions, the Postal Service proposal to eliminate the distinct surcharge for one-ounce nonmachinable letters merely sought to simplify the overall rate schedule by suggesting that such letters be charged the next higher initial-ounce rate applicable to flats.

characterization, “the absence of a nonmachinable surcharge in the higher weight increments is compensated for by the extra-ounce charge.”

As a result of the Commission’s Docket No. R2006-1 opinion, the long-standing rate differential between nonmachinable one-ounce and two-ounce letters has been recommended for elimination as indicated below, without explanation:

<u>Docket No. R2006-1 Recommended</u>	
<u>1-oz nonmachinable letter</u>	<u>2-oz letter nonmachinable letter</u>
58¢ (41¢ + 17¢ surcharge)	58¢ (41¢ cents + 17¢ add. oz. rate)

In justifying a continuation of the long-standing nonmachinable surcharge rate design approach, the Commission’s opinion recognizes the importance of the distinction between machinability and shape. See PRC Op. R2006-1 at 162, ¶5210. In the absence of any justification for elimination of the rate differential depicted above on page 4, the Postal Service considers that the rate schedule should continue to reflect for these two categories, as it has for decades, a differential that explicitly recognizes the separate impact of both additional weight and nonmachinability. As indicated by the example above, the importance of this distinction is not reflected in the recommended rate schedule.

At page 5 of its Initial Comments, GCA asserts that, earlier in Docket No. R2006-1, no parties addressed the issue of whether the nonmachinable surcharge “should be redesigned to apply at higher weights.” However, it should be observed that the Postal Service’s additional-ounce proposal in Docket No. R2006-1, after accounting for the impact of the proposed recognition of shape in the overall rate design, continued the long-standing practice of accounting for

nonmachinability of additional-ounce pieces through a proposed additional-ounce rate. The requested 20-cent additional-ounce rate reflected a very substantial proportion of the proposed 42-cent initial-ounce rate and, as reflected above, preserved the long-standing rate differential between one-ounce nonmachinable letters and two-ounce nonmachinable letters.² The even greater reductions in the additional-ounce rates recommended by the Commission, without explanation, eliminate altogether any rate differential between one-ounce nonmachinable letters and two-ounce nonmachinable letters.

At page 7 of its Initial Comments, GCA highlights the simplicity of the having the same 17-cent rate being applicable to cover postage for either an additional ounce or for a nonmachinable surcharge. However, GCA fails to justify why the rate for nonmachinable two-ounce letters (whether as part of the additional-ounce rate as before, or through a separate surcharge) should reflect an assessment for the additional weight but none for nonmachinability, or *vice versa*.

GCA characterizes the testimony of witness Andrea Sue Liss (GCA-T-4, at 13-14; Tr. 28/99490) as the “only testimony of record on the volume effect of the nonmachinable surcharge.” However, her testimony bears no resemblance to reliable quantitative or demand analysis which would have justified the Commission giving it any weight during its initial Docket No. R2006-1 deliberations. See, PRC Op. R2006-1 at 162, ¶5208. No issue raised on

² It also should be observed that the Postal Service requested a 62-cent rate for nonmachinable one-ounce letters, meaning that nonmachinable two-ounce letters would be assessed a total of 82 cents in postage, when additional-ounce postage was added.

reconsideration provides a basis for enhancing the value of that testimony at this stage of the proceeding.

Further at page 6 of its Initial Comments, GCA asserts that the Postal Service's proposal that the Commission consider preserving a rate differential between nonmachinable one-ounce and two-ounce letters "entails the risk of losing high-contribution First-Class [Mail] volume."³ However, if, as recommended by the Commission, the additional ounce-rate that currently covers the cost of additional weight and nonmachinability no longer is designed to cover the latter, the foundation for characterizing nonmachinable, manually-processed mail as "high contribution" seems much less firm.

At page 163, ¶5212 of its Docket No. R2006-1 opinion, the Commission appears to offer its recommended rate design as an explicitly imperfect transitional measure, which could be cured when mail processing operations are considered in the context of some future examination of the rate schedule. The Postal Service believes that the long-standing separate recognition the impact of nonmachinability and additional weight should be preserved in the interim. Accordingly, the Postal Service urges the Commission to reconsider its recommended decision and design rates that recognize both the impact of additional ounces and nonmachinability for First-Class Mail letters weighing more than one ounce.

³ It should first be observed that, even if First-Class Mail, as a whole, can be regarded as "high contribution" mail, that honor is not necessarily earned by each First-Class Mail rate category, especially nonmachinable letters with cost-generating characteristics that are not recognized in the rates those pieces pay.

Reply to Pitney Bowes Regarding Priority Mail Flat-Rate Box

Only one party, Pitney-Bowes, Inc., has commented on the Priority Flat-Rate Box, noting that the Commission's partial use of Postal Service volume variable estimates "appears to be [an] error," and stating that "we have every confidence that the Commission will recommend a revised rate." Comments of Pitney-Bowes, Inc., in Response to the Notice of Request for Reconsideration at 4.

No party has questioned the Governor's conclusion that there was an error, nor has any party argued that the recommended price for the Priority Mail Flat-Rate Box should remain at \$9.15. For the reasons stated in its initial comments, the Postal Service believes that the recommended rate, when calculated using the Commission's cost estimates with the Postal Service's pricing model, should be \$8.95.

Respectfully submitted,

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April 24, 2007

CERTIFICATE OF SERVICE

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

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