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

POSTAL RATE AND FEE CHANGES, 1997	)	Docket No. R97-1

DIRECT TESTIMONY
OF
KENNETH L. BRADSTREET
ON BEHALF OF
ASSOCIATION OF ALTERNATE POSTAL SYSTEMS

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I. INTRODUCTION

My name is Kenneth L. Bradstreet. I am the Vice President and General Manager of Advertisers Postal Service (APS) in Gaylord, Michigan. APS is a private enterprise delivery system in rural northern Michigan. In addition to private delivery, APS also operates a mailing service which does mail preparation for various shopping guides, newspapers, and retailers in the area.

I joined APS in April of 1977 as Assistant District Manager. I worked at that position until September 1977, at which time I was asked to coordinate special projects for APS. In September of 1978 I was promoted to Assistant General Manager. I became General Manager in 1982 and Vice President in 1985.

In August of 1983, APS joined the Association of Private Postal Systems (APPS), which is a trade association made up of private delivery companies similar to APS. In February 1984, I was appointed to the Postal Affairs Committee of APPS.

Also, in early 1984 I helped to establish the Coalition of Non-Postal Media (CNPM), and I served as its Vice-Chairman. In that capacity I submitted testimony to the Postal Rate

Commission in Dockets R84-1 and R87-1. CNPM was a common interest group of publishers, alternate delivery companies, and other media that compete with the USPS.

In February 1987, I was elected to the Board of Directors of APPS. In February 1989, I was elected President of APPS, and I served two terms as President of APPS. In February 1990, the name, Association of Private Postal Systems, was changed to the Association of Alternate Postal Systems (AAPS). AAPS participated in R90-1 as a limited participant. In R90-1 I submitted testimony on behalf of AAPS. AAPS again participated in the MC95-1 classification case, and I submitted testimony in that case.

In addition to personal participation in three rate cases and a classification case, I have also represented the alternate delivery industry on various panels at a number of conferences and forums. I participated as a speaker at the Cato Institute forum on postal privatization in April 1988. In March 1990, the morning following the filing of R90-1, I appeared opposite Postmaster General Anthony Frank on a morning news show produced by WWOR in the New York City market, and broadcast to cable systems throughout the United States. The segment was a discussion of the 1990 postal rate proposal.

On June 1, 1995 I assumed the duties of Executive Director of AAPS, a position which carries with it the responsibility for representing the interests of the alternate delivery industry. It is in that capacity that I offer testimony in this proceeding.

My 20 years of experience as a competitor of the Postal Service, as a mailer, and more recently as president and representative of a trade association of private delivery companies, has given me a great deal of exposure to postal issues, particularly as they affect private delivery companies throughout the country. Given that one of the criteria for the establishment of postal rates is the consideration of the effect of rates on, among others, "enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters," I consider it essential that competitors of the U.S. Postal Service participate in the ratemaking process.

Our industry learned in 1981 that we could not afford to sit back and assume that the Postal Service will deal fairly with us. As a result of the 1981 rate decision, the third class rates with which we compete were reduced precipitously, putting many of our number out of business. Since that time, the well-being of the alternate delivery industry has been tied more to postal rates than to any other factor.

II. PURPOSE AND SUMMARY OF TESTIMONY

My testimony is not technical. It is written almost exclusively by me -- not by a group of consultants and attorneys -- from the perspective of certain competitors of the USPS, many of them very small businesses. My testimony is written to remind the United States Postal Service, and the Commission, of the basic mission of the USPS as defined by Congress. It is written to remind the USPS, and the Commission, that the rate-setting criteria established by Congress include the consideration of competition and competitors, something that, in my experience, the USPS has not been doing appropriately.

It is clear to me as a layperson, from a reading of the Postal Reorganization Act, that the USPS was intended by Congress to be a public service, not an aggressive competitor. It is also clear from observing the USPS over the past eighteen years that in many regards it considers itself more a competitor than a public service.

My testimony will encourage the Commission to view the USPS as Congress viewed it - as a public service. It will encourage the Commission to shape rates for monopoly mail and for competitive mail accordingly, following carefully the criteria of the Postal Reorganization Act.

And it will encourage the Commission to follow not only the letter of the Act, but to catch the spirit of the Act as well, and to shape postal rates accordingly.

More specifically, I will first address the importance of the Postal Service monopoly. Next, I will address the great pride the Postmaster General has taken in driving a "competitor" out of business, and then turn to a discussion of the Postal Reorganization Act and its ratemaking criteria. I will next discuss the proposal in this case, including "Ramsey Pricing," the over-reliance upon cost coverage, the inadequate weight/cost study, the anticompetitive and unsupportable proposal to lower the ECR pound rate, the failure to attribute all attributable costs, the failure to recognize cost differences between letters and non-letters and between loose and bound pieces, and the proposed shape surcharge as an inappropriate justification for the pound rate reduction. I conclude with an appeal to the Commission to again reject an anticompetitive, unjustifiable rate proposal.

III. THE ASSOCIATION OF ALTERNATE POSTAL SYSTEMS

The Association of Alternate Postal Systems is a trade association of approximately 100 private, door-to-door delivery companies located in 30 states. Many of these member companies are solely private postal systems; that is, they are independently owned and are not an affiliate of any particular publication. A number of member companies are owned, and are an operating division of, a weekly or daily newspaper. Still others are owned and operated by publishers of shopping guides or "penny-savers."

By far the majority of items delivered by AAPS members would qualify as saturation or near saturation Standard A flats. Therefore, AAPS members, all of whom compete with the USPS for the delivery of Standard ECR saturation or high density advertising, are vitally concerned with any USPS proposal that affects Standard ECR rates.

AAPS members are mainly engaged in the delivery of weekly TMC shopping guides, saturation shopping guides and accompanying preprinted inserts. In addition, most AAPS members distribute community and telephone directories and product samples. The USPS proposal would significantly harm these businesses, especially in competing for those items weighing 4 ounces and above. Some AAPS members also distribute second-class magazines and periodicals to specific addresses.

IV. THE UNIQUE NATURE OF THE POSTAL SERVICE'S MONOPOLY POSITION

When it comes to operating a business in the private sector, there are, or at least should be, few restrictions on the operating environment. Businesses should be free to set their own rates. They should be free to enter or withdraw from new markets, new products, new services. As long as a business operates within the framework of the law and does not operate in an anticompetitive manner, a business is, or at least ought to be, free to compete unrestricted in the open marketplace of goods and services.

While this is true of private business operating in a free market economy, the same cannot be said of legal or natural monopolies. This freedom to operate unencumbered carries with it the presumption that the business in question enjoys no special advantages such as a legal monopoly, or special treatment with respect to governmentally granted advantages. On the other hand, utilities that provide an essential service and that have a monopoly on that service are not, and should not be, allowed to set rates independently or to compete unrestrained in other areas of the open market. The opportunities for abuse are too great, and therefore utilities are, and have historically been, highly regulated businesses.

The United States Postal Service has a monopoly on the carriage of "letters." This monopoly is mandated by federal law embodied in the Private Express Statutes. Moreover, the

USPS has the power to define what a letter is. No private company may compete with the USPS in the delivery of letters. This monopoly represents about $42 billion per year of protected revenue for the USPS (if you consider First Class and Regular Standard to be protected).

Further, the USPS enjoys special pricing advantages that go far beyond its protected monopoly, advantages that even private sector regulated utilities do not enjoy. First, regulated utilities must build a profit margin into their rates, even if that margin is regulated. The dollars of profit are dollars in the rates collected from customers.

Second, privately owned utilities pay real estate taxes, income taxes, all the taxes to which a business in the private sector, like APS, is subject. This cost factor increases the rates a regulated utility must charge by the collective amount of the taxes payable.

The USPS is virtually unique among organizations, companies or utilities. The USPS rates do not reflect either of the factors mentioned above. The USPS operates on a break even basis, so USPS rates are significantly lower than they would be if the USPS were obligated to factor in, say, a 10% profit margin. Also, the huge amount of taxes that the USPS would otherwise pay if it were not tax exempt is also absent from USPS rates. As a result of these and other unique advantages (does USPS get and pay parking tickets, business licensing fees?), USPS rates are substantially lower than they would be without these special privileges.

Beyond the advantages of a utility-type monopoly, its tax exempt status and rates that reflect no need for a profit margin give the USPS an advantage far beyond its mere monopoly advantage. Therefore, the USPS must be regulated far more carefully than if its only advantage were a monopoly privilege. Tax exempt status, added to non-profit status, added to a monopoly revenue base of $42 billion create a potential for abuse unique only to the U.S. Postal Service.

Persistent USPS cries, both at the Commission and before Congress, for relaxation of rate controls reek with the likelihood of abuse. These cries are ominous to competitors and should be just as ominous to most mailers and to the general public. With a $42 billion base guaranteed by law, with tax exempt status, and with non-profit status, even if there is no evidence of abuse present, certainly the *potential* for abuse is ever present. It is important that the Commission constantly evaluate the USPS with respect to its competitive performance.

Most importantly, the Postal Reorganization Act places solely upon the Commission the responsibility to assure that the interests of the public, of mailers, and of competitors are protected. Small competitors of the USPS have no other recourse but to rely on the Commission to prevent abuses that, as we shall see, have characterized the actions of the USPS over the past fifteen to twenty years.

V. "ONE HELL OF A COMPETITOR"

It is clear from USPS declarations and actions that the USPS chafes under this necessary regulation. It is equally clear, and understandable, that it does not agree with a high level of regulation. Certainly no entity appreciates regulation that prevents it from doing what it is otherwise inclined to do. Utilities no doubt would prefer to set rates independently of public service commissions. But the Postal Service has been more than persistent in attempting to free itself of accountability. From friendly customer "blue ribbon" task forces, to pressure on Congress to let it set its own rates, the Postal Service has done everything it can think of to escape PRC review.

The USPS obviously views itself more as a private business, and yearns for the opportunity to compete freely without any restraint. This self-perception is evident in the USPS treatment of Third Class/Standard mail since the late 1970s. It is further demonstrated by the USPS special treatment of Advo Corporation, and of other shared and saturation mailers.

It is clear from observing the USPS over the past 16 years, and from participating in several rate and classification cases, that the USPS views itself as an aggressive competitor. While that self-view is not what Congress intended for the USPS, as I will discuss below, it has nonetheless shaped Postal Service's mission, rates and proposals since the early 1980s at least.

Saturation Third Class/Standard mail has been targeted by the USPS for special treatment since the late 1970s. ECR saturation and high density mail are the only significant part of the Standard Mail mailstream open to competition. It is interesting to track the history of First and third class rates since the mid-1970s. Saturation advertising has time after time been the recipient of favorable proposals and favorable rates, albeit (thanks to the Commission) less favorable rates than proposals.

Following is a chart that tracks the history of the rates paid by saturation third class/Standard mailers. The chart compares the lowest rate for saturation flats, typically the most competitive, with the highest (or least sorted) rate for regular bulk third class, typically those third class/Standard mailers with few or no options. It also compares the rate for monopoly First-class letters and the rate for subsequent ounces for First-class mail.

There are two key elements in the rates for competitive advertising. These are the minimum piece rate and the pound rate. As shown above, the piece rate separation between competition and monopoly advertising matter has been dramatic. The rates in 1978 were the same for all third class mail, except for that which was "bound." Though the lower rate for bound materials made sense from a cost standpoint, it didn't make competitive sense, to be sure. Most bound material had no alternatives. That rate distinction disappeared in 1981.

The first key element that affects the competitive balance is the minimum piece rate. As you can see from Table A, the piece rate for the most competitive saturation advertising has increased just 36% since 1978. The slight increase in R97-1 proposed piece rate would increase that 20-year spread to 40%

The other key element of postal rates that affects the competitive balance is the pound rate for saturation advertising. Shopping guides and free distribution newspapers make choices based more upon the pound rate than on the piece rate. This is because the typical publication weighs between 3 and 6 ounces. However, publishers, like shared mail companies, sell the delivery of preprinted inserts to advertisers. With one or more regular inserts, the combined weight of the publication and its inserts is in the 4 to 10 ounce range, and often higher. The cost of the incremental weight is a major consideration on the part of a publisher whether to use the Postal Service, to use an alternate delivery provider, or perhaps even whether to start a delivery system of his own. The cost of weight determines, to a large extent, the cost of handling preprinted inserts.

Certainly the U.S. Postal Service is aware of this key rate, as it clearly explained in MC95-1, and acknowledges again in R97-1. That the proposed pound rate is only 17% higher than the rate paid by saturation advertisers in 1978 shows just how protected this rate has been. By way of comparison, the pound rate for mailers with the fewest competitive alternatives, or perhaps none, is now 67.7 cents, 88% higher than in 1978. The proposed rate of 65 cents would bring that 20 year increase to 81%, compared to the 17% increase for the most competitive of saturation advertising over that same 20 years. Indeed, the US Postal Service has been so intent on making this pound rate the focus of its attack on alternate delivery competitors that it has rigged at least three separate weight studies to give its rate preference the appearance of legitimacy from a cost standpoint.

I would venture to guess that if the public were generally aware that the U.S. Postal Service were proposing a change whereby major advertising interests, which had experienced cumulative rate increases over the past 19 years of only 53%, would now get a reduction, there would be some serious pressure for change. I suspect that the reaction would not favor the USPS or saturation advertisers.

I can't include a discussion of the history of such favored treatment without pointing out that it could be worse, and it indeed would have been worse had the USPS gotten all that it had asked for. In R90-1, the USPS proposed to reduce the lowest saturation rate from $0.101 to $0.091 per piece, a 10% reduction. The Commission recommended instead that the low rate be .105 for saturation flats, an increase of only 4%, but an increase none-the-less. In 1995 during the re-classification case, the USPS proposed a pound rate for saturation advertising of as little as 39.9 cents per pound. The Commission recommended instead the current rate of 55.2 cents and above.

In spite of the positive contributions of the Commission over the past several cases, this highly competitive class of mail has escaped the large increases experienced by other mailers. Not content, however, the Postal Service once again is proposing substantial *decreases* in the rates paid by this privileged class of mailers, decreases of as much as 18%. We urge the Commission to consider the history of rates for this privileged class, and to consider that it is one of the most highly competitive classes in the mailstream.

Probably by far the largest shared mail company in the United States is Advo. For its fiscal year ending September 27, 1997, Advo mailed 3.11 billion shared mail packages (representing more than 10% of commercial ECR) containing more than 26.5 billion pieces. It is therefore understandable that the USPS greatly values Advo as a customer. Advo has been a regular active participant in postal matters, and you will have to pardon me for observing that the USPS and Advo are generally on the same side of most issues. That may even qualify as a gross understatement.

In R84-1 it was revealed by us that USPS officials had been ordering mail handlers to give Advo mailings special treatment, far above the service standards for third class mail. In a memo authored by then MSC Postmaster Cooper McCauslen in Grand Rapids, Michigan, individual postmasters were ordered, "Delivery of the [Advo] mailing <u>MUST</u> be made on Tuesday and Wednesday, each week Delivery <u>MUST NOT</u>, under any circumstances, be made on or before Monday. It is for Tuesday and Wednesday delivery only." (Emphasis in original)

McCauslen went on to say, "The intent of this program is to recapture the advertisement that was lost to the newspapers, as supplements to their papers several years ago. In many cities the program has been quite successful and the potential for the USPS to recapture significant advertising business rests with our ability to handle the job well."

Efforts to get the USPS and its witnesses to comment on this memo, or the "program" described in it, were fruitless. The USPS refused to answer our questions about the memo or program, and the USPS defied an order from the Commission to produce answers.

The infamous memo, and supporting personal experience from newspapers and alternative delivery companies throughout the United States, established clearly that Advo was getting a value of service that often exceeded the service standards for First class mail. An exchange between Chairman Gleiman and USPS witness Moeller in MC95-1 demonstrated that Montgomery Ward was getting similar special treatment. (MC95-1;Tr. 4352-55)

The current competitive drive of the USPS is well illustrated by a speech made by Postmaster General Marvin Runyon shortly after the results of the MC95-1 case were in. In that case, the Postal Service made it abundantly clear that its prime targets were alternate delivery companies that through the early 1990s were gaining a small foothold in the delivery of subscriber magazines.

In the early 1990s, Time Warner started a company named Publishers Express (PubEx) to organize the private delivery of subscription magazines. At that time another company, Alternate Postal Delivery (APD) of Grand Rapids, Michigan, had demonstrated the feasibility of delivering subscription magazines, and had developed delivery capability in a number of major markets. With the addition of Publishers Express, by 1994 more than 80 markets were being served by either APD or PubEx affiliates, most of which were members of AAPS. The fact that the volumes delivered outside the mail were extremely small did not stop the Postal Service's search and destroy mission.

Thus, the USPS proposal in MC95-1 would have split regular rate periodicals into two subclasses, producing rate reductions for favored large magazine publishers (those whose density made them prospects for APD and PubEx) at the expense of large rate increases for small magazines that did not produce the density to make alternate delivery viable for them. Although the Rate Commission rejected this aspect of reclassification, it did order rate decreases for the mass circulation periodicals, leading to the abandonment of alternate delivery by several major magazine publishers. As a result, Publishers Express announced in mid-February, 1996, that it would cease operations.

Just days later, on February 20, Postmaster General Marvin Runyon, in a speech to the NAPUS Leadership Conference in Washington, DC addressed the demise of Publishers Express with unmistakable glee:

> I would like to close with a story that tells it all. Remember the alternate delivery company called Publishers Express? They came on the scene a few years back with a lot of fanfare and tough talk. They said they were going to deliver magazines and advertisements faster and cheaper than us. Eleven days ago, they quietly went out of business. They said that they were no longer needed. They had no more customers. We ran them out of business, by improving service and keeping costs low!
>
> I can't say that I am sorry to see them go. But they taught us two valuable lessons. First, if we don't do our jobs, somebody else will. And, second, when we get our act together, we can be one hell of a competitor.

Certainly, that doesn't "tell it all." Actions say it all - not speeches. Those actions say loudly and clearly that the Postal Service is intent on manipulating rates in such a way as to lower rates for competitive mail and increase rates for mail that has no competitive options. It would be comic, if it were not so serious, that when the Postal Service succeeds by creative pricing in driving a competitor out of business, the PMG publicly seizes the credit - chalking it up to "improving service and keeping costs low." I wasn't there, but I wonder if he delivered that line with a straight face. I wonder if he cared about the jobs he "ran out," and about the investment by small companies in magazine delivery that the Postal Service wiped out. Apparently, people in our industry contributed to the millions of dollars of bonuses paid to postal executives.

Clearly the Postal Service has embraced a mission of aggressive competition. It views itself as "one hell of a competitor" first and foremost. It proposes rates and classifications purely for competitive reasons, and for the purpose of harming its competitors. It seeks postal "reform" that would free it from PRC accountability, so that it can compete even more effectively. Its cost computations are not trustworthy. It computes rates in such a way as to make monopoly mail seem expensive and to make competitive mail seem inexpensive. In short, it does not accept the mission and the public service role established for it by the U.S. Congress.

VI. THE POSTAL SERVICE ACCORDING TO CONGRESS

In the private sector, companies respond all the time to pressures from customers. They make concessions to valued customers, they lower rates, they add free services. What's wrong with the Postal Service doing the same thing?

The answer to that question should be obvious, but in view of the current proposal, and the recent MC95-1 case, it appears that the answer has gotten lost somewhere in the jumble of detail. Quite simply, any entity that enjoys governmentally protected monopoly revenue of $42 billion dollars, non-profit status, and tax-exempt status must be carefully regulated both in areas inside as well as outside the parameters of its monopoly. That is the main purpose of the Postal Rate Commission, and that was one of the main concerns of Congress as manifested in the Postal Reorganization Act.

Certainly the potential for abuse in the competitive areas is obvious, and it was obvious to Congress when it wrote the Postal Reorganization Act. In light of the Act, I am baffled by the trend of the USPS toward aggressive competition and the increased talk in recent years at the USPS concerning the need to be more competitive. It is clear from the Act that Congress did not intend for the USPS to be aggressively competing with the private sector.

From the beginning of the Republic, the postal service was regarded as a vital governmental service. It was the purpose of the postal system (the Post Office Department) to provide the nation with a common, universally accessible medium of communication. In a far less technical environment, without the postal service, communication would come to a standstill, and it was not feasible for private enterprise to provide that service.

Communication was essential in order for freedom of expression and enterprise to flourish. It was particularly vital as the western expansion increased the boundaries of the nation. And to make the postal service more viable, private individuals and companies were prohibited from delivering letters in the limited areas where it might be economically feasible to do so.

There was no hint or suggestion then that the purpose of the postal service was to compete with and destroy private businesses. In those days, government did what private enterprise would not or could not do, for the common benefit of all. The postal service was regarded as an essential service. It was not a profit making entity, but a necessary medium of communication, virtually the only medium of personal communication out of earshot.

But by the late 1960s the Post Office Department was in serious condition. Far from the lofty ideals that viewed the service as a vital service, the post office had become the means of repaying political debts. Postal management jobs were rewards for political loyalists. Service broke down as labor morale suffered, and management accountability was non-existent. In 1970 Congress decided that the postal service needed reform.

It is clear from reading the Postal Reorganization Act that Congress's goal was threefold. First, it sought to restore the high view of the postal service in its historic sense, free of political favors and considerations. Second, it sought to provide a framework within which the postal service could operate in an orderly, efficient manner, with accountability throughout. Third, throughout the Act are numerous protections from the potential abuse by the USPS of its position of special privilege. The USPS described in the Postal Reorganization act was never meant by Congress to be "one hell of a competitor."

A. The Historical View

It is obvious that the Postal Reorganization Act was written to regain that historical view of the postal service, wherein the service is viewed as an essential service of government. To establish that view of the USPS, Congress began the entire Act with the following definitive statement, Section 101;

> (a) The United States Postal Service shall be operated *as a basic and fundamental service provided to the people by the Government of the United States*, authorized by the Constitution, created by Act of Congress, and supported by the people. The Postal Service shall have as its basic function the obligation to provide postal services to bind the Nation together through the personal, educational, literary, and business correspondence of the people. It shall provide prompt, reliable, and efficient services to patrons in all areas and shall render postal services to all communities. The costs of establishing and maintaining the Postal Service shall not be apportioned to impair the overall value of such service to the people. (emphasis added)

Needless to say, there is not a hint of reference to a competitive role for the USPS. Certainly this opening, definitive statement has all the marks of the historic postal service role as essential government service. It would be incorrect to suggest that the absence of a reference to competition in the introductory section of the Act should be automatically construed to suggest that competition was not anticipated or was non-existent. Certainly competition existed at that time, and before that time. But it is clear from the Act that the USPS was expected to act cautiously in that area.

B. A "Business-Like" Postal Service

The second objective of Congress was to create an efficient postal service. I have often heard it said that Congress intended to create a more "business-like" postal service. I have no problem with the concept of a "business-like" postal service. "Business-like" to me suggests efficiency, careful accounting and accountability. But over the past years it has come to mean more than that.

"Business-like" in discussions of USPS issues has come to imply a competitive posture, and I take issue with that implication. First, an aggressive, competitive USPS contradicts the spirit and the letter of the Postal Reorganization Act. As I have pointed out, Congress viewed the new USPS as a government service in the historic sense of the old postal service. The criteria for establishing rates require the Commission to go to some length to assure that neither captive postal customers nor the USPS's competitors are intentionally harmed by postal rates.

Second, despite the oft-repeated phrase that Congress wanted a "more business-like postal service," it is worth noting that Congress never stated in the law itself that it wanted a "business-like" postal service. References to speed and efficiency are plentiful, but never is the concept of an aggressive, competitive USPS even hinted at. To the contrary, we shall see that Congress took special precautions to guard against such a competitive postal service.

One aspect of this more "business-like" service was the USPS's new responsibility to determine the timing of its own rate increases. Prior to the Act Congress itself established postal rates and changed rates as it saw fit. Of course if it is Congress's desire that the Postal Service operate efficiently, with better accountability, and with more direct responsibility for its own success or failure, the USPS would need to have the capability to increase its overall revenue as overall economic conditions required.

A few years ago a segment on public radio detailed how the U.S. Marine Corps was studying Wal-Mart's inventory control system, in order to enable the Marines to operate in "a business-like manner." Does that suggest that the USMC needs to be more competitive? Of course there is no such thing as a free enterprise competitor to the Marine Corps. In this case it had nothing to do with competition. It simply meant to borrow some good ideas from a successful business for the purpose of increasing efficiency.

C. Special Protections Against Competitive Abuse

The current, popular self-view of the USPS as an aggressive competitor in the open market clearly runs counter to the Act. Quite to the contrary, Congress understood that a tax exempt postal service, operating without a profit margin, and possessing a legally mandated monopoly has the potential for abuse. Because of this, in 1970 it established three specific criteria to protect competitors and to protect mailers from suffering the results of anticompetitive rate structures. Implied clearly is that Congress did not view the USPS in a competitive role.

The Postal Reorganization Act, Section 3622,(b), lists the criteria for the development of postal rates. In this section of the Act, the Postal Rate Commission is directed to "make a recommended decision on the request for changes in rates or fees in each class of mail or type of service in accordance with the policies of this title and the following factors..." There follow nine specific criteria for setting rate and service levels. Of those nine, Criteria 3, 4, and 5 taken together reveal Congress's view and its clear intent with respect to competition. These three criteria are as follows:

> (3) the requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to that class or type plus that portion of all other costs of the Postal Service reasonably assignable to such class or type.
>
> (4) the effect of rate increases upon the general public, business mail users, and *enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters*; (emphasis added)
>
> (5) the available alternative means of sending and receiving letters and other mail matter at reasonable costs.

It is significant to note that these specific criteria were new concepts. There were no such specific protections for competitors in the former Title 39, which the Postal Reorganization Act rewrote. The former Title 39 was very general in its rate criteria, Congress being the rate setters.

The general concept contained in Criterion 3 wasn't entirely new, but the specificity was. Sections 2302 and 2304 of the former Title 39 in a very general sense provided for cost review every two years, and specific adjustment recommendations were to come from the Postmaster General to Congress every two years. Further, the law was very general (in Section 2304) as to attributable costs or coverage of costs by rates for each class. There was no specific requirement that each class or subclass pay at least its own costs.

Similar to the current Criterion 4 above, the former law also contained a general "protection" clause, but the protection was only for mailers. The old law declared that Congress would consider "the effect of postal services and the impact of postal rates and fees on users of the mails." (former Title 39; Section 2302,(c),(1),(D))

Finally, there was nothing to correspond with the present Criterion 5 protection. Nothing in the former Title 39 specifically addressed the need to protect mailers that had few or no alternatives.

It should be obvious that the protections being extended for the first time to the USPS's competitors, and to mailers with no alternatives, were added in 1970 as a counterweight to the increased freedom and independence being granted the USPS by the Postal Reorganization Act. With the newfound level of independence, and armed with the letter monopoly, the resulting new potential for abuse was to be tempered by new protections for those most likely to be victims of that abuse.

The language of Criterion 4 is especially interesting. It directs the Commission to consider the effect of "increases" upon, among others, competitors of the USPS. The implication clearly is that "increases" for competitive classes of mail that are so low (or negative) as to hurt competitors are to be avoided. Within the context of these criteria, there can be no other logical inference. In other words, not only is the USPS not allowed to lower rates for the purpose of hurting fair competition, it is clearly instructed to consider the impact of "increases" to avoid hurting competitors.

The word "increases" is certainly significant. It should be clear from the spirit and the context of the Act that Congress did not consider the possibility that the USPS would go out of its way to *reduce* competitive rates for competitive purposes. The implication is unmistakable that Congress assumed that periodic rate changes would take the form of an increase, and that the increases should be high enough so as not to harm fair competition.

In the present case, the USPS has apparently taken the novel, and ludicrous, position that the Criterion 4 consideration of competitors is dropped from the Act in the event of a rate *decrease*. AAPS was required to file a motion with the Presiding Officer to compel USPS to answer AAPS/USPS-6, which asked whether the Postal Service had conducted or commissioned a study or report on alternative delivery since the Strategic Analysis, Inc. (SAI) report that had been dragged into the light during MC95-1. The Postal Service, after admitting that such work had been done, strenuously objected to providing it or revealing what it contained.

One of the subjects that the USPS ultimately acknowledged is contained in the new study is information that analyzed the "reaction" of the alternate delivery industry to price change. AAPS contended that this is exactly the kind of information that must be considered under Criterion 4. The Postal Service incredibly responded that while the Act required that the effect of *increases* on competitors had to be considered, the effects of *decreases* could be ignored! "The (b)(4) criterion only requires an evaluation of 'rate increases' on alternative delivery; the statute is silent with respect to rate *decreases*." (Emphasis in original). Supposedly the new, super-aggressive Postal System can now lower competitive rates with impunity without any consideration of Criterion 4.

To whatever extent the attempts to satisfy the rate setting criteria were altruistic, the USPS never made any serious attempt to apply Criterion 4 to its proposals. We raised the Criterion 4 issue repeatedly in R84-1, in R87-1, and in R90-1. Though attempting to satisfy the other criteria, USPS conducted itself as if the competition clause of Criterion 4 did not exist.

Yet when it served its own purpose before the U. S. Court of Appeals for the Second Circuit in Time Inc. v. USPS in 1982, the USPS, in a specific reference to alternate delivery, correctly pointed out in its January 20, 1982 initial brief that Criterion 4, "mandates that the effect on competing businesses is an additional factor to be considered in establishing postal rates." Note use of the word "mandates" and reference to "establishing" rates, not just "increasing" them.

Even though the USPS demonstrated its familiarity with the competitors' clause in Criterion 4, in R84-1 Criterion 4 received no attention, not even lip service. USPS witnesses admitted that they made no effort to study the alternate delivery industry (Tr. 1251, Docket R84-1) and that they did not even discuss private delivery among themselves in preparing the rate proposal (Tr. 2004-05, Docket R84-1).

R87-1 was no better. In his initial testimony, USPS witness Lyons suggested that the proposal considered "the continued competitiveness of newspapers and private delivery firms." When questioned about that consideration, Lyons referred to an article he had read in Advertising Age which did mention newspapers but did not mention private delivery (see Tr. 3844, Docket R87-1).

In R90-1 witness Lyons proposed a rather novel interpretation of Criterion 4. It was apparently his testimony that Criterion 4 was automatically satisfied as long as Criterion 3 was satisfied. The new doctrine was that as long as rates covered their direct cost (direct testimony at 39 and 41), and as long as rates are not specifically designed to hurt competitors (Tr. 4293-94), then that amounted to due consideration of competitors and satisfied Criterion

4. (This is similar to Donald J. O'Hara's view in the present case. He concludes, "Given the very high cost coverage of the ECR sub-class, this rate increase *[decrease?]* does not result in unfair competition for its competitors." Testimony, page 35.)

Of course, making Criterion 4 dependent upon Criterion 3 writes Criterion 4 out of the Act. It should go without saying that if Congress did not mean something additional to Criterion 3 in writing Criterion 4, then Criterion 4 is redundant and unnecessary. Obviously, since it was added as a separate criterion, it means (and requires) something additional.

In MC95-1 the Postal Service proposed rates under new classification headings that it freely admitted were developed for competitive reasons. Its "consideration" of competitors was apparently a consideration of how to put them out of business. It was to some extent successful, as the PMG's speech concerning Publishers Express cited above demonstrates.

In R97-1, the Postal Service, with tongue firmly planted in cheek, claims that none of the rate proposals has been made for competitive reasons. Nowhere in R97-1 have I discovered the USPS witnesses referring to Standard ECR rates as competitive, as they did in MC95-1. They mention only vaguely that there is competition for Standard ECR mail.

Indeed, in the same objection cited above concerning AAPS/USPS-6, the Postal Service states, "Nowhere in the Postal Service's testimony is there a claim that the existence of a 'competitive threat' from alternative delivery forms the basis for any of the rate and classification proposals in this docket." Two years ago, competition was the driving force behind reclassification. Now it's gone from the radar screen.

That being the case, or alleged as the case, it is curious that the USPS is so secretive about its new SAI study with regard to alternate delivery competitors. While it has steadfastly refused to disclose the contents, beyond the highly censored and therefore useless version produced, it claims to be unaffected by these competitors in requesting new, more competitive rates.

The USPS fought hard to avoid releasing the complete new SAI study. The study was apparently so controversial - and perhaps inconsistent with the testimony of its witnesses - that the Postal Service didn't even let the witness that testified about impact on competition and competitors (O'Hara) see it or learn of its existence! O'Hara was to "describe what efforts the Postal Service made to determine whether the rate decreases proposed will have an adverse impact on competitors or on competition." He responded, "...A quantitative assessment of the effects on competitors would require information on competitors' costs, prices, and volumes, and as far as I am aware this information is not available... ." TR. 116. Unbeknownst to Mr. O'Hara, this type of information was indeed available. The powers that be just decided not to tell him.

Witness Moeller, who was charged with the rate design for the highly competitive ECR rates, was obviously not aware of the SAI study either. He acknowledged that he had not reviewed competitors' rates for two and a half years. He thought he might have logged onto some web sites for information, but couldn't remember seeing any rate information. He had acknowledged studying competitive rates, however, in preparation for MC95-1. One cannot help but question the integrity of a process that collects information vital to a key rate-setting consideration and then fails to disclose not only the actual data but the fact that it even exists to those charged with setting the rates. Combine this disgraceful behavior by a governmental public service with gloating by its leader when it crushes a private sector competitor, and it becomes apparent why the alternate delivery industry is so skeptical about Postal Service data, claims and motives.

In this regard, why should we, or the Commission believe that what was a serious competitive threat in MC95-1, a threat that formed the very basis of reclassification, is no longer a threat in R97-1. And what credibility can be given to the assertion that the competitive basis for a huge pound rate reduction for Standard ECR in MC95-1 is presumably not a factor in proposing another huge pound rate reduction for Standard ECR in R97-1.

I encourage the Commission to view the USPS as Congress viewed it in the Postal Reorganization Act. It is not a competitor first and foremost. It is first and foremost a government service charged with serving the public good. I encourage the Commission to apply all the criteria of the Act, including Criteria 3, 4, and 5, to each USPS rate proposal.

VII. ANOTHER PROPOSAL WITH SERIOUS FLAWS

In early December the US Postal Service announced that it would earn a surplus of $1.3 billion for fiscal 1997. Because the present rate request proposed fairly low average increases to begin with, it seemed that the proposed rates were more opportunistic in terms of adjusting the competitive balance than they were necessary in raising needed revenue.

Add to that good news the continuing volume increases – particularly in advertising mail – and a rate case at this time is curious to say the least. It does make sense, however, if we consider that the USPS mailstream consists mainly of two large classes of mail, First Class and Standard Mail, and any significant effect on the USPS, good or bad, will be the result of First Class and Standard Mail rate shifts. It goes without saying that First Class mail is safe, that whatever the rate being charged, mailers will have to pay it since only the Postal Service can legally deliver "letters." I recognize the possibility of substantial diversion to electronic media, but submit that such diversion is much more a function of technological change than First Class rates

The current proposal calls for a one -cent increase in the price of First Class letter stamps, and no increase in the rate for additional First Class ounces. Standard mail is a mixed bag. Most of Standard Mail Regular is part of the letter monopoly, but most of Standard Mail ECR is mail for which the Postal Service must compete. So it is no surprise to find the USPS proposing moderate increases for Standard Mail Regular, and decreases for much of the highly competitive Standard Mail ECR in this proceeding, decreases of as much as 18%.

Certainly the engine that drove MC95-1 was the desire to drive an even larger wedge between the competitive portion of third class mail and the monopoly portion, and to make the rates for the competitive porttion of third class mail more "competitive." Witness Joseph D. Moeller's direct testimony (MC95-1, at 14) confirmed that a major purpose for reclassification was to develop "more competitive rates for local, high-density advertising." The concept of competition and the need to address the serious problem of the "Diversion of Mail Volume" to "alternative hard-copy delivery [companies]" were paramount in the MC95-1 testimony of Charles C. McBride.

The USPS-sponsored testimony in R97-1 is different from the MC95-1 testimony in one respect. In MC95-1, McBride and Moeller made no bones about the purpose of reclassification. They made it surprisingly clear that competitive considerations were driving the whole process. By way of contrast, the R97-1 testimonies of Moeller and O'Hara are certainly better disguised. But the results of a major decrease are just as damaging to competitors as if they had again fully described their intentions.

A. Ramsey Pricing and Rate Elasticity

This rate case breaks some new ground with respect to competition. The introduction by the USPS of Peter Bernstein's testimony officially praising the application of Ramsey Pricing to postal ratemaking speaks as loudly to competitors as would a formal cover letter from the PMG himself accompanying the rate case testimony declaring that his objective it to put our whole industry out of business (not just the subscription magazine part).

I am certainly not an economist, but it is clear to me from what I have read in this case (and in prior cases) that sponsoring Ramsey Pricing in a postal context is tantamount to ignoring Congress and tossing nearly the entire ratemaking criteria section out of the Postal Reorganization Act. While Ramsey pricing concepts have been introduced by other witnesses in the past, and have been debated and discussed in past cases, this is the first time the Postal Service has officially endorsed and sponsored Ramsey Pricing testimony.

No one from the USPS is actually proposing any rates based upon Ramsey Pricing, going only so far as to say that it is a useful guide. That's what makes the sponsorship of Mr. Bernstein's testimony a bit curious. The effect of Bernstein's testimony appears to be simply to lurk in the background, perhaps to be relied upon by others, and to serve as a basis for lower competitive rates when the USPS can't support them through application of proper postal ratemaking criteria.

And of course the bottom line is that Mr. Bernstein has concluded that highly competitive Standard ECR mail *should really* be priced at about an average 8 cents per piece, roughly one half its current average rate. In that event, according to Mr. Bernstein, Standard ECR mail volumes would grow by 36%, from 31 billion pieces to over 42 billion pieces (Tr. 5088). Mr. Bernstein would venture no guess publicly where that volume increase would come from (TR. 5089-90). What is obviously difficult for a highly trained economist to figure out, however, is fairly simple for an AAPS member competing for its small share of those 12 billion pieces that are up for grabs.

Naturally the Postal Service has generously decided not to cut these competitive rates in half. Armed with this ideal, however, it has decided to cut the rate for some of the most competitive of Standard mail as much as 18%. While this is consistent with past proposals, Mr. Bernstein has given the Postal Service some intellectual cover this time.

The USPS's semi-embracing of the Ramsey Pricing is no surprise. Ramsey Pricing is the product of calculating price elasticity, one of Postal Service's favorite ratemaking tools. Much postal rate elasticity results from the artificial result of the Private Express Statutes, so that Ramsey Pricing calls for high rates for monopoly mail and low rates for competitive mail. And that result is consistent with what the USPS has been trying to do with only limited success during the past several rate and classification cases.

B. An Over-Reliance on Cost Coverage

AAPS has been critical of the Postal Service's over-reliance on percentage cost coverage since it began participating in these rate cases. For example, as we stated at page 33 of our initial brief in R90-1, the saturation mailers will argue that the rates for saturation mail "are too high because the 'attributable cost coverage' is higher for that particular type of mail than for other particular types of mail."

It was AAPS's position then, and it is AAPS's position now, that the USPS's embrace of percentage cost coverage (whether attributable, incremental or volume variable) has "elevated a convenient but misleading tool of comparison into the exclusive rate making tool." In fact, in the words I used while testifying in R90- 1 (Tr. 18490), the percentage attributable cost coverage concept has "evolved into a rigged system where first-class mailers are forced to pay a hugely disproportionate share of institutional costs, whereas third-class mailers pay a meager share of the total."

In his dissent in R84-1, Commissioner Crutcher (at page 3) was critical of a "strict adherence to percentage markups" which, he said, "ignores absolute unit cost contribution to institutional costs." Mr. Crutcher was simply reiterating what the Commission found in R80-1. There it explained (at page 455, footnote 1) that use of percentage cost coverage "can misrepresent" institutional cost burdens where there are substantial differences in attributable costs and that, consequently, the Commission "must be guided more by the per piece cost contributions than by percentage cost coverage" in comparing first-class letters and third-class bulk mail.

To its credit, the Commission recognized this important concept in evaluating the Postal Service's proposals in recent rate cases, and, as a result, has tempered the first-class increases and rejected USPS attempts to impose either small or negative rate increases on Third Class/Standard ECR saturation mailers. The Commission should consider the disproportionately low burden now being borne by Standard ECR in assessing the USPS's proposal to reduce even further the rate for many saturation flats.

As AAPS, and I, have contended in previous cases, the shortcomings of the percentage markup analysis become more pronounced as mailers bypass attributable costs and, therefore, attempt to free themselves from institutional costs burdens as well. I repeat below footnote 16 from page 36 of the AAPS initial brief in Docket No. R90-1, which predicted the dilemma that the Postal Service is just beginning to recognize here:

> In earlier cases, the Coalition of Non-Postal Media had hypothesized a class of mail handed to the letter carrier on the way out the door, in which the attributable costs are to be extremely low and which would, therefore, be 'assigned' a very low percentage of institutional carrier street time, contrary to all logic. The Postal Service's deep discounts in this case for walk-sequenced, delivery office mail show that our earlier hypothetical analogy is becoming frightfully real.

With today's rates, First Class mailers now must pay about 63% of the institutional cost load, despite the fact that First Class makes up only about 52% of the volume. Standard A mail collectively represents about 41% of USPS pieces but only 21% of the contribution to institutional costs. Standard, Commercial ECR mail, comprising an estimated 15% of the volume and a higher percentage of the total weight, picks up only about 9% of the total institutional cost burden. As "attributable" costs continue to be bypassed, the concept of coverage is becoming nearly meaningless. Stated otherwise, assessment of cost coverage is difficult for mail that typically uses little more than the Postal Service's delivery function, especially because 60-65% of those costs are deemed to be institutional. See Tr. 3151-52, where the Presiding Officer raised this point with Witness Moeller.

The unit contribution to institutional costs will continue to show a much more severe burden on First Class than on Standard mail pieces. According to witness O'Hara, Tr. 190, under the R97-1 proposal, each piece of First Class mail will make a contribution of between 17.17 cents and 18.04 cents toward institutional costs. Standard Regular will contribute 7.52 cents, and Standard ECR will contribute 8.43 cents per piece, both less than half the First Class per piece contribution.

Add to these per-piece contributions the fact that the average Standard Commercial mail piece weighs approximately three times what the average First Class piece weighs, and you have a First Class per-pound contribution of about six times the per-pound contribution of Standard Commercial. Yet despite these glaring discrepancies, the USPS continues to rely on attributable cost coverage percentages to try to widen these gaps still further.

C. Still Another Very Selective Weight Study

Of course it should come as no surprise that the USPS makes invalid comparisons to pursue its rate objectives. It is even understandable that the USPS would rely on favorable, albeit illogical, cost coverage numbers in proposing competitively beneficial rates. However it seems somewhat inappropriate to engineer a weight study in an incomplete, selective manner that tends to fulfill the desired ends at the price of distorting the truth.

In MC95-1 we made this point concerning the weight study performed by Christensen Associates, referred to there as Library Reference MCR-12. This study presumed to measure the relationship between weight and cost for third class regular rate mail. The study was, without question, incomplete. Page one of the study listed the factors considered, "The costs included in the analysis are those associated with mail processing, window service, and city carrier in-office activities."

If the USPS really wanted to determine the relationship between weight and cost, this study had no value. It ignored obvious weight driven cost segments, and it relied instead on cost segments that were entirely in-house and were only affected minimally by weight.

This is not said in order to impugn the integrity of Christensen Associates. Without doubt the study was conducted as ordered by the USPS. I point out only that the USPS-ordained scope of the study was inadequate for anything other than to serve as a pretext for still lower competitive rates.

In MC95-1 USPS witness Moeller, though relying on this weight study for his proposed rate of 51 cents per pound for Enhanced Carrier Route mail, recognized the incomplete nature of the study, and the fact that the Commission has repeatedly asked for better information. "The Commission has repeatedly expressed its desire for a study of the weight-related costs in third-class. . . The Postal Service shares this desire, but a study of weight that excludes the effect of other cost-causing factors has been difficult to conduct." (Direct Testimony, Page 12)

Moeller was at least in part correct. The Commission has pressed for a weight study since at least 1983, when AAPS (then APPS) participated in the Joint Postal Service/ Postal Rate Commission/Mailers Study Group on Third Class Bulk Mail. In a letter written to this study group, dated September 26, 1983, James Anderson, then the APPS Director of Governmental Affairs, stated the following:

> We are vitally concerned with the approach to this study because as competitors to the Postal Service it is very important that the Postal Service properly identify and assign its operating costs. If the Postal Service properly identifies its costs and structures rates to adequately cover those costs, private sector competitors like ourselves can fairly compete for the business.
>
> Our experience tells us that weight and shape have a significant impact on costs even though we are not involved in the areas of sortation and processing that this study is focusing on.
>
> We have heard from the Postal Service that weight and shape are not significant factors in other cost segments. We are here to testify that weight and shape have an eminently significant impact on operating costs. It is difficult for us to understand how the Postal Service can move these same products and not recognize that impact.
>
> Our objections to this study as presently proposed are as follows: *First, the study focuses only on in-house processing and sorting functions that are largely bypassed by the carrier route presorted mail that is subject to competition from the private sector.* As presently structured this study will reveal nothing about the effect of rate (sic) and shape on that portion of the mail stream that is subject to competition. (emphasis added)

This was written more than fourteen years ago. Despite our efforts and the efforts of the Consumer Advocate that date back at least as far as 1983, the USPS has refused to identify costs for weight driven cost segments other than those segments that furthered its purpose. The result in 1983 was a study that included only in-office costs. A similar study was conducted in MC95-1 by Christensen Associates. And now, for a third time, the USPS in R97-1 has commissioned the Christensen Associates once again to conduct another carefully controlled study (R97-1; LR-H-182, Exhibit 44B) which, like the 1983 study and the Christensen Study in 1995, are preordained to produce the desired answer: weight has little effect on cost for highly competitive Standard ECR mail.

In private delivery, and I submit from personal experience, in any delivery, there is a significant weight/cost relationship at the point of delivery. Another weight/cost relationship is experienced in transporting materials. A third is in the warehousing and handling element. It has been my experience that weight drives in-office costs very little, if at all. Most in-office handling costs are piece related, not weight related, and certainly the Postal Service is aware of that. An over-reliance on in-office costs only discredits the USPS's cost data.

Any weight/cost study that fails to study the impact of weight on the most obvious weight driven costs, but simply assumes there is none, is a rigged study. Understandably, it does serve the purpose of proving that Enhanced Carrier Route rates should be low by comparison. The only costs the USPS selected for study are those which are low to begin with, and which disappear with local entry and route pre-sorting and pre-sequencing.

Imagine two postal employees. One works at a work station in a postal facility. He sorts pieces of mail. The other is a walking carrier who services 600 houses on his route.

The first handles pieces of mail. He moves skids or carts of mail to his work station, and he sorts through the pieces. Some of the pieces are heavy and some of the pieces are light. But the weight makes little difference, other than the small amount of his time that he spends moving the skid or cart to his work station. In sorting pieces, he can move through a stack of Standard Mail catalogs about as quickly as he can a stack of Standard Mail letters. His speed is predominately piece related. More importantly to the Postal Service, most highly competitive ECR mail avoids this first employee.

Consider the city carrier with those 600 stops on his route. That carrier cases his mail before delivering the route. He sits in front of a sorting rack and he sorts pieces of mail into that rack. At this point it doesn't really matter very much if the pieces weigh 1 ounce or 8 ounces. Since he is sorting one piece at a time, he can sort heavier pieces just about as fast as he can sort light pieces. It would seem logical that this part of his job will take about twice as long if he has twice as many pieces to sort.

The carrier finishes the sorting process. At this point the piece-related work is done. Unfortunately, at this point the Christensen Associates study ends as well. What remains for the carrier is by far the greater part of his labor hours. Any variability from this point on from the normal amount of labor hours is dependent not upon pieces but upon weight and bulk. The individual pieces have all been put in order. The only question concerning whether this carrier can accomplish his normal loops is whether he can carry all the load to complete each loop or whether he will have to make extra trips due to extra weight or bulk. It has nothing at all to do with the number of pieces.

However, in response to an interrogatory concerning the most recent Christensen Associates study, "Please explain why city carrier street costs are distributed to weight increment in proportion to mail volume," witness Moeller answered, "This assumption was made in interests of simplifying the analysis. Although there may be some weight related costs in city carrier street time, it is believed that the majority of costs are piece related." (Tr. 7708) How can that be? The piece work at this point has been finished. The number of stops and regular loops are fixed - the same every day. The only variables now are weight and bulk. (It seems also that simplicity, rather than accuracy, was the primary goal of the study. See also Tr. 7778.)

Witness Moeller appears far less than certain in this answer, probably because it is so counterintuitive. Indeed the next question was, "Is it your opinion that weight has no effect on city carrier street costs?" Moeller answered, "No." Yet carrier street time was not calculated or considered in the Christensen Associates study once again.

Back to our street carrier. Once sorted, the pieces are loaded into his vehicle for delivery to the 600 homes. Consider that a carrier may comfortably carry only about 30 to 35 pounds of mail at a time. Consider also the difference in 600 ECR saturation pieces that weigh 1/4 ounce each, and 600 ECR saturation pieces that weigh even a modest 3.3 ounces each. These two different pieces collect the same amount of postage.

The 1/4 ounce piece represents 9.4 pounds of mail, easily absorbed into the carrier's delivery routine. However, the 3.3 ounce pieces add an extra 124 pounds of mail. That 124 pounds is not quite so easily absorbed. It means slower progress and likely some extra trips to the vehicle. Simply put, extra weight translates into extra time, which translates into extra labor cost.

If we can assume 10 minutes to go to the vehicle and replenish the pouch, 4 trips means 40 added minutes. If we can assume the carrier earns $25 per hour in wages and benefits, which may be low, that's 2.8 cents per piece more in direct labor cost, roughly one cent per ounce. Yet, the USPS proposes that the 1/4 ounce piece and the 3.3 ounce piece should be priced the same.

As if to add insult to injury, the USPS has suggested, through its current weight study, Exhibit 44B, that if the piece weighs 13 ounces (meaning that this piece will add 487 pounds to a typical carrier), that carrier will presumably find it easier to handle than if it weighs 4 ounces. The R97-1 Christensen Associates study has concluded that it costs 7.1 cents to handle a 4 ounce ECR piece, and 6.6 cents to handle a 13 ounce ECR piece. Moreover, that 14th ounce is the back-breaker. According to this study, it costs 13.0 cents to handle a 14 ounce piece, about twice as much as the cost to handle a 13 ounce piece. This and other strange results of the study could not be explained (See Tr. 7699-7700 and 7790-7793). Perhaps the study's flaws result from the very thin data (Tr. 7797-7798; 7800).

Of these two postal employees, the USPS has made the calculated decision to consider the first one, the guy at his work station inside the postal facility, and to consider the second one only for that portion of his day that he is sorting mail at his case rack. But once the carrier leaves the post office and actually begins to lug the weight around his route, the cost experts stop watching.

The Postal Service tried to argue around these obvious problems. In response to AAPS/USPS-T36-8, redirected from witness Moeller (Tr. 7654-7655), the USPS described a similar city carrier but loaded this carrier not with 14 ounce pieces but with non-credible assumptions.

Question: "Assume that on day one a carrier delivers 500 identical Standard pieces each weighing 1 ounce, for a total of 31.25 pounds, and on day two he delivers 500 standard pieces each weighing 7 ounces, for a total of 218.75 pounds. Assume further that all other mail to be delivered is identical. Will there be any difference in carrier street costs on the two days? Please explain."

The USPS didn't like the realistic assumption posed by AAPS, so it substituted its own assumptions before answering the question. "In interests of simplicity, let us further assume that both the one ounce pieces and the seven ounce pieces are the same shape, say flats. *[fair enough]* Also assume that the carrier has no other mail on these two days *[we had asked him to assume that other mail was identical, not non-existent!]*, and that the 500 pieces on each day are addressed to the same 500 stops."

After loading the assumptions to produce a scenario that this carrier delivers no mail except 500 one-ounce pieces the first day, and no mail except 500 seven-ounce pieces the second day, a scenario that could never happen in the real world, the Postal Service concludes that there will be no difference in the carrier street costs.

Any reasonable observer will notice the obvious - that it is not the seven ounce pieces by themselves that are likely to increase the carrier's street time, it is the seven ounce pieces in addition to the other mail that would normally be delivered at the same time that causes additional dismounts and extra trips back to the vehicle, thus increasing carrier street time.

The point is that the USPS continues to base its conclusions about weight on untested, unproven, and unquestionably incorrect assumptions about street time.

When AAPS/USPS-T36-10 pointed out several serious anomalies in the study, such as that the cost for a 13-ounce piece was the same as the cost for a one-ounce piece, that the cost per piece actually declines from one ounce to three ounces, that a 4-ounce piece costs 39% more than either a 3-ounce piece or a 5-ounce piece, that a 9-ounce piece costs 14% less than an 8-ounce piece, the Postal Service responded that "the study presented in Library Reference H-182 was not intended to measure specific cost relationships between individual weight cells, but rather to provide the overall relationship between weight and cost for Standard Mail(A)." (Tr. 7657)

If a study intended to establish weight/cost relationships cannot even come close to measuring "specific cost relationships between individual weight cells" without more questionable cost numbers than realistic numbers, and if it can't even produce a clearly discernable graphic trend between 1-ounce and 13-ounce pieces, *what good is it?* Why would the Postal Service be so anxious to embrace such results?

Asked to explain some of the anomalies of the weight study, USPS Witness McGrane could not come up with any real explanation (Tr. 7699,7700). Asked whether there was any point at which he might begin to get uncomfortable with such anomalous results, McGrane answered (Tr. 7792), "It depends on what you mean by uncomfortable. I think that you can make a solid conclusion from the study that the relationship weight with cost for ECR mail is not nearly as great as what the current pound rate is set at," which, of course, is exactly the preordained result of the study.

A study that ignores obvious weight related factors and addresses only in-office costs would be an inadequate basis for any "solid conclusion," even if it were accurate and had the appearance of a logical progression. A study that ignores obvious weight related factors and is illogical at the same time would hardly qualify as the basis for solid conclusions.

Certainly it would be speculative on my part to try to assume or estimate the unknown costs. I freely admit I do not know the exact level of costs involved for additional weight for carriers, just as I don't know how much Advo's (and others') odd-shaped, loose sets add to carrier time and cost, compared to bound or enclosed material (although as the Presiding Officer surmised (Tr. 7831-7832), they are considerable). But certainly there are costs involved, and I doubt that anyone, other than the Postal Service, would argue seriously that there are none. In fact, even witness McGrane (who is not a postal employee) admitted that bulkiness and "openness" could have an effect on unit costs (Tr. 7788-7789).

My own experience with U. S. postal carriers confirms this conclusion. In developing private delivery in a number of communities, our employees involved in development are commonly aided by postal carriers who are anxious to help us with routing information. Their attitude is that they will do anything they can to help us, hoping that we will transfer material from their route out of the mail first.

Normally, when we succeed, we are taking a weekly newspaper or shopping guide out of the mail. With printed inserts, these typically weigh 10 to 12 ounces per set, representing an additional 300 to 500 pounds of mail for that carrier one day each week. The reason Postal carriers tend to be very helpful is because they want to get rid of the extra load and extra work. It is safe to say that if this material did not represent extra time and effort they would not care, nor would they volunteer their assistance to a competitor.

Carrier street time is not the only missing cost segment. I could add vehicle service drivers and rural carriers. I could add the obvious capital cost for purchasing additional vehicles, or vehicles capable of hauling heavier loads. I could add the cost of maintaining a larger fleet of vehicles.

The Commission should disregard the Christensen Associates' weight study and the USPS conclusions that rely on it. It inappropriately includes only in-office cost segments, and it continues a fourteen year trend of avoiding a complete study that could provide some accurate cost data for the Commission's consideration. A misleading study is worse than no study at all.

D. 42 Cents Per Pound vs. $3.68 Per Pound

One thing is certain with respect to the study of weight-related costs. The in-office personnel who were studied by the Christensen Associates had to be different postal employees than those studied to justify the $3.68 pound rate for First Class mail. Based on the 23 cent charge for the second ounce of First Class mail, other postal employees must have found it was nearly twice as difficult and took nearly twice as long to handle a First Class piece weighing 2 ounces as a piece weighing 1 ounce.

Currently the basic pound rate for Standard ECR mail ranges from 55.2 to 66.3 cents per pound, depending on Destination Entry Discounts. Although this is slightly lower than the pound rate that was being paid for comparable saturation Third Class prior to MC95-1, it was far more favorable than what the USPS had proposed. We owe the Commission a debt of thanks for that. The USPS proposal in MC95-1 was for a huge reduction in the Third Class pound rate, to an ECR range of 39.9 to 51 cents. That proposed reduction was based upon the first Christensen Associates weight study, which had the same basic flaws as the more recent study.

It is beyond question that Standard ECR mail is more subject to competition than is Standard Regular. Witness Moeller confirms (Tr.2799) that the weight reduction for Standard is 4% (65 cents) and the weight reduction for ECR is 20% (53 cents). He further confirms that he *selected* rather than calculated the 53 cent rate. He confirms that his reasons for proposing this reduction in this case were about the same reasons he proposed similar reductions in MC95-1, which the Commission rejected. He confirms (Tr.. 2791) that, "the rates for other advertising media were an additional consideration in the pound rate proposal." Perhaps this is witness Moeller's way of considering competitors under Criterion 4.

There is no rational cost justification to support an incremental weight rate of $3.68 per pound for First Class mailers and an incremental rate of $.42 to $.53 for mailers of saturation advertising. The First Class "pound" rate is an obvious effort to generate excessive revenues from those who have no delivery alternatives. This huge discrepancy exists despite Congress' clear instruction to give special rate consideration to mailers with no alternatives. The equally extreme (extreme on the low side) pound rate for saturation advertising is an obvious effort to generate volume in a highly competitive subclass of mail.

Small delivery companies have been successful over the past ten years in building business volumes on weekly newspapers, TMC advertisements, phone books, and product samples. USPS volume and profit figures demonstrate that these privately delivered materials have not negatively impacted the USPS. There is more advertising mail volume than ever. Certainly a reduction of as much as 18% per piece for this type of mail would have a severe impact on the private delivery of these heavier pieces. How many more notches does the Postmaster General need on his gunstock?

E. Attributable Costs That Are Not Attributed

Over the past several cases I have mentioned a number of costs related to direct-mail advertising that go un-attributed. In the present case, another example has surfaced and is worth mentioning.

According to witness Takis, in response to a UPS interrogatory, of the $235 million spent in advertising, only $66 million is attributed to a specific class of mail. Tr. 4732. Presumably the other $169 million is regarded as an institutional cost. It's been a long time since I saw an advertisement from the Postal Service to use its services for my one-ounce First

Class mail - in fact I have yet to see one. However, First Class mailers get to pay the bulk of this $169 million advertising expense, as they pay the lion's share of institutional costs.

As for direct advertising mailers, they are charged with a whopping $1.5 million of that advertising expense (0.6% of the total). Tr. 4702. According to witness Takis, advertising directed to "direct mail" or "advertising mail" can refer to more than one subclass, so the costs are not assigned to any class, Tr. 4703, which means in reality the costs are predominately borne by First Class mailers. I think we all understand that pitches for more advertising mail, such as the fancy, multimedia collection discussed at Tr. 4783-85, is a pitch for Standard mail even though, of course, ads may be sent as First-Class mail. In fact, in my experience, the predominant use of First Class for advertising is by mailers that insert ads to "use up" their one ounce, a practice that produces greater postal costs without greater revenues.

F. Failure to Recognize Cost Difference Between Letters and Non-Letters

Even though there are substantial differences in the cost of handling flats compared with letters, the USPS has elected to pass through only 35% of the difference to mailers of ECR letters. Indeed, the differential at the basic level is 0%. Saturation flats are the most competitive of the ECR volumes, and anything that results in a more competitive rate for saturation flats seems to play well at the Postal Service.

The USPS in MC95-1 proposed no difference between letters and flats for the ECR subclass. It maintained that ECR mail was intended to be a category predominately for flats, so there should be no difference. The Commission rejected that reasoning and established a difference between the two. Now the USPS is intent on minimizing that difference. It tends to be quick to recognize discounts and cost factors (not to mention studies) that result in lower rates for saturation flats. Real cost data that would drive the rate for saturation flats higher tend to be ignored.

G. The Proposed Shape Surcharge

Once again the Postal Service has proposed a competitive rate shift that will cost it a little volume in exchange for a lot of volume. By a huge margin, most of the volume being carried outside the mailstream by alternate delivery is saturation or high density flats. This is a highly competitive type of mail, and it makes up most of the Postal Service's Standard ECR volume as well. That is where the volume and the dollars are.

Occasionally an alternate delivery company will carry a product sample, and even though such samples are important sources of revenue, they usually come no more frequently than once or twice a year. The flats, on the other hand, are distributed every single week and are the lifeblood of our industry. Our systems could not exist to deliver samples if we did not have to flats to deliver on a regular basis. In some more rural markets, there are rarely if ever product samples to deliver. In my own rural market in Northern Michigan, we deliver printed advertising every Saturday evening. In addition, several times during the year we do special deliveries in the middle of the week. We have delivered no parcels or samples for several years.

The Postal Service is now proposing a 10 cent surcharge for pieces that are neither letters nor flats. No doubt this will offset some of the proposed pound rate reduction for the odd-sized pieces, but alternate delivery companies are already getting quite a bit of sample business in the more major markets under the current rate structure. Therefore, with an appropriate pound rate, the surcharge is not necessary to assure fair competition at the higher weights. While a higher effective rate for product samples is appealing to alternate delivery, that appeal is lost if the surcharge is used to reduce an inadequate and anticompetitive pound rate.

As with the selective weight study, the surcharge proposal is competitively selective as well. It is interesting that the Postal Service does not differentiate between flats that are difficult to handle and those that are easy to handle, as it once did. Throughout the 1970s the Postal Service charged a lower third class rate for pieces that were "bound" than it charged for pieces that were clumsy to handle.

From my experience handling and delivering both, this distiction made good sense from a cost standpoint, but it didnt make sense from competitive standpoint. Loose, clumsy advertising was charged a higher rate, but it accounted for considerable volume that could be lost to alternate delivery. Bound catalogs were charged a lower rate, but they were pretty much low-volume, address specific matter not susceptible to a competitive threat. The favorable rate for bound third class mail was dropped in the early 1980s as the Postal Service became increasingly obsessed with competing and competition.

AAPS would be supportive of a surcharge that recognizes the difference between a bound catalog and a shared mail set containing several odd-sized slippery pieces that can fall all over the place when handled. Such a surcharge would be more appropriate in that it would at recognize the cost of handling all different kinds of ECR mail.

However, we're not holding our breath waiting for the Postal Service to conduct a shape study that explores the difficulty in handling some of the Postal Service's most competitively favored customers. Since the Commission directed the Postal Service fourteen years ago to study the weight issue, it has have yet to produce anything other than a competitive pretext.

AAPS therefore supports rejection of the surcharge in conjunction with significant increase in the pound rate.

VIII. AN APPEAL TO THE COMMISSION

As I have pointed out, the USPS was established by Congress as a public service. The Commission is instructed in numerous places in the Postal Reorganization Act to apply criteria to rates and classifications that protect mailers with no alternatives, consider the value of content of the mail, and consider the impact of rates on, among others, the USPS's competitors.

As I have also pointed out, the USPS does not view itself as Congress viewed it. While it insists on retaining all its advantages, it views itself as a competitor in the open market that should have every right to compete, with little restraint.

Unfortunately, the playing field will never be level under the present arrangement. Tens of billions in guaranteed business, tax exempt status, no profit margin, these all make for a very tilted playing field. In view of these USPS advantages, Congress has entrusted to the Commission the responsibility of making the playing field as level as possible.

We urge the Commission to apply all the criteria of the Postal Reorganization Act to this current rate proposal, and in particular, Criteria 3, 4, and 5 as they pertain to competitors of the Postal Service. Clearly the present proposal by the Postal Service utterly fails to consider Criteria 4 and 5, and its supporting studies cast doubt on Criterion 3 as well.

The Postal Service has become obsessed with competition. It has exploited its monopoly customers for competitive purposes. Our survival as an industry will largely be determined, over this and the next few rate cases, by the proper application of these ratemaking criteria.

We ask that the Commission recognize the USPS proposal to reduce a highly competitive rate for what it is - an overt attempt by the Postal Service to grab additional volumes from its competitors. We ask that the Commission, at the very least, maintain the present level of rate relationships, and that any new attempt to lower the highly competitive Standard ECR pound rates be denied. We don't want our demise to be the subject of the next Postmaster General speech.