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

POSTAL RATE AND FEE CHANGES, 2006: Docket No. R2006-1

REPLY OF THE McGRAW-Hill COMPANIES, INC TO PARTIAL OBJECTION OF TIME WARNER INC. TO MOTIONS OF AMERICAN BUSINESS MEDIA AND McGRAW-Hill TO COUNTER-DESIGNATE EVIDENCE FROM PRIOR DOCKET

The McGraw-Hill Companies, Inc. (McGraw-Hill) hereby replies to the Partial Opposition of Time Warner Inc. to Motions of American Business Media and McGraw-Hill to Counter-Designate Evidence From Prior Docket (Partial Opposition), filed by Time Warner on August 30, 2006.

Time Warner is mistaken in suggesting in its Partial Opposition that portions of the testimony of McGraw-Hill witness Schaeffer in Docket C2004-1 that McGraw-Hill has counter-designated pursuant to section 31(e) of the Rules of Practice for inclusion in the record of this proceeding,[1] in response to the August 9, 2006 Motion of Time Warner Inc. to Designate Evidence From Other Commission Dockets (Time Warner Motion), are somehow not relevant to the testimony of Time Warner witness Mitchell from Docket C2004-1 that Time Warner has so designated in the present proceeding (and/or to issues likely to be raised by witness Mitchell or other witnesses in related testimony to be filed in the present proceeding). The designated testimony of McGraw-Hill witness Schaefer in Docket C2004-1 is directly responsive to the designated

[1] See Motion of The McGraw-Hill Companies, Inc. to Counter-Designate Evidence From a Prior Commission Docket, filed August 23, 2006.

testimony of Time Warner witness Mitchell in that proceeding, as demonstrated point by point below, addressing each portion of the designated testimony of witness Schaefer which Time Warner seeks to exclude from the record in this proceeding.

1. Witness Schaefer testimony, page 5 (Tr. 1923) line 8 through page 7 (Tr. 1925) line 4; page 27 (Tr. 1945) line 23 through page 29 (Tr. 1947) line 9.

The above-referenced testimony of witness Schaefer explains why McGraw-Hill believes that the Commission should consider carefully the impact on smaller-circulation publications of any substantial de-averaging of Periodicals costs and rates, whether of the type proposed by Time Warner in Docket C2004-1 or otherwise. The testimony shows the diversity of the many McGraw-Hill publications, in terms of size of subscriber base[2] and otherwise, that in many ways mirrors the diversity of the Periodicals as a whole, and explains why McGraw-Hill has opposed cost and rate de-averaging that did not take appropriate account of the adverse impact on smaller-circulation publications, even though such de-averaging would result in net overall savings to McGraw-Hill:

> Due largely to their lower circulation, smaller publications already bear a substantially higher cost burden than larger-circulation publications, and would not likely be able to avoid onerous rate increases by changing their mailing practices. Beyond the adverse impact on most of McGraw-Hill's own publications (which must stand on their own financially), we are concerned that the extensive de-averaging of costs and rates proposed by Complainants would undermine maintenance of a broad, vibrant and diverse Periodicals class, and could bring into question its long-term viability. [Schaefer testimony, page 6 line 18 through page 7 line 1].

[2] Ranging from nearly one million subscribers to *Business Week* (which is 98% palletized and mostly sorted to carrier route and drop-shipped to DSCF) to the approximately 74,000 subscribers to *Engineering News Record* (which is less amenable to palletization, presortation and drop-shipping) to the handfuls of subscribers to highly specialized publications for the construction industry.

* * * *

> All Periodicals, regardless of the size of their distribution, contribute to the purpose of the class and the reasons for its preferential treatment. The Periodicals rate structure should therefore continue to accommodate a broad range of publications, not simply high-circulation/low cost publications. A rate structure that marginalized small publications could ultimately marginalize the Periodicals class itself and call into question its long-term viability. Generally speaking, therefore, it seems that rate averaging is to a considerable degree the glue that holds the class together, and the price for the preferential rates afforded the class as a whole – including both *Business Week* and Complainants' publications. [Schaefer testimony, page 29 lines 1 through 9].

This testimony of McGraw-Hill witness Schaefer (and his related impact testimony) is responsive to the designated testimony of Time Warner witness Mitchell advocating "[r]ates that are better aligned with . . . associated costs, as proposed in this Complaint" (page 18 lines 9-10), and asserting that "[t]he rates being proposed" would "giv[e] mailers more appropriate signals" (page 44 lines 10-11) because "[t]he proposed rates . . . align[] preparation decisions with the value of the service and its associated costs" (page 56 lines 6-8). Moreover, the designated testimony of witness Schaefer would certainly remain relevant to the designated testimony of witness Mitchell even if Time Warner were to propose in this case a somewhat modified version of the rates that it proposed in Docket C2004-1, which remains to be seen. The designated testimony of witness Mitchell presents the same foundation on which the highly de-averaged rates proposed in Docket C2004-1 were predicated, and the testimony of witness Schaefer is relevant to any proposed rate de-averaging that is predicated on such foundation. Just as Time Warner is accorded latitude, through the designated testimony of witness Mitchell, to advocate cost considerations as the primary basis for ratemaking for

Periodicals mail, McGraw-Hill should likewise be accorded latitude, through the designated testimony of witness Schaefer, to urge consideration of the impact of rate de-averaging on the maintenance of a broad, vibrant and diverse Periodicals class.

By no means is the designated testimony of witness Schaefer "largely predicated on the alleged effects on smaller publications of the elimination of the opportunity to engage in extensive use of 'skin sacks'" (Partial Opposition at 3), nor does Time Warner make any such assertion with respect to the testimony of witness Schaefer specifically. To the contrary, witness Schaefer testified in Docket C2004-1 that "[m]any McGraw-Hill publications have sack minimums set high at 24 pieces" (page 15 lines 1-2). Nor does Time Warner object to any designated testimony of witness Schaefer as focusing on Time Warner's proposal in Docket C2004-1 to replace the flat editorial pound charge with zoned editorial pound charges. See Partial Opposition at 4-5. That issue is not the focus of the designated testimony of witness Schaefer (even though the designated testimony of witness Mitchell presses that issue at pages 17-18 and pages 22-25).

2. Witness Schaefer testimony, page 7 (Tr. 1925) lines 6-15; page 9 (Tr. 1927) lines 2-6; page 11 (Tr. 1929) lines 8-14.

Time Warner objects to the following passages from the designated testimony of witness Schaefer:[3]

> IV. Complainants' Proposal Is Fundamentally Misdirected Because Smaller-Circulation Publications Have in Fact Borne the Brunt of the Cost Increases Upon Which the Complainants Focus.
>
> Testimony presented by witness Mitchell focuses on the inordinate rise in mail processing costs attributed to Periodicals since the late 1980's (Tr. 3/805-808) as the point

[3] Time Warner objects to designation of the unbracketed testimony below. The bracketed testimony below is presented for context. Time Warner has not objected to designation of the bracketed testimony.

of departure for Complainants' proposal in this proceeding to de-average Periodicals costs and rates, which would result in enormous savings to Complainants (without any change in their mailing practices, or any cost savings to the Postal Service) while exposing most smaller Periodicals to corresponding rate increases. [Schaefer testimony, page 7 lines 6-15].

* * * *

[Chart A makes clear that the constant-markup rates [over the period 1985-2002] for *Engineering News Record* exceeded the CPI-U by approximately twice as much as do the corresponding rates for *Business Week*. This indicates that smaller-circulation publications like *ENR*, rather than large-circulation publications like those of Complainants, have borne the brunt of the costs attributed to Periodicals since 1985. Moreover, the rate differential continues to grow at an alarming rate. Even more troubling, borrowing a phrase from witness Mitchell, the actual situation could become worse than the picture.**]**[4] The rate differential would widen significantly under the proposed rate structure, with *Business Week* experiencing an 11% decrease in rates and *Engineering News Record* a 13% increase. Even if *ENR* were able to take steps to mitigate some of the increase, as the Complainants suggest, the rate disparity would still grow considerably. [Schaefer testimony, page 9 lines 2-6 (emphasis in original)].

* * * *

[…Chart B above makes clear that the actual aggregate postage increases incurred since 1985 by *Business Week* – and presumably other high circulation publications like those of Complainants – have *not* generally exceeded the CPI-U, while smaller-circulation publications like *ENR* have incurred aggregate postage increases nearly *double* the CPI-U. Indeed, the increase for at least some of Complainants' publications appears to be well *below* the rate of inflation, and under the proposed**]**[5] rates, their postage will have *decreased* over the past decade.

In this light, the remedy advocated by Complainants – a radical de-averaging of Periodicals rates that would provide

[4] See note 3, supra.

[5] See note 3, supra.

> an enormous windfall to a relatively few large-circulation publications such as those of Complainants, even with no change in their mailing practices, while exposing most smaller-circulation publications to corresponding rate increases – seems wholly misaligned with the chronic problem of above-inflation cost increases attributed to Periodicals mail that Complainants purport to address. [Schaefer testimony, page 11 lines 8-14 (emphasis in original) (footnotes omitted)].

This testimony directly rebuts to the designated testimony of witness Mitchell (pages 8-11), which points to the inordinate cost attribution to Periodicals mail as a whole over the years as justification for extensive de-averaging of Periodicals costs and rates that would greatly benefit large-circulation publications and commensurately burden smaller-circulation publications. As demonstrated by witness Schaefer, extensive de-averaging is an inappropriate response to the problem because it would impose an even greater burden on smaller-circulation publications that are already bearing the brunt of the inordinate cost attribution over the years, and already pay much higher rates per piece than large-circulation publications. This designated testimony of witness Schaefer does not focus on the "specific rate schedule proposed in C2004-1" (Partial Opposition at 3), but rather on the disparate rate burden borne by smaller-circulation publications historically.

While Time Warner indicates that it will advocate a "substantially different rate proposal" in this proceeding (id.), that remains to be seen. The designated testimony of witnesses Mitchell and Stralberg indicate that Time Warner will propose largely the same rate structure that it proposed in Docket C2004-1. See also Time Warner Motion at 2. Even if the benefit to large-circulation publications, and the corresponding burden on smaller-circulation publications, may be somewhat less under Time Warner's

forthcoming proposal, the designated testimony of witness Schaefer would remain relevant, given the disproportionate cost burden borne by smaller-circulation publications over the years. The Commission is certainly capable of placing this testimony in appropriate context to the extent that Time Warner may propose somewhat different rates in this proceeding than it proposed in Docket C2004-1.

3. Witness Schaefer testimony, page 16 (Tr. 1934) line 24 through page 19 (Tr. 1937) line 10.

The above-referenced testimony of witness Schaefer demonstrates that to the extent that co-mailing or co-palletization may be a feasible option for some publications, the added costs that would thereby be incurred by such publications (generally amounting to at least one-half the postage saved by co-mailing or co-palletization) should be considered as part of the potential impact of proposed rate increases – an issue that will doubtless be important in considering Time Warner's forthcoming proposals in this proceeding. Witness Schaefer pointed out that witness Mitchell had overlooked such costs, which undermines the theme in the designated testimony of witness Mitchell (pp. 9, 11. 14 16 18, 44, 56) that de-averaging postal costs and rates would broadly "improve the lot of publishers", including smaller-circulation publications.

Witness Schaefer illuminated the importance of the costs of co-mailing and co-palletization in this regard by incorporating them into a hypothetical presented by witness Mitchell which purported to show the extent to which a smaller-circulation publication could mitigate the impact of the rates proposed in Docket C2004-1. The contrary analysis of witness Schaefer -- based on costs of co-mailing or co-palletization that generally amount to one-half the postage saved by co-mailing or co-palletization --

is equally applicable to analyzing the impact of any proposed rate increase on any smaller-circulation publication. By no means is the testimony of witness Schaefer rendered irrelevant by the fact the Time Warner may propose different rates in this proceeding than it proposed in Docket C2004-1.

4. Witness Schaefer testimony, page 24 (Tr. 1942) line 5 through page 25 (Tr. 1943) line 16.

The above-referenced testimony of witness Schaefer, based on his "long experience with the practical aspects of optimizing mail streams of Periodicals publications in terms of postage and delivery-speed as well as manufacturing and distribution costs", addresses the complexity that would be created by the *rate structure* proposed by witness Mitchell in Docket C2004-1. Time Warner has indicated that it will propose a similar rate structure in this proceeding based on the designated testimony of both witness Mitchell and witness Stralberg. See Time Warner Motion at 2. Indeed, the primary focus of that testimony is to lay the foundation once again for a proposed rate structure that includes (in addition to piece and pound charges) an array of bundle charges based on the presort level of both the bundle and its container, as well as an array of container charges based on container type, the presort level of the container, and its entry point. The testimony of witness Schaefer regarding the complexity of such *rate structure* is not at all affected by the fact that Time Warner may propose, within such rate structure, different rates than it did in Docket C2004-1.

In particular, witness Schaefer pointed out that under such rate structure, "files would need to be presorted with various parameters numerous times to determine the optimal balance of service and cost" and that "[m]ail.dat software, which is extensively

used for mail planning today, would be of little value for this type of optimization" because "[i]t is not possible . . . to use a mail.dat file to vary the number of copies in a bundle – the key cost driver under the proposed rate structure." Witness Schaefer concluded this portion of his testimony by stating that while "[l]arge mailers may be able to marshal the resources and expertise needed to undertake optimization of their Periodicals mailings" under the proposed rate structure, "I question whether small mailers would be able to do so." The designated testimony of witness Schaefer in this regard remains quite relevant to the rate structure that Time Warner has indicated that it will again propose in this proceeding based on the designated testimony of Time Warner witnesses Mitchell and Stralberg.

CONCLUSION

For the foregoing reasons, the Partial Objection of Time Warner lacks any merit as to the Motion of The McGraw-Hill Companies, Inc. to Counter-Designate Evidence From a Prior Commission Docket, which should be granted in full. McGraw-Hill likewise

supports the Motion of American Business Media for Counter-Designations of Evidence From a Prior Docket (filed August 23, 2006).

Respectfully submitted,

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