

005894 ORIGINAL

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

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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

SPECIAL SERVICES REFORM, 1996

Docket No. MC96-3

RESPONSE OF UNITED STATES POSTAL SERVICE TO PRESIDING OFFICER'S
INFORMATION REQUEST NO. 5, QUESTION 1
(November 15, 1996)

The United States Postal Service hereby provides a response to Presiding Officer's Information Request No. 5, question 1, issued on November 13, 1996. The response to question 2 will follow.


The question is stated verbatim and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.
Chief Counsel, Ratemaking


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November 15, 1996

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BTP

Answer of Richard Patelunas to
Presiding Officer's Information Request No. 5
to United States Postal Service

POIR No. 5 Question 1.

Evaluation of cost coverages requires reliable cost, revenue, and volume estimates. While cost coverage is the ratio of revenue to attributable cost for a particular subclass or service, volume is an input to both variables and thereby affects coverage. In particular, revenue and cost estimates must be based on the same volume measure in order to have meaningful coverages. The aim of this Presiding Officer Information Request is to clarify the record concerning the cost coverages for Certified Mail Service.

a. Please confirm that attributable costs of \$281,429,000 presented in Exhibit USPS-T-5A, page 8, for the Base Year FY 1995, are "pure" certified costs using the Postal Service's proposed attribution methodology; i.e., the costs do not include any costs for any other mail or special service, such as for merchandise return receipt. If not confirmed, please identify what other costs were included and how they were derived.

b. Is the Certified Mail Service costing approach reflected in your answer to a. above consistent with the approach presented in the most recent omnibus rate request, Docket No. R94-1? If not, please discuss all of the differences.

POIR No. 5 Question 1 Response.

a. Confirmed.

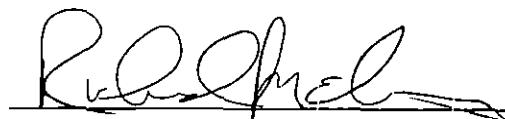
b. Assuming that the question is asking whether or not the Certified

Mail Service costs presented in Docket No. R94-1 were "pure" as defined in part

a.; the answer is yes, they were pure in Docket No. R94-1.

DECLARATION

I, Richard Patelunas, declare under penalty of perjury that the foregoing answers are true and correct, to the best of my knowledge, information, and belief.

A handwritten signature in cursive script, appearing to read "Richard Patelunas", is written over a horizontal line.

Dated: 11-15-96

Answer of W. Ashley Lyons to
Presiding Officer's Information Request No. 5
to United States Postal Service

POIR No. 5 Question 1 (Parts c., d., e., f., g., h., and i.)

Evaluation of cost coverages requires reliable cost, revenue, and volume estimates. While cost coverage is the ratio of revenue to attributable cost for a particular subclass or service, volume is an input to both variables and thereby affects coverage. In particular, revenue and cost estimates must be based on the same volume measure in order to have meaningful coverages. The aim of this Presiding Officer Information Request is to clarify the record concerning the cost coverages for Certified Mail Service.

c. Please confirm that the FY 1995 billing determinants show that pure certified mail volumes for Base Year FY 1995 are 266,431,397 and that certified mail plus return receipt volumes are 288,826,806. Tr. 2/272.

d. Please confirm that the projected Test Year FY 1996 Before and After Rate volumes of 289,613,000 (Exhibit USPS-T-5G, page 23) and 277,803,000 (USPS-T-1, WP D, page 1), respectively, are derived from the use of forecasted Certified Mail Service volumes for Base Year FY 1995, i.e., 279,028,000 (Exhibit USPS-T-5D).

e. If the response to c. above confirms that 266,431,397 represents actual FY 1995 pure Certified Mail Service volume, please discuss the proposition that a Test Year volume forecast based on this pure Base Year volume would be more accurate than the result achieved using a forecasted volume of 279,028,000 for the Base Year.

f. If available, please provide the projected Test Year volumes when billing determinant volume for Base Year FY 1995 Certified Mail, i.e., 266,431,397, is used as the starting point.

g. If the estimate requested in f. above is not available, please provide an estimate of the differences that result in both the before and after rate Test Year volumes from the use of the two different starting point (billing determinants of 266,431,397 versus the forecasted number of 279,028,000).

h. If the number requested in f. above is not available, please provide an estimate of the time required to produce the forecasted Test Year volumes starting from the billing determinant volume for Base Year Certified Mail Service.

i. Please discuss the appropriateness of an adjustment of the test year volumes to reflect actual FY 1995 certified mail billing determinants. One possible adjustment would be multiplying billing determinant volume by the ratio of currently forecasted test year volume to forecasted base year volume, i.e., $(266,431,397) \times (289,613,000 / 279,028,000)$. Table 1, lines 1, 2 and 3, present the unadjusted numbers currently on the record and lines 4 through 8 present the results of this adjustment. Please comment on the reasonableness of using the Table 1 numbers in this docket. If problems are identified with

Table 1, please provide a superior method of developing an adjustment to reflect billing determinants and pure certified mail numbers.

RESPONSE:

c. Confirmed.

d. Confirmed.

e. The question posed in this subpart raises many types of concerns. To begin with one of the most general concerns, the subpart seeks a reaction to the proposition that one forecast "would be more accurate" than another forecast. Until actual historical data become available, however, it will be impossible to determine which forecast "would be more accurate." Between two competing prospective forecasts, however, it certainly may be possible to state that one forecast can reasonably be expected to be more accurate.

As another general matter, the question poses a contrast between a base volume which is based entirely on actual historical data, and a base volume which includes an element of forecasted data. In general, the most recent information, which is to say, the base volume based entirely on actual historical data, would be expected to generate the more accurate forecast. However, this general principle has not been relied upon as a blanket excuse, in the absence of other factors, to justify wholesale updating of inputs in ongoing proceedings. Selective updating, on the other hand, can also cause problems.

Moving to more specific concerns, while this subpart inquires about the accuracy of a "Test Year volume forecast," it is somewhat unclear with regard

to the question, Test Year volume forecast of what? As a general proposition, it would seem to be correct to expect that a volume forecast of pure Certified Mail would be more accurate if based on a base volume of pure Certified Mail and applied to a forecasting model designed to forecast pure Certified Mail volume, than if based on a larger aggregation of Certified Mail Service volume, applied to the same model. Conversely, however, if the object of the exercise is a volume forecast of aggregate Certified Mail Service, a base volume of aggregate Certified Mail Service applied to a model designed to forecast aggregate volume for Certified Mail Service would reasonably be expected to result in a more accurate forecast.

Although I am not a forecasting expert, I understand that other concerns arise if one tries to go beyond the above generalities. Forecasting models are designed for a particular level of aggregation. There may be any number of factors at work which determine what level of aggregation is appropriate. I am informed, for example, that availability of a sufficient amount of disaggregated data, and possible substitutions back and forth between disaggregated categories, are factors which might be considered. To the extent that I understand the question posed in this subpart, it appears to involve issues of the optimal level of aggregation (aggregate Certified Mail Services or pure Certified Mail volume). A far greater amount of analysis than is possible under the existing time constraints would be required to properly consider all of the potential ramifications of such an exercise.

- f. No such estimate is available.
- g. Without the actual estimate requested in subpart f., it is difficult to provide the further estimate requested in this subpart. One source of difference would be the lower base volume (266,431,397 vs. 279,028,000). A lower base volume would be expected to lower the forecasts. In general, it would appear that subpart i. suggests a more fruitful line of inquiry than this subpart. Please see the response to subpart i.
- h. As explained in response to subpart e. above, what appears to be requested may not necessarily be an appropriate application of the existing forecasting model. While the logistics of inputting different numbers and running the model again are not that difficult, and probably could be done within a week, such an exercise does not appear to be warranted, given the available alternative set forth in subpart i.
- i. The approach suggested in Table 1 makes the reasonable assumption that, everything else being equal, the growth rate developed in the initial forecast may be applied to the actual FY 1995 Certified Mail billing determinants. Without the benefit of any additional information, this adjustment arguably puts the available information to its best use.

TABLE 1

**DEVELOPMENT OF ATTRIBUTABLE UNIT COST FOR CERTIFIED MAIL
USING POSTAL SERVICE COSTING METHODOLOGY (000)**

Item	FY 1994	FY 1995	TYBR	TYAR
Unadjusted Volumes:				
1 Attributable Cost	\$ 277,437	\$ 281,429	\$ 297,811	\$ 285,880
2 Transaction Volumes	234,776	266,431	289,613	277,803
3 Attributable Unit Cost	\$ 1.182	\$ 1.056	\$ 1.028	\$ 1.029
Adjusted Volumes:				
4 Attributable Cost	\$ 277,437	\$ 281,429	\$ 297,811	\$ 285,880
5 Adjusted Transaction Volumes	234,776	266,431	276,538	265,261
6 Attributable Unit Cost	\$ 1.182	\$ 1.056	\$ 1.077	\$ 1.078
7 Certified Mail Fee	\$ 1.00	\$ 1.10	\$ 1.10	\$ 1.50
8 Cost Coverage (L.7/L.6)	84.6%	104.1%	102.1%	139.2%

Source for Unadjusted Amounts:

FY 1994 attributable cost from FY 1994 Cost Segments and Components, p 8
 FY 1994 transaction volumes from FY 1994 CRA, p.16 or FY 1994 Billing Determinants, K-1
 FY 1995 attributable cost from Exhibit USPS-T-5A, p. 8
 FY 1995 transaction volumes from USPS-T-1, WP D, page 1
 TYBR attributable cost from Exhibit USPS-T-5E, p.8
 TYBR transaction volumes from USPS-T-1, WP D, page 1
 TYAR attributable cost from Exhibit USPS-T-5H, p.8
 TYAR transaction volumes from USPS-T-1, WP D, page 1
 Fees from USPS-T-8 at 65

Source For Adjusted Amounts:

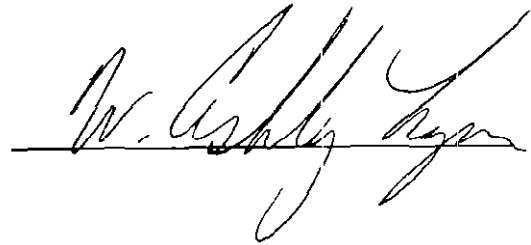
- (1) Attributable costs are not adjusted and come from line 1
- (2) FY 1994 and FY 1995 volumes are not adjusted and come from line 2
- (3) TYBR and TYAR volumes are adjusted; See table below

Development of Adjusted TYBR and TYAR Volumes

Item	Source	Amount
(a) Roll Forward Base Year Volume	Exhibit USPS-T-5D	279,028
(b) Roll Forward TYBR Volume	Exhibit USPS-T-5G, p.23	289,613
(c) Roll Forward TYAR Volume	USPS-T-1, WP D, page 1	277,803
(d) Ratio. TYBR to Base Year	(b) / (a)	1.037935
(e) Ratio. TYAR to TYBR	(c) / (b)	0.959221
(f) Base Year Billing Determinants	USPS-T-1, WP D, page 1	266,431
(g) Adjusted TYBR Billing Determinants	(d) x (f)	276,538
(h) Adjusted TYAR Billing Determinants	(e) x (g)	265,261

DECLARATION

I, W. Ashley Lyons, declare under penalty of perjury that the foregoing answers are true and correct, to the best of my knowledge, information, and belief.

A handwritten signature in cursive script, appearing to read "W. Ashley Lyons", is written over a horizontal line.

Dated: 11-15-96

CERTIFICATE OF SERVICE

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


Susan M. Duchek

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November 15, 1996