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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

USPS-T-34

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

POSTAL RATE AND FEE CHANGES, 1997

Docket No. R97-1

DIRECT TESTIMONY
OF
ALTAF H. TAUFIQUE
ON BEHALF OF
UNITED STATES POSTAL SERVICE

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AUTOBIOGRAPHICAL SKETCH

My name is Altaf H. Taufique. I am an economist in the office of Pricing at the United States Postal Service. I first appeared before this Commission in December 1996 as a rebuttal witness during the special services reform case, Docket No. MC96-3. Prior to joining the Postal Service, I was employed by Gulf States Utilities (GSU) in Beaumont, Texas from 1980 to 1994. At GSU, I served as an economic analyst in the Corporate Planning department and was subsequently promoted to Economist, Senior Economist and finally to the position of Director, Economic Analysis and Forecasting. My responsibilities at GSU included the preparation of the official energy, load and short-term revenue forecasts, and the economic forecasts for the regions served by the Company. I have testified before the Public Utility Commission of Texas in Austin and the Federal Energy Regulatory Commission in Washington, D.C. My testimony defended GSU's energy and load forecasts.

I received a Master's Degree in Economics from Central Missouri State University in Warrensburg, Missouri in 1976, and a Bachelor's Degree in Economics and International Relations from Karachi University in Karachi, Pakistan. I have also completed thirty-three credit hours of course work towards a Ph.D. in Economics at Southern Illinois University. I taught economics at Chadron State College in Chadron, Nebraska between 1978 and 1980, and during my employment at GSU in Texas, I taught courses in economics at Lamar University in Port Arthur, Texas.

1 **I. PURPOSE**

2 The purpose of my testimony is to present the Postal Service's rate and
3 classification proposals for the Regular Rate and Within County Periodicals subclasses.
4 My testimony begins with proposal highlights, which include the proposed rates for both
5 Regular and Within County subclasses, followed by a short description of the
6 characteristics of these subclasses, and a summary of recent changes that have taken
7 place in these subclasses. I then discuss the classification change proposed for these
8 subclasses, which consists of splitting the existing 3/5-digit rate category into 3-digit and
9 5-digit rate categories. Finally, my testimony presents the rate design methodology
10 employed for the two subclasses.

11
12 **II. PROPOSAL HIGHLIGHTS**

13 The average price changes for the classes are as follows¹:

14
15 **Table 1**

	TEST YEAR RATES COMPARISON		
	Current	Proposed	Percent
	Avg.\$/Piece	Avg.\$/Piece	Change in Rates
Regular Rate	\$ 0.226	\$ 0.234	3.5%
Within County	\$ 0.089	\$ 0.092	3.4%

16

¹ The average rates do not include fees. Within County rates are phase 5 rates applicable in the test year.

1

Tables II through IV present the proposed rates.

TABLE II - REGULAR RATE	Proposed Rates
Pound Rates	
ZONED ADVRTSG DELIVERY UNIT	\$ 0.158
ZONED ADVRTSG SCF	\$ 0.180
ZONED ADVRTSG ZONES 1&2	\$ 0.203
ZONED ADVRTSG ZONE 3	\$ 0.216
ZONED ADVRTSG ZONE 4	\$ 0.251
ZONED ADVRTSG ZONE 5	\$ 0.305
ZONED ADVRTSG ZONE 6	\$ 0.361
ZONED ADVRTSG ZONE 7	\$ 0.416
ZONED ADVRTSG ZONE 8	\$ 0.474
NONADVERTISING	\$ 0.174
Piece Rates	
BASIC NON-AUTOMATION	\$ 0.263
BASIC AUTOMATION LETTER	\$ 0.182
BASIC AUTOMATION FLAT	\$ 0.221
NON-AUTOMATION 3-DIGIT	\$ 0.217
AUTOMATION 3-DIGIT LETTER	\$ 0.166
AUTOMATION 3-DIGIT FLAT	\$ 0.188
NON-AUTOMATION 5-DIGIT	\$ 0.214
AUTOMATION 5-DIGIT LETTER	\$ 0.162
AUTOMATION 5-DIGIT FLAT	\$ 0.186
CARRIER ROUTE BASIC	\$ 0.128
CARRIER ROUTE HIGH DENSITY	\$ 0.116
CARRIER ROUTE SATURATION	\$ 0.102
PERCENTAGE EDITORIAL DISCOUNT	\$ (0.059)
DISCOUNT FOR DELIVERY OFFICE ENTRY	\$ (0.023)
DISCOUNT FOR SCF ENTRY	\$ (0.012)

1

TABLE III - WITHIN COUNTY - Full	Proposed Rates
Pound Rates	
ZONED ADVRTSG DELIVERY UNIT	\$ 0.117
GENERAL	\$ 0.131
Piece Rates	
BASIC NON-AUTOMATION	\$ 0.090
BASIC AUTOMATION LETTERS	\$ 0.063
BASIC AUTOMATION FLATS	\$ 0.078
NONAUTOMATION 3-DIGIT	\$ 0.080
AUTOMATION 3-DIGIT LETTER	\$ 0.061
AUTOMATION 3-DIGIT FLAT	\$ 0.066
NONAUTOMATION 5-DIGIT	\$ 0.077
AUTOMATION 5-DIGIT LETTER	\$ 0.059
AUTOMATION 5-DIGIT FLAT	\$ 0.063
CARRIER ROUTE	\$ 0.045
HIGH DENSITY	\$ 0.040
SATURATION	\$ 0.038
DISCOUNT FOR DELIVERY OFFICE ENTRY	\$ (0.004)

2

TABLE IV - WITHIN COUNTY - Phase 5	Proposed Rates
Pound Rates	
ZONED ADVRTSG DELIVERY UNIT	\$ 0.117
GENERAL	\$ 0.130
Piece Rates	
BASIC NON-AUTOMATION	\$ 0.090
BASIC AUTOMATION LETTERS	\$ 0.062
BASIC AUTOMATION FLATS	\$ 0.077
NONAUTOMATION 3-DIGIT	\$ 0.079
AUTOMATION 3-DIGIT LETTER	\$ 0.060
AUTOMATION 3-DIGIT FLAT	\$ 0.066
NONAUTOMATION 5-DIGIT	\$ 0.076
AUTOMATION 5-DIGIT LETTER	\$ 0.058
AUTOMATION 5-DIGIT FLAT	\$ 0.062
CARRIER ROUTE	\$ 0.044
HIGH DENSITY	\$ 0.040
SATURATION	\$ 0.038
DISCOUNT FOR DELIVERY OFFICE ENTRY	\$ (0.004)

1 **III. CHARACTERISTICS**

2 Periodicals mail consists of a wide range of periodical publications, principally
3 magazines, newspapers, newsletters and bulletins. Most of these contain both
4 advertising and non-advertising material. The non-advertising material is commonly
5 referred to as "editorial" content, which gives Periodicals mail its high educational,
6 cultural, scientific, and informational value.

7 The Periodicals class is divided into four subclasses: 1) Regular Rate, which is
8 intended for commercial publications (with the exception of Science of Agriculture
9 publications); 2) Within County; 3) Nonprofit, and 4) Classroom. The last three are
10 preferred rate subclasses and are entitled to lower cost coverages by law.

11 Through 1993, full rates for preferred rate subclasses had been set with a 100
12 percent target test year coverage. Additional revenues were to be appropriated to the
13 Postal Service by the Congress to maintain a cost coverage below that for commercial
14 (i.e. Regular) rate to compensate for the revenue forgone. As a result of the Revenue
15 Forgone Reform Act of 1993 (RFRA), Nonprofit , Classroom and Within County mail
16 now pay phased rates, based on a cost coverage that rises in six steps, until the
17 markup is one-half the markup on Regular Rate mail. The phasing schedule began in
18 1994 and operates through 1999. My testimony presents Within County rates for phase
19 6 (1999) based on full markup (50 percent of Regular Rate). I also, for informational
20 purpose only, present phase 5 rates. Witness Kaneer (USPS-T-35) proposes rates for
21 Nonprofit and Classroom.

1 **IV. Volume, Revenue and Rate History - Regular Rate and Within County**

2 Witness Tolley (USPS-T-2) provides a detailed description of the volume
3 fluctuations and factors affecting the volume forecast for the Regular Rate subclass.
4 Library Reference H-187 also provides the volume and revenue history from 1970 to
5 1996. From its peak of 6,996 million pieces in 1991, Regular Rate volume declined in
6 1992, then showed a gradual increase to 6,984 million pieces in FY1996. The
7 compound annual growth rate between FY1992 and FY1996 was 1.3 percent. Annual
8 revenue growth for the same period was 4.2 percent, and revenue per piece grew from
9 \$0.202 to \$0.226, a compound annual growth rate of 2.8 percent.

10 Within County mail volume has been on a steady decline since its peak in 1985.
11 As Witness Tolley discusses in his testimony, the reasons for this decline include price
12 increases in 1986 and 1987, and changes in sampling procedures and eligibility
13 regulations.

14 **V. CLASSIFICATION CHANGES**

15 Section 3623 (c) of Title 39, United States Code requires that classification
16 changes be made in accordance with the following factors:

- 17 1. The establishment and maintenance of a fair and equitable classification
18 system for all mail;
- 19 2. the relative value to the people of the kinds of mail matter entered into
20 the postal system and the desirability and justification for special
21 classifications and services of mail;
- 22 3. the importance of providing classifications with extremely high degrees of
23 reliability and speed of delivery;
- 24 4. the importance of providing classifications which do not require an
25 extremely high degree of reliability and speed of delivery;
- 26
- 27
- 28
- 29

1 5. the desirability of special classifications from the point of view of both the
2 user and the Postal Service; and

3
4 6. such factors as the Commission may deem appropriate.

5
6 I have evaluated the change proposed for Periodicals Regular Rate and Within
7 County and concluded that they satisfy these criteria.

8
9 **A. 3-Digit / 5-Digit Rate De-averaging**

10 I propose to split the 3/5-digit classification into separate 3-digit and 5-digit
11 classifications to better reflect costs in the piece rate design. The plan is to include
12 pieces sorted to non-unique 3-digit ZIP codes in the proposed 3-digit classification.
13 Currently, non-unique 3-digit ZIP codes are included in the basic (required) presort
14 category. Under this proposal, all Periodicals subclasses will have 3-digit and 5-digit
15 piece rates for both letters and flats for automation compatible mail.

16 This proposed change in classification is consistent with classification criterion 1
17 since it provides a fair and equitable allocation of costs based on the work actually done
18 by the mailers in presorting their mail. Also, mailers providing mail sortation to non-
19 unique 3-digit locations would qualify for a rate that better reflects their worksharing
20 efforts. Criterion 5 is satisfied because this classification change is desirable from the
21 point of view of both the Postal Service and its customers. The value to the Postal
22 Service customer, sorting to 3-digit ZIP Code prefixes, is more fully reflected in the rate
23 schedule, thereby recognizing customer efforts. The Postal Service receives a benefit in
24 terms of cost savings by providing an increased incentive for mailers to presort to the 3-
25 digit level.

1 The Postal Service in Docket No. MC95-1 proposed creating Regular and
2 Publications Service subclasses for regular rate periodicals “to recognize the cost and
3 market characteristics of low cost, high-workshare mail.”² Given the context of that
4 proposal, the Postal Service retained a combined 3/5-digit rate for Regular, and
5 compressed the presort tiers even more for the proposed Publications Service
6 subclass. The Commission, however, did not recommend the proposed split in the
7 existing Regular Rate subclass.

8 The current proposal attempts to recognize low cost, high-workshare mail by
9 splitting the 3/5-digit presort tier, and shifting the non-unique 3-digit mail from Basic to
10 the 3-digit presort tier. The choice of passthroughs in this proposal for these resulting
11 cost savings is a deliberate attempt to mitigate the “rate shock” effect on the higher cost
12 presort tiers. I will address the 3/5-digit split and the non-unique 3-digit shift separately.

13 **B. 3/5 Split**

14 MPA witness Cohen in her direct testimony in Docket No. MC95-1, criticized the
15 Postal Service for not recognizing mailer worksharing efforts:

16 There is one area in which I feel that Pickett’s proposal fails to provide
17 adequate recognition of degree of preparation. In his rate design for the
18 Publications Service subclass, Pickett collapsed the presort tiers (levels A,
19 B, C) to two, basic and carrier-route, apparently to simplify the rate
20 structure. (USPS-T-19, p.12) In the regular subclass, Pickett retains the
21 three presort categories, but moves non-unique 3-digit mail from Level A
22 to Level B.

23
24 I think that the Postal Service is moving in the wrong direction in
25 collapsing presort categories. To provide adequate recognition of the
26 degree of presortation and its effect upon reducing costs to the Postal

² Docket No. MC95-1, USPS-T-19, p. 1

1 Service, it really should have four presort categories in both subclasses:
2 basic, 3-digit, 5-digit, and carrier-route.³
3

4 In light of the Commission's rejection of the proposed Publications Service
5 subclass in Docket No. MC95-1, the Postal Service believes that expanding the number
6 of presort tiers is a better mechanism to reflect postal operations in postal rates.
7

8 **C. Shift of Non-Unique 3-Digit Mail from Basic to 3-Digit tier**

9 In its opinion in Docket No. MC95-1, the Commission stated the following, with
10 regard to the change in the presort tiers:

11 Preoccupation with the ramifications of the Publications Service proposal
12 appears to have overtaken deliberate review of the presort changes in the
13 Regular subclass. There was little meaningful discussion on this record
14 about the consequences of the redefinition of the presort tiers."⁴
15

16 In rejecting the proposal for elimination of the existing unique 3-digit makeup
17 requirement, the Commission relied on the argument that the shift of the non-unique 3-
18 digit tier from level A or Basic presort would leave a much smaller volume in the Level A
19 or Basic category. With regard to this volume, the Commission stated:

20 This is a very small proportion, and gives rise to questions whether this
21 volume should become the benchmark for discounts for the subclass.
22 Accurate cost tracking, in particular, could become a problem. Given
23 these concerns, the Commission recommends retention of the current
24 presort tiers at this time; the question of whether they should be
25 expanded, perhaps along the lines suggested by MPA witness Cohen, or
26 constricted, as proposed by the Service, deserves further study.⁵
27

³ Docket No. MC95-1, Tr. 15/6759

⁴ PRC Opinion and Recommended Decision, Docket No. MC95-1, V-139

⁵ Ibid. V139-140

1 The costs that witness Seckar (USPS-T-26) develops in this case, as inputs to
2 the ratemaking exercise, are not dependent upon mail volume within the benchmark or
3 any other category. Specifically, witness Seckar states:

4 In summary, piece distribution; bundle sorting; and in turn, volume
5 variable mail processing costs are developed using wage rates,
6 productivities, and other inputs in a manner essentially independent of the
7 mail volume."⁶
8

9 In accordance with this assessment, the volume in the Basic or any other presort
10 category should not affect the reliability of the costs for the category.

11 The Governors' Decision in Docket No. MC95-1 also addressed the issue of
12 non-unique 3-digit ZIP Codes. The Decision stated:

13 In particular, witnesses explained to the Commission that today's
14 operations plans do not distinguish among the 3-Digit ZIP Codes in the
15 manner prescribed in the old rate schedule. Under that schedule, second-
16 class mail, when prepared to 5-Digit ZIP Codes, and to what are called
17 unique 3-Digit cities, is charged one rate. When prepared to all other 3-
18 Digit ZIP codes, this mail is charged another, higher rate. Today the cost
19 incurrence is the same, whether the 3-Digit ZIP Code represents a city, or
20 any other geographical area.⁷
21

22 Therefore, the Postal Service believes that non-unique 3-digit mail should be included
23 in the 3-digit ZIP Code presort tier.

24 **D. Methodology for Determining the TYAR Volumes - 3/5 Split and Non-Unique 3- 25 Digit Shift**

26
27 The Billing Determinants for TYBR and TYAR were determined using the mail
28 characteristics study provided in Library Reference H-190, and the base year (FY1996)
29 Billing Determinants. The mail characteristics study provided Regular Rate mail pieces

⁶ USPS-T-26

⁷ Decision of the Governors on Docket No. MC95-1, p. 15

1 by container type and presort level, and within each container type, by package presort
2 level. Each such breakdown was further divided between mail bearing barcodes and
3 mail that did not bear barcodes.

4 The mail characteristics study was used to determine the percentages of mail
5 volume qualifying for the new rate categories. For example, the total amount of
6 nonautomation rate mail was determined from the mail characteristics study. This total
7 volume of nonautomation rate mail was then distributed to the new rate categories
8 based on the package level, and where appropriate, the container level. The
9 percentage of nonautomation mail at each of the new rate categories, based on the
10 total volume of mail from the mail characteristics study, was then applied to the total
11 amount of nonautomation mail from the base year Billing Determinants. The same
12 process was used to distribute the volume of mail to each new automation rate
13 category. The carrier route (basic, high density and saturation) and letter categories
14 were not affected by this shift, and retained the same relative volumes as the base
15 year. Following are additional criteria that were used when distributing mail volume to
16 rate categories using the mail characteristics study.

17 Since firm packages do not qualify for barcode rates, and there are no carrier
18 route barcode rates for Periodicals, any firm and carrier route packages or sacks that
19 were recorded as bearing barcodes in the mail characteristics study were removed from
20 barcoded mail categories and shifted to comparable cells on the non-barcoded side to
21 better reflect the rates for which the pieces qualified. In addition, since optional city is
22 no longer a valid presortation category, mail recorded as being prepared in optional city

1 packages and sacks in the mail characteristics study was assumed to now be prepared
2 in 3-digit packages and sacks.

3 Automation (barcode) rate flats currently qualify for presort rate levels based on
4 the presort level of the package in which the pieces are contained, regardless of the
5 presortation level of the sack or pallet in which the package is placed. Accordingly, the
6 volume of mail distributed to the various new automation flat rates was based on the
7 presortation level of the package, regardless of the outer container in which the
8 package was placed. Nonautomation rate flats that are prepared on pallets currently
9 qualify for presort rate levels based on the presort level of the package in which the
10 pieces are contained. Accordingly, the volume of mail distributed to the various new
11 nonautomation rate categories for mail prepared on pallets was based on the presort
12 level of the package. Nonautomation rate flats prepared in sacks currently qualify for
13 presort rate levels based on the presortation level of the sack in which the packages
14 are contained. Therefore, the volume of mail distributed to the various new
15 nonautomation rate categories for sacked mail was based on the presortation level of
16 the sack.

17 Under all preparation methods, there currently must be a minimum of 6 pieces in
18 a package for an individual carrier route, individual 5-digit, or qualifying individual 3-digit
19 destination (unique 3-digit currently, all 3-digits under the proposed new rates) to qualify
20 for carrier route rates, or 3/5-digit rates (or 5-digit or 3-digit rates under the proposed
21 new rates), respectively. A firm package by itself is considered one piece for rate
22 application purposes. As a single piece for a particular destination, a firm package by
23 itself would qualify only for Basic rates. Adequate information is unavailable to

1 determine, for firm packages, when the Basic rates applied (because the firm package
2 was the only piece for a particular presort destination), or to determine when a firm
3 package qualified for a lower rate based upon there being at least another 5 pieces
4 within an individual mailing properly packaged to the same presort destination as the
5 firm package. Accordingly, firm packages were assigned rates based on their sack or
6 pallet level for all mail.

1 VI. RATE DESIGN

2 A. Regular Rate

3 Rates for the Periodicals Regular Rate subclass are designed to recover volume
4 variable costs and make an appropriate contribution to non-volume-variable costs. The
5 appropriate contribution to non-volume-variable costs is reflected in the cost coverage
6 of 107 percent established by witness O'Hara, USPS-T-30. The rate structure for
7 Periodicals consists of two basic elements: per piece charges and per pound charges.
8 The per piece charges depend on the level of presortation by the mailer, with discounts
9 to recognize entry in the destination SCF or delivery office, walk sequencing at the level
10 of saturation or high density (125 pieces per route), and automation compatibility
11 (prebarcoding). The per-piece charges are also adjusted to recognize the proportion of
12 editorial content. The per-pound charges are dependent on content. For advertising
13 content, the per-pound charges vary with distance by the postal zones and whether the
14 publication is entered at the destination SCF or delivery office. The per pound charge
15 for editorial content is designed to be lower, and does not vary with zone or entry point.

16 1. Pound Rates

17 The calculation of proposed pound rates differs from the earlier rate design
18 scheme resulting from Docket No. MC95-1 in three major respects. First, the editorial
19 pound rate has been calculated independently of any of the zoned rates. Second, the
20 pound rate revenue is proposed to generate 41 percent of total revenue, compared to
21 40 percent in the past. Finally, distance-related transportation costs are allocated to
22 zones without a markup, based exclusively on pound miles. In past rate designs, part of

1 the transportation cost was allocated based on pound miles, and the remainder was
2 included as an additive factor based on pounds.

3 The rate design for the editorial pound rate is straightforward. The total per
4 pound rate (pound related revenue, without markup, divided by total pounds) is
5 calculated without a markup as a benchmark for the editorial pound rate. In Docket No.
6 R94-1, the Commission expressed concern that the editorial matter should cover its
7 costs. It stated:

8 The Commission expressed concern in Docket No. R87-1 that the implicit
9 cost coverage on editorial matter should not be below 100 percent. PRC
10 Op. Docket No. R87-1, para. 5393, fn. 76. A similar concern exists here.
11 The Postal Service and the parties should examine this issue in future
12 proceedings.⁸

13
14 The proposed method of calculating the editorial pound rate will provide a
15 straightforward way to assure 100 percent cost coverage for the editorial pounds in the
16 future. In achieving the overall proposed cost coverage for Periodicals, the 100 percent
17 implicit cost coverage for editorial pounds would require a hefty increase (almost 20
18 percent for more than 50 percent of the pounds). The proposed editorial pound rate is,
19 therefore, set at 90 percent of this benchmark to mitigate the impact of the rate change
20 on high editorial content mail. The Postal Service is proposing methodological changes
21 to gradually achieve this goal without causing a significant rate impact for its customers.

22 Distance related transportation cost is allocated to the zones using pound miles
23 (pounds multiplied by average haul). The non-distance related transportation cost is
24 distributed based on pounds in zones 1 and 2 through 8, plus the DSCF dropship

⁸ PRC Op. , R94-1, p. V-48.

1 pounds. The DDU pounds do not bear any portion of the transportation cost. The non-
2 transportation cost is distributed based on all the advertising pounds including the DDU
3 pounds. This distribution ensures that the DDU dropshipment related pounds do not
4 bear any portion of the transportation costs, while the DSCF dropshipment related
5 pounds only bear the burden of non-distance related transportation cost. Rates for
6 zones 7 and 8 were reduced by 1.2 cents to minimize the rate impact on mailers mailing
7 to higher zones (Criterion 4).

8 9 **2. Piece Rate Development**

10
11 Three significant factors affect the development of piece rates. First, TYAR
12 pieces are derived using the base year billing determinants, the volume forecast, and
13 the mail characteristics study (Library Reference H-190). As stated earlier, the 3/5-digit
14 split, as well as the shift of non-unique 3-digit from basic to 3-digit, are estimated using
15 the mail characteristics study. Second, for the reasons discussed by witness Moeller
16 (USPS-T-36), the costs used to estimate the automation and presort discounts are
17 based on a study that isolates the effect of automation compatibility. Third, pass-
18 through discounts are chosen primarily to mitigate the effect of the increase for various
19 rate cells.

20 **a. Basic Piece Rate**

21 The piece rate for Basic presort is a by-product of the following factors:

- 22 1. Subclass cost coverage (107 percent);
- 23 2. Share of subclass revenue recovered from the piece rates (59 percent);
- 24 3. Magnitude of the editorial piece discount (\$0.059 per percent of editorial content);

- 1 4. The reclassification of the 3/5-digit rate into separate 3-digit and 5-digit rate
- 2 categories;
- 3 5. The migration of non-unique 3-digit mail; and
- 4 6. Cost savings and passthroughs underlying the worksharing discounts.

5 The piece rate for Basic presort that results from this analysis is 26.3 cents, an
6 increase of 9.6 percent from the current 24 cents. A major factor affecting this increase
7 is the shift of non-unique 3-digit mail to the 3-digit presort tier. Approximately 5 percent
8 of the subclass is affected by this increase. Furthermore, this rate was reduced by 0.01
9 cents to minimize the impact on customers mailing in this category.

10 **b. Presort Discounts**

11 Presort discounts were chosen to dampen significant increases in any of the rate
12 cells. Cost avoidance estimates for mail processing were based on witness Seckar's
13 (USPS-T-26) Periodicals Regular Rate flats models using constant mail entry profiles.
14 The mail delivery cost avoidance estimates were based on costing models developed
15 by witness Daniel (USPS-T-29).

16 The proposed rate for 3-digit presort is 21.7 cents, a discount of 4.6 cents from
17 basic rate, based on a 76 percent passthrough. The proposed 3-digit rate is a 7.4
18 percent increase from the current 3/5-digit rate of 20.2 cents. However, for the non-
19 unique 3-digit mail that shifts from the Basic presort tier, the proposed rate is actually a
20 reduction of 9.6 percent.

21 The proposed 5-digit presort rate is 21.4 cents, a discount of 0.3 cents from the
22 proposed 3-digit rate. The passthrough of cost savings of 10.1 cents from the Basic rate

1 is 49 percent. This cell exhibits a 5.9 percent increase and affects 16 percent of the
2 pieces.

3 The proposed Carrier Route presort rate is 12.8 cents, a discount of 8.6 cents
4 from the 5-digit rate. This discount reflects an 81 percent passthrough on cost savings
5 of 16.7 cents from the Basic rate. This cell exhibits a 7.6 percent increase and affects
6 approximately 39 percent of the pieces in the test year.

7 Carrier route high density and saturation discounts are based on witness
8 Daniel's cost estimates (USPS-T-29). The proposed rate for carrier route high density is
9 11.6 cents, a discount of 1.2 cents from the Carrier Route rate, based on a 73 percent
10 passthrough of cost savings of 20.2 cents from the Basic rate. This rate exhibits a 4.5
11 percent increase from the current rate of 11.1 cents. The proposed rate for Carrier
12 Route Saturation is 10.2 cents, a discount of 2.6 cents from the Carrier Route rate,
13 based on a 78 percent passthrough on cost savings of 20.7 cents from the Basic rate.
14 This rate exhibits a 7.4 percent increase from the current rate of 9.5 cents and affects
15 only 0.2 percent of the pieces in the test year.

16 **c. Automation Discounts**

17 Prebarcode discounts, once again, were proposed with the goal of mitigating the
18 effect of the rate increase on mailers. As stated earlier in my testimony, the cost study
19 provided by witness Seckar (USPS-T-26) isolated the effect of prebarcoding by keeping
20 the mail flow constant for the two types of mail.

21 Prebarcoded letters are discussed below. The proposed rate for prebarcoded
22 flats for the Basic presort tier is 22.1 cents, a discount of 4.2 cents, using a passthrough

1 of 76 percent. The proposed rate is 5.7 percent higher than the current rate of 20.9
2 cents, and affects 1.5 percent of the pieces in the test year.

3 The proposed 3-digit prebarcoded flat rate is 18.8 cents, a 2.9 cents discount
4 from the 3-digit non-automation tier. A passthrough of 88 percent is proposed for the
5 cost avoidance of 8.5 cents from Basic in this category. The result is a 7.4 percent
6 increase from the current 3/5-digit rate of 17.5 cents, which affects 8 percent of the
7 pieces in the test year.

8 The proposed 5-digit prebarcoded flat rate is 18.6 cents, a 2.8 cents discount
9 from the 5-digit non-automation tier. A passthrough of 62 percent is proposed for the
10 cost avoidance of 12.4 cents from Basic. The proposed rate is 6.3 percent higher than
11 the current 3/5-digit rate of 17.5 cents, and affects 15 percent of the pieces in the test
12 year.

13 **d. Letters**

14 Within Periodicals, the non-automation mail rates do not distinguish between
15 letters and flats. But this distinction based on shape has been present for prebarcoded
16 mail. I propose to include shape and barcode discounts for automation compatible
17 letters. These savings are calculated using estimates provided by witness Daniel
18 (USPS-T-29) for letters and witness Seckar (USPS-T-26) for flats.

19 The proposed rate for prebarcoded letters in Basic presort tier is 18.2 cents, a
20 6.2 percent reduction from the current rate of 19.4 cents. The proposed rates for 3-digit
21 and 5-digit prebarcoded letters are 16.6 cents and 16.2 cents, respectively. For 3-digit,
22 the proposed rate is reduced by 4 percent, while for 5-digit prebarcoded letters, the
23 proposed rate is 6.4 percent below the current combined 3/5-digit prebarcoded letter

1 rate of 17.3 cents. The passthroughs in the above cases are between 43 and 48
2 percent.

3 **e. Editorial Piece Discount**

4 The piece discount for editorial content is applied to the actual percentage of
5 editorial content in a given publication. This discount, along with the lower unzoned
6 editorial pound rate, is provided to recognize the ECSI value of the Periodicals class.
7 Presently, this discount is \$0.057 for every percent of the editorial content in a
8 publication. The proposed discount of \$0.059 is calculated based on the overall
9 increase in revenue per piece (not including fees) for the regular subclass.

10 This recognition of ECSI value (both in pound and piece rate design), as
11 required in criterion 8 of the pricing criteria (39 U.S.C. 3622(b)), leads to editorial matter
12 covering approximately 89 percent of its costs in this instance. As discussed earlier,
13 the Postal Service is attempting to move in the direction of editorial matter covering its
14 cost by de-coupling the pound rates from any of the zoned rates.

15 **f. Non-Transportation Related Drop Shipment Discounts**

16 Recognition of non-transportation drop shipment cost savings (Library
17 Reference H-111) for the destination delivery unit (DDU) and DSCF is proposed for
18 piece rates exclusively. This is a break from the past practice of splitting these savings
19 between piece and pound rates. The proposal provides clear dropship incentive for the
20 pound rates by not allocating any transportation costs to the DDU pounds, and only the
21 non-distance related transportation costs to the DSCF pounds. The proposed pound
22 rate for DDU mail is 15.8 cents, a 6.5 percent reduction from the current rate of 16.9
23 cents, while the proposed pound rate for DSCF mail is 18 cents, a 5.3 percent reduction

1 from the current rate of 19 cents. Therefore, my proposal applies non-transportation
2 related cost savings to piece rates only. A passthrough of approximately 50 percent is
3 used to estimate both DDU and DSCF discounts. The original cost savings are 4.6
4 cents and 2.4 cents for DDU and DSCF dropshipment, respectively. The proposed
5 discounts are 2.3 cents for DDU and 1.2 cents for DSCF, a 9 percent increase from the
6 current rates in both cases. These additional incentives for the piece rates provide a
7 more accurate signal to the mailers on whether to “buy”, or “provide their own”
8 transportation.

9 **B. Within County**

10 The rates for Within County mail are once again designed to cover volume
11 variable costs and provide a contribution to non-volume-variable costs. The target full
12 cost coverage of 103.5 percent (the actual phase 6 cost coverage is 103.7 percent,
13 slightly higher than the target) , applicable in phase 6 (FY 1999), is half of the 107
14 percent applicable to the Regular Rate. The test year cost coverage is 102.7 percent,
15 reflecting phase 5 of the RFRA requirements (the target for the test year is 102.9
16 percent, slightly higher than the actual cost coverage achieved for TYAR). The 3/5-digit
17 split for Within County mail was estimated using the billing determinants data, similar to
18 the approach for Regular Rate described above.

19 **1. Pound Rates**

20 The pound rates for the Within County subclass are estimated for two rate cells,
21 delivery unit entry and all other. The non-transportation dropship cost savings are used
22 as a basis to provide a discount for delivery unit entry. The passthroughs used for
23 Within County rates are by necessity much smaller than other classes, because the

1 cost study used is for Nonprofit mail. Also, mitigation of the rate shock is another
2 compelling reason in the choice of passthrough levels.

3 **2. Piece Rates**

4 The piece rate design follows a similar method to that adopted for the Regular
5 Rates subclass. The level of passthrough for the various cells is lower, because of the
6 nature of the cost study and the rate impact mitigation.

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