

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

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POSTAL RATE COMMISSION  
OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES, 2000

Docket No. R2000-1

**RESPONSE OF UNITED STATES POSTAL SERVICE  
WITNESS MOELLER TO INTERROGATORIES OF VAL-PAK DIRECT  
MARKETING SYSTEMS, INC., VAL-PAK DEALERS' ASSOCIATION, INC.,  
AND CAROL WRIGHT PROMOTIONS, INC.  
(VP-CW/USPS-T35—1-8)**

The United States Postal Service hereby provides the responses of witness Moeller to the following interrogatories of Val-Pak Direct Marketing Systems, Inc., Val-Pak Dealers' Association, Inc., and Carol Wright Promotions: VP-CW/USPS-T35—1-8, filed on February 18, 2000.

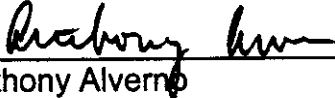
Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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VP-CW/USPS-T35-1. Please refer to USPS-LR-166, WP 1, page 10.

- a. In what part of your testimony do you use the costs shown in lines 5-6 for letters, and where do you use the alternative costs shown in lines 32-33?
- b. Where do you use the unit costs shown for Basic Automation flats in line 10, and where do you use the unit cost for Basic Automation flats shown in line 37?
- c. Why is the mail processing unit cost for Basic Automation flats in line 37 higher than the mail processing unit costs shown in line 10?

RESPONSE:

- a. I use lines 5-6 in Worktable 1 on page 11 of WP 1, and in lines 8 and 10 of Column (1) on page 12 of WP 1. I use lines 32 and 33 in the calculations in Worktable 2 on page 11 of WP1.
- b. Line 10 is not used. Line 37 is used in line 2 of column (1) on page 12 of WP 1.
- c. On page 12 of Appendix 1 of my testimony, I note that, in some instances, there are two separate measurements of mail processing costs for some categories in order to isolate the particular worksharing savings underlying the discounts or rate differentials. Not surprisingly, since in some instances there are two distinct measurements, one is going to be higher. For discussion of how the measurements were determined, see witness Yacobucci's testimony (see USPS-T-25).

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VP-CW/USPS-T35-2.

At page 18 (lines 5-8) your testimony states:

In Docket No. MC95-1, the Postal Service proposed and the Commission recommended the creation of the Enhanced Carrier Route subclass so that the distinct cost and market characteristics of mail within this subclass could be more fully recognized.

- a. Were the proposed rates for ECR mail in this case designed so that the distinct cost and market characteristics of ECR mail could be more fully realized? If so, explain how this was done.
- b. Please indicate the rates or rate levels that in your view would constitute full recognition of the distinct cost and market characteristics of ECR mail to which you refer in your testimony quoted above.
- c. At current rates, how far away is ECR mail from achieving full recognition of the distinct cost and market characteristics of ECR mail?
- d. If your proposed rates for ECR mail were to be adopted, how far away would ECR mail be from achieving full recognition of the distinct cost and market characteristics of ECR mail?
- e. Comparing your proposed rates for ECR mail with current rates, how much closer do your proposed rates get to achieving full recognition of the distinct cost and market characteristics of ECR mail compared with current rates?

RESPONSE:

- a. It is my understanding that since ECR is a subclass, it is assigned a cost coverage based on the relevant pricing criteria. The market characteristics are considered in the cost coverage in criteria 2 and 5, and the cost characteristics are also considered in that the coverage is applied to the separately-measured subclass costs for ECR as provided by criterion 3. See witness Mayes testimony (USPS-T- 32) at pages 38 and 39. The proposed rates flow directly from the cost measurement and the cost coverage. This is more recognition of the cost and market characteristics

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than would be the case if carrier route were still a rate category, rather than a subclass.

- b. The rate level itself is beyond the scope of my testimony. As described in response to subpart a, the creation of the subclass leads to recognition of cost and market characteristics, along with all of the other pricing criteria. It is not clear in any event what this interrogatory intends by reference to the "full recognition" of the distinct cost and market characteristics. As noted in my response to subpart a, the pricing criteria require that the market characteristics and costs be considered. While I note that witness Mayes states that, considered in isolation, many of the criteria would indicate a coverage lower than the proposed coverage (See witness Mayes, USPS-T-32, at page 39, lines 14-16), it is my understanding that all of the pricing criteria must be considered in determining the cost coverage. Balancing the implications of the pricing criteria against each other might result in a cost coverage that does not seem to follow from one pricing criterion in isolation. This does not imply, however, that cost characteristics or market characteristics were not "fully recognized."

- c-e. See responses to (a) and (b).

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VP-CW/USPS-T35-3. Please refer to your testimony at the top of page 21 (table).

- a. [This interrogatory as filed did not include a subpart a.]
- b. Please confirm that the piece-rated data include both letters and flats. If you do not confirm, please explain what the piece-rated data represent.
- c. For all piece-rated ECR nonletters, what is the unit revenue, unit cost and implicit coverage, respectively, both before and after rates?
- d. For all ECR non-letters combined (i.e., both piece and pound-rated), what is the unit revenue, unit cost and implicit coverage, respectively, both before and after rates?
- e. For all piece-rated ECR letters, what is the unit revenue, unit cost and implicit coverage, respectively, both before and after rates?
- f. The unit cost in your table for pound-rated matter using costs with a 3.0 and a 3.5 ounce dividing line is, respectively, \$0.0901 and \$0.0916. What is the estimated cost per pound that was used to determine these different unit costs? Should your answer be to the effect that no explicit unit cost estimate was used to derive these figures, please explain fully.

RESPONSE:

- a. N/A
- b. Confirmed.
- c. As far as unit costs are concerned, witness Daniel's testimony (USPS-T-28)

at page 16 lines 2-5 explains:

*Since the IOCS weight data do not allow costs to be calculated exactly at the breakpoint used in rate design (i.e., 3.3 ounces), either the average cost of pieces above and below 3.0 or 3.5 ounces can be used to proxy for the cost of pound-rated and piece-rated mail.*

The cost estimates in USPS-T-28, Table 3, page 17 show that the TYBR unit cost for ECR non-letters weighing less than 3.0 ounces is \$0.0657 and the TYBR unit cost for ECR non-letters weighing less than 3.5 ounces is \$0.0674. New unit costs are not calculated for TYAR.

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The revenue per piece for piece-rated nonletters is \$0.13078 before rates, and \$0.13962 after rates. (See WP 1, page 34). In order to isolate the effect of the rate change, the volumes underlying these figures, as well as the volumes used in other subparts of this response, are held constant before and after rates. These estimates do not attempt to incorporate the effect of the residual shape surcharge, which would be minimal.

Implicit coverages, similar to those in the referenced table on page 21 of my testimony, would be 199.1 percent or 194.0 percent (using the 3.0 and 3.5 breakpoints, respectively) before rates, and 212.5 percent and 207.2 percent (for 3.0 and 3.5, respectively) using after rates revenues. Since after rates costs are not available, the before rates costs are used for the comparison with after rates revenues. Any change in costs in the after rates environment would be due to a change in volume mix. Since the volumes are being held constant for the revenue calculation, it would be inappropriate to use after rates costs, even if they were available, for this comparison of implicit cost coverages.

- d. The cost estimates in witness Daniel's testimony (USPS-T-28, Table 3, page 17) show that the TYBR unit cost for all ECR non-letters is estimated to be \$0.0757. New unit costs are not calculated for TYAR. The unit revenue is \$0.15544 before rates, and \$0.16104 after rates.

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The implicit coverages, therefore, calculated as described in subpart c, are 205.8 percent before rates and 212.7 after rates.

- e. See response to subpart (c). The cost estimates in witness Daniel's testimony (USPS-T-28, Table 3, page 17) show that the TYBR unit cost for ECR letters weighing less than 3.0 ounces is \$0.0669 and the TYBR unit cost for ECR letters weighing less than 3.5 ounces is \$0.0678. New unit costs are not calculated for TYAR. The unit revenue is \$0.13614 before rates, and \$0.14724 after rates. The coverages would be 203.5 percent or 200.8 percent (using the 3.0 and 3.5 breakpoints, respectively) before rates, and 220.0 percent and 217.2 percent (for 3.0 and 3.5, respectively) using after rates revenues.
- f. No explicit unit cost estimate per pound was used to derive these figures. The costs are summarized in witness Daniel's testimony (USPS-T-28, Table 3, page 17) and were derived in USPS LR-I-92 using a methodology described in USPS-T-28 pages 3-10.

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VP-CW/USPS-T35-4. Did you or the Postal Service develop the unit cost estimates that underlie any of the individual cells for your proposed rates for Standard A Mail shown on pages 17 and 28 of your testimony? If so, please provide such estimates, and indicate where these unit costs estimates can be found.

RESPONSE:

Cost estimates underlying the cited rate cells were not developed.



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VP-CW/USPS-T35-5. Please refer to USPS-LR-I-166, WP 1, page 20.

- a. Please confirm that after the parameters and data shown in lines 1-13 have been specified, the rate design formula shown on this page will determine (i) the rate for piece-rated flats, and (ii) the piece rate for pound-rated pieces. Please explain any non-confirmation.
- b. Would you agree that it is the inputs to the formula on page 20 that determine the design of the rates for individual cells, and not the formula shown on lines 14-18? If you do not agree, please explain.

RESPONSE:

- a. Confirmed. More specifically, though, the piece rates that are outputs are for the Basic tier.
- b. If "design" of the rates is intended to mean the relationships between rate cells that result from selection of the various passthroughs, then yes, it is the inputs that generate these rate relationships. The formula produces the base rates necessary to generate the required revenue.

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VP-CW/USPS-T35-6. Your testimony at page 4 (lines 17-18) states that "in consideration of the effect on users (criterion 4), the rate design employs an upper bound on the amount by which an individual rate cell is proposed to increase."

- a. Please confirm that your reference to "criterion 4" is to 39 U.S.C. section 3622(b)(4).
- b. When designing rates for the two subclasses of Standard A Commercial Mail, did you consider or rely on any of the other non-cost criteria contained in section 3622(b) of the statute? If so, please state which criteria you relied upon, which rate cells were affected by your reliance on each of those other criteria, and how your overall rate design was affected by reliance on those other criteria. If not, please explain why you relied upon only one non-cost criterion and did not consider or apply any of the other non-cost criteria.
- c. When designing the rates for Standard A Mail, did you consider criterion 4 to be more important than all the other non-cost criteria?
- d. In your opinion, should the Postal Service and the Commission apply the non-cost criteria of section 3622(b) to the rate design within individual subclasses?

RESPONSE:

- a. Confirmed.
- b. The criteria are to be considered explicitly for rate level determination, however, they do embody fundamental principles for rate design, as well. Not all of them are relevant at the rate design level; however, the broad notion of fairness and equity seems applicable. Certainly, it should not be an objective of the rate design to be unfair and inequitable. For example, while consideration of the effect of rate increases might lead to a passthrough selection of greater than 100 percent, consideration of fairness and equity may come into play since tempering the rate increase for one rate cell has a push-up effect on other rate cells. Fairness and equity, therefore, would argue for some limitation on how much some cells are increased in

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order to avoid even larger increases for other cells. Degree of preparation is broadly considered in that the rate design includes discounts that require certain levels of preparation. (See witness Mayes, USPS-T-32, at page 9.)

Simplicity is also considered in rate design when deciding whether to complicate the rate structure with additional rate categories. In the Standard Mail (A) proposal, a barcode discount is proposed for parcels after determination that such a discount would provide incentive for mailer-applied barcodes without unnecessarily complicating the rate structure.

- c. I did not judge the relative importance of the factors embodied in the criteria. The effect of rate increases, however, did play an important role in the rate design.
- d. As stated in my response to subpart b, I believe some of the principles have applicability at the rate design level.

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VP-CW/USPS-T35-7. Please confirm that in this docket the Postal Service proposes the following percentage increases for ECR letters and piece-rated non-letters (without any destination entry discounts – see PRC Order No. 1279, Attachment B, p. 17).

	Letters	Non-Letters
High Density	9.4%	2.0%
Saturation	10.0%	5.7%

If you do not confirm, please explain.

- a. The Postal Service press release which accompanied the filing, in explaining why business rates are increasing, states that:

In general, rate increases for each subclass reflect overall cost trends for that subclass. As a result of the letter automation program, increases for letter-shaped items, particularly First-Class Mail, are generally smaller.... At the same time, costs have increased more rapidly for flat-shaped items, such as Periodicals, Standard Mail catalogs and Bound Printed Matter.... The proposal calls for larger-than-average increases for those categories.

In light of the cost trends asserted in the Postal Service press release, please explain why your rate design reflects rate increases for ECR letters that substantially exceed the rate increases proposed for ECR non-letters.

- b. For High-Density and Saturation ECR letters and non-letters, what is the estimated unit cost in the Base Year?  
c. What was the estimated unit cost for the above-mentioned items in the Base Year of Docket No. R97-1?

RESPONSE:

- a. I presume the reference to increasing costs for Standard Mail catalogs relates to the rate increases for automation flats. These cost changes are not as critical for ECR flats since they avoid most of the piece-distribution operations that automation flats incur. In any event, the rate design for ECR relies on the cost differentials referred to in my testimony. The difference in

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the rate change percentages for letters and flats relates to these cost differentials, and the applied passthroughs.

- b. To my knowledge, costs for High-Density and Saturation ECR letters and nonletters were not calculated in Base Year terms.
- c. To my knowledge, costs for High-Density and Saturation ECR letters and nonletters were not calculated in Base Year terms.

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VP-CW/USPS-T35-8. Your testimony at page 24 (lines 7-9) states that "The surcharge only applies if the sample is not letter- or flat-shaped, or is prepared as a parcel."


- a. In FY 1999, how many flat-shaped pieces were prepared as parcels under the current rates?
- b. What incentive(s) do mailers have to prepare flat-shaped pieces as parcels under current rates?
- c. What incentive(s) do mailers have to prepare flat-shaped pieces as parcels under your proposed rates?

**RESPONSE:**

- a. The "prepared as a parcel" language is applicable to pieces (primarily machinable parcels) that may meet the dimensional criteria of a flat, but are prepared according to parcel preparation requirements. It is my understanding that there are no volume estimates of how many pieces that meet the flat-shaped definition were nevertheless prepared as parcels.
- b. Some mailers of pieces that would meet the flat shape definition may choose to mail the pieces as machinable parcels for simplicity in the mail preparation requirements. Machineable parcels need only be prepared to BMC (unless there is enough volume to warrant 5-digit presort), whereas flats must be prepared to 3-digit (which is a finer depth of sort than BMC), to receive the 3/5-digit presort rate. Also, to the extent the mailing includes pieces that exceed the dimensions of a flat, a mailer may find it easier to combine all of the machinable parcels in one mailing, rather than cull those pieces that could be mailed as flats.
- c. The same type of incentives exist under the proposed rates as the current rates.

## CERTIFICATE OF SERVICE

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

  
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