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

POSTAL RATE AND FEE CHANGES, 2000 | **Docket No. R2000–1**

RESPONSES OF KEYSPAN ENERGY WITNESS BENTLEY TO INTERROGATORIES OF THE UNITED STATES POSTAL SERVICE

KeySpan Energy hereby provides the responses of witness Bentley to the following interrogatories of the United States Postal Service: USPS/KE-T1-16-26, filed on June 16, 2000. Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

KEYSPAN ENERGY

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Dated: Round Hill, Virginia
June 30, 2000

CERTIFICATE OF SERVICE

I hereby certify that I have served the following interrogatory responses upon the United States Postal Service, Ted P. Gerarden, the Designated Officer of the Commission, and participants who requested service of all discovery documents
Dated this 30th day of June 2000.

Michael W. Hall

USPS/KE-T1-16

On page 4, lines 10-11 of your testimony, you propose a $1,000 monthly equivalent of the QBRM quarterly fee as opposed to the quarterly fee of $850 proposed by witness Mayo.

(a) Please confirm that an implicit cost coverage of 420 percent ($1,000/$237.93) results from the establishment of the QBRM Quarterly fee at $1,000 per month. If you do not confirm, please explain and provide the implicit cost coverage you believe is accurate.

(b) Under your proposed QBRM per piece and monthly fees, at what monthly volume level will a mailer achieve breakeven?

RESPONSE:

(a) I can confirm your mathematical computation. However, my monthly fee is not based on an implicit cost coverage but is based more on the need to determine an appropriate "breakeven" volume. As I state on page 10 of my testimony,

> [I]n order to establish a reasonably high breakeven volume, I recommend that the monthly fee be $1,000, an amount that far exceeds the relevant costs. Such a fee is also much greater than any markup that might be reasonably justified from application of the statutory criteria of the Act.

In addition, please bear in mind that your cost figure of $237.93 includes a 2.5% contingency that, testifying on behalf of Major Mailers Association, I recommend the Commission not accept. *See* MMA-T-1 at 32.

(b) There is no monthly breakeven volume because the monthly fee must be paid on an annual basis. However, if one were to assume that annual volumes are received on a constant basis, then the average

monthly breakeven volume would be 300,000 pieces divided by 12 months or 25,000 pieces per month.

USPS/KE-T1-17

Please refer to your testimony at page 20, lines 12-15. If an otherwise low volume QBRM mailer expected to receive 50,000 replies during a one month period, would it be economical for that mailer to sign up for the high volume QBRM service during that quarter? If not, please explain why not.

RESPONSE:

No. Your question suggests that, under the Postal Service's proposal, QBRM recipients would be able to opt-in and opt-out of High Volume service on a quarterly basis. That is not my understanding of the Service's proposal. Witness Mayo confirmed that the "breakeven" volume under the Postal Service's proposal is 113,000 ***per year***. *See* USPS-LR-I-168 at footnote 5 and TR 14/5566-67. From this I infer that a High Volume QBRM recipient must pay the quarterly fee for a full year. In other words, under the Postal Service's proposal, the annual fee is $3,400 but, simply for the convenience of QBRM recipients, it is payable in quarterly installments of $850 each.

For it to be "economical" for the mailer in your question to sign up for High Volume QBRM service, he would still have to receive in excess of 113,000 pieces ***per year***, the breakeven volume under Ms. Mayo's proposal. Therefore, receiving 50,000 pieces in a one-month period would not make the High Volume QBRM service cost effective for that mailer.

Moreover, your question appears to misinterpret my testimony. My statement regarding the 1300th largest QBRM recipient (based on CBCIS data furnished by USPS witness Campbell) that you cite clearly referred to a recipient who received 50,000 during a one year period. Such a recipient would not choose

to pay the annual $3,400 fixed annual fee under the Postal Service's newly proposed QBRM category. The $3,400 in fixed expenses is much higher than the potential $1,500 per piece savings (50,000 pieces x 3 cents = $1,500).

The purpose of the statement you reference is to further prove that Ms. Mayo significantly overstated the number of accounts likely to take advantage of the High Volume QBRM service. According to the CBCIS data, the 1300th largest QBRM account received fewer than 50,000 pieces per year. *See* Library Reference KE-LR-1. This is less than 45 percent of Ms. Mayo's proposed 113,000 annual breakeven volume. Certainly, her estimate of 1,358 accounts seriously overstates the universe of potential High Volume QBRM recipients.

USPS/KE-T1-18

Please confirm that your testimony does not identify new cost saving opportunities, but rather, it identifies areas where you believe costs are not properly assigned. If you do not confirm, please identify the proposals in your testimony that will result in increased, future cost savings.

RESPONSE:

I do not identify "new cost saving opportunities" as this is not the purpose of my testimony. However, I do recommend that the Commission should not allow the Postal Service to base QBRM fees on inefficient operations or unsupported assumptions that grossly overstate QBRM processing costs.

The purpose of my testimony is to show, among other things, that the Postal Service has significantly overstated the unit costs to process high and low volume QBRM pieces, and that the corresponding per piece fees proposed by the Service are much too high. As part of that analysis, I show that the Postal Service has assumed that QBRM processing is very inefficient when, in fact, this is not the case. The telephone survey conducted by USPS witness Campbell, as discussed on page 16 of my prepared testimony, KE-T-1, refutes the 1997 BRM Practices Study's estimates that only 14.2% of QBRM would be processed by BRMAS equipment, an estimate which USPS witness Campbell assumed would be representative for the Test Year in this case. Mr. Campbell's assumption implies that 65.5 million pieces of the total 461.6 million QBRM pieces will be processed on BRMAS equipment. As Exhibit KE-1D at 4 demonstrates, the Postal Service currently uses BRMAS equipment to process more than twice that amount, 141.7 million pieces, **just for 74 of the highest volume recipients** for which data are

available. In addition, when Mr. Campbell checked with offices that utilized various methods for counting QBRM, in every instance, manual counting was not used for the high volume recipients. See footnote 13 on page 14 of my testimony. Thus, Mr. Campbell's assumption, based on the 1997 BRM Business Practices Study, that 66.5% of QBRM is counted manually, is way off base.

I am not sure what is meant by costs being "not properly assigned". The unit costs derived by USPS witness Campbell for high and low volume QBRM are unreasonable because they are based on a flawed study design and unsupported assumptions. It is fundamentally illogical for USPS witness Campbell to charge different QBRM per piece fees based on the volumes received, and then to simply assume that the average unit cost of processing high volume QBRM pieces is identical to the cost of processing low volume pieces. *See* KE-T-1 at 6, footnote 6. Similarly, Mr. Campbell failed to follow the directive given to him by the Board of Governors to study "the extent to which reply mail volume should influence fees charged to different recipients". *See* KE-T-1 at 2. Regarding his field visits to observe QBRM processing, it is a serious shortcoming that he failed to consider QBRM volume received as the primary cost driver. Note Mr. Campbell's explanation at TR 14/5978, which he repeated again at TR 14/5980 and again at TR 14/5982:

> I do not have specific recollection of discussions with Postal Service personnel regarding whether the QBRM reply letters they were counting were addressed to high volume recipients or addressed to low volume recipients.

This is Mr. Campbell's fundamental flaw. He ultimately recommends a very logical proposal, for two separate per piece fees based on the volume of QBRM

received; but his failure to study processing differences based on QBRM volume received leaves him no reasonable basis to support that proposal. My testimony corrects these defects in his analysis. Moreover, the Service has effectively asked the Commission to base fees for both high and low volume QBRM on the assumption that counting such pieces will be grossly inefficient, a concept that I recommend the Commission reject outright.

See also my answer to interrogatory USPS/KE-T1-20.

USPS/KE-T1-19

Please refer to your testimony at page 20, lines 23-25. If your proposed Quarterly QBRM fee of $1,000 per month were rejected by the Commission and the USPS proposed fee were approved, would you continue to view the difference in the contribution to institutional costs as inconsequential? If yes, please explain your position.

RESPONSE:

I do not propose a quarterly QBRM fee of $1,000 per month. I propose a $12,000 annual QBRM fee that is payable in monthly installments of $1,000.

I cannot answer the question posed in this interrogatory without knowing the per piece fees you wish to me assume. For example, the annual breakeven volume is determined by the relationship between the annual fixed fee and the difference between the two per piece fees for high and low QBRM. The breakeven volume, in turn, determines the number of recipients and volume likely to fall into each of the two fee categories. Without this information, I cannot be very specific in my response. Moreover, I have estimated revenues and costs for only one set of fees, those that I have proposed. Therefore, my proposed set of fees result in a breakeven volume of 300,000 pieces per year. I have not developed estimates for volume variable costs, revenues and contributions to institutional costs for any other combination of QBRM fees.

As a general response, let me add that the impact of almost any set of alternative QBRM fees will probably not impact the Postal Service's overall breakeven requirement. The QBRM volume and related fee revenue is simply too small. In addition, if the Commission accepts my proposed QBRM unit costs for high and low volumes, as well as the volume levels I estimate, I do not see how it

could, at the same time, accept the Postal Service's proposed per piece fees. Such a recommendation would result in an extremely high QBRM cost coverage that, in my view, would be difficult to justify to the Board of Governors.

Please also note that for purposes of illustration, my computations shown in Exhibit KE-1F that apply to the Postal Service accept USPS witness Mayo's estimate that 1,358 accounts will pay the $3,400 annual fee and that 153.870 million pieces will pay the lower 3-cent per piece fee. As I discuss in my testimony, the 1,358 is much too high and the 153.870 million is much too low.

USPS/KE-T1-20

Please confirm that your testimony does not identify new cost saving opportunities, but rather, it identifies areas where you believe costs are not properly attributed. If you do not confirm, please identify the proposals in your testimony that will result in increased, future cost savings.

RESPONSE:

Please see my responses to USPS/KE-T1-18 and 19. The Postal Service does not derive accurate unit costs for QBRM processing. The Service's derived unit costs for high volume and low volume QBRM are much too high. Accordingly, the Service's proposal "assigns" an extraordinarily large amount of institutional costs to be "covered" by QBRM pieces.

USPS/KE-T1-21

Please confirm that the table below accurately summarizes the changes in revenue from the USPS proposal to your proposal presented in Exhibit KE-1F. If not, please make any changes required to accurately reflect your proposal as compared to the USPS's revenue projection. If there are any other revenue differences between the two proposals, please identify them.

	USPS ($000)	Keyspan ($000)	Difference (USPS-Keyspan) ($000)
High Volume Accounts			
Quarterly/Monthly Fee	$4,617	$3,600	$1,017
QBRM Per Piece Fee	$4,616	$1,725	$2,891
Low Volume Accounts			
Per Piece Fee	$18,464	$5,247	$13,217
Total	$27,697	$10,572	$17,125

RESPONSE:

Confirmed. Please also note that for purposes of illustration, my computations shown here accept USPS witness Mayo's estimate that 1,358 accounts will pay the $3,400 annual fee and that 153.870 million pieces will pay the lower 3-cent per piece fee. As I discuss in my prepared testimony, the estimate of 1,358 potential High Volume QBRM recipients is much too high and the 153.870 million is much too low.

USPS/KE-T1-22

Please refer to Exhibit KE-1F, Page 1 of 1.

(a) Please confirm that the total contribution to institutional costs resulting from your proposal is $5,146,000. If you cannot confirm, please provide the total amount of contribution that results from your proposal.

(b) Please confirm that of the total contribution to institutional costs, $2,764,000 is generated from the quarterly QBRM fee. If you cannot confirm, please provide the correct amount of contribution resulting from the Quarterly QBRM fee.

(c) Please confirm that 54.7% of the contribution to institutional costs is generated from the Quarterly QBRM fee. If you cannot confirm, please provide the correct percentage.

(d) Does the Keyspan volume variable cost of $2,785 for the annual fee include a contingency? If yes, what is the contingency percentage? If not, why was a contingency not incorporated?

(e) Does your "USPS proposal" volume variable cost of $2,784 for the annual fee include a contingency? If yes, what is the contingency percentage? If not, why was a contingency not incorporated?

(f) Why is there a difference in the Keyspan volume variable cost for the annual fee and your "USPS proposal" volume variable cost for the annual fee?

RESPONSE:

(a) Confirmed.

(b) Confirmed.

(c) Not confirmed. I do not propose a "Quarterly QBRM fee". I propose a $12,000 annual QBRM fee that is payable in monthly installments of $1,000. I also compute the percent of the institutional cost contribution derived from the fixed QBRM fee to be 53.7%. The computation is as follows: 2,764 / 5,146 = .537. This computation includes no contingency.

As discussed in my response to Interrogatory USPS/MMA-T1-16(a), my proposed $12,000 annual fee is "much greater than any markup that might be reasonably justified from application of the statutory criteria of the Act." Consequently, the fixed fee contribution to institutional costs is extremely high and explains why 53.7% of the contribution derives from the fix fee portion of the fee structure.

(d), (e) No. For my purposes of this comparison, I decided it was not necessary to include a contingency in either figure. The 2.5% contingency proposed by the Postal Service in this case is controversial and it was not necessary to include a contingency amount for my purposes of comparing the respective institutional cost contributions under the Postal Service and KeySpan proposals.

(f) KeySpan's total volume variable cost for the annual fee is based on the Postal Service's annual cost per account and an estimate that the Postal Service will incur those costs for 300 high volume recipients. The Postal Service's total volume variable cost for the annual fee is based on the same annual cost per account and an estimate that the Postal Service will incur those costs for 1,358 high volume recipients. Therefore, the total volume variable costs are different.

USPS/KE-T1-23

Your testimony at page 10 recommends a monthly fee of $1000 to cover the fixed costs associated with rating and billing QBRM. You indicate at line 16 that a $1000 monthly fee establishes an annual breakeven volume of 300,000 pieces.

(a) Please confirm that you believe 300,000 pieces is a "reasonably high breakeven volume" (see page 10, lines 16-17).

(b) How does one determine what is a "reasonably high breakeven volume"?

(c) Please explain how you determined that 300,000 pieces is a "reasonably high breakeven volume."

(d) Please explain the basis for your statement in lines 16-18 that a "reasonably high breakeven volume serves to maximize the opportunity for the Postal Service to realize cost savings from counting QBRM returned in high volumes." On what information do you rely for this determination? In your response, identify and provide all information that forms the foundation for this assertion.

RESPONSE:

(a) – (c) My proposed breakeven volume of 300,000 is reasonably high. Since High Volume QBRM is a newly proposed fee category, in my opinion it is more prudent to be conservative. All things being equal, the higher the breakeven volume, the higher daily volumes received will be, and the higher the probability that cost savings for counting QBRM can accrue.

My proposed breakeven quantity of 300,000 pieces annually is high compared to the USPS proposed breakeven volume (200,000 pieces per year) for PRM in Docket No. R97-1, high compared to the current annual breakeven volume (103,000 pieces) for nonletter-size BRM, high compared to the USPS proposed annual breakeven volume (80,000 pieces) for

nonletter-size BRM in this case, and high compared to the USPS proposed annual breakeven volume (113,000) for High Volume QBRM in this case.

The final determination of whether a specific breakeven volume is "reasonable" will depend upon mailers' reactions. If the newly proposed category meets its objectives for volumes, revenues and costs, and results in a more equitable rate structure, then the breakeven volume is reasonable. If it does not, then perhaps the breakeven quantity should be raised or lowered, as appropriate.

Another reason why I consider the proposed annual breakeven quantity of 300,000 pieces to be reasonably high is that it implies that the average daily volume is much higher than the 400 pieces per day that I estimate is necessary for weight averaging to be more efficient than hand counting. See my response to USPS/KE-T1-10(a).

(d) Please refer to my response to parts (a) – (c) where I state that "All things being equal, the higher the breakeven volume, the higher the probability that cost savings for counting QBRM can accrue." Thus a higher minimum breakeven volume maximizes opportunities for the Postal Service to realize cost savings by employing highly efficient methods, such as BRMAS, EOR reports, weight averaging, and special counting machines, to count QBRM received in high volumes. When developing my proposed annual fixed fee, I considered setting that fee at amounts less than $12,000 per year. Doing so resulted in lower breakeven volumes. Ultimately, I rejected the lower amounts in favor of a 300,000 piece per

year breakeven volume as a conservative measure for a newly proposed QBRM fee category. *See* also my response to parts (a) - (c).

I also note that even though USPS witness Campbell proposes separate per piece fees for high and low volume QBRM, he made no studies to determine at what volumes high volume QBRM becomes more efficient to process. *See* TR 14/5926-29. Therefore, the Postal Service has provided no useful data for determining a more specific volume figure that "maximizes opportunities for the Postal Service to realize cost savings by employing highly efficient methods, such as BRMAS, EOR reports, weight averaging, and special counting machines, to count QBRM received in high volumes."

USPS/KE-T1-24

Please refer to page 10, lines 18-20 of your testimony where you state that your "breakeven volume compares well with the proposed 200,000 minimum for PRM in Docket No. R97-1."

(a) Please confirm that your breakeven volume is 300,000 pieces. If not confirmed, please explain.

(b) Please confirm that the Postal Service's proposed breakeven in this docket is volume is 113,000 pieces. If not confirmed, please explain.

(c) Please confirm that the USPS breakeven volume of 113,000 is closer to the proposed PRM breakeven volume than your breakeven volume of 300,000. If not confirmed, please explain.

(d) Please explain what you mean when you say that your breakeven volume "compares well with the proposed 200,000 minimum for PRM."

RESPONSE:

(a) Confirmed.

(b) Confirmed. The Postal Service's breakeven volume is 113,000 pieces per year.

(c) Confirmed. My proposed breakeven volume is higher by 100,000 pieces. The Postal Service's proposed breakeven volume is lower by 87,000 pieces. As discussed in my response to interrogatory USPS/KE-T1-23, a higher breakeven volume is more conservative and better insures that cost savings for counting QBRM will accrue.

(d) My proposed breakeven volume of 300,000 is the same order of magnitude as the breakeven volume the Postal Service proposed for PRM service in Docket No. R97-1. Moreover, because my proposed breakeven volume is higher, the odds of a particular recipient receiving higher daily volumes, resulting in more opportunities for the Postal

Service to use highly efficient counting methods, is greater. Therefore, my proposed breakeven volume compares well with the PRM breakeven volume.

USPS/KE-T1-25

On page 19, lines 3-5, you state that you "believe the most reliable CRA proportional adjustment factor...is the one computed for all presort letters."

(a) Please explain how a CRA adjustment factor for *presort* letters is appropriate for adjusting modeled worksharing costs of *handwritten single-piece* mail.

(b) Please confirm that witness Campbell incorporates a CRA adjustment factor of 0.995 in his model that uses the Commission's cost methodology for attributing costs (see USPS LR I-146, page 1).

(c) Please confirm that when you modify the CRA adjustment factor from 0.995 to 1.19, the modeled worksharing cost difference between a QBRM piece and a handwritten mail piece increases, thus inflating the cost avoidance estimate.

RESPONSE:

(a) As I state on page of 18 my testimony,

> The CRA proportional adjustment factor measures how well the mail flow model simulates the true cost. If the models are reliable and consistent, then the CRA proportional adjustment factors for the various categories of letters should be somewhat similar.

The Postal Service provides no CRA cost data for QBRM letters or hand addressed letters. Therefore there is no way to directly reconcile the mail flow model derived unit costs for these First-Class mail categories.

USPS witness Campbell decided to use the non-automation CRA adjustment factor as a means to indirectly reconcile his model derived unit costs to the CRA. His reason for using this factor is that "[T]he non-automation presort mailstream serves as a good proxy for the single-piece mailstream, which includes both QBRM and handwritten mail pieces." See TR 14/5935-37. I do not particularly agree with Mr. Campbell's reasoning since non-automation letters are not prebarcoded and often are

not even automation-compatible, two key attributes that characterize 100 percent of QBRM. Therefore, while QBRM is part of the First-Class mailstream, it is not well represented by non-automation letters. Moreover, I feel that the accuracy of the mail flow models is determined more by the design and input data than it is by the type of mail being studied.

In addition, Mr. Campbell also chooses to compare the mail flow model derived unit costs to the CRA derived unit costs for a First-Class category with relatively low volumes. According to USPS witness Miller's analysis, base year non-automation volumes (4.4 billion letters) accounted for only 11% of all presort letters. This introduces additional sampling errors because some of the cost pool data for non-automation letters could be "thin." The Commission has also expressed its concerns about the accuracy of the CRA costs for non-automation letters. *See* Presiding Officer's Information Request No. 9, dated April 21, 2000, Question 4.

As further discussed in my testimony, "I believe the most reliable CRA proportional adjustment factor, which reflects the overall accuracy of the mail flow cost models, is the one computed for all presort letters." *See* KE-T-1 at 19. The CRA factor for all presort letters is most reliable since it combines the cost pools for three categories of First-Class mail: non-automation, automation non-carrier route, and carrier route. During the base year, these three categories accounted for a total of 40.1 billion letters, clearly providing a more stable and reliable means to reconcile the

mail flow unit cost derivations to the CRA than using any of the three categories taken separately.

By using the relationship between the mail flow model-derived costs and the CRA-derived costs, I have indirectly reconciled the QBRM and handwritten addressed letter mail flow model costs to the CRA in the most reasonable manner that I could.

(b) Confirmed. As discussed in MMA-T-1, Mr. Miller's workshare cost savings analysis is flawed because of the removal of several relevant cost pools from the analysis. This flaw also affects his derived CRA proportional adjustment factors.

(c) I did not "modify the CRA adjustment factor from 0.995 to 1.19" as you imply. I derived the CRA adjustment factor independently as shown in Library Reference MMA-LR-1 at 8. The CRA adjustment factor that I derive is the ratio between the weighted averaged CRA-derived unit cost to the weighted averaged mail flow model-derive unit cost, for all presorted mail.

Mathematically, the higher the CRA proportional adjustment factor, the greater the cost difference between two unit costs will become, as computed in Exhibit KE-1A. My derived CRA adjustment factor for Non-Automation letters is 1.31. *See* MMA-LR-1 at 3. Had I used this CRA adjustment factor, which was Mr. Campbell's recommendation, my derived prebarcoded cost savings would have been 3.94 cents or 10 % higher. However, as discussed above, I do not agree with Mr. Campbell's stated

reason for using the non-automation CRA adjustment factor and, accordingly, rejected its use.

USPS/KE-T1-26

In Docket No. MC99-2, USPS witness Ellard performed a special study to "determine the level of interest in new accounting methods and fees for nonletter-size Business Reply Mail (BRM)". See Docket No. MC99-2, USPS-T-2, p.1. In that study, he attempted to find out what mail recipients would be interested in such a classification and how much mail could be expected to be returned under the newly proposed BRM nonletter fee. Did you perform any similar study with respect to QBRM received in high volumes? If so, please provide the results of your study.

RESPONSE:

KE counsel asked Postal Service witnesses this same question. For Mr. Campbell, the question is virtually identical, word for word. *See* TR 14/5932. Mr. Campbell's answer was that no such study was performed. Ms. Mayo indicated that no such study was necessary. *See* TR 14/5572-73. Apparently, the Postal Service was willing to proceed with its proposal without the benefit of any marketing studies.

I have not attempted to conduct a new, similar study to that provided by Mr. Ellard in Docket MC 99-2. Nor am I very familiar with that study. However, I have used extensive actual up-to-date QBRM market data that was available to, but not used by, Postal Service witnesses Campbell and Mayo. *See* Library Reference KE-LR-1. I have already provided the results of my study as part of my direct testimony. Using those data, I estimate the number of accounts likely to take advantage of the lower per piece fee for High Volume QBRM, the likely number of pieces received by High Volume QBRM recipients, and the manner in which those pieces are likely to be counted. *See* Exhibits KE-1B, 1D, 1G and KeySpan Library Reference KE-LR-1.

These data also indicates several weaknesses inherent in the Postal Service's presentation perhaps caused by its failure to consider marketing data in formulating its QBRM fee proposals.

DECLARATION

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

Richard E. Bentley

Dated: June 30, 2000
Vienna, Virginia