

USPS-T-29

BEFORE THE  
POSTAL RATE COMMISSION  
WASHINGTON, DC 20268-0001

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POSTAL RATE AND FEE CHANGES, 2001

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Docket No. R2001-1

DIRECT TESTIMONY  
OF  
MAURA ROBINSON  
ON BEHALF OF  
THE UNITED STATES POSTAL SERVICE

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1 **Autobiographical Sketch**

2 My name is Maura Robinson. I have been employed by the United States  
3 Postal Service as an Economist in Pricing and Product Design since March 1998.  
4 My primary duties include development of First-Class Mail rate design. I  
5 previously testified before the Postal Rate Commission on the Postal Service's  
6 proposed Priority Mail rates in Docket No. R2000-1.

7 Prior to joining the Postal Service, I worked for the Baltimore Gas and  
8 Electric Company from 1992 through 1998. During my last year at BGE, I held  
9 the position of Pricing Analyst with responsibility for preparing analyses  
10 supporting the company's gas rate filings with the Maryland Public Service  
11 Commission and for analyzing natural gas pipelines' FERC rate proposals and  
12 their impact on BGE. From 1992 to 1997, I was a Forecaster with responsibility  
13 for preparation of the company's gas system sales and peak forecast used in gas  
14 capacity planning. This forecast was included in the company's annual Gas  
15 Purchase and Conservation Plan filed with the Maryland Public Service  
16 Commission. In addition, I prepared BGE's 1992-1995 Fuel Price Forecasts  
17 which were included in the company's electric Integrated Resource Plan filed with  
18 the Maryland PSC.

19 I graduated from the University of Maryland at College Park with a  
20 Master's of Arts degree in Economics and also hold Bachelor of Science in  
21 Economics and a Bachelor of Arts in French from Iowa State University.

1 **I. Purpose and Scope of Testimony**

2 My testimony presents the Postal Service's proposed rates for First-Class  
3 Mail. The proposed rates for First-Class Mail meet the cost coverages of 212.0  
4 percent for the Letter and Sealed Parcels subclass and 158.7 percent for the  
5 Cards subclass as proposed by witness Moeller (USPS-T-28). In addition, I am  
6 proposing several classification changes which:

- 7 • deaverage the Automation Basic rate tiers for letters, flats and cards;
- 8 • redefine the Nonstandard Surcharge as a Nonmachinable Surcharge  
9 applicable to mail which cannot be processed on automation or for which  
10 the mailer requests manual processing;
- 11 • update the Domestic Mail Classification Schedule language applicable to  
12 the preparation of cards.

13 An electronic version of the attachments to this testimony will be filed as USPS-  
14 LR-J-102. I am also sponsoring USPS-LR-J-130 which supports an adjustment  
15 to the additional ounce forecasting methodology.

16 In this case, the Postal Service proposes a 37-cent First-Class Mail first-  
17 ounce, single-piece letter rate, an increase of 3 cents or 8.8 percent from the  
18 current 34 cent rate. For the first time, the proposed additional ounce rates for  
19 single-piece and workshare letters differ. For single-piece letters, the additional  
20 ounce rate would remain at 23 cents; however, for workshare mailers, the  
21 additional ounce rate would decrease 0.5 cents or 2.2 percent to 22.5 cents. The  
22 workshare discounts for automation letters, flats and cards would increase 0.5  
23 cents.

**Table 1**  
**First-Class Mail Proposed Rates**  
**Letters and Sealed Parcels**

	<u>Current Rate (cents)</u>	<u>Proposed Rate (cents)</u>
Regular		
Single-Piece: First-Ounce	34.0	37.0
Qualified Business Reply Mail	31.0	34.5
Nonautomation Presort	32.2	35.2
Additional Ounce		
Single Piece	23.0	23.0
Presort	23.0	22.5
Nonmachinable Surcharge		
Single Piece	11.0	12.0
Presort	5.0	5.5
Automation-Presort		
Letters		
Mixed AADC Presort	28.0	30.9
AADC Presort	28.0	30.1
3-Digit Presort	26.9	29.4
5-Digit Presort	25.5	28.0
Carrier-Route Presort	24.5	27.5
Flats		
Mixed ADC Presort	31.2	34.1
ADC Presort	31.2	33.3
3-Digit Presort	29.7	32.2
5-Digit Presort	27.7	30.2
Additional Ounce	23.0	22.5
Nonmachinable Surcharge	5.0	5.5
Heavy Piece Discount	-4.6	-4.1

**Cards**

	<u>Current Rate (cents)</u>	<u>Proposed Rate (cents)</u>
Regular		
Single-Piece	21.0	23.0
Nonautomation Presort	19.0	21.2
Qualified Business Reply Mail	18.0	20.5
Automation-Presort		
Mixed AADC Presort	17.4	19.4
AADC Presort	17.4	18.7
3-Digit Presort	16.8	18.3
5-Digit Presort	16.1	17.6
Carrier-Route Presort	15.0	17.0

1 The discounts for nonautomated presort letters, carrier-route letters and carrier-  
 2 route cards would remain at the levels resulting from Docket No. R2000-1.  
 3 Lastly, I propose the single-piece postcard rate increase from 21 cents to 23  
 4 cents or 9.5 percent.

5 The proposed rates would result in average changes in First-Class Mail  
 6 revenue per piece (including fee revenue) of:

7	Letters and Sealed Parcels Subclass	8.2%
8	Cards Subclass	9.7%
9	Total First-Class Mail	8.2%

## 10 **II. First-Class Mail Characteristics**

11 First-Class Mail consists of mailable matter weighing 13 ounces or less  
 12 including business and personal correspondence, cards, sealed parcels, bills,  
 13 invoices, remittances, financial statements, and advertising. All mailable matter  
 14 weighing 13 ounces or less may be sent as First-Class Mail. In FY2000, First-  
 15 Class Mail volume was 103.5 billion pieces, resulting in total revenue of \$35.5  
 16 billion. First-Class Mail was the largest mail classification in both volume and  
 17 revenue, contributing 50 percent of domestic mail volume and 59 percent of  
 18 domestic mail revenue (excluding special services). First-Class Mail volume has  
 19 increased in every year since 1976; and, over the ten years from 1991 to 2000,  
 20 First-Class Mail volume grew at an average annual rate of 1.5 percent. Similarly,  
 21 over the ten years from 1991 to 2000, First-Class Mail revenue grew at an



1 average annual rate of 2.9 percent.<sup>1</sup> A complete revenue and volume history is  
2 available in USPS-LR-J-91.

### 3 **III. Rate History**

4 The First-Class Mail rate history is included in USPS-LR-J-90. Since  
5 reorganization, the First-Class Mail, single-piece, first-ounce rate increased 11  
6 times to 34 cents, the rate resulting from Docket No. R2000-1. The additional  
7 ounce rate is charged for each ounce or fraction of an ounce a mail piece weighs  
8 above the first ounce. This rate is uniform for all ounce increments above one  
9 ounce and, historically, has been the same for single-piece and workshared mail.  
10 As discussed below, in this docket, I propose that the additional ounce rate differ  
11 for single-piece and workshare mail. The “degression” (or amount that the  
12 additional ounce rate is below the single-piece, first-ounce rate) has increased  
13 over time to the current 11 cents (34 cents less 23 cents). This proposal  
14 increases the degression to 14 cents for single-piece letters.

15 The Postal Service first introduced worksharing in First-Class Mail with the  
16 establishment of a 3/5-digit presorted letter rate in 1976. Workshare  
17 opportunities have increased with the introduction of carrier route presort  
18 discounts in 1981, ZIP+4 discounts in 1983, and barcode discounts in 1988.  
19 While the requirements for these discounts have evolved over time, most notably  
20 following Docket No. MC95-1, the Postal Service’s goal of increasing the  
21 automation compatibility of First-Class Mail (particularly of letter-shaped pieces)  
22 has been implemented largely through the rate structure.

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<sup>1</sup> USPS-LR-J-91.

1 **IV. Rate Design**

2 **A. Calculation of Test-Year Volumes**

3 Witness Tolley (USPS-T-7) projects volumes for the major First-Class Mail  
4 rate categories. Based on this forecast, I am projecting volumes for several  
5 smaller rate elements,<sup>2</sup> as well as test-year additional ounce volume. The  
6 methodology for projecting volume associated with each of these rate elements  
7 applies a “base-year ratio” to the projected test-year volume by rate category.  
8 The base-year ratio is defined as the ratio of base-year transactions divided by  
9 the rate category volume. For example, for the Nonautomation Presort heavy  
10 piece discount, the base year ratio is the number of pieces paying the heavy  
11 piece discount divided by the total number of Nonautomation Presort pieces.  
12 This ratio is multiplied by the test-year Nonautomation Presort volume yielding  
13 the projected number of Nonautomation Presort pieces which will pay the heavy  
14 piece discount in the test year.

15 As described below, several adjustments were necessary to ensure that  
16 the test-year volume projections (both before- and after-rates) for all rate  
17 elements in this case were accurate. I discuss volume adjustments affecting only  
18 the test-year-after rates with the associated rate design analysis.

19 **1. Census Adjustment**

20 The United States Census Bureau conducted the decennial national  
21 population census in March 2000 and, in a series of mailings, entered over 393

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<sup>2</sup> Qualified Business Reply Mail, nonmachinable surcharge, and heavy-piece discount.

1 million pieces of First-Class Mail concentrated in the single-piece letter and  
2 nonautomation presort rate categories. The Census will not recur in the test-  
3 year, and therefore, before calculating the base-year ratios, I adjusted the base  
4 year volume to exclude Census 2000 mail pieces. Attachment B.

## 5 **2. Docket No. R2000-1 Automation 3/5-Digit Presorted Flat** 6 **Adjustment**

7 As a result of Docket No. R2000-1, the Automation 3/5-Digit Presorted  
8 Flats rate category was deaveraged into Automation 3-Digit Presorted Flats and  
9 Automation 5-Digit Presorted Flats. Because these rates have only been in  
10 effect for a short time, I project test-year volumes for these two new rate  
11 categories using mail characteristics data accepted by the Commission in its  
12 R2000-1 Recommended Decision. Consistent with the Commission's  
13 Recommended Decision, I assumed that the majority (89.1 percent) of  
14 Automation 3/5-Digit Presorted Flats are 5-Digit Flats and the remainder (10.9  
15 percent) are 3-Digit Flats.<sup>3</sup>

## 16 **3. Additional Ounce Forecast**

17 In its R2000-1 Recommended Decision, the Postal Rate Commission  
18 discussed two alternate forecasting methodologies for additional ounces. PRC  
19 Op. Docket No. R2000-1 at 246-250. Method 1 assumed that the number of  
20 additional ounces per single-piece letter and the number of additional ounces per  
21 workshared letter by rate category were constant between the Docket No.  
22 R2000-1 base year and test year. Method 2 assumed that the additional ounces  
23 per piece for all mail in the Letters subclass and for the workshared portion (by

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<sup>3</sup> Docket No. R2000-1, PRC Op. at 244.

1 rate category) of the Letters subclass would remain the same between the  
2 Docket No. R2000-1 base year and test year. In evaluating these two methods  
3 for use in First-Class Mail rate design, I became aware that changes in the  
4 additional ounce data series make long-term trend analysis difficult<sup>4</sup> and result in  
5 a short period of data (GFY 1998 – GFY 2000) for which I could estimate the  
6 impact of the data series changes and “wash out” some of the inconsistencies.<sup>5</sup>

7 Using data from three different base periods (GFY 1998, GFY 1999, and  
8 the four postal quarter period PQ3FY1999 - PQ2FY2000), I estimated the  
9 number of First-Class Mail additional ounces for GFY 1999 and GFY 2000 and  
10 compared these estimates to the number of additional ounces reported in the  
11 Postal Service’s billing determinants for those years. It appears that Method 1  
12 underestimates additional ounces while Method 2 overestimates additional  
13 ounces. Therefore, neither method is ideal for postal ratemaking. However, due  
14 to the short time available to prepare the Postal Service’s proposal for this case  
15 and the inherent inconsistencies in the additional ounce data series, I did not  
16 attempt to analyze alternate methods for forecasting additional ounces.

17 Faced with the choice between two imperfect methods, I decided to  
18 forecast additional ounces using Method 1 (the method used by the Postal

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<sup>4</sup> These changes include: (1) the implementation of the Docket No. MC95-1 classification changes; (2) a change in the methodology used to calculate additional ounces beginning in GFY 1998; and (3) the Docket No. R97-1 First-Class Mail and Standard (A) Mail classification changes.

<sup>5</sup> The additional ounce data for even this short period are not consistent. To use these data, I needed to make adjustments for (1) a reclassification increasing the maximum weight for First-Class Mail following Docket No. R97-1 and (2) the 2000 Census. See USPS-LR-J-130.

1 Service and the Postal Rate Commission in omnibus rate cases prior to Docket  
2 No. R2000-1), with an adjustment of 1 percent in additional ounce volume added  
3 in recognition of the observed underestimation. This adjustment is conservative  
4 but recognizes that the revenue generated by First-Class Mail additional ounces  
5 is likely to be greater than that projected by a strict application of a relatively  
6 simplistic forecasting methodology. Alternatively, Method 2 could have been  
7 used to forecast additional ounces. However, if I had chosen this option, a  
8 similar (but negative) adjustment would have been required to recognize the  
9 observed overestimation of additional ounces.

## 10 **B. Rate Design Issues**

11 Witness Moeller's testimony (USPS-T-28) explains why the First-Class  
12 Mail rate proposal is consistent with statutory postal ratemaking criteria. In  
13 designing First-Class Mail rates, I also considered the following rate design  
14 issues.

### 15 **1. Benchmarks**

16 To design First-Class Mail rates, an appropriate point of comparison – or  
17 benchmark – must be established to determine worksharing-related cost savings.  
18 The benchmark is the mail type used as the standard for computing cost savings  
19 associated with worksharing. Witness Miller (USPS-T-22) computed the cost  
20 avoidances and describes why the chosen benchmarks represent the mail most  
21 likely to take advantage of additional worksharing opportunities.

22 The Commission discussed benchmarks in its Docket No. MC95-1  
23 Opinion, generally concluding that discounts should be based on the costs that

1 the worksharing activity (presortation, mailer barcoding) avoids. Setting  
2 discounts to compensate mailers only for the costs avoided by the Postal Service  
3 provides bulk mailers an incentive to presort or apply a barcode only if they can  
4 do so at lower cost than the Postal Service. Benchmarked cost avoidances  
5 provide important data on the Postal Service's avoided costs; however, they do  
6 not necessarily form a complete picture of the Postal Service's cost structure.

## 7 **2. Postal Service Automation Goals and Discount Trends**

8 The Postal Service relies on automation to control the costs of mail  
9 processing and delivery functions and, as witness Kingsley discusses, is working  
10 toward a mailstream that is as barcoded and automation compatible as  
11 practicable. USPS-T-39. In consideration of the importance of the automation  
12 program, the proposed discounts must recognize the need for continued mailer  
13 participation in the automation program. Table 2 highlights the recent trend in  
14 discounts for both 3-Digit and 5-Digit letters. In FY 2000, these two rate  
15 categories comprised 76 percent of workshared First-Class Mail Letters. As  
16 indicated in Table 2, discounts for 3-Digit and 5-Digit Automation letters have  
17 increased between Docket No. R94-1 and Docket No. R2000-1.<sup>6</sup>

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<sup>6</sup> The unique circumstances surrounding Docket No. R2000-1 resulted in a decrease in the 5-digit automation letter rate in July 2001.

**Table 2**  
**First-Class Mail 3-Digit and 5-Digit Letters**  
**Discount Summary**  
**(in cents)**

<u>Rate Category</u>	Discount from Single-Piece Letter Rate			
	<u>Docket No.</u> R94-1	<u>Docket No.</u> MC95-1	<u>Docket No.</u> R97-1	<u>Docket No.</u> R2000-1
3-Digit Letter	5.6	6.6	6.9	7.1
5-Digit Letter	6.2	8.2	8.7	8.5

1           Witness Miller (USPS-T-22) estimates smaller avoided cost differences  
2 between automation tiers than the discounts resulting from Docket R2000-1. As  
3 a result, if the proposed workshare discounts were tied strictly to avoided costs,  
4 many discounts would be reduced, thus threatening the continued success of the  
5 Postal Service's automation program. Instead, the Postal Service's proposal in  
6 this docket generally increases workshare discounts for automation letters and  
7 cards.

8           This rate decision recognizes three factors. First, the Postal Service  
9 chose to target its automation program at letter-shaped mail, with the result of  
10 considerable success in reducing the costs of processing this mail. A departure  
11 from the incentives already established may jeopardize the gains that reduced  
12 overall operating costs for mailers.

13           Second, on average, the automation mail stream appears to be relatively  
14 low-cost as compared to nonautomation mail. Witness Miller's cost avoidance  
15 estimates (USPS-T-22) are designed to capture the costs of avoided Postal  
16 Service operations and his estimates may not reflect factors such as mail  
17 characteristics or additional activities that the Postal Service does not perform  
18 (and thus cannot be "avoided"), but which do provide a benefit to the Postal

1 Service. Calculation of revenues as a percent of volume variable costs indicates  
2 that the automation mail stream provides a high relative contribution to the Postal  
3 Service's institutional costs. In the base year (which does not include the effect  
4 of either the R2000-1 rate increases or the R2001-1 proposed rate increase), that  
5 implicit coverage was 281.6 percent, considerably higher than has been implied  
6 by the Postal Rate Commission's recent Recommended Decisions.<sup>7</sup>

7 Third, the Postal Service is concerned about the impact on these  
8 customers whose efforts have played a part in the success of our automation  
9 program. All First-Class Mail customers have enjoyed the benefits of the  
10 moderate rate increases resulting from the relatively low cost increases for  
11 workshared mail. This can be seen in the relatively high implicit cost coverages  
12 for workshared mail. If the Postal Service rigidly adhered to a policy of 100  
13 percent passthroughs of avoided costs, automation discounts would decrease by  
14 up to 13 percent.<sup>8</sup>

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<sup>7</sup> Methodological differences in the estimation of costs do not permit straightforward comparisons between the Postal Service's and the Postal Rate Commission's calculated ratio of revenue to costs for workshared mail. Using the Postal Rate Commission's costing methodology, the ratio of revenue to costs for workshared mail in the base year is 256 percent. USPS-LR-J-74. For the test-year-after rates, using the PRC's costing methodology, this ratio is 267 percent. USPS-LR-J- 89. Compare this ratio to the similar ratio from the Docket No. MC95-1 Recommended Decision – 237.1 percent. (Docket No. MC95-1, PRC Op. at Appendix F) and the ratio from the Commission's R2000-1 Recommended Decision – 248.1 percent. (Revenues: Docket No. R2000-1, PRC Op. at Appendix G, p. 2; costs: Docket No. R2000-1, PRC Op. at Appendix J, p. 1.)

<sup>8</sup> The estimated cost avoidance for a 5-Digit automation letter is 7.425 cents. USPS-T-22 at Table 1. If this cost avoidance passthrough were approximately 100 percent, the resulting discount would be 7.4 cents or a 12.9 percent reduction in the 5-Digit automation discount [= (7.4-8.5)/8.5] or a 16.1 percent increase (to 29.6 cents) in the 5-Digit automation rate.



1           The treatment of workshare discounts in instances where they have been  
2 an important component in controlling costs is an issue ripe for longer-term  
3 investigation in First-Class Mail rate design. As efforts to encourage worksharing  
4 are successful, avoided costs appear to decline. The result is larger rate  
5 increases (on a percentage basis) for customers who have been critical to the  
6 Postal Service's success. This must be addressed, in the long-term, as well as  
7 the more traditional workshare signals sent through the discount structure.

8           While neither the Postal Service nor the Postal Rate Commission has  
9 generally considered implicit cost coverage calculations below the rate subclass  
10 level to be a primary basis for First-Class Mail rate design, a review of this  
11 information provides additional evidence that the net rate increase for automation  
12 rate mail should be mitigated.

13           **C.     First-Class Mail Rate Proposal: Letters and Sealed Parcels**  
14                   **Subclass**

15                   **1.     Single-Piece Letters, Flats and Parcels**

16           The current, single-piece letters, flats and parcels rate structure consists  
17 of four components:

- 18                   •     the single-piece, first-ounce rate;
- 19                   •     the Qualified Business Reply Mail (QBRM) rate;
- 20                   •     the additional-ounce rate;
- 21                   •     the nonstandard surcharge

22           The Postal Service proposes one change to this rate structure. As discussed  
23 below, I am proposing that the current nonstandard surcharge be extended to  
24 mail that is nonmachinable, either due to physical characteristics or because the

1 mailer requests manual processing. The surcharge will be renamed the  
2 “nonmachinable surcharge” to reflect this change.

3 **a) First-Ounce Rate**

4 The basic one-ounce rate is the most visible and important rate in the  
5 eyes of the general public. In FY 2000, the first-ounce rate alone accounted for  
6 about 28.3 percent of domestic mail revenue (excluding special services), more  
7 than any other rate category in any other class of mail. The Postal Service is  
8 proposing an increase of three cents, or 8.8 percent, in the basic rate. This  
9 increase is consistent with the Postal Service’s revenue requirement and the  
10 statutory ratemaking criteria of the Act. Given the revenue requirement  
11 developed by witness Tayman (USPS-T-6), any smaller increase in this rate  
12 would impose unreasonably large rate increases in other classes of mail.  
13 Conversely, a larger increase in the basic rate would unfairly relieve other mail  
14 classes of their fair share of the institutional cost burden. For administrative ease  
15 and to avoid unnecessary complexity for the mailing public, the Postal Service  
16 considers that rates widely used by the general public should continue to be  
17 priced in whole cents.

18 **b) Qualified Business Reply Mail**

19 Qualified Business Reply Mail (QBRM) receives a postage discount in  
20 recognition of the costs avoided by the Postal Service because the mail piece  
21 design is automation-compatible. QBRM recipients pay both discounted  
22 postage, discussed below, and per-piece fees discussed in the testimony of  
23 witness Mayo (USPS-T-36). The Postal Service proposes a 3.5-cent increase in

1 the QBRM postage rate, from 31.0 to 34.5 cents. This is an 11.3 percent rate  
2 increase and reflects a reduction of 0.5 cents in the postage discount from 3.0  
3 cents to 2.5 cents.

4 The cost study prepared by witness Miller (USPS-LR-J-60) shows a cost  
5 avoidance of 0.846 cents, a significant reduction from the calculated Docket No.  
6 R2000-1 cost avoidance. Therefore, the proposed discount of 2.5 cents implies  
7 a cost avoidance passthrough of 296 percent. While this passthrough is high, I  
8 did not reduce the discount further in recognition of the potential impact on  
9 QBRM recipients. Overall, QBRM recipients will see an increase of 10.3 percent  
10 in the per-piece rate (postage and per-piece fee) for QBRM pieces.<sup>9</sup>

#### 11 **c) Single-Piece Additional Ounce Rate**

12 This rate is charged for every ounce (or fraction thereof) above the first-  
13 ounce in weight of a single-piece First-Class Mail piece. I propose that the  
14 additional ounce rate for single-piece First-Class Mail pieces remain unchanged  
15 at 23 cents.<sup>10</sup> This proposal increases the “degression” between the single-  
16 piece, first-ounce rate and the single-piece additional ounce rate from 11 cents to  
17 14 cents.

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<sup>9</sup> The per-piece (postage and fee) rate for QBRM is currently 32 cents (31 cents postage plus 1 cent fee); under the Postal Service’s proposed rates and fees the per-piece rate for QBRM is 35.3 cents (34.5 cents postage plus 0.8 cents fee). See USPS-T-36 for the fee design.

<sup>10</sup> Currently, the additional-ounce rate is the same for single-piece and workshared First-Class Mail. As discussed below, I am proposing that the additional ounce rate for workshared First-Class Mail differ from the single-piece additional ounce rate.



1 apply to all nonmachinable mail. As discussed in the testimony of witness  
2 Kingsley,<sup>11</sup> certain letter-mail pieces that:

- 3 (a) are polybagged or polywrapped;
- 4 (b) have clasps, strings, buttons or similar closures;
- 5 (c) are non-rectangular;
- 6 (d) contain rigid or odd-shaped items such as pens or pencils; or
- 7 (e) have other characteristics that interfere with machinability

8 increase the Postal Service's letter mail processing costs by forcing processing  
9 to manual operations. In addition, some mailers specifically request manual  
10 processing of mail that otherwise would be automation-compatible thus imposing  
11 costs on the Postal Service that would have been avoided if the mail pieces were  
12 processed on automation. Extending the surcharge to include nonmachinable  
13 mail and manual processing requests meets the criteria specified in Postal  
14 Reorganization Act §3623(c). It is fair and equitable (criterion 1) since it requires  
15 mailers to pay rates that recognize some of the higher costs associated with  
16 nonmachinable and manual-request mail. At the same time, those mailers who  
17 prepare machinable mail will not be unfairly penalized by the upward pressure on  
18 costs caused by nonmachinable pieces. In the case of manual processing  
19 requests, the extension of the classification also recognizes the higher value of  
20 service (criterion 2) which mailers receive when the Postal Service fulfills manual  
21 processing requests.

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<sup>11</sup> USPS-T-39 at sections IIA3 and IIA4.

1           Witness Miller (USPS-T-22) estimates that the additional mail processing  
2 costs for single-piece nonstandard pieces (under the current definition) is 23.754  
3 cents. While costs for single-piece nonmachinable pieces (the expanded  
4 definition) are not estimated separately, the cost estimates for nonautomation  
5 presort nonmachinable mail suggest that they are significant. Even the very  
6 conservative assumption that nonmachinable, single-piece costs would be no  
7 greater than the average cost for nonmachinable, nonautomation presort pieces  
8 suggests that this mail imposes an additional cost of at least 12.809 cents per  
9 piece on the Postal Service.<sup>12</sup> The surcharge has not been increased since  
10 1995, following the implementation of Docket No. R94-1. The modest increase  
11 proposed in this case is amply supported by the cost data. The nonmachinable  
12 surcharge will play an important role in signaling mailers that the cost of  
13 processing nonmachinable pieces is significantly higher. However, we generally  
14 believe that it is appropriate for mail with widely disparate costs to be charged  
15 appropriately. Not only does this spread the processing cost burden equitably,  
16 but it provides appropriate signals to mailers so they can evaluate the relative  
17 costs of making their mail pieces machinable.

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<sup>12</sup> This assumption is conservative because it assumes that some proportion of the single-piece mail stream would be presorted. This is not a requirement for single-piece rates.

1                   **2.     Workshared Letters**

2                           **a)     First-Ounce Rates**

3                                   **(1)    Nonautomation Presort**

4           The Postal Service proposes a nonautomation presort rate of 35.2 cents,  
5 or 1.8 cents below the proposed single-piece rate. This proposal maintains the  
6 current discount and reflects the measured cost avoidance for machinable  
7 nonautomation presort letters of 0.795 cents, as compared to the benchmark. In  
8 prior dockets, the cost avoidance was computed for all nonautomation presort  
9 including nonmachinable pieces; in this filing, the cost avoidance for this rate  
10 category is calculated for machinable letters only.

11           The resulting passthrough is 226 percent. That alone might have  
12 suggested a further reduction in the discount. However, a further reduction in the  
13 discount (above the 0.7 cent reduction resulting from Docket No. R2000-1) in  
14 conjunction with the extension of the nonmachinable (formerly nonstandard)  
15 surcharge could result in a significant impact for customers mailing at the  
16 nonautomation presort rate. Therefore, I chose to mitigate the impact on  
17 nonautomation presort mailers and maintain the discount at the current level.  
18 However, if the apparent cost trends continue, mailers may expect further  
19 discount reductions.

**Table 3**  
**Unit Cost Savings and Discounts for Automation Letters**

	Unit Cost Savings (cents)	Proposed Discount (cents)	Pass Through
<u>Bulk Metered Letters</u>			
Mixed AADC	5.117	6.1	119%
AADC	5.985	6.9	115%
3-Digit	6.299	7.6	121%
5-Digit	7.425	9.0	121%

1 **(2) Automation Letters**

2 The current rate structure for bulk automation letters consists of four tiers:  
3 Basic, 3-Digit, 5-Digit, and Carrier Route. The Postal Service is not proposing  
4 any changes in the piece minimums associated with the rate structure. In  
5 addition, all existing automation tiers will be retained, with the exception that we  
6 propose that the current basic automation tiers for both letters and flats be  
7 disaggregated into a mixed AADC rate and an AADC rate.<sup>13</sup>

8 Table 3 shows the unit cost savings for the bulk automation letter tiers in  
9 relation to the bulk metered mail benchmark. The passthroughs and the  
10 discounts that underlie the proposed rates were selected to balance several  
11 goals, including: (1) achieving the cost coverage target provided by witness  
12 Moeller (USPS-T-28); (2) recognizing the value of mailer worksharing; (3)  
13 avoiding changes in discount levels which result in disruptive rate impacts; (4)  
14 acknowledging the importance of mailer barcoding and presortation in overall

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<sup>13</sup> Concurrent with the implementation of Docket No. R2001-1, the Postal Service intends to make 3-digit sortation optional. Therefore the deepest level of sortation required for automation letters will be an AADC sort.



1 postal operations, and; (5) recognizing that, overall, automated letters are a low  
2 cost, high contribution mail stream. Mailers have invested significantly in  
3 automation equipment and changed their mail processes as a result of the recent  
4 expansion in worksharing incentives, and it would be unfair to sharply reverse  
5 these incentives. At the same time, the Postal Service could experience  
6 operational difficulties if a large portion of the workshared First-Class Mail pieces  
7 reverted to the Postal Service for sorting and barcoding.

8         The issues surrounding the relative cost contribution of automation mail  
9 have been discussed above. The relatively high implicit cost coverage for  
10 workshared mail would appear to suggest that the rates for automation letters are  
11 higher than otherwise would be warranted. However, this is contrasted with the  
12 cost avoidances calculated by witness Miller, which suggest that the discounts  
13 for automation letters should not be increased. In balancing these two factors, I  
14 have determined that a 0.5 cent increase in automation letter discount will  
15 mitigate the impact of this proposed rate increase on automation mailers with  
16 resulting in passthroughs that are only modestly above 100 percent.

17         For operational reasons, as discussed in the testimony of witness  
18 Kingsley,<sup>14</sup> the Postal Service is proposing that the Basic Automation rate tier be  
19 deaveraged into Mixed-AADC and AADC rate tiers. Letters in Mixed-AADC trays  
20 require no specific presortation and are relatively expensive to process. A  
21 requirement to sort mail to the AADC level will encourage finer presortation by  
22 mailers when the necessary volume exists. This will send the proper rate signals

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<sup>14</sup> USPS-T-39 at Chapter II, section A4.

1 to mailers about the costs of processing their mail and will eliminate a current  
2 incentive for mailers to “split” mailings and reduce density to avoid a mandatory  
3 AADC sort. Mail characteristics data indicate that 48.3 percent of Basic  
4 Automation letters are sorted to the mixed-AADC level and 51.7 percent are  
5 sorted to the AADC level. These data were used to project test-year-after-rates  
6 volume and revenue for the new rate categories.

7 I am proposing that the discount for Carrier Route letters remain the same  
8 at 9.5 cents per piece. The 1.620 cents cost avoidance might suggest that the  
9 discount should be expanded, but this would neglect the relative costs of Carrier  
10 Route and 5-Digit presorted mail. While a carrier-route sortation has a high value  
11 where it is permitted (hence the high cost avoidance as compared to the  
12 manual/CSBCS 5-Digit sites benchmark), the relative work-sharing related unit  
13 cost of a Carrier Route piece is greater than that of a 5-Digit piece. USPS-T-22  
14 at Table 1. Therefore, an increase in the automation carrier-route discount as  
15 compared to the single-piece, first-ounce rate would be inappropriate.

### 16 (3) Automation Flats

17 The current rate structure for bulk automation flats consists of three tiers:  
18 Basic, 3-Digit, and 5-Digit. The Postal Service is not proposing any changes in  
19 the piece minimums associated with the rate structure. In addition, all existing  
20 automation tiers will be retained, with the exception that we propose that the  
21 current Basic Automation tier for flats be disaggregated into a mixed-ADC rate  
22 and an ADC rate similar to automation letters. Mail characteristics data indicate  
23 that 65.1 percent of Automation Basic flats are sorted to the mixed-ADC level

1 and 34.9 percent are sorted to the ADC level. These data were used to estimate  
2 the test-year-after-rates volume and revenue for the new rate categories.

3 For operational reasons, as discussed in the testimony of witness Kingsley  
4 (USPS-T39), the Postal Service is proposing that the Basic Automation rate tier  
5 be deaveraged. Flats in Mixed-ADC trays require no specific presortation and  
6 are relatively expensive to process. An increased rate incentive to sort mail to  
7 the ADC level will encourage finer presortation by mailers when the necessary  
8 volume exists. This will send the proper rate signals to mailers about the costs of  
9 processing their mail and will eliminate a current incentive for mailers to “split”  
10 mailings and reduce density to avoid mandatory ADC sort.

11 The Postal Service proposes a one-half cent increase in the discounts for  
12 all automation flats. The proposed bulk automation flat rates are designed  
13 primarily to preserve the appropriate rate relationships between letters and flats  
14 in the automated arena, and between automation flats and the nonautomation  
15 presort rate that applies to both letters and flats. With the proposed rate  
16 relationships, barcoded flats pay less postage than nonautomation presort flats,  
17 and more postage than barcoded letters at all automation tiers. This design is  
18 consistent with the postal ratemaking criterion which calls for simple, identifiable  
19 relationships among rates.

20 **b) Nonmachinable Surcharge**

21 The Postal Service is proposing to increase the current nonstandard  
22 surcharge for presorted pieces from 5 cents to 5.5 cents. For the reasons  
23 discussed above, in recognition of an extension of the mail characteristics to

1 which the surcharge will apply, I am proposing that the surcharge be renamed  
2 the “nonmachinable surcharge.” The cost data provided by witness Miller  
3 (USPS-T-22) amply support the increase in the surcharge for presorted mail.  
4 Consistent with the results in prior dockets, the additional cost associated with  
5 processing a nonstandard piece is 9.463 cents, significantly above the proposed  
6 surcharge. In addition, even at the finest level of sortation, the additional cost for  
7 a nonmachinable piece is 7.197 cents above the cost for a machinable piece –  
8 again considerably above the proposed surcharge. As a result of the extension  
9 of the surcharge to nonmachinable letters, approximately 24.5 percent<sup>15</sup> of  
10 Nonautomation Presort mailers will pay the surcharge if they do not alter their  
11 mail piece characteristics. Mailers can control whether to pay the nonmachinable  
12 surcharge by evaluating mail piece design and making an economic decision,  
13 weighing the costs and benefits of changing mail piece design versus paying the  
14 surcharge.

15 **c) Workshared Additional Ounce Rate**

16 In this case, the Postal Service proposes different additional-ounce rates  
17 for single-piece letters and workshared letters. The rate for single-piece letters  
18 has been discussed above. The proposed workshared additional ounce rate is  
19 22.5 cents, a 0.5 cent or 2.2 percent decrease from the current rate. While the  
20 institution of a different, fractional, additional ounce rate for workshared mail  
21 would complicate the rate schedule somewhat, the overall impact on the affected

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<sup>15</sup> USPS-LR-J-60 at 50. The proportion used for the volume of nonmachinable mail is based solely on the physical characteristics of the mail piece. Some additional (unquantified) volume would be subject to the nonmachinable surcharge as a result of manual processing requests.



1 R2000-1, use of the cost differential between any two ounce increments as a  
2 basis for rate design is problematic.<sup>17</sup> Despite this, the Heavy Piece Discount  
3 assumes a bright line implying that the marginal cost to the Postal Service of the  
4 second additional ounce of a workshared mailpiece is less than the marginal cost  
5 of either the first or the third or the twelfth additional ounce. This assumption  
6 simply overanalyzes the limited cost data available. In recognition of this and in  
7 conjunction with the proposal to reduce the additional ounce rate for presorted  
8 Letters, the Postal Service intends to move toward eliminating the Heavy Piece  
9 discount in the long-run and incorporating any observed cost differentials  
10 between single-piece and presorted mail into the additional ounce rate for  
11 presorted Letters.

12         However, given the current size of the Heavy Piece Discount, it would  
13 cause significant disruption for some mailers if the Heavy Piece Discount were  
14 completely eliminated as a result of this docket. Therefore, the gradual step of  
15 reducing the Heavy Piece discount in conjunction with the institution of a  
16 degression of the presort additional ounce rate from the single-piece additional  
17 ounce rate will move in the desired direction.

18         **D. First-Class Mail Rate Proposal: Cards Subclass**

19                 **1. Single-Piece Cards**

20         Single-piece cards account for 56 percent of base-year card revenues,  
21 more than any other card rate category. The Postal Service is proposing  
22 a 9.5 percent increase in the single-piece card rate from 21 cents to 23 cents. As  
23 in the past, this rate is proposed in whole cents for administrative ease and to

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<sup>17</sup> Docket No. R2000-1, USPS-T33 at 24.

1 avoid unnecessary complexity for the general mailing public. Coincidentally, the  
2 proposed single-piece postcard rate and the proposed single-piece additional  
3 ounce rate are the same. Implementation of these rates would further decrease  
4 the complexity for the general mailing public, since the same stamp could be  
5 used for both purposes.

6 The single-piece postcard rate was developed consistently with the Cards  
7 subclass cost coverage of 158.6 percent proposed by witness Moeller (USPS-T-  
8 28). If the ratio of revenues to costs were computed for single-piece cards alone,  
9 it would be very low – 112.6 percent. However, a larger rate increase for single-  
10 piece postcards was not proposed because of the potential impact on mailers.

11 Qualified Business Reply Mail postcards receive a postage discount in  
12 recognition of the costs avoided by the Postal Service because the card is  
13 automation-compatible. QBRM recipients pay includes both discounted postage,  
14 discussed below, and per-piece fees discussed in the testimony of witness Mayo  
15 (USPS-T-36). The Postal Service proposes a 13.8 percent increase in the  
16 QBRM postcard rate from 18.0 to 20.5 cents. This reflects a reduction of 0.5  
17 cents in the postage discount from 3.0 cents to 2.5 cents.<sup>18</sup> To qualify for the  
18 discounted rate, mailers need to be pre-approved and prepare prebarcoded,  
19 automation-compatible Business Reply Mail cards. As discussed above, the cost  
20 study prepared by witness Miller shows a significant reduction in the cost  
21 avoidance applicable to both letters and cards. This proposal passes through  
22 294 percent of the estimated cost savings. However, I chose not to further

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<sup>18</sup> See the testimony of witness Mayo, USPS-T-36 for a discussion of BRM fees.

1 reduce the QBRM cards postage discount in recognition of the effect on QBRM  
2 mailers.

## 3 **2. Workshared Cards**

### 4 **a) Nonautomation Cards**

5 The Postal Service proposes a 2.2-cent increase in the nonautomation  
6 presort card rate. This proposal restores the parity between the nonautomation  
7 presort discounts for letters and cards.<sup>19</sup> The cost avoidance for nonautomation  
8 presort letters is the best proxy for the costs avoided by nonautomation presort  
9 cards.

### 10 **b) Automation Presort Cards**

11 The current rate structure for bulk automation cards consists of four tiers:  
12 Basic, 3-Digit, 5-Digit, and Carrier Route. The Postal Service is not proposing  
13 any changes in the piece minimums associated with the rate structure. In  
14 addition, all existing automation tiers will be retained, with the exception that,  
15 consistent with letters, I propose that the current Basic Automation tiers for cards  
16 be disaggregated into a mixed-AADC rate and an AADC rate.<sup>20</sup>

17 For operational reasons, as discussed in the testimony of witness Kingsley  
18 (USPS-T39), the Postal Service is proposing that the Basic Automation rate tier  
19 be deaveraged into Mixed-AADC and AADC rate tiers. Cards in Mixed-AADC  
20 trays require no specific presortation and are relatively expensive to process. A

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<sup>19</sup> The Governor's Docket No. R2000-1 Modification resulted in the discount for nonautomation cards being greater than the discount for nonautomation letters.

<sup>20</sup> Concurrent with the implementation of Docket No. R2001-1, the Postal Service intends to make 3-digit sortation optional. Therefore, the deepest level of sortation required for automation cards will be an AADC sort.



1 requirement to sort mail to the AADC level will encourage finer presortation by  
2 mailers when the necessary volume exists. This will send the proper rate signals  
3 to mailers about the costs of processing their mail and will eliminate a current  
4 incentive for mailers to “split” mailings and reduce density to avoid a mandatory  
5 AADC sort.

6         The cost analysis performed for this docket indicates the cost savings for  
7 all automation tiers are now smaller than the current discounts for these tiers.  
8 USPS-T-22 at Table 1. Consequently, if the proposed workshare discounts for  
9 automation cards were tied strictly to avoided costs, these discounts would need  
10 to be reduced. Instead, as was the case with letters, the passthroughs and the  
11 discounts that underlie the proposed rates were selected to balance several  
12 goals, including: (1) achieving the cost coverage target provided by witness  
13 Moeller; (2) recognizing the value of mailer worksharing, including the high  
14 relative contribution of workshared cards; (3) avoiding changes in discount levels  
15 which result in disruptive rate impacts; and (4) acknowledging the importance of  
16 mailer barcoding in overall postal operations. As a result, the Postal Service’s  
17 rate proposal in this docket expands Automation cards discounts by 0.5 cents.  
18 The Carrier Route discount remains at its current level of 6 cents.

1           **E.     Preparation Requirements for First-Class Cards**

2           The Postal Service proposes updating card preparation requirements by  
3 deleting the specific requirements listed in Domestic Mail Classification Schedule  
4 section 222.2. Some of these requirements are outdated and do not conform to  
5 the current card processing requirements. Mailers will be required to prepare  
6 cards as specified by the Postal Service; however the changes to the preparation  
7 requirements are expected to be minimal and are expected to have little impact  
8 on mailers.