

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

Experimental Periodicals
Co-Palletization Dropship Discounts
For High Editorial Publications

Docket No. MC2004-1

INTERROGATORIES OF TIME WARNER INC.
TO WITNESS TAUFIQUE (TW/USPS-T1-14-22)
(April 2, 2004)

Pursuant to sections 25 and 26 of the Rules of Practice, Time Warner Inc. (Time Warner) directs the following interrogatories to United States Postal Service witness Taufique (USPS-T-1). If witness Taufique is unable to respond to any interrogatory, Time Warner requests that a response be provided by an appropriate person capable of providing an answer.

Respectfully submitted,

s/_____
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INTERROGATORIES TO WITNESS TAUFIQUE (USPS-T-1)

TW/USPS-T1-14. On page 5 of your testimony, line 16, you say: “The challenge for the Postal Service is to find a middle ground between leaving these publications in sacks, and proposing a more fundamental change in the current rate structure at this time.”

- a. Do you agree that the new rates you propose will put in place a set of incentives and options that did not exist before. Explain any disagreement.
- b. Do you agree that mailers and possibly their agents are likely to make changes and invest money in response to these new incentives? Explain any disagreement.
- c. Do you agree that if “more fundamental change[s]” are made to the rate structure at some point in the future, the specific incentives in the current proposal will in all likelihood be withdrawn and the mailers will then be faced with a new set of incentives and options? Explain any disagreement.
- d. (1) Do you believe it is fair and equitable to expect mailers to invest and make changes aligned with the rates in the current proposal and then in a reasonably short period of time to invest and make changes aligned with a “more fundamental” change in the rate structure? (2) Please explain whether you believe it is likely that after adjusting to the second change, mailers might wish they had not adjusted to the first change.
- e. In order to help mailers and their agents to adjust to the changes proposed at this time, please provide information about the nature and timing of any “more fundamental change[s]” that are likely to be proposed in the future.
- f. Assuming “more fundamental” changes are proposed in the future, please explain your opinion on whether the implementation of the more fundamental changes should be tempered so that the adjustment from the proposed rates is limited, thus placing a constraint on the more fundamental changes and decreasing their effectiveness.
- g. Please present any analysis you have done of the extent to which the rates being proposed are in line in a fair and progressive way with any more fundamental changes that are likely to be proposed in the future.

TW/USPS-T1-15. Consider a zone-8 print location that prints 4 journals that weigh 9 ounces each. Two of the journals have 65 percent advertising and can be made eligible for the co-pallet-I discount by co-palletizing the journals and achieving a 300-pound pallet with 533 pieces on it. The other two journals have 15 percent advertising and can be made eligible for the co-pallet-II discount by the same procedure of co-palletizing and achieving a similar 300-pound pallet with 533 pieces. There is nothing in

the operations of the printer (or any transportation agent) that is sensitive to the split between editorial and advertising. In other words, they view all 4 of these publications as operational identical. The printer and the associated publisher are considering DSCF entry.

- a. Please confirm that the co-pallet of 65-percent-advertising publications could under R2001-1 rates receive a dropship discount of \$94.37 ($=533*(0.159047$ discount on advertising + 0.008 per-piece DSCF discount + 0.01 per-piece pallet discount)). Explain any disagreement.
- b. Please confirm that with the co-pallet-I discount of 1 cent per piece, this same pallet of 65-percent-advertising pieces could obtain a dropship discount of \$99.70 ($=94.37 + 533 * 0.01$ co-pallet-I discount). Explain any disagreement.
- c. Please confirm that for this mailer the co-pallet-I experiment is to see if an increase in the discount of 5.6 percent, from \$94.37 to \$99.70 will cause otherwise nonparticipating mailers to begin to participate.
- d. Consider now the co-pallet of 15-percent-advertising publications, and confirm that it could under R2001-1 rates receive a dropship discount of \$29.16 ($=533*(0.0367$ discount on advertising + 0.008 per-piece DSCF discount + 0.01 per-piece pallet discount)).
- e. Confirm that if the co-pallet of 15-percent-advertising publications takes advantage of the proposed co-pallet-II discount, it would receive a dropship discount of \$62.30 ($=29.16 + 533 * \text{the proposed } 0.13 * \text{the editorial weight}$).
- f. Please confirm that for 15-percent-advertising publications, the proposed co-pallet-II discounts become an experiment to see if increasing the dropship discount by 113.6%, from \$29.16 to \$62.30, will cause otherwise nonparticipating mailers to begin to participate.
- g. If there are any mailers similar to the 65-percent-advertising mailers in this example who are not already co-palletizing and dropshipping under current rates for a discount of \$94.37 (even before co-pallet-I discounts are applied), do you believe it is reasonable to expect that 15-percent-advertising mailers similar to those in this example will co-palletize and dropship for a discount of \$62.30?
- h. Has the Postal Service done any analysis to determine the characteristics of mailers already co-palletizing and dropshipping (even before the co-pallet-I discounts became effective) to help assess the likelihood that mailers will find the discounts in co-pallet-II attractive? If it has, please present the results of that analysis. If it has not, please explain whether you believe it is reasonable to expect an organization like to the Postal Service to perform such analyses to use in guiding experiments?
- i. If the Postal Service has not done any analysis allowed by the current rates, as suggested above, would you characterize the proposed experiment as

unsupported by a priori analysis, as suggested on lines 3 through 7 of page 1 of your testimony?

TW/USPS-T1-16. On page 23 of your testimony, lines 12-13, you indicate that your proposal will “help maintain the widespread dissemination of editorial matter.” Please discuss the nature of the test you would use to determine whether the dissemination of editorial matter is less widespread or more widespread under your proposal. Focus only on the concept of the test and not on how to carry it out or on whether it is difficult to carry it out.

TW/USPS-T1-17. On page 1 of your testimony, lines 11-12, you indicate that some “small publications do not find the current discounts attractive enough to change their behavior.”

- a. Please explain whether you have reached a preconceived conclusion that some mailers should change their behavior.
- b. Please explain whether you view the result of whether mailers change their behavior as an indicator of whether the current discounts are adequate. If you do, please provide references to any theoretical literature indicating that the efficiency of a set of rates can or should be measured by whether buyers change their behavior.
- c. Please explain whether you believe that the efficient component pricing rule is based on a presumption that efficient rates can be set without knowing how mailers will respond and then allowing mailers to make their own decisions.
- d. If under the efficient component pricing rule a mailer decides to purchase a high-cost service instead of a low-cost service, do you know of any basis for concluding that this is an undesirable outcome? Explain.

TW/USPS-T1-18. On page 5 of your testimony, lines 6-7, you indicate that the current incentives “do not have a sufficient impact on high-editorial publications.” Please explain how you can tell whether any particular set of rates has a “sufficient” impact on any particular publication.

TW/USPS-T1-19. On page 14 of your testimony, beginning on line 3, you say: “I did not separately analyze potential cost savings, because the differences between the zoned advertising pound rates reflect all pound-related transportation and non-transportation cost savings that accrue to the Postal Service when mail is entered closer to its destination.” Then in a footnote following this sentence, you say: “Further, the pound-related portion of non-transportation cost savings is fully passed through to estimate the destination entry advertising pound rates.”

For purposes of this question, please consider all dropship discounts provided through the advertising pound rates to involve the sum of two components. The first component is from zone z down to zones 1&2 and the second component is from zones 1&2 down to the DSCF, where z can take on values from 3 through 8.

- a. Do you contend that the non-transportation savings of the Postal Service for the first component, from zone z down to zones 1&2, are reflected or recognized in any degree whatsoever in the zoned pound rates from which the dropship discount is calculated? If you do, please provide references to the cost study on which this cost savings is based and describe in detail, using your rate design spreadsheet from Docket No. R2001-1, where and how these savings are built into the zone rates.
- b. If you do not so contend, would you agree that the sentence beginning on line 3, quoted above, is in error? If not, please explain. If so, please provide a corrected sentence.
- c. Please identify the cost study on which the non-transportation savings between zones 1&2 and the DSCF, the second component outlined above, is based, and explain how the pound-related non-transportation costs are developed from it.
- d. If your answer to the question in part a above is essentially “no,” please explain whether the Postal Service has any analysis or other information relating to the non-transportation savings for sacks, and/or pallets, and/or both across the first component, from zone z down to zones 1&2. If it does, please provide that analysis.

TW/USPS-T1-20. On page 14 of your testimony, beginning on line 13, you say: “The existing . rate structure allows the mailer of advertising pounds to make an economic decision regarding dropshipping based on the existing advertising pound rate differentials.”

- a. By “economic decision,” please explain whether you mean that the mailer sees reflected in the rates the postal-resource implications of dropshipping vs. not dropshipping. If you mean something fundamentally different from this, please explain in detail what you mean, including the framework within which the decision is made and any attendant assumptions made.
- b. Do you agree that if any non-transportation costs are *not* reflected in the zoned pound rates, an economic decision of the kind you reference cannot really be made, even for advertising? Explain any disagreement.
- c. Do you agree that periodicals generally have some editorial content and therefore that for any actual publication, an economic decision of the kind you discuss cannot be made, even neglecting questions about how non-transportation costs are recognized? Explain any disagreement.

d. Do you agree that, apart from the rates you propose, mailers of publications that are 100 percent editorial have no information whatever on the postal-resource implications of any decision they might make and therefore that they cannot be expected to make economic decisions?

e. Would you agree generally that if the rates you propose are adopted, mailers of advertising could make economic decisions (except for certain non-transportation costs), most mailers of publications with non-zero portions of editorial could make distorted economic decisions, most mailers of all-editorial publications could make severely distorted economic decisions, and mailers that use the rates you propose could make moderately distorted economic decisions? Explain any disagreement and explain where you see any fairness and equity in partitioning mailers into these camps.

TW/USPS-T1-21. On page 16 of your testimony, beginning on line 21, you say: "Using a 100 percent passthrough of the cost savings would mean providing discount levels that are inappropriately high relative to the base rate."

a. Please explain whether you mean that the base rate minus the discount would result in a negative pound rate for the editorial pounds.

b. Suppose the base postage for a publication is 25 cents, including all piece and pound rates. Now assume this publication dropships and the Postal Service saves 30 cents in transportation costs and 8 cents in non-transportation costs. (1) Do you agree that if 100 percent of the transportation savings were given as a discount, the final postage paid by the mailers would be negative 5 cents? That is, the Postal Service would pay the mailer 5 cents for each piece submitted. Explain any disagreement. (2) Do you agree that for each piece that is both dropshipped and given 5 cents, the Postal Service comes out 8 cents ahead financially? Explain any disagreement. (3) In the general case, please explain why the Postal Service would be opposed to a rate arrangement under which it gained 8 cents for each participating (or cooperating) piece. (4) Please explain in general the nature of the conditions that must exist for rate arrangements involving negative rates to benefit the Postal Service.

TW/USPS-T1-22. Under your proposal, the mailer (or agent) would have to both create the co-pallet and dropship the co-pallet to get the proposed discount. Relative, then, to the possibility of providing a discount for co-pallets entered at the origin office, your proposal involves bundling two separate activities, a co-palletization activity and a dropship activity. Without doing both, no discount is available, even though both cause savings. Please explain the justification for bundling these two activities together instead of offering separate discounts and explain how your proposal aligns with the economic literature suggesting that it is inefficient and inconsistent with the notion of lowest combined cost to bundle separate activities.