

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

EXPERIMENTAL PRIORITY MAIL FLAT-RATE
Box, 2004

Docket No. MC2004-2

RESPONSE OF UNITED STATES POSTAL SERVICE
WITNESS THOMAS M. SCHERER TO OCA INTERROGATORIES
(OCA/USPS-T1-1-16)
(July 1, 2004)

The United States Postal Service hereby files the response of witness Thomas M. Scherer to the following interrogatories of the Office of the Consumer Advocate: OCA/USPS-T1-1-16, filed on June 18, 2004.

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

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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RESPONSE OF POSTAL SERVICE WITNESS SCHERER
TO OCA INTERROGATORY

OCA/USPS-T1-1. Your testimony at pages 4-5 indicates the need to recognize in the pricing of the flat-rate box that the new service "may well attract shipments that are heavier-weight and/or longer-distance than average." You further assume, for purposes of pricing, a base rate of \$5.92 as the estimated average realized revenue from a flat-rate box of .34 cu feet. This assumes "the average is between the Zone 4 and Zone 5 rates, but closer to Zone 4" (testimony page 4) and an average weight for a base line parcel of 2.28 pounds.

Further, your testimony indicates at page 5 that if the average flat-rate box were to "settle" with a relatively small change in those current averages to Zone 5 (less than a whole zone) and to "settle" at 3 pounds (0.72 pounds or only 11.52 ounces greater than your assumed current average of 2.28 pounds) the base rate would jump to \$7.45, only 0.25 cents below the proposed \$7.70 postage rate.

- a. Please confirm that if the average flat-rate box settled at Zone 6 but the weight was 3 pounds, the "base rate" by your method of calculating using Table 6 in Library Reference USPS-LR-1 (the rounded midpoint between the 3 pound rate for Zone 6 of \$7.15 and the 4 pound rate for Zone 6 of \$8.50) would be \$7.83. If you cannot confirm, please explain.
- b. Please confirm that if the average flat-rate box settled at Zone 5 but the weight was 4 pounds, the "base rate" by your method of calculating using Table 6 in Library Reference USPS-LR-1 (the rounded midpoint between the 4 pound rate for Zone 5 of \$8.05 and the 5 pound rate for Zone 5 of \$9.30) would be \$8.68. If you cannot confirm, please explain.
- c. Please confirm that if the average flat-rate box settled at Zone 6 and the weight settled at 4 pounds, the "base rate" by your method of calculating using Table 6 in Library Reference USPS-LR-1 (the rounded midpoint between the 4 pound rate for Zone 6 of \$8.50 and the 5 pound rate for Zone 6 of \$9.85) would be \$9.13. If you cannot confirm, please explain.

RESPONSE:

As clarification, the estimated average realized revenue of \$5.92 ("base rate") is not for a flat rate box of 0.34 cubic feet, but rather for "existing Priority Mail parcels of comparable size." Please see USPS-T-1 at 4, line 18.

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Response to OCA/USPS-T1-1 (Cont.)

Also, my testimony does not indicate or suggest that the changes in average weight and zone resulting in the example of a \$7.45 rate interpolated from the Priority Mail rate schedule are “relatively small.”

(a) Confirmed.

(b) Confirmed.

(c) Not confirmed. The correct interpolated rate is \$9.18.

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TO OCA INTERROGATORY

OCA/USPS-T1-2. Please confirm that currently, the postage for Priority Mail is not impacted by the cubic size of the box.

RESPONSE:

Not confirmed. The Priority Mail rate schedule includes a “balloon charge” for parcels weighing less than 15 pounds but measuring more than 84 inches in combined length and girth. Such parcels are charged the applicable rate for a 15-pound parcel. The length + girth measure is intended as a proxy for cubic volume. So, in some instances, the postage is impacted by the cubic size of the box.

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OCA/USPS-T1-3. Do you agree that if the postage for Priority Mail is not impacted by the cubic size of the box that, on average, customers will use boxes larger than they would otherwise if the postage were greater for larger box sizes?

RESPONSE:

As I said in my response to OCA/USPS-T1-2, the postage for Priority Mail can be impacted by the cubic size of the box. Having said that, I agree that if the postage for Priority Mail is not impacted by the cubic size of the box, some customers might use boxes larger than they would otherwise.

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OCA/USPS-T1-4. Please confirm that if the cubic box size is reduced to ship a given item by Priority Mail, the weight per cubic foot (density) would increase.

RESPONSE:

Confirmed, with a minor caveat. While, as a general matter, a parcel's density will increase if the cubic box size is decreased and the contents stay the same, a counter example can be found. When a parcel with relatively high-density packing material (filler) is reduced in size, it may be possible in some instances for the density to decrease if the packing material is replaced with lower-density packing material (or is not replaced with packing material).

Conversely, when a parcel with relatively low-density packing material (filler) or no packing material is increased in size, it may be possible in some instances for the density to increase if the packing material is replaced with higher-density packing material or if packing material is added for the first time.

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OCA/USPS-T1-5. Your testimony in note 10 at page 7 recognizes some parcels may contain soft goods and could be repackaged to smaller dimensions but no basis for quantifying this potential could be identified. However, have you or anyone else undertaken any study to determine how much customers would reduce the cube size of boxes currently used for Priority Mail, not to repackage compressible goods, but to reduce postage from unnecessarily oversized box cubes, particularly in the lower weight categories under 5 pounds? If not, are there any plans to undertake such a study?

RESPONSE:

Neither I nor to anyone else to my knowledge at the Postal Service has undertaken such a study, nor am I aware of any plans to do so.

The proposed flat-rate box's flat rate and fixed cubic volume will enable some customers to save postage costs by reducing package size – as long as the size is reducible (e.g., the package is “unnecessarily oversized”) and exceeds 0.34 cubic feet. Density (pounds per cubic foot) will increase for such parcels that migrate to the flat-rate box (with the exception of the caveat noted in my response to OCA/USPS-T1-4).

On the other hand, even if the package size is reducible, it will not be possible to achieve an increase in density from parcels that are smaller than 0.34 cubic feet (aside from the condition noted in the second paragraph of my response to OCA/USPS-T1-4). On the contrary, density will *decrease* for such parcels that migrate to the flat-rate box.

The net impact on average density – from migrating parcels bigger than 0.34 cubic feet and smaller than 0.34 cubic feet – is indeterminate.

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TO OCA INTERROGATORY

OCA/USPS-T1-6. Please confirm that if the density of the Priority Mail as calculated in the Postal Service studies is too low by 10 (ten) percent, following your methodology, the average weight for a .34 cubic foot box would rise to 2.51 pounds. If you cannot confirm, please explain.

RESPONSE:

Not confirmed. If the 6.70 pounds per cubic foot calculated by witness Loetscher in USPS-T-3 is “too low by 10 percent” (a hypothetical assumption), then the actual density is $6.70/0.9 = 7.44$ pounds per cubic foot, and the average weight of Priority Mail parcels at 0.34 cubic feet – following the methodology in my testimony – would be $0.34 \times 7.44 = 2.53$ pounds.

Note that if the 6.70 pounds per cubic foot calculated by witness Loetscher in USPS-T-3 is too *high* by 10 percent (also a hypothetical assumption), then the actual density is $6.70/1.1 = 6.09$ pounds per cubic foot, and the average weight of Priority Mail parcels at 0.34 cubic feet – following the methodology in my testimony – would be $0.34 \times 6.09 = 2.07$ pounds.

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OCA/USPS-T1-7. Please confirm that if the average weight for a .34 cubic foot box were 2.51 pounds, the base rate using your methodology would be \$6.25 (the 3 pound weight increment Priority Mail rate). If you cannot confirm, please explain.

RESPONSE:

Not confirmed. Since 2.51 pounds exceeds the assumed average of 2.5 pounds at the 3-pound weight increment, the base rate would have to be interpolated between the average realized revenue per parcel across all zones at the 3-pound and 4-pound weight increments. The former is \$6.25, the latter is calculated in my response to OCA/USPS-T1-9 as \$7.42. Assuming an average weight of 3.5 pounds at the 4-pound weight increment, the base rate would be interpolated as $\$6.25 + [(\$7.42 - \$6.25) \times ((2.51 - 2.50)/(3.50 - 2.50))] = \6.26 .

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OCA/USPS-T1-8. Please confirm that if the density of the Priority Mail as calculated in the Postal Service studies is too low by 20 (twenty) percent, following your methodology, the average weight for a .34 cubic foot box would rise to 2.73 pounds. If you cannot confirm, please explain.

RESPONSE:

Not confirmed. If the 6.70 pounds per cubic foot calculated by witness Loetscher in USPS-T-3 is “too low by 20 percent” (a hypothetical assumption), then the actual density is $6.70/0.8 = 8.38$ pounds per cubic foot, and the average weight of Priority Mail parcels at 0.34 cubic feet – following the methodology in my testimony – would be $0.34 \times 8.38 = 2.85$ pounds.

Note that if the 6.70 pounds per cubic foot calculated by witness Loetscher in USPS-T-3 is too *high* by 20 percent (also a hypothetical assumption), then the actual density is $6.70/1.2 = 5.58$ pounds per cubic foot, and the average weight of Priority Mail parcels at 0.34 cubic feet – following the methodology in my testimony – would be $0.34 \times 5.58 = 1.90$ pounds.

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OCA/USPS-T1-9. Please provide the volume weighted average rate (revenue per parcel) for the 4 pound increment as you have provided for the 2 and 3 pound increments at page 4 of your testimony and USPS-LR-1, Attachment 1, Table 14.

RESPONSE:

\$7.42.

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OCA/USPS-T1-10. Please calculate the estimated base rate using your methodology if the Priority Mail density were 2.73 pounds for a cubic foot box and the 4 pound volume weighted average rate (revenue per parcel).

RESPONSE:

I will assume what is requested is a base-rate calculation based on an average *weight* of 2.73 pounds for a *0.34* cubic foot box. Assuming, also, an average weight of 3.5 pounds at the 4-pound weight increment: $\$6.25 + [(\$7.42 - \$6.25) \times ((2.73 - 2.50)/(3.50 - 2.50))] = \6.52 .

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OCA/USPS-T1-11. Please explain in more detail what characteristics of the box size and other factors supporting your statement on page 6 of your testimony that the box sizes are considered "qualitatively appropriate."

RESPONSE:

The 0.34 cubic feet was consistent with Postal Service's aim for a box size roughly in the range of 0.25 to 0.50 cubic feet. Box sizes below this range ("too small") were judgmentally thought to have limited applicability. Box sizes above this range ("too big") would have carried a relatively high rate that would have been out of proportion to the postage typically borne by Priority Mail parcels.

The 0.34 cubic feet chosen also permitted the dimensions discussed as appropriate in Section III.A of witness Barrett's testimony (USPS-T-2).

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OCA/USPS-T1-12. In your judgment, what is the least amount of total premium you believe is necessary to account for the flat-rate box product's added value and as protection against the possible attraction of relatively heavy and/or long distance shipments to the flat-rate box?

RESPONSE:

As discussed at page 5 of my testimony, I applied my best judgment in aiming for a total premium of \$1.50 to \$2.00. The "least amount" I was willing to posit was therefore \$1.50.

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OCA/USPS-T1-13. Did you seriously consider prices other than two times the one-pound and flat-rate envelope stamp rate? If so, what were those rates and please discuss the reasons you rejected them.

RESPONSE:

Some hypothetical rate calculations were made for different box sizes ranging roughly from 0.25 to 0.5 cubic feet (all the while, maintaining my judgmental \$1.50 to \$2.00 premium over the base rate). Those rates were approximately in the range of \$7.00 to \$8.50, as I recall. However, once it was realized that a \$7.70 rate, conveniently equal to two \$3.85 postage stamps, could be attained with a box size of 0.34 cubic feet, this was the only rate seriously considered.

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OCA/USPS-T1-14. Your testimony suggests at page 5 that in the future if there is a permanent classification for the flat-rate box service, a dedicated stamp could be produced. In your opinion, would that detract from the value added of this service as it would reduce the simplicity of using the same stamps for several types of Priority Mail.

RESPONSE:

I am not an expert on matters concerning methods of postage payment, including the use of stamps, but in my opinion, it might be somewhat more convenient for mailers to be able to keep a supply of just one stamp denomination having three applications (one-pound rate, flat-rate envelope, flat-rate box).

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OCA/USPS-T1-15. Please comment on how this new service relates to the services offered by the competitors of the Postal Service and whether this service is expected to compete favorably with any particular service offered by the competition.

RESPONSE:

As mentioned at page 11 of my testimony, no domestic product comparable to the proposed flat-rate box is currently offered by any Postal Service competitor. As such, the flat-rate box is not positioned against any particular services offered by the competition.

It is my understanding that UPS and FedEx both offer 10 kg and 25 kg (maximum weights) flat-rate boxes for international parcel delivery. However, while these flat rates do not vary by weight, they do vary by zone.

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OCA/USPS-T1-16. Have you or anyone in the Postal Service studied or estimated the potential impact on window service costs or carrier costs resulting from providing this service to current Priority Mail users, considering particularly the increased use of carriers to pick up the flat-rate boxes. If so, please provide the estimated impact on costs.

RESPONSE:

No such cost impacts have been studied. This proposal for an experimental flat-rate box is based on the existing Priority Mail rate schedule without any reexamination of the underlying costs supported by the record in Docket No. R2001-1.

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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July 1, 2004