

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

RATE AND SERVICE CHANGES TO IMPLEMENT
FUNCTIONALLY EQUIVALENT NEGOTIATED
SERVICE AGREEMENT WITH HSBC NORTH
AMERICA HOLDINGS INC.

Docket No. MC2005-2

RESPONSES OF UNITED STATES POSTAL SERVICE WITNESS DAUER TO
INTERROGATORIES OF THE OFFICE OF THE CONSUMER ADVOCATE
(OCA/USPS-T1-1-5)
(March 22, 2005)

The United States Postal Service hereby provides the responses of
witness Dauer to the following interrogatories of the Office of Consumer
Advocate: OCA/USPS-T1-1-5, filed on March 15, 2005.

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

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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Response of Postal Service Witness Dauer to Interrogatories of the OCA

OCA/USPS-T1-1. Please refer to your testimony at page 13, line 3, where you state that you used an “ACS cost savings of \$8.1 million.”

- a. Provide an electronic spreadsheet of this computation.
- b. Explicitly state any assumptions made and the rationale for making them.
- c. Cite or provide any inputs to the computation.
- d. State whether or not you employed the Commission’s method for calculating ACS cost savings. If you did not, please explain your reasons.

Response:

- a.) A spreadsheet is attached.
- b.) Consistent with the assumptions underlying all of my cost models, all costs reflect an annual inflation rate of 4 percent, and a contingency of 3 percent.
- c.) See the attached spreadsheet.
- d.) The Commission’s methodology was employed, subject to the above assumptions.

Calculation of Stop-Loss Cap in Response to OCA/USPS-T1-1

	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Total NSA</u>
A. Effects of ACS (Savings Estimate)				
First-Class Mail Marketing Letters:				
(1) Before Rates Avg. Cost	0.1382	0.1438	0.1495	
(2) Avg. Savings from Returns	0.0090	0.0094	0.0097	
(3) Avg. Savings (Cost) from Forwards	-	-	-	
(4) Total Avg. Savings from ACS	0.0090	0.0094	0.0097	
(5) After Rates Avg. Cost	0.1293	0.1344	0.1398	
(6) Before Rates Volume	196,842,621	298,877,229	363,314,190	
(7) Net Contribution Gain from ACS (Savings)	1,770,784	2,796,228	3,535,049	8,102,061
B. Effects of Lost Contribution (Revenue Leakage)				
(8) Before Rates First-Class Volume	679,863,892	817,284,750	919,784,128	
(9) Volume Threshold for Discounts	615,000,000	725,000,000	810,000,000	
(10) Before Rates Volume Eligible for Discounts	64,863,892	92,284,750	109,784,128	
(11) Average Discount on "Exposed" Volume	0.0273	0.0303	0.0322	
(12) Total Discounts on Before Rates Volume (Leakage)	(1,770,784)	(2,796,228)	(3,535,049)	(8,102,061)
(13) Net Increase in Contribution (before rates volume)	0	0	0	0
(14) Savings from ACS at Break-Even Volume	8,102,061	/1		
(15) Pass-through Percentage	100%			
(16) Stop-Loss Cap Amount	8,102,061			
(17) Ratio of DFS "Competitive Cap" to PRC Cap	1.1009			
(18) Cap with "Competitive Adjustment"	8,919,559			

Citations

- (1) USPST1_Appendix A revised.3.22.05.xls, pg. 11, (7)
- (2) USPST1_Appendix A revised.3.22.05.xls, pg. 11, (7) - (8)
- (3) No forward savings are recognized
- (4) (2) + (3)
- (5) USPST1_Appendix A revised.3.22.05.xls, pg. 11, (8)
- (6) Breakeven Volume
- (7) (4) * (6)
- (8) USPST1_Appendix A revised.3.22.05.xls, pg. 2 + (6)
- (9) USPST1_Appendix A revised.3.22.05.xls, pg. 7
- (10) (8) - (9)
- (11) (7) / (10)
- (12) -((8) -(9)) * (11)
- (13) (7) + (12)
- (14) Total NSA (7)
- (15) MC2004-3 Opinion and Recommended Decision, pg. 68
- (16) (14) * (15)
- (17) MC2004-4 Opinion and Recommended Decision, pg. 36, 42
- (18) (16) * (17)

Response of Postal Service Witness Dauer to Interrogatories of the OCA

OCA/USPS-T1-2. Please refer to Appendix B, page 1. You explain that you have used an inflationary cost growth factor, projected by the Postal Service, of 4 percent.

a. Did you make an independent determination to use a 4 percent growth factor or were you advised by others to do so? Please explain.

b. If it is your independent determination, please explain your rationale for using this growth factor.

c. If others advised you to use this factor, please state their name(s) and position(s). What was the rationale of those identified to use the 4 percent growth factor?

Response:

a- c. I did not make an independent determination of the 4 percent growth factor.

Rather, I relied upon the growth factor used in the models presented by witnesses

Plunkett and Ayub in Docket Nos. MC2004-3 and MC2004-4. That growth factor was

accepted by the Commission in both cases, and was therefore employed in my models

for this case.

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OCA/USPS-T1-3. At the time witness Crum estimated the savings resulting from providing Capital One with electronic return of its solicitation First-Class Mail in lieu of physical return of this mail, was PARS deployed in any postal facilities involved in the physical or electronic return of First-Class Mail?

- a. If so, please list all facilities in which PARS was deployed.
- b. If not, then please confirm that witness Crum's savings estimates did not reflect the use of PARS in the physical or electronic return of First-Class Mail.
- c. Is PARS currently being deployed in any postal facilities?
- d. If so, then please list all facilities in which it is being deployed. Please provide the annual volume of First-Class Mail that is processed through facilities in which PARS is currently being deployed.
- e. What is the target date for the full deployment of PARS?
- f. Is it correct that the use of PARS to effect the physical and electronic return of First-Class Mail involves different operations than those involved in facilities where PARS has not yet been deployed?
- g. If so, please provide a detailed step-by-step comparison of the operations performed on UAA mail in facilities that employ PARS versus facilities that do not employ PARS.
- h. Is it reasonable to expect that the cost of returning UAA mail via facilities that utilize PARS may be different from the cost of returning UAA mail via facilities that do not utilize PARS? Please explain.
- i. Please provide any quantitative information collected or developed by the Postal Service on the difference in cost between UAA mail returned via PARS versus UAA mail returned without PARS.
- j. Please provide any qualitative information collected or developed by the Postal Service on the difference in cost between UAA mail returned via PARS versus UAA mail returned without PARS.

Response:

No.

- a.) Not applicable.
- b.) Confirmed. The cost data on which witness Crum based his analysis were from a pre-PARS environment.
- c.) Phase I was deployed to 49 processing plants by the end of November 2004.

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d.)

PARS Combined Schedule 9/16/2004

Serial Number	Site Name	ST	Area	Site Type
1a	Mid Florida	FL	SE	P&DC
1b	Mid Florida	FL	SE	P&DC
2	Orlando	FL	SE	P&DC
3a	Santa Clarita	CA	PA	P&DC
3b	Santa Clarita	CA	PA	P&DC
4a	Dulles	VA	CM	P&DC
4b	Dulles	VA	CM	P&DC
5	Middlesex-Essex	MA	NE	P&DC
6	North Bay	CA	PA	P&DC
7	North Metro	GA	SE	P&DC
8	Northern Virginia	VA	CM	P&DC
9	Nw Boston (Waltham)	MA	NE	P&DC
10	Charleston WV	WV	EA	P&DC
11	Flint	MI	GL	P&DC
12	Colorado Springs	CO	WE	P&DC
13	Fort Worth	TX	SW	P&DC
14	Abilene TX (Rioss) / Fort Worth (Host)	TX	SW	RIOSS
15	Pasadena	CA	PA	P&DC
16	Mojave CA (Rioss) / Pasadena (Host)	CA	PA	RIOSS
17	Baltimore	MD	CM	P&DC
18a	Cincinnati	OH	EA	P&DC
18b	Cincinnati	OH	EA	P&DC
19	Syracuse	NY	NE	P&DC
20	Watertown NY (Rioss) / Syracuse (Host)	NY	NE	RIOSS
21	Monmouth (Eatonton)	NJ	NY	P&DC
22	Minneapolis	MN	WE	P&DC
23	Oxnard	CA	PA	P&DC
24	Santa Barbara	CA	PA	P&DC
25	Queens	NY	NY	P&DC
26	Gary	IN	GL	P&DC
27	Seattle	WA	WE	P&DC
28	Industry (Alhambra)	CA	PA	P&DC
29	Charleston SC	SC	EA	P&DC
30	Youngstown	OH	EA	P&DC
31	Madison	WI	GL	P&DC
32a	Dallas	TX	SW	P&DC
32b	Dallas	TX	SW	P&DC
33	Bowling Green	KY	EA	P&DC
34	Brooklyn	NY	NY	P&DC
35	Staten Island NY (Rioss) / Brooklyn (Host)	NY	NY	RIOSS
36	Suburban MD P&DC	MD	CM	P&DC
37	North Texas (Coppell)	TX	SW	P&DC
38	Everett	WA	WE	P&DC

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39a	Oakland	CA	PA	P&DC
39b	Oakland	CA	PA	P&DC
40	Portland OR	OR	WE	P&DC
41	Lexington	KY	EA	P&DC
42	Columbus	OH	EA	P&DC
43	Milwaukee	WI	GL	P&DC
44	Salt Lake City	UT	WE	P&DC
45	Provo (Rioss) / Salt Lake City (Host)	UT	WE	RIOSS
46	Anchorage	AK	WE	P&DC
47	East Texas (Tyler)	TX	SW	P&DC
48a	New York City (Morgan Station)	NY	NY	P&DC
48b	New York City (Morgan Station)	NY	NY	P&DC
49	Bronx	NY	NY	P&DC

For FY 2005, slightly less than one-quarter of UAA machinable letter volume was expected to be processed through the original PARS I sites.

e.) The target date for full deployment is October 2007, although meeting that target is contingent upon many factors, including development of technical improvements, completion of internal review processes, and approval by the Board of Governors.

f.) Yes, it is correct.

g.) PARS will intercept mail at the first machine handling, significantly reducing the mailstream processing cost of forwarding and returning mail. For presort mail, however, the ability to take advantage of savings opportunities is reduced. The first machine handling for presort mail is often not until the destination facility. The bulk of the PARS savings, however, arise when the first machine handling is at the origin facility, not the destination facility. Relative to single-piece mail, presort mail offers little potential for interception by PARS at an origin facility.

Furthermore, PARS will only intercept mail pieces that are undeliverable for move-related reason, and which match in name and address to the PARS change of address database. If sent by mailers who run their address list through NCOA, many of the

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mailpieces that otherwise would be intercepted by PARS will have addresses which already would have been corrected by the NCOA process. Compared with single-piece mail, presorted First-Class Mail in general is much more likely to come from an address list that has been run against NCOA. Specifically, the Capital One NSA (MC2002-2) and all functionally equivalent NSAs (MC2004-3, MC2004-4, and MC2005-2) all have strict NCOA requirements. Therefore, NCOA will already have been run on the pieces, further reducing the impact of PARS implementation on how such mail moves through the mailstream.

As stated above, PARS will not intercept a significant portion of non-forwardable, UAA, presort, First-Class Mail before it reaches the carrier. Once such mail does reach the carrier, however, the below chart provides a step-by-step comparison of the operations performed on UAA mail in facilities that employ PARS versus facilities that do not employ PARS.

Non-PARS	PARS
At delivery unit	At delivery unit
Received by Carrier	Received by Carrier
Identify return to sender mail	Identify return to sender mail
Hand stamp reason for return	Separate by reason for return by use of special processing cards*
Separate into ACS and non-ACS	Place into trays (no longer needs to be identified as ACS and non-ACS)
Send ACS to CFS unit	Send to plant
Send non-ACS to plant	
	<i>*In most cases no longer needs to be hand stamped</i>

h.) See Attachment 2, Interrogatory response APWU/USPS-7, filed February 5, 2003 in Docket No. MC2002-2 addressing the impacts of PARS on the Capital One NSA.

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- i.) There is no quantitative information at this time.
- j.) As indicated by the different activities at PARS and non-PARS delivery units listed in response to subpart (g) of this interrogatory, it is reasonable to expect that the cost of returning UAA mail via facilities that utilize PARS may be different from the cost of returning UAA mail via facilities that do not utilize PARS.

Further, it bears repeating that reducing UAA costs would not necessarily reduce the NSA cost savings since PARS will likely affect the ACS success rate and the cost of electronic returns as well as the cost of physical returns.

In fact, two likely impacts of PARS would increase, not reduce, NSA cost savings. First, the processing of UAA mail at mechanized terminals in CFS units will be replaced with automated processing on PARS. This is expected to reduce the cost of electronic returns more than the cost of physical returns. Second, standardizing the way ACS mail is handled and eliminating the requirement to separate ACS and non-ACS mail is likely to increase the ACS success rate.

Another likely effect – changing the activities that are performed at the delivery unit for both physical and electronic returns – would have minimal effect on NSA cost savings because changing these activities would reduce the cost of electronic and physical returns by a similar absolute amount.

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OCA/USPS-T1-4. What was the base year for the data used by witness Crum to develop cost estimates in the Capital One baseline case?

a. Is it possible that the base year for cost estimates in the next rate case will be different from that used by witness Crum in the Capital One baseline case?

Please explain.

b. Is it possible that the period of time during which the HSBC NSA will be in effect will generally coincide with the test year of the next rate case (at least in part) and years following the test year? Please explain.

Response:

Witness Crum used BY2000 to develop cost estimates in the Capital One baseline case.

a.) I am informed that, unless the Postal Service were to seek a waiver of the Commission's rules, those rules would not permit the Postal Service to utilize the same base year as employed by witness Crum in a yet-to-be-filed omnibus rate case, whenever in the future such a case were to be filed.

b.) It is certainly possible that some part of Years 1-3 of the HSBC NSA will overlap with the test year in the next omnibus rate case, but I have no opinion whether any such overlap would properly be characterized as "generally" coinciding with the test year and years following. .

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OCA/USPS-T1-5. In Appendix C of your testimony you present the HSBC NSA Proposed Data Collection Plan. Does the Postal Service plan to submit data collection reports for the HSBC NSA that are closely modeled on the Capital One Data Collection Report that was filed with the Commission on January 31, 2005? Please explain.

Response

Yes. The data collection reports for the HSBC NSA will be closely modeled after the Capital One Data Collection Report.

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document in accordance with Section 12 of the Rules of Practice and Procedure.

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