

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

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POSTAL RATE AND FEE CHANGES  
PURSUANT TO PUBLIC LAW 108-18

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Docket No. R2005-1

RESPONSES OF UNITED STATES POSTAL SERVICE WITNESS  
MICHAEL W. MILLER TO INTERROGATORIES OF VALPACK DIRECT  
MARKETING SYSTEMS, INC., AND VALPAK DEALERS' ASSOCIATION, INC.,  
REDIRECTED FROM WITNESS TAUFIQUE  
(VP/USPS-T28-5, 6(a)-(e), (g), 7(a)-(b)(iv))  
(May 4, 2005)

The United States Postal Service hereby files the responses of witness Michael W. Miller to interrogatories VP/USPS-T28-5, 6(a)-(e), (g), 7(a)-(b)(iv), filed on April 20, 2005. These interrogatories were redirected from witness Taufique.

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 MILLER TO INTERROGATORY OF  
VALPAK DIRECT MARKETING SYSTEMS, INC., AND VALPAK DEALERS'  
ASSOCIATION, INC., REDIRECTED FROM WITNESS TAUFIQUE**

**VP/USPS-T28-5.**

- a. Please refer to VP/USPS-T28-3. For the 19.729-cent mail processing cost for Standard Regular Basic presort flats, referenced therein, please confirm that the source is the "CRA ADJ UNIT COSTS" sheet of the file STANDARD.XLS in library reference USPS-LR-J-61 of Docket No. R2001-1, and that it is the sum of (i) a "Non Worksharing Unit Cost" of 4.003 cents and (ii) a "Worksharing Related Unit Cost" of 15.726 cents. If you do not confirm, please provide the appropriate figure and give the source.
- b. Please confirm that the updated figure for the 19.729-cent mail processing cost for Standard Regular Basic presort flats, referenced in preceding part a, is 26.468 cents, **34.2 percent higher than the current cost**, and is found on the first sheet in file STANDARD FLATS PRC.xls of library reference USPS-LR-K-102. If you do not confirm, please provide the appropriate figure and give the source.

**RESPONSE:**

The cost estimates discussed in VP/USPS-T28-3 were from my Docket No. R2001-1 testimony (USPS-T-24). Those estimates were used to support rate design and final adjustments as discussed in Section I of USPS-T-24. In contrast, the estimates provided in the instant proceeding only support final adjustments as discussed in the purpose of my testimony (USPS-T-19, Section I).

(a) Confirmed.

(b) Not confirmed. The Test Year 2003 19.729-cent cost estimate for Standard Mail nonautomation basic flats was calculated in Docket No. R2001-1, USPS-LR-J-61, page 69, and was developed using the Postal Service's volume variability cost methodology. In the instant proceeding, the Test Year 2006 cost estimate for Standard Mail nonautomation flats (using the Postal Service's cost methodology) is 23.148 cents and

**RESPONSE OF POSTAL SERVICE WITNESS MILLER TO INTERROGATORY OF  
VALPAK DIRECT MARKETING SYSTEMS, INC., AND VALPAK DEALERS'  
ASSOCIATION, INC., REDIRECTED FROM WITNESS TAUFIQUE**

can be found in USPS-LR-K-43, page 69. This figure represents a 17.3-percent increase over the estimate developed in Docket No. R2001-1.

The PRC version of the cost estimates for Docket No. R2001-1 and Docket No. R2005-1 are 22.370 cents (USPS-LR-J-85, page 69) and 26.468 cents (USPS-LR-K-102, page 69), respectively. Using these figures, the increase is 18.3 percent.

**RESPONSE OF POSTAL SERVICE WITNESS MILLER TO INTERROGATORY OF  
VALPAK DIRECT MARKETING SYSTEMS, INC., AND VALPAK DEALERS'  
ASSOCIATION, INC., REDIRECTED FROM WITNESS TAUFIQUE**

**VP/USPS-T28-6.** Regarding the 4.003-cent non-worksharing unit cost of processing Standard Regular Basic presort flats in VP/USPS-T28-5, part b.

- a. Please describe the nature of what the cost measures.
- b. Please explain why the 4.003-cent cost is not related to worksharing.
- c. Assume that the rate for basic, non-prebarcoded, minimum-per-piece flats, which is currently 34.4 cents, were to be reduced and resulted in a volume increase in line with the appropriate elasticity. Please state whether you would expect the cost of each additional unit of volume to reflect any part of this 4.003 cents, and explain why you come to the conclusion you do.
- d. Please explain whether the 4.003-cent cost figure is designed to be a marginal cost. If it is not, please explain the nature of the costing concept which it embodies.
- e. Please explain what worksharing the 4.003 cent figure is not sensitive to, describing the specific nature of the work that may (or may not) be shared.

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- g. Please explain whether mailing a flat, as opposed to an identically prepared and entered letter, causes the Postal Service to do work that could have been done by the mailer.

**RESPONSE:**

The cost estimates discussed in this interrogatory were from my Docket No. R2001-1 testimony (USPS-T-24). Those estimates were used to support rate design and final adjustments as discussed in Section I of USPS-T-24. In contrast, the estimates provided in the instant proceeding only support final adjustments as discussed in the purpose of my testimony (USPS-T-19, Section I).

In Docket No. R2001-1, the cost pool classifications were discussed in USPS-T-24, Section III.B.1. It should be noted that the cost pool classifications do not have the impact on the flats cost estimates that they do on the cost estimates developed in other studies. For example, First-Class Mail presort letters have an established cost

**RESPONSE OF POSTAL SERVICE WITNESS MILLER TO INTERROGATORY OF  
VALPAK DIRECT MARKETING SYSTEMS, INC., AND VALPAK DEALERS'  
ASSOCIATION, INC., REDIRECTED FROM WITNESS TAUFIQUE**

benchmark, Bulk Metered Mail (BMM) letters, to which the rate category cost estimates are compared during the development of the worksharing related savings. The specific cost pool classifications for First-Class Mail presort letters can affect the savings results.

In contrast, the flats cost studies only include total mail processing unit cost estimates by rate category. In previous cases, those total cost estimates were relied upon by the pricing witnesses during rate design. Worksharing related savings estimates have not historically been calculated for flats rate categories. Even if the non-worksharing related fixed cost pools were all reclassified as worksharing related fixed, the total mail processing unit cost estimates by rate category would not change.

(a) The Docket No. R2001-1 Standard Mail Regular flats cost pools can be found in USPS-LR-J-61, page 71. The cost methodology used to develop those cost pools and the operations which were mapped to those cost pools can be found in USPS-LR-J-55. Descriptive information can also be found in USPS-LR-J-1.

(b) The costs mapped to those cost pools represented operations that were determined not to be influenced by the presorting and prebarcoding of flat-shaped mail, which was the focus of the cost models.

(c) I am unable to provide a response to this question, because in my view the situation is much more complicated than this question suggests. A price change could influence other factors, such as mail characteristics, which would also affect costs. In addition, wage rates generally increase over time, while flats technology enhancements would result in cost decreases over time. Finally, I have not conducted any analyses that

**RESPONSE OF POSTAL SERVICE WITNESS MILLER TO INTERROGATORY OF  
VALPAK DIRECT MARKETING SYSTEMS, INC., AND VALPAK DEALERS'  
ASSOCIATION, INC., REDIRECTED FROM WITNESS TAUFIQUE**

attempt to determine how prices and subsequent volume changes affect unit costs over time.

(d) The cost data found in Docket No. R2001-1, USPS-LR-J-61, were designed to estimate marginal costs, in the sense that the productivity data used in the analysis represented marginal productivity figures that were adjusted using Postal Service volume variability factors. The mail processing unit costs by shape were also developed using volume variability data.

(e) The purpose of the cost models was to isolate the effects of mailer presorting and prebarcoding efforts. Other worksharing activities, such as dropshipping, were covered by other postal witnesses.

(g) I am unable to provide a response to this question. I imagine that whether any particular mailer chooses to engage, or not engage, in any particular “work that could [be] done by the mailer” is influenced by a variety of factors concerning mailer operations, of which I am not an expert.

**RESPONSE OF POSTAL SERVICE WITNESS MILLER TO INTERROGATORY OF  
VALPAK DIRECT MARKETING SYSTEMS, INC., AND VALPAK DEALERS'  
ASSOCIATION, INC., REDIRECTED FROM WITNESS TAUFIQUE**

**VP/USPS-T28-7**

- a. For the 15.726-cent worksharing-related unit cost referenced in VP/USPS-T28-5, part a, please confirm that, according to library reference USPS-LR-J-61 in Docket No. R2001-1, it is equal to a model unit cost of 15.329 cents times a Cost and Revenue Analysis ("CRA") adjustment factor of 1.023 plus a worksharing related fixed cost of 0.047 cents. If you do not confirm, please provide the appropriate figure and give the source.
- b. For the model unit cost of 15.329 cents referenced in preceding part a, please provide a narrative description of the nature of this cost and answer the following questions.
  - (i) Is this 15.726-cent worksharing-related unit cost an estimate of a marginal cost? If not, please explain the costing concept that guides this estimate.
  - (ii) Is this 15.726-cent worksharing-related unit cost constrained or limited in any way? If yes, please explain each constraint and the reason for it.
  - (iii) If the associated rate for basic, non-prebarcoded, minimum-per-piece flats, which is now 34.4 cents, were to be reduced and the volume were to increase in line with the elasticity, please explain whether you would expect the 15.726-cent figure to increase on a per-additional-unit basis.
  - (iv) Is this 15.726-cent worksharing-related unit cost specifically designed or estimated to relate to any particular concept of worksharing? If so, please specify the piece of work that may or may not be shared.

**RESPONSE:**

The cost estimates discussed in this interrogatory were from my Docket No. R2001-1 testimony (USPS-T-24). Those estimates were used to support rate design and final adjustments as discussed in Section I of USPS-T-24. In contrast, the estimates provided in the instant proceeding only support final adjustments as discussed in the purpose of my testimony (USPS-T-19, Section I).

(a) Confirmed.

**RESPONSE OF POSTAL SERVICE WITNESS MILLER TO INTERROGATORY OF VALPAK DIRECT MARKETING SYSTEMS, INC., AND VALPAK DEALERS' ASSOCIATION, INC., REDIRECTED FROM WITNESS TAUFIQUE**

(b) The cost models found in Docket No. R2001-1, USPS-LR-J-61, estimated piece distribution and bundle distribution costs, which were then tied to CRA mail processing unit costs by shape, as described in USPS-T-24/R2001-1. The cost spreadsheets and mail flow spreadsheets depicted the operations that were modeled.

(i) The cost data found in Docket No. R2001-1, USPS-LR-J-61, were designed to estimate marginal costs, in the sense that the productivity data used in the analysis represented marginal productivity figures that were adjusted using Postal Service volume variability factors. The mail processing unit costs by shape were also developed using volume variability data.

(ii) I do not understand this question.

(iii) Please see my response to VP/USPS-T28-6(c).

(iv) The flats cost models found in Docket No. R2001-1 represented total mail processing unit cost estimates by rate category, which were developed to isolate the impact related to mailer presorting and/or prebarcoding efforts. The pricing witnesses subsequently relied on the total mail processing unit cost estimates during rate design.