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

POSTAL RATE AND FEE CHANGES, 2005) Docket No. R2005-1

VALPAK DIRECT MARKETING SYSTEMS, INC. AND VALPAK DEALERS' ASSOCIATION, INC. THIRD INTERROGATORIES AND REQUESTS FOR PRODUCTION OF DOCUMENTS TO UNITED STATES POSTAL SERVICE WITNESS ALTAF H. TAUFIQUE (VP/USPS-T28-38-47)

(May 27, 2005)

Pursuant to sections 25 and 26 of the Postal Rate Commission rules of practice, Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. hereby submit interrogatories and document production requests. If necessary, please redirect any interrogatory and/or request to a more appropriate Postal Service witness.

Respectfully submitted,

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May 27, 2005

VP/USPS-T28-38.

Using PRC costing, in Docket No. R2001-1, the cost of **Basic automation letters** in ECR was 6.514 cents and, in Docket No. R2005-1, it is 6.341 cents, constituting a **decline** of 2.66 percent. Mail processing costs declined 6.28 percent and delivery costs declined 1.45 percent. For Docket No. R2001-1 costs, *see* USPS-LR-J-83 (mail processing) and PRC-LR-7 (delivery). For Docket No. R2005-1 costs, *see* USPS-LR-K-107 (mail processing) and USPS-LR-K-101 (delivery).

a. Please confirm the numbers above. In any are incorrect, please make needed corrections, explain the corrections fully, supply corresponding proportionate changes, and answer the remainder of this question based on your corrections.

b. Please identify and discuss all factors accounting for the decline in mail processing costs, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement and in particular how it improves the estimation of marginal cost and volume variable costs.

c. Please identify and discuss all factors accounting for the decline in delivery costs, including factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure idendified, please explain why the change is an improvement, and in

particular how well it improves the estimation of marginal cost and volume variable costs.

d. Please explain and quantify the effect that witness Bradley's new carrier analysis (USPS-T-14) had on the delivery cost.

e. With regard to both the mail processing cost and delivery cost, please explain and quantify the effect that increased delivery point sequencing had on the results.

VP/USPS-T28-39.

Using PRC costing, in Docket No. R2001-1, at PRC costing, the cost of **Basic (non-automation) letters** in ECR was 9.641 cents and, in Docket No. R2005-1, it is 13.125 cents now, constituting an **increase** of 36.14 percent. Mail processing costs increased 14.86 percent and delivery costs increased 45.69 percent. For Docket No. R2001-1 costs, *see* USPS-LR-J-83 (mail processing) and PRC-LR-7 (delivery). For Docket No. R2005-1 costs, *see* USPS-LR-K-107 (mail processing) and USPS-LR-K-101 (delivery).

a. Please confirm the numbers above. If any are incorrect, please make needed corrections, explain the corrections fully, supply corresponding proportionate changes, and answer the remainder of this question based on your corrections.

b. Please identify and discuss all factors accounting for the increase in mail processing costs, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing

method or procedure identified, please explain why the change is an improvement, and in particular how it improves the estimation of marginal cost and volume variable costs.

c. Please identify and discuss all factors accounting for the increase in delivery costs, including factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how it improves the estimation of marginal cost and volume variable costs.

d. Please explain and quantify the effect of witness Bradley's new carrier analysis (USPS-T-14) on the delivery cost.

e. With regard to both the mail processing cost and the delivery cost, please explain and quantify the effect of the increase in delivery point sequencing.

VP/USPS-T28-40.

Using PRC costing, in Docket No. R2001-1, the cost of **Basic flats (non-automation, non-letters)** in ECR was 10.017 cents and, in Docket No. R2005-1, it is 9.393 cents , constituting a **decline** of 6.23 percent. Mail processing costs declined 11.67 percent and delivery costs declined 3.11 percent. For Docket No. R2001-1 costs, *see* USPS-LR-J-83 (mail processing) and PRC-LR-7 (delivery). For Docket No. R2005-1 costs, *see* USPS-LR-K-107 (mail processing) and USPS-LR-K-101 (delivery).

a. Please confirm the numbers above. If any are incorrect, please make needed corrections, explain the corrections fully, supply corresponding proportionate changes, and answer the remainder of this question based on your corrections.

b. Please identify and discuss all factors accounting for the decline in mail processing costs, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how it improves the estimation of marginal cost and volume variable costs.

c. Please identify and discuss all factors accounting for the decline in delivery costs, including factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how it improves the estimation of marginal cost and volume variable costs.

d. Please explain and quantify the effect of witness Bradley's new carrier analysis (USPS-T-14) on the delivery cost.

VP/USPS-T28-41.

This interrogatory concerns the processing of Basic letters in the ECR subclass, which generally would not be prebarcoded by the mailer.

a. In Base Year 2004, what percentage of all ECR Basic letters was delivered by city carriers, and what percentage was delivered by rural carriers?

b. Of the total volume of ECR Basic letters delivered by city carriers, what percentage was cased manually, and what percentage was delivery point sequenced? If you do not know, please provide your best estimate.

c. If any ECR Basic letters were delivery point sequenced, please provide a cost comparison of manual casing versus delivery point sequencing (including delivery) in Base Year 2004.

VP/USPS-T28-42.

This interrogatory concerns the processing of Saturation letters in the ECR subclass, which mailers are required to prebarcode and sequence by line of travel.

a. In Base Year 2004, what percentage of ECR Saturation letters was cased manually by carriers?

b. What percentage of ECR Saturation letters did carriers take directly to the route as sequenced mail in a separate bundle?

c. What percentage of ECR Saturation letters was delivery point sequenced? If you do not know, please provide your best estimate. If any ECR Saturation

letters are delivery point sequenced, please provide a cost comparison of each different method of handling (including delivery).

d. Please compare your percentages to those provided by witness McCrery (USPS-T-29) at page 10, lines 11 through 23.

VP/USPS-T28-43.

In the costs presented and discussed in interrogatories VP/USPS-T28-38 and 39, the cost of processing and delivering (i) ECR Basic letters is 13.125 cents and (ii) ECR Basic automation letters is 6.341 cents. The difference is 6.784 cents.

a. Please discuss the extent to which you view the difference between these two categories as involving worksharing.

b. Do you believe that the cost difference of 6.784 cents is an estimate of how much the Postal Service saves when a Basic letter becomes barcoded and shifts to the automation category? Please explain.

c. Do you believe that, if a letter in the automation category were to have the barcode removed and shift back to the Basic letter category, the Postal Service would experience an increase in cost of 6.784 cents? Please explain.

d. Please consider (i) an automation letter, and (ii) a Basic letter that is candidate for applying a barcode and thereby becoming machinable like an automation letter. Please discuss the differences in the way the two pieces would be handled and provide an estimate of the costs associated with these differences.

VP/USPS-T28-44.

Using USPS costing, from Docket No. R2001-1 to Docket No. R2005-1, the mail processing costs of the following categories of Standard Regular commercial automation letters **declined** by the percentages indicated: mixed AADC by 12.99 percent; AADC by 15.85 percent; 3-digit by 16.48 percent; and 5-digit by 20.64 percent (USPS/2001 from USPS-LR-J-60; USPS/2005 from USPS-LR-K-48).

At PRC costing, the corresponding declines are 14.15 percent, 15.58 percent, 16.49 percent, and 21.96 percent.

In the face of underlying inflation creep, all declines must be viewed as large (PRC/2001 from USPS-LR-J-84; and PRC/2005 from USPS-LR-K-110).

a. Please provide the percentages of these categories that were delivery point sequenced by mail processing personnel during the periods reflected by the costs cited. If you do not know, please provide estimates.

b. Please identify and discuss all factors accounting for the above-noted declines in mail processing costs, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how it improves the estimation of marginal cost and volume variable costs.

VP/USPS-T28-45.

Using USPS costing, from Docket No. R2001-1 to Docket No. R2005-1, at the non-workshare-related cost of **Basic** and **3/5-digit non-automation** letters in the Standard Regular commercial category (used for the letter/flat differential and the presort discounts) increased 32.34 percent and 29.63 percent, respectively. The Docket No. R2005-1 cost of each, respectively, is 22.819 cents (17.409 mail processing plus 5.410 cents delivery) and 21.306 cents (15.022 mail processing plus 6.284 delivery). Mail processing and delivery costs are shown for both categories in USPS-LR-J-60 in Docket No. R2001-1, and in USPS-LR-K-48 in Docket No. R2005-1.

a. Focusing separately on the mail processing component, please identify and discuss all factors accounting for the increased cost, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how well aligned it is with the concepts of marginal cost and volume variable costs.

b. Focusing separately on the delivery component, please identity and discuss all factors accounting for the increased cost, including factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why

the change is an improvement and in particular how well aligned it is with the concepts of marginal cost and volume variable costs.

VP/USPS-T28-46.

Table 1, set out below, is taken from the first spreadsheet of file LR-K-48STDLETRS.xls of library reference USPS-LR-K-48, showing workshare-related costs for various categories of letter-size Standard Regular mail at USPS costing. A corresponding table in Docket No. R2001-1 is in USPS-LR-J-60, revised November 15, 2001.

Table 2, set out below, shows the proportionate changes in costs from the corresponding table in Docket No. R2001-1 to those shown in Table 1.

For ease of reference, certain costs are shaded in each table. Please note that not all rows in the tables, including the indented rows, are for categories recognized in rates.

a. Please confirm that if the Postal Service were designing rates for Regular letters, based on current costs, and were following the procedures of Docket No. R2001-1, it is the costs in the shaded rows in Table 1 that would be used. If you do not confirm, please present alternative costs, provide their source, and respond to the following parts of this question based on your alternative costs.

b. Please refer to Table 2, column 3, and identify and discuss all factors accounting for the 97.586 percent increase in the worksharing-related delivery costs of nonautomation, nonmachinable letters at the mixed ADC, ADC, 3-digit, and 5-digit levels, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in

the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how it improves the estimation of marginal cost and volume variable costs.

c. Please refer to Table 2, column 3, and identify and discuss all factors accounting for the increase of only 0.649 percent in the worksharing-related delivery costs of nonautomation, machinable letters at the mixed AADC and AADC levels, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how it improves the estimation of marginal cost and volume variable costs.

d. In Docket No. R2001-1, the worksharing-related delivery costs were the same for nonautomation, machinable AADC letters and corresponding 3- and 5-digit letters. In Docket No. R2005-1, they are different, as shown in Table 1, column 3 — 3.879 cents for the first two and 3.682 cents for the last two.

(i) Please explain why these costs were the same before and now are different.

(ii) Are these Docket No. R2005-1 estimates considered to be marginal costs? If yes, please explain the assumptions necessary for them to be marginal costs. If no, please explain the costing theory behind the costs.

(iii) If these costs are marginal costs, are they based on different mixes? Is an assumption being made that any extra pieces on which a marginal cost is based have the same mix (possibly involving processing proportions) as the existing pieces in the category? Please explain the basis for any such assumption.

e. Please refer to Table 2, column 2. The increase of 31.029 percent in the worksharing-related mail processing cost of nonautomation Basic presort letters is a weighted average of its components, shown immediately below to be 38.702 percent, 35.312 percent, 22.109 percent, and 22.109 percent. Please identify and discuss all factors accounting for the increases of these four components, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how well aligned it is with the concepts of marginal cost and volume variable costs. Please also discuss the role of delivery point sequencing as regards the extent of the increase in cost.

f. Please refer to Table 2, column 2, last four rows. Despite inflation and increased delivery point sequencing, the worksharing-related mail processing costs of the four categories of automation letters (mixed AADC, AADC, 3-digit, and 5-digit) all decreased by, in the same order, 12.981 percent, 15.835 percent, 16.461 percent, and 20.623 percent. Please identify and discuss all

factors accounting for these decreases, such as factor prices, changes in productivity, changes in technology, changes in the methods and procedures used in costing, changes in the way the mail is handled, and any other factors. For all changes in costing method or procedure identified, please explain why the change is an improvement, and in particular how well aligned it is with the concepts of marginal cost and volume variable costs. Please also discuss role of increased delivery point sequencing.

Attachment to VP/USPS-T28-46
Table 1

Table 1. Cost Estimates					
		Mail Processing		Delivery	Total
			Worksharing	Worksharing	Worksharing
		Total	Related	Related	Related
		Unit Cost	Unit Cost	Unit Cost	Unit Cost
		(1)	(2)	(3)	(4)
RATE CATEGORY					
Nonauto Basic Presort Flats		23.148	n/a	9.290	32.438
Nonauto 3-Digit/5-Digit Presort Flats		14.528		9.290	23.818
Nonautomation Presort Letters		16.263	11.007	6.062	17.068
Nonautomation Basic Presort Letters		17.409	12.153	5.410	17.563
	Nonautomation Nonmachinable Mixed ADC	37.485	32.229	11.049	43.278
	Nonautomation Nonmachinable ADC	29.347	24.091	11.049	35.140
	Nonautomation Machinable Mixed AADC	13.157	7.901	3.879	11.780
	Nonautomation Machinable AADC	13.157	7.901	3.879	11.780
Nonautomation 3-Digit/5-Digit Presort Letters		15.022	10.614	6.284	16.899
	Nonautomation Nonmachinable 3-Digit	26.409	21.153	11.049	32.202
	Nonautomation Nonmachinable 5-Digit	17.812	12.556	11.049	23.605
	Nonautomation Machinable 3-Digit	12.683	7.427	3.682	11.109
	Nonautomation Machinable 5-Digit	12.683	7.427	3.682	11.109
Automation Mixed AADC Presort Letters		4.662	3.491	4.104	7.595
Automation AADC Presort Letters		3.943	2.772	3.890	6.662
Automation 3-Digit Presort Letters		3.691	2.519	3.794	6.313
Automation 5-Digit Presort Letters		2.817	1.646	3.538	5.184

Attachment to VP/USPS-T28-46
Table 2

Table 2. Percentage Changes from Docket No. R2001-1

	Mail Processing		Delivery	Total
		Worksharing	Worksharing	Worksharing
	Total	Related	Related	Related
	Unit Cost	Unit Cost	Unit Cost	Unit Cost
	(1)	(2)	(3)	(4)
RATE CATEGORY				
Nonauto Basic Presort Flats				
Nonauto 3-Digit/5-Digit Presort Flats				
Nonautomation Presort Letters				
Nonautomation Basic Presort Letters	33.531%	31.029%	28.615%	30.275%
Nonautomation Nonmachinable Mixed ADC	38.841%	38.702%	97.586%	50.124%
Nonautomation Nonmachinable ADC	36.077%	35.312%	97.586%	50.196%
Nonautomation Machinable Mixed AADC	28.577%	22.109%	0.649%	14.098%
Nonautomation Machinable AADC	28.577%	22.109%	0.649%	14.098%
Nonautomation 3-Digit/5-Digit Presort Letters	23.658%	26.571%	42.291%	31.994%
Nonautomation Nonmachinable 3-Digit	35.507%	34.504%	97.586%	51.050%
Nonautomation Nonmachinable 5-Digit	26.368%	21.513%	97.586%	48.226%
Nonautomation Machinable 3-Digit	28.447%	21.519%	-2.926%	12.157%
Nonautomation Machinable 5-Digit	28.447%	21.519%	-2.926%	12.157%
Automation Mixed AADC Presort Letters	-7.575%	-12.981%	5.583%	-3.846%
Automation AADC Presort Letters	-8.850%	-15.835%	1.646%	-6.440%
Automation 3-Digit Presort Letters	-8.837%	-16.461%	-0.472%	-7.534%
Automation 5-Digit Presort Letters	-9.303%	-20.623%	-5.350%	-10.800%

VP/USPS-T28-47.

Table 1, set out below, is taken from the first spreadsheet of file LR-K-48STDLETRS.xls of USPS-LR-K-48, and shows workshare-related costs for various categories of letter-size Standard Regular mail at USPS costing. For ease of reference, certain costs are shaded. Please note that not all of the lines in the table, including the indented lines, are for categories recognized in rates. A corresponding table in Docket No. R2001-1 is found in USPS-LR-J-60, revised November 15, 2001.

a. Please confirm that if the Postal Service were developing discounts for automation (*i.e.*, prebarcoded) letters based on current costs, and were following the procedures used in Docket No. R2001-1, it is the workshare-related unit costs in the shaded rows of column 4 in Table 1 that would be used. If you do not confirm, please present the costs that would be used, provide their source, and respond to the following parts of this question.

b. Please confirm that an automation discount for mixed AADC letters would be based on a cost difference of 17.563 – 7.595 = 9.968 cents.

c. Please explain the extent to which you view the discount for automation mixed AADC letters to be a worksharing discount. To the extent that you do not so view it, please explain why. To the extent that you do so view it, please explain the nature of the work that is being shared.

d. To the extent to which you view the discount for automation mixed AADC letters to be a worksharing discount, please explain the extent to which you believe this discount should be based on a cost avoidance. If you do not believe it should be

based on an avoidance, please explain why. If you do so believe, please explain how that avoidance should be defined, *i.e.*, its concept and the costs that should be used to implement the concept.

e. Recognizing that the 17.563-cent workshare related cost for nonautomation presort letters shown in column 4 (and its mail processing and delivery components in columns 2 and 3) is a weighted average of the four costs shown immediately below it in the table, please explain the extent to which you view the cost difference of 9.968 cents to be an amount that would be avoided if a candidate basic presort letter shifts to become an automation mixed AADC letter.

f. If an automation mixed AADC letter were to revert back to being nonautomation, is it your position that the Postal Service would experience an increase in cost of 9.968 cents? If you do, please explain how and why that cost increase would occur, and any assumptions on which it is based. If you do not, please explain why it is the appropriate cost on which to base the automation discount.

g. As shown in Table 1, the workshare-related mail processing cost of (i) nonautomation, machinable letters is 7.901 cents at both the mixed AADC and AADC levels, and of (ii) corresponding automation letters is 3.491 cents at the mixed AADC level and 2.772 cents at the AADC level.

   (i) Please explain how the difference between the costs of 7.901 cents and 3.491 cents, for mixed AADC letters, relates to the cost the Postal Service would incur to read the address and place a barcode on the nonautomation piece.

(ii) Please explain why the worksharing-related mail processing cost of automation mixed AADC letters is 3.491 cents while the corresponding cost for AADC letters is only 2.772 cents.

(iii) Please explain why the two nonautomation costs are the same while the two automation costs differ.

Attachment to VP/USPS-T28-47
Table 1

Table 1. Cost Estimates					
		Mail Processing		Delivery	Total
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	Nonautomation Machinable Mixed AADC	13.157	7.901	3.879	11.780
	Nonautomation Machinable AADC	13.157	7.901	3.879	11.780
Nonautomation 3-Digit/5-Digit Presort Letters		15.022	10.614	6.284	16.899
	Nonautomation Nonmachinable 3-Digit	26.409	21.153	11.049	32.202
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Automation AADC Presort Letters		3.943	2.772	3.890	6.662
Automation 3-Digit Presort Letters		3.691	2.519	3.794	6.313
Automation 5-Digit Presort Letters		2.817	1.646	3.538	5.184