

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

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

Docket No. R2005-1

RESPONSES OF POSTAL SERVICE WITNESS KELLEY
TO INTERROGATORIES OF MMA (MMA/USPS-T16-7 -16)
(May 27, 2005)

The United States Postal Service hereby provides the responses of witness Kelley to the following interrogatories of MMA, filed on May 13, 2005: MMA/USPS-T16-7 -16. Preparation of the response to question 17, filed with these questions, has not been completed.

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

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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May 27, 2005

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major
Mailers Association

MMA/USPS-T16-7

In your answer to Interrogatory MMA/USPS-T16-1C, you indicate that the delivery cost methodology employed by the Postal Service and accepted by the Commission for Docket No. R2000-1 is “not current”. What is the current Commission-accepted methodology for estimating workshare delivery cost savings? Please explain your answer.

Response

Refer to Docket 2001-1/PRC-LR-7 for the current Commission accepted methodology for calculating unit delivery costs.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-8

In your answer to Interrogatory MMA/USPS-T16-3E, you state the “change in methodology used in USPS-LR-K-67 gives more accurate unit delivery costs as compared to that used in USPS-LR-K-101” (emphasis added). When you refer to the “change in methodology” do you mean a change to correct the problem suggested in Interrogatory MMA/USPS-T16-3E, where the derived unit delivery costs for FY 93 in USPS-LR-K-101 are subject to understatement? If not, please answer the original question with respect to that one specific problem that was pointed out to you.

Response

No. I do not agree that the unit costs in USPS-LR-K-101 are necessarily understated. One specific issue where I feel that USPS-LR-K-67 is more accurate than USPS-LR-K-101 is the method used to distribute city carrier street time costs and total rural carrier costs. USPS-LR-K-67 uses actual delivered volumes by city and rural carriers to distribute city carrier street time costs and total rural carrier costs to rate categories as opposed USPS-LR-K-101 which uses a combination of several systems – some of which include deliveries to post office boxes – to distribute the same costs (refer to my direct testimony USPS-T-16 page 7 lines 6 through 18). If costs are understated for one rate category, however, they are necessarily overstated for one or more other rate categories. Thus, I do not know if the cost for First Class Mail presorted letters is understated or overstated. This difficulty is avoided by the proposed new methodology in USPS-LR-K-67 because it uses delivered volume proportions to distribute costs to products.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-9

Please refer to your answers to Interrogatory MMA/USPS-T16-4A-C, where you state that you did not attempt to estimate the delivery unit costs for bulk metered mail (BMM), metered mail, or single piece machinable mail. You state that estimates for such types of mail are “not needed” for rate design purposes.

A. Before you performed your new delivery cost study, were you aware that the Postal Service has historically utilized BMM as the benchmark from which workshare savings were measured, for both processing and delivery costs?

B. Before you performed your new delivery cost study, were you aware that Postal Service witness Abdirahman required an estimate for the BMM unit delivery cost, and, when none was available, was forced to make an assumption that the unit delivery costs for nonautomation, machinable mixed AADC letters could be used as a proxy for BMM? If you were not aware of this situation, please explain why not.

C. Before you performed your new delivery cost study, were you aware that Postal Service witness Miller in Docket No. R2001-1 required an estimate for BMM unit delivery costs, and, when none was available, was forced to make an assumption that the unit delivery costs for nonautomation, machinable mixed AADC letters could be used as a proxy for BMM? If you were not aware of this situation, please explain why not.

D. Before you performed your new delivery cost study, were you aware that Postal Service witness Miller in Docket No. R2000-1 required an estimate for BMM unit delivery costs, and, when none was available, was forced to make an assumption that the unit delivery costs of nonautomation letters could be used as a proxy for BMM? If you were not aware of this situation, please explain why not.

E. Before you performed your new delivery cost study, were you aware that the Commission in Docket No. R2000-1 required an estimate for BMM unit delivery costs, and, when none was available, was forced to adopt Postal Service witness Miller’s assumption that the unit delivery costs for nonautomation letters could be used as a proxy for BMM? If you were not aware of this situation, please explain why not.

F. Before you performed your new delivery cost study, were you aware that, in R97-1, the Commission required an estimate for BMM unit delivery costs, and, when none was available, was forced to adopt Postal Service witness Hatfield’s assumption that the unit delivery costs for nonautomation letters could be used as a proxy for BMM? If you were not aware of this situation, please explain why not.

G. Before you performed your new delivery cost study, were you aware that, in Docket No. R2001-1, MMA presented the Commission with a unit delivery cost estimate for BMM letters, which was obtained from data for single piece metered mail. If you were not aware of this situation, please explain why not.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

Response

A. No.

B. I was not aware. USPS-LR-K-67 utilizes information from existing systems or studies to derive unit delivery costs by rate category. My task was to update USPS-LR-J-117 in Docket R2001-1 and to implement methodological improvements where possible and produce unit delivery cost estimates for the same rate categories as in R2001-1. The previous effort was accepted by the Commission in Docket R2001-1/PRC-LR-7. In addition, BMM is not currently captured by neither IOCS nor CCS so a proxy needs to be used to estimate its delivery costs.

C. No.

D. No.

E. No. In reviewing the Opinion and Recommended Decision from Docket No. R2000-1, I can not find your assertion that the Commission required an estimate for unit delivery costs for BMM.

F. No. In reviewing the Opinion and Recommended Decision from Docket No. R1997-1, I can not find your assertion that the Commission required an estimate for unit delivery costs for BMM.

G. No.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-10

In your answer to Interrogatory MMA/USPS-T16-4G, you state that the purpose of de-averaging the nonautomation unit delivery cost into 8 separate categories was to support the expansion of the nonmachinable surcharge first presented by the Postal Service in R2001-1.

A. Please confirm that the unit delivery cost for one of your 8 separate categories -- nonautomation, machinable mixed AADC letters -- was used by USPS witness Abdirahman as a proxy for BMM delivery costs so that he could modify the latest Commission-approved methodology for estimating workshare cost savings? If you do not confirm, please explain.

B. Why did you fail to mention USPS witness Abdirahman's use of your unit delivery cost for nonautomation, machinable mixed AADC letters as a proxy for BMM delivery costs as the explanation in part A of this interrogatory as the most important aspect of your delivery cost analysis?

C. Please confirm that USPS witness Abdirahman used your unit delivery cost estimate for nonautomation, machinable mixed AADC letters as a proxy for BMM unit delivery costs, and this single assumption, along with the use of your derived unit delivery cost, reduced the Postal Service's derived unit cost savings by 3.01 cents? See USPS witness Abdirahman's response to Interrogatory MMA/USPS-T21-10F.

Response

A. I can confirm that witness Abdirahman used the proxy you describe, but I cannot confirm your characterization of his motivation for doing so.

B. I did not answer in the manner you suggest because I did not think it was the most important part of my delivery cost analysis.

C. I confirm that witness Abdirahman used the estimate for nonautomation, machinable mixed AADC letters as a proxy for BMM unit delivery costs. I supply witness Abdirahman with USPS-LR-K-67, but do not sponsor how its results are used to derive workshare savings.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-11

In your answer to Interrogatory MMA/USPS-T16-5B, you discuss the impact that worksharing has on delivery costs if a particular letter is DPSed. Please confirm that you are claiming that, if two letters are DPSed, it is your contention that, except for collection costs incurred by non-workshare letters, delivery costs are unaffected by worksharing. If this is not your contention, please explain. Please provide any documents or other information you have to support your position on this matter.

Response

Confirmed. The justification for this position rests in my understanding in the manner in which DPS mail is handled by the carrier. DPS mail is not handled at the piece level in the office and is only touched at the piece level at the delivery point. As a result, the delivery cost for two DPS letters, regardless of the worksharing level, should be the same.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-12

In your answer to Interrogatory MMA/USPS-T16-5C, you discuss the impact that worksharing has on delivery costs if a particular letter is not DPSed. Please confirm that if two letters are not DPSed, it is your contention that, except for collection costs incurred by non-workshare letters, street time delivery costs should be unaffected by worksharing, but in-office delivery costs will be lower for the workshared letter. If this is not your contention, please explain. Please provide any documents or other information you have to support your position on this matter.

Response

Confirmed. The justification for the in-office costs being lower for the workshared piece is included in my response to MMA/USPS-T29-5, redirected from witness McCrery. My understanding is that the street time costs will be the same for the two letters because the carrier will handle and deliver those pieces on the street, on average, the same way.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-13

Are collection costs included in your nonpresorted unit delivery cost of 7.189 cents as shown in USPS-LR-K-67 (revised)? If yes, please provide the nonpresorted unit delivery cost excluding collection costs, and include all computations and sources.

Response

Collection costs are included in the single piece test year unit delivery cost of 7.189 cents. The single piece test year unit delivery cost without collection costs is 6.981 cents per piece. The difference between the two unit costs is 0.207 cent (round off error). Multiplying the cost differential by the test year single piece letter volume of 38.9 billion pieces gives the test year total collection costs to be \$80.8 million, which consists of \$75.7 city carrier cost and \$5.1 million of rural carrier costs.

To reproduce these calculations, perform the following steps within the library reference USPS-LR-K-67. Steps 1 and 2, as described below, remove the single piece letter cost of collections due to city carriers and steps 3 and 4, as described below, take out the costs from rural carriers.

1. In workbook "CS06&7.K67.xls" worksheet '7.0.6' change the values in cells C11, H11, J11, and K11 to zero.
2. In workbook "CS06&7.K67.xls" worksheets '7.0.6.5', '7.0.6.6', '7.0.6.7', '7.0.6.8', and '7.0.6.9' change the values in cell G11 to zero.
3. In workbook "LR-K-67_Revised.xls" worksheet '8.RrICwIkRevSatBxds.Rev.Prcls' change the values in cells J6 and K6 to zero.
4. Step 3 results in a division by zero in worksheet '6.Rural cost.' within

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

“LR-K-67_Revised.xls” in cells I36 and J36. To address that issue input values of 0.0175010162562571 and 1.44065284401532 in cells I36 and J36 respectively in worksheet ‘6.Rural cost.’ within the workbook

“LR-K-67_Revised.xls”.

After completing steps 1. through 4 the test year unit delivery costs without collection costs will be 6.981 cents and is reflected in cell C4 on worksheet ‘Table 1’ in workbook “LR-K-67_Revised.xls”.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-14

Please refer to your answer to Interrogatory MMA/USPS-T16-5C. For letters that are not DPSed, please explain why the in-office delivery costs will be lower for a workshared letter than for a machinable, nonworkshared letter that is not prebarcoded?

Response

Please refer to my response to Interrogatory MMA/USPS-T-29-5, redirected from witness McCrery.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-15

Please refer to your answer to Interrogatory MMA/USPS-T16-5C. Are you aware that, in R2001-1, Postal Service data indicated that when letters are not DPSed, the unit delivery cost for a single piece letter and a workshare letter are 6.36 cents and 4.11 cents, respectively. (See R2001-1, TR 5/867 (MMA-X-4); Exhibit MMA-4A, page 3, Table 2). In light of your answer to Interrogatory MMA/USPST16-12, can you explain the 2.25-cent differential?

Response

I was not aware of the issue you reference in the question. I do not sponsor the results presented in the table (MMA-X-4) shown in Docket No. R2001-1, Tr. 5/867. However, in my response to Interrogatory MMA/USPST-29-5, redirected from witness McCrery, I explain my intuition that the in-office costs should be lower for some workshared letter pieces that are not DPSed as compared to single piece letters that are not DPSed, and the results in the table seem to be consistent with that notion, but I do not endorse the magnitude of the difference between the workshared letters and the nonworkshared letters presented in MMA-X-4.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

MMA/USPS-T16-16

In your answer to Interrogatory MMA/USPS-T16-5D, you provided the presorted First-Class unit delivery costs for Non-DPSed and DPSed letters derived from LR-USPS-K-67.

A. Please provide the exact source (and derivation, if necessary) for the unit delivery costs of these DPSed letters and Non-DPSed letters.

B. Would the TY06 unit delivery cost for single piece letters that are not DPSed be more, less, or approximately the same as the 9.60 cent cost estimate you derived for presorted letters that are not DPSed? Please fully explain your answer.

C. Would the TY06 unit delivery cost for single piece letters that are DPSed be more, less or approximately the same as the 2.70 cent cost estimate you derived for presorted letters that are DPSed? Please fully explain your answer.

D. Please confirm that the 81.85% average DPS % obtained from your delivery cost study is simply a volume weighted average of the DPS %'s that you obtained from Mr. Abdiraham for each of the 8 separate rate categories. If you cannot confirm, please explain in detail exactly how your average DPS % was computed and provide the formula and sources for that calculation.

E. Please confirm that for Automation letters (excluding those delivered by 5-digit CSBCS/Manual offices), your implied average DPS % is 86.24%. If you cannot confirm, please provide your computation of the implied DPS % for all Automation letters (excluding those delivered by 5-digit CSBCS/Manual offices) and provide the sources for that calculation.

F. Please reconcile the DPS % resulting from your response to Part E with USPS witness McClery's (sic) estimate that 89% of all barcoded letters were DPSed in FY04. (See USPS-T-29 at 10)

G. Please assume for purposes of this question that your 2.70 cent unit delivery cost for presorted letters that are DPSed can be used as a proxy for the unit delivery cost for nonpresorted letters that are DPSed. Assume further that your 9.60 cent unit delivery cost for presorted letters that are not DPSed can be used to as a proxy for the unit delivery cost for nonpresorted letters that are not DPSed. Using the data from Library Reference LR-USPS-K-67, please confirm that the implied DPS % would be 35.0%. If you cannot confirm, please provide your computation of the implied DPS % under this assumption

H. Please explain why, in your opinion, the assumptions you were asked to make for purposes of Part G are or are not valid.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

Response

A. Refer to the attached pages. The spreadsheet that performs the calculations is also attached electronically. The source of the data in the attached pages is LR-K-67_Revised.xls. The test year and base year unit delivery costs for presorted First Class NonDPS and DPS letters presented in my response to Interrogatory MMA/USPS-T16-5D were derived incorrectly. The corrected test year unit delivery costs are 10.92 and 2.41 cents for NonDPS and DPS letters, respectively (the incorrect previous test year estimates were 9.60 and 2.70 for NonDPS and DPS letters, respectively). The corrected base year unit delivery costs are 10.35 and 2.28 cents for NonDPS and DPS letters, respectively (the incorrect previous base year estimates were 9.14 and 2.54 cents presorted NonDPS and DPS letters, respectively).

B. I do not know. I have not compared the unit delivery costs between a workshared letter and a single piece letter that is not DPSed.

C. I do not know. I have not compared the unit delivery costs between a workshared letter and a single piece letter that are DPSed.

D. Confirmed.

E. Confirmed.

F. Witness McCrery's statement in his testimony refers to all barcoded letters, not just presorted First Class Mail, excluding those delivered by 5-digit CSBCS/Manual offices. The 86.24% is the DPS percentage is for presorted First Class Mail excluding those delivered by 5-digit CSBCS/Manual offices. Since the two populations of letters in question are not identical, there is no reason to expect that the DPS percentage for the two would be the same.

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

G. Methodology confirmed. However, with the revised NonDPS and DPS unit delivery costs of 10.92 and 2.41 cents respectively, the implied DPS percentage is 43.8 percent rather than 35 percent.

H. I contend that DPS and NonDPS unit delivery costs for presorted pieces are not necessarily reasonable proxies for similar types of single piece letters. In choosing a proxy for cost per originated piece, it is important to assess not only how the proxy and the target products are handled in any one activity, but also how much of the various activities they each use. For example, even if two products would take the same amount of time to case one piece, their in-office costs per originating piece could differ because one has a higher percentage of delivery point sequencing than the other. If so, it would require less average casing time per originated piece because, on average, fewer pieces require casing. In addition, one product may be delivered by city and rural carriers more than the other product, which may be delivered more widely through firm pickups or post office boxes.

In addition, the physical and delivery characteristics of single piece letters are much more heterogeneous as compared to presorted letters. Single piece letters are comprised, on the one hand, of handwritten (legible and illegible) and typed addresses in various locations and of questionable reliability, and, on the other hand, courtesy envelope remittance mail. In contrast, presorted pieces more uniformly meet higher address reliability standards found in the DMM (e.g. 5 digit ZIP that matches the address). These factors could result in different DPS percentages and casing productivities between the two categories. In addition, single piece letters incur collection costs and have different delivery characteristics than presorted letters. A higher proportion of single piece letter volume is delivered directly to firms, rather than by city or rural carriers. These factors

Response of Postal Service Witness John Kelley to Interrogatories Posed by Major Mailers Association

could have a significant cost impact on the unit delivery costs, although the influence is perhaps more significant for NonDPS letters.

In summary, since single piece and presorted letters consume resources in different proportions in cost segments 6, 7 and 10, coupled with the fact that the physical and delivery characteristics of presorted and single piece letters are not similar, the unit delivery cost for presort letters is not a good proxy for the unit delivery cost of single piece letters.

BY04 COSTS AND VOLUMES	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(000s)			(\$0.000)
Mail Category	6.1 IN-OFFICE DIRECT LABOR, CASING	6.1 IN-OFFICE DIRECT LABOR, NON-CASING	6.2 IN-OFFICE OVERHEAD, PLUS THE PORTION OF IN-OFFICE DELIVERY PREP THAT IS BURDENED ON OFFICE DIRECT	7.1 DIRECT DELIVERY ACTIVITIES	7.2 DELIVERY ACTIVITIES SUPPORT	6.2 IN-OFFICE DELIVERY PREP BURDENED ON STREET DIRECT	10 RURAL CARRIERS	TOTAL PIGGYBACKED CITY CARRIER COSTS	TOTAL PIGGYBACKED RURAL CARRIER COSTS	GRAND TOTAL PIGGYBACKED COSTS	PERMIT VOLUME	UNIT CITY DELIVERY COST	UNIT RURAL DELIVERY COST	UNIT TOTAL DELIVERY COST
First-Class Presort Letters Subclass - Non DPS Letter Pieces	350,080	8,589	97,934	98,302	11,981	4,247	136,460	713,197	160,372	873,569	8,442,593	\$0.0845	\$0.0190	\$0.1035
First-Class Presort Letters Subclass - DPS Letter Pieces	0	38,728	10,575	443,231	54,022	19,150	135,960	706,419	159,785	866,204	38,066,649	\$0.0186	\$0.0042	\$0.0228
First-Class Presort Letters Subclass - All Letter Pieces	350,080	47,317	108,509	541,533	66,004	23,398	272,420	1,419,616	320,157	1,739,773	46,509,242	\$0.0305	\$0.0069	\$0.0374

TY06 COSTS AND VOLUMES	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(\$000s)	(000s)	(\$0.000)	(\$0.000)	(\$0.000)
Mail Category	6.1 IN-OFFICE DIRECT LABOR, CASING	6.1 IN-OFFICE DIRECT LABOR, NON-CASING	6.2 IN-OFFICE OVERHEAD, PLUS THE PORTION OF IN- OFFICE DELIVERY PREP THAT IS BURDENED ON OFFICE DIRECT	7.1 DIRECT DELIVERY ACTIVITIES	7.2 DELIVERY ACTIVITIES SUPPORT	6.2 IN-OFFICE DELIVERY PREP BURDENED ON STREET DIRECT	6.2 CAG K	10 RURAL CARRIERS	TOTAL PIGGYBACKED CITY CARRIER COSTS	TOTAL PIGGYBACKED RURAL CARRIER COSTS	GRAND TOTAL PIGGYBACKED COSTS	PERMIT VOLUME	UNIT CITY DELIVERY COST	UNIT RURAL DELIVERY COST	UNIT TOTAL DELIVERY COST
First-Class Presort Letters Subclass - Non DPS Letter Pieces	368,323	9,037	103,823	104,259	12,699	4,508	11	150,805	763,031	178,227	941,258	8,621,419	\$0.0885	\$0.0207	\$0.1092
First-Class Presort Letters Subclass - DPS Letter Pieces	0	40,746	11,210	470,093	57,257	20,325	49	150,252	759,260	177,574	936,834	38,872,954	\$0.0195	\$0.0046	\$0.0241
First-Class Presort Letters Subclass - All Lettter Pieces	368,323	49,783	115,033	574,352	69,955	24,833	60	301,057	1,522,291	355,801	1,878,092	47,494,372	\$0.0321	\$0.0075	\$0.0395

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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