

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 UNITED STATES POSTAL SERVICE WITNESS ROBINSON  
TO INTERROGATORIES OF MAJOR MAILERS ASSOCIATION  
[MMA/USPS-T27-2 THROUGH 4]

The United States Postal Service hereby provides the responses of witness Robinson to the above-listed interrogatories of Major Mailers Association, filed on June 15, 2005. The interrogatories are stated verbatim and are followed by the responses.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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**RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS ROBINSON  
TO INTERROGATORY OF MAJOR MAILERS ASSOCIATION**

**MMA/USPS-T27-2**

Please refer to your response to Interrogatory MMA/USPS-T27-1 B where you provide TY 2006 postal finances using the Commission's attributable cost methodology.

- A. Please confirm that, in R2000-1 and R2001-1, the Postal Rate Commission recommended rates for First-Class letters that resulted in cost coverages of 179 and 192, respectively. If you cannot confirm, please provide the correct cost coverages, explain how they were derived, and provide complete references to all source materials used.
- B. Please confirm that the Postal Service's proposed rates in R2005-1 result in a cost coverage for First-Class letters equal to 218. If you cannot confirm, please provide the correct cost coverage, explain how it was derived, and provide complete references to all source materials used.
- C. Please confirm that, in R2000-1 and R2001-1, the Postal Rate Commission recommended rates for First-Class letters that reflected markup indices of 138 and 145, respectively. If you cannot confirm, please provide the correct markup indices, explain how they were derived, and provide complete references to all sources used.
- D. Please confirm that the Postal Service's proposed rates in R2005-1 result in a markup index for First-Class letters equal to 148. If you cannot confirm, please provide the correct markup index, explain how it was derived, and provide complete references to all sources used.
- E. Please explain why the Postal Service's proposed 5.4% across-the-board rate increase significantly raises the cost coverage and markup index for First-Class mail in this case.

**RESPONSE**

- A. Confirmed. See the Attachment to MMA/USPS-T27-2, columns (1) and (2).
- B. Confirmed assuming the Postal Rate Commission costing methodology is used. See the Attachment to MMA/USPS-T27-2, column (3)

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**RESPONSE TO MMA/USPS-T27-2 (continued):**

- C. Not confirmed. The markup index for First-Class Mail Letters and Sealed Parcels subclass for the Commission's recommended rates was 1.342 in Docket No. R2000-1 and 1.420 in Docket No. R2001-1. See Docket No. R2001-1, PRC Op. Appendix G at 37 and the Attachment to MMA/USPS-T27-2, column (1) and (2).
- D. Not confirmed. In this case, for the First-Class Mail Letters and Sealed Parcels subclass, the Postal Service's rate proposal results in a markup index of 1.472 using the Postal Service's costing methodology and 1.520 using the Postal Rate Commission's costing methodology. See the Attachment to MMA/USPS-T27-2 columns (3) [PRC] and (4) [USPS]
- E. The increase in the markup index for First-Class Mail Letters is not caused by the across-the-board proposed rate increase. In the absence of other changes in costs, an across-the-board rate increase will cause the markup indices for the individual subclasses to move towards the average markup index for the postal system as a whole.

While the increase in the cost coverage for First-Class Mail is, in part, driven by the across-the-board rate increase proposed in this case, this is not the sole reason for the increase. The increases in both the cost coverage and the markup index for First-Class Mail Letters are in large measure the result of successful efforts to control Postal Service costs and may also be affected by changes in the characteristics of First-Class

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**RESPONSE TO MMA/USPS-T27-2 (continued):**

Mail Letters. One result of the successful efficiency efforts is that, if the escrow obligation did not exist, the Postal Service would have been able to forgo a rate increase at this time. Instead, as discussed by witness Potter, the sole reason this increase has been proposed is to recover the Congressionally-mandated escrow obligation.

**Attachment to MMA/USPS-T27-2  
Calculation of Markups and Markup Indices  
Dockets No. R2000-1, R2001-1 and R2005-1**

Costing Methodology	R2000-1 PRC (1)	R2001-1 PRC (2)	R2005-1 PRC (3)	R2005-1 USPS (4)
<b>First-Class Mail Letters and Sealed Parcels</b>				
(a) Revenue	35,749,605	37,781,209	35,901,564	35,901,564
(b) Costs	19,989,490	19,677,353	16,453,261	15,621,298
(c) = [(a) / (b)] Cost Coverage	178.8%	192.0%	218.2%	229.8%
(d) = [(a) / (b)] - 1 Markup	78.8%	92.0%	118.2%	129.8%

**First-Class Mail Presorted and Automation Letters**

(e) Revenue	13,172,716	15,915,988	15,382,830	15,382,830
(f) Costs	5,305,138	5,985,539	4,912,741	4,636,166
(g) = [(e) / (f)] Implicit Cost Coverage	248.3%	265.9%	313.1%	331.8%
(h) = [(e) / (f)] - 1 Implicit Markup	148.3%	165.9%	213.1%	231.8%

**All Mail and Services**

(i) Revenue	68,789,970	74,741,743	71,968,364	71,968,364
(j) Costs	43,336,799	45,361,242	40,486,419	38,236,154
(k) = [(i) / (j)] Cost Coverage	158.7%	164.8%	177.8%	188.2%
(l) = [(i) / (j)] - 1 Markup	58.7%	64.8%	77.8%	88.2%
(m) = (d) / (l) Markup index FCM Letters	1.342	1.420	1.520	1.472
(n) = (h) / (l) Implicit Markup index presort FCM Letters	2.525	2.561	2.741	2.628

<u>Sources</u>	(1)	(2)	(3)	(4)
(a) App. G at 1	App. G at 1	App. G at 1	Exhibit USPS-27B*	Exhibit USPS-27B*
(b) App. G at 1	App. G at 1	App. G at 1	MMA/USPS-T27-1B	Exhibit USPS-27B*
(e) App. G at 2	App. G at 2	App. G at 2	Exhibit USPS-27B*	Exhibit USPS-27B*
(f) App. J at 1	App. F at 1	App. F at 1	MMA/USPS-T27-1B	Exhibit USPS-27B*
(i) App. G at 1	App. G at 1	App. G at 1	Exhibit USPS-27B*	Exhibit USPS-27B*
(j) App. G at 1	App. G at 1	App. G at 1	MMA/USPS-T27-1B	Exhibit USPS-27B*

\* Revised 6/10/2005

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**MMA/USPS-T27-3**

Please refer to your response to Interrogatory MMA/USPS-T27-1 B where you provide TY 2006 postal finances using the Commission's attributable cost methodology. Please also refer to USPS witness Taufique's response to Interrogatory GCA/USPS-T28-1 where he states, in relevant part:

...although workshared First-Class Mail is not a subclass, the proposal along the lines suggested in your question would cause these workshare rate categories, which have an implicit cost coverage exceeding all of the subclasses and whose unit cost has in fact declined 2.8 percent (between FY2000 and FY2004), to bear a disproportionate share of the escrow burden.

- A. Please confirm that, in R2000-1 and R2001-1, the Postal Rate Commission recommended rates for First-Class workshared letters that resulted in implicit cost coverages of 248 and 266 for, respectively. If you cannot confirm, please provide the correct cost coverages, explain how they were derived, and provide complete references to all source materials used.
- B. Please confirm that, in R2005-1, the Postal Service's proposed rates for First-Class workshared letters result in an implicit cost coverage equal to 313. If you cannot confirm, please provide the correct cost coverage, explain how it was derived, and provide complete references to all source materials used.
- C. Please confirm that, in R2000-1 and R2001-1, the Postal Rate Commission recommended rates for First-Class workshared letters that resulted in implicit markup indices of 260 and 261, respectively. If you cannot confirm, please provide the correct markup indices, explain how they were derived, and provide complete references to all source materials used.
- D. Please confirm that, in R2005-1, the Postal Service has proposed rates for First-Class workshared letters that result in an implicit markup index equal to 267. If you cannot confirm, please provide the correct markup index, explain how it was derived, and provide complete references to all sources used.
- E. Please confirm that, according to USPS witness Abdirhaman's workshare R2005-1 cost savings analysis (as shown in LR-USPS-K-47), the Postal Service's proposed discounts for First Class workshared letters allegedly exceed the purported cost savings. If you cannot confirm, please provide

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**MMA/USPS-T27-3 (continued):**

- the correct discounts and related cost savings, explain how they were derived, and provide complete references to all source materials used.
- F. Please explain why, in spite of increased discounts for First Class workshared letters that allegedly exceed the purported cost savings, the Postal Service's proposed 5.4% across-the-board rate increase in R2005-1 would result in significant increases in the implicit cost coverage and implicit markup index for such workshared mail.

**RESPONSE**

- A. Confirmed. See the Attachment to MMA/USPS-T27-2, column (1) and (2).
- B. Confirmed assuming the Postal Rate Commission costing methodology is used. See Attachment to MMA/USPS-T27-2 column (3).
- C. Not confirmed. In Docket No. R2000-1, the Postal Rate Commission recommended an implicit markup for First-Class Mail Presorted and Automation Letters and Sealed Parcels of 2.525. In Docket No R2001-1, the Postal Rate Commission recommended an implicit markup for First-Class Mail Presorted and Automation Letters and Sealed Parcels of 2.561. See the Attachment to MMA/USPS-T27-2 columns (1) and (2).
- D. Not confirmed. In this case, for the First-Class Mail Presorted and Automation Letters and Sealed Parcels subclass, the Postal Service's rate proposal results in an implicit markup index of 2.628 using the Postal Service's costing methodology and 2.741 using the Postal Rate Commission's costing methodology. See the Attachment to MMA/USPS-T27-2 columns (3) [PRC] and (4) [USPS]

**RESPONSE TO MMA/USPS-T27-3 (continued):**

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E. Confirmed.

F. The proposed 5.4 percent across-the-board rate increase (including the proposed rate increases for presorted First-Class Mail) is not the only factor affecting the cost coverage and implicit markup for presorted and automation First-Class Mail. In addition to the proposed rate change, changes have occurred in underlying operational costs and, possibly, in mail characteristics (weight, destination, level of presortation) which also affect the costs that underlie the implicit cost coverages.

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**MMA/USPS-T27-4**

Please refer to your response to Interrogatory MMA/USPS-T27-1 B where you provide TY 2006 postal finances using the Commission's attributable cost methodology. Please also refer to page 9 of USPS witness Thress' direct testimony where he provides estimated price elasticities for various categories of mail.

- A. Please confirm that, according to USPS witness Thress, the own price elasticity for First-Class workshared letters has increased dramatically from  $-0.071$  in R2001-1 (USPS-T-8, p. 22) to  $-0.329$  in R2005-1. If you cannot confirm, please explain.
- B. Please confirm that, according to USPS witness Thress, the own price elasticity of  $-0.329$  for First-Class workshared letters is now higher than the own price elasticity of  $-0.267$  for standard regular letters. If you cannot confirm, please explain.
- C. Please explain how you took into consideration the own price elasticity for workshared letters, which has more than quadrupled, when determining that the proposed 5.4% across-the-board rate increase, the resulting cost coverage, and the resulting markup index were all fair and equitable according to the standards established in Section 3622(B) of the Act.

**RESPONSE:**

- A. Confirmed that the estimated elasticity for First-Class Mail workshared letters in this docket is  $-0.329$  and that this elasticity was estimated to be  $-0.071$  in Docket No. R2001-1. For an explanation of First-Class Mail elasticity estimates, changes in elasticity, and how to interpret them, please see witness Thress's testimony, Section II.B.7, "Understanding First-Class Letters Price Elasticities" and witness Thress's response to ABA&NAPM/USPS-T7-2.
- B. Confirmed that the own-price elasticity of  $-0.329$  for workshared First-Class Mail is greater in absolute value than the own-price elasticity of  $-0.267$  for Standard Mail Regular subclass. But, for a fuller explanation,

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**RESPONSE TO MMA/USPS-T27-4 (continued):**

please see the references to witness Thress's testimony cited in the response to part a above.

- C. As indicated by witness Thress in his response to ABA&NAPM/USPS-T7-2, a change in the estimated elasticity does not necessarily mean that the actual elasticity has changed. In preparing any rate proposal, the Postal Service reviews elasticity estimates as one measure of the economic value of service, indicating how the volume of a product customers purchases changes in response to a price change. Generally, the higher the elasticity in absolute value, the lower the economic value of service. A relatively low economic value of service would tend to support a lower markup that would a higher economic value of service. However, in addition to reviewing elasticity estimates, the Postal Service also reviews the intrinsic value of service to both the sender and the recipient. Elasticity estimates may not capture fully the value of service to the recipient which also must be considered under section 3622(b).

In preparing this proposal, I did review the relative value of service and the extent to which it was reflected in the current rates for workshared First-Class Mail. I also considered the circumstances surrounding the escrow obligation. On balance, given that the escrow requirement was

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**RESPONSE TO MMA/USPS-T27-4 (continued):**

not a cost associated with the provision of mail services, the decision was made that an across-the-board increase to recover the escrow obligation was the most fair and equitable approach in this docket.