

**BEFORE THE  
POSTAL RATE COMMISSION  
WASHINGTON, DC 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**

**REBUTTAL TESTIMONY  
OF  
ANTOINETTE CROWDER  
ON BEHALF OF  
ADVO, INC.**

**Communications with respect to this document should be sent to:**

**John M. Burzio  
Thomas W. McLaughlin  
Burzio & McLaughlin  
1054 31<sup>st</sup> Street, N.W., Suite 540  
Washington, D.C. 20007-4403  
(202) 965-4555; Fax (202) 965-4432  
[burziomclaughlin@covad.net](mailto:burziomclaughlin@covad.net)**

**Counsel for ADVO, Inc.**

**September 8, 2005**

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1 **I. INTRODUCTION, PURPOSE, AND SUMMARY**

2 **A. Purpose and Summary**

3 The purpose of this testimony is to provide evidence that rebuts the  
4 direct testimonies of Valpak witnesses Robert Mitchell (VP-T-1) and John Haldi  
5 (VP-T-2). In their direct testimonies, Mr. Mitchell and Dr. Haldi fixate on one  
6 element of the ECR rate structure – the letter-flat rate differential. Mr. Mitchell  
7 contends that the Postal Service’s proposed ECR letter-flat rate differentials are  
8 too low and should be increased, even to the point of applying a “cost coverage”  
9 markup well above 100 percent of the letter-flat cost differential. Mr. Mitchell’s  
10 arguments reflect fundamental misunderstandings of (1) the nature of the letter-  
11 flat cost differential, and (2) the proper relationship of the letter-flat rate  
12 differential to the ECR pound rate in setting appropriate and rational ECR rates.  
13 Dr. Haldi offers multiple arguments why he believes the Saturation letter cost is  
14 overstated relative to that of Saturation flats. In one case, he correctly identifies  
15 an understatement of detached address labels in the USPS analysis. But in all  
16 others, his testimony on these issues is unsupported, misleading, and wrong.

17 **The USPS-Proposed Letter-Flat Rate Differentials Should Not be**  
18 **Increased**

19  
20 Mr. Mitchell recommends that the Commission consider expanding the  
21 ECR letter-flat piece rate differentials so they equal at least 100 percent of their  
22 respective cost differentials. At the Basic-Rate level, he also recommends that  
23 the rate differential should equal the cost differential marked-up by the ECR  
24 subclass mark-up percentage. His rationale for this latter is that ECR letters and  
25 flats should be treated as two different products with equal cost coverages.

1           Whether he treats ECR letters and flats as simply workshared variants of  
2 the same ECR product or he treats them as completely different products, he is  
3 wrong. With respect to treating them as workshared variants of one ECR  
4 product, he simply misses the fact – acknowledged by the Commission in Docket  
5 R2000-1 and by Valpak-Carol Wright witness Haldi in R97-1 – that the letter-flat  
6 cost differential reflects not just shape-related cost differences but also weight-  
7 related cost differences due to the heavier average weight of flats versus letters.  
8 In R2000-1, the Commission stated,

9                        “As the pound rate is supposed to reflect the effect of weight on  
10                       costs, passing through a substantial portion of the ECR  
11                       letter/flat differential amounts to a double counting of the effect  
12                       of weight.” R2001-1 PRC Opinion 2000-1 at 365.  
13

14           On this basis alone, Mr. Mitchell’s proposal to pass through “at least 100  
15 percent” of the letter-flat cost differential is wrong. Given the ECR pound rate,  
16 the letter-flat passthrough must be set at a level significantly below 100 percent  
17 to avoid double-charging flat mailers for weight. Alternatively, if the passthrough  
18 and resulting letter-flat rate differential were to be increased above the level  
19 proposed by the USPS (as Valpak argues), then the pound rate must be reduced  
20 correspondingly.

21           With respect to treating letters and flats as different products, Mr. Mitchell  
22 misconstrues the nature of product pricing. He claims that ECR letters and flats  
23 are two different products and advocates that the passthrough of the letter-flat  
24 cost differential should be “marked up” above 100 percent, so that it will equalize  
25 contribution from letters and flats (page 83). But, that is wrong, both in concept  
26 and execution.



1 High-Density/Saturation letters. There is no need to passthrough any more of  
2 the High-Density/Saturation letter-flat cost differential than already proposed by  
3 the USPS. However, if the Commission chooses to increase the letter-flat rate  
4 differential, it should concomitantly reduce the ECR pound rate.

5 **The Revised DAL Estimates Provide No Excuse to Change USPS-**  
6 **Proposed ECR Saturation Rates**

7  
8 Dr. Haldi, based on data provided by ADV0, has noted that the number of  
9 detached address labels estimated by the USPS in its delivery cost analysis was  
10 understated. In this testimony, I provide the corrected USPS- and PRC-version  
11 delivery cost estimates based on Dr. Haldi's proposed adjustment. The  
12 corrected costs do not support an increase in the Saturation letter-flat rate  
13 differential and do not change the fact that the High-Density/Saturation flat  
14 product makes a greater percentage contribution than does the High-  
15 Density/Saturation letter product.

16 **Dr. Haldi's Implication that Saturation Letter Costs Are Excessive**  
17 **Compared to Saturation Flat Costs is Unsupported**

18  
19 Implying that the letter costs are overstated and flat costs are understated,  
20 Dr. Haldi makes some interesting but misleading comments on the development  
21 of Saturation letter and flat costs. First, because of the way USPS witness Kelley  
22 developed the distribution key for city carrier sequenced delivery cost, Dr. Haldi  
23 claims that Saturation flats are attributed too little city carrier delivery cost,  
24 relative to Saturation letters. However, his analysis of the situation was not taken  
25 to its ultimate conclusion. When that is done, the opposite conclusion is reached

1 – that Saturation flats are attributed too much city carrier delivery cost relative to  
2 Saturation letters.

3           Second, Dr. Haldi asserts that mail processing costs to process some  
4 “unknown, but possibly large and growing, volume of DAL [that] are being  
5 attributed to letters.” (page 21) This is completely untrue. ADVO data, supplied  
6 to Valpak, indicate that DALs are not automation compatible. There are also  
7 other operational reasons why DALs are not processed at mail processing plants.  
8 Further, the USPS data provided in response to Valpak discovery requests also  
9 indicates that DAL costs are attributed to their host flats or parcels.

10           Third, Dr. Haldi describes various postal cost data problems he believes  
11 cause letters (defined as letter-shapes 3.5 ounces or less) to bear too much cost.  
12 However, what he considers “mismatches” are really part of a proper  
13 methodology for matching up operational volumes with operational costs.  
14 Although there is some minor imprecision in some of the data, there is no  
15 discernable bias. There is no evidence of cost bias against Saturation letters but  
16 some evidence that Saturation flats bear too much cost.

17           **Dr. Haldi’s Capacity Constraint Theory Does Not Describe the Real**  
18           **World And His Modeled Delivery Costs Are Unnecessary**

19  
20           Dr. Haldi also introduces a novel new theory in this case. It relates to the  
21 fact that city carriers can avoid cost by taking out Saturation mailings (without  
22 first casing them) as extra bundles or extra trays. Because of the cost avoidance,  
23 those mailings are lower cost than mailings that must be cased. He explains,  
24 though, that there is a limit to the number of extra bundles and extra trays city  
25 carriers may take out. And he implies that the carriers are extremely close to

1 their limit and that they reserve their remaining capacity for Saturation flats to the  
2 harm of Saturation letters. Because of this, he implies that the Saturation letter  
3 and flat marginal city delivery costs should be based on cased delivery costs  
4 rather than extra-bundle/tray delivery costs. He therefore proposes the use of  
5 modeled Saturation letter and Saturation flat cased delivery costs to determine  
6 the Saturation letter-flat cost and rate differential.

7 Dr. Haldi's theory is completely off base: (1) he ignores the fact that city  
8 carriers have a variety of ways to expand their extra-bundle/tray capacity, (2) he  
9 does not review available evidence on the subject, (3) he ignores any other  
10 reasons why some Saturation mail is not handled as extra-bundles/trays, and (4)  
11 he ignores the fact that the USPS cost data already reflect conditions where  
12 some Saturation mail is DPSed or cased rather than treated as extra-  
13 bundles/trays. Data from the new City Carrier Street Time Survey (CCSTS)  
14 confirm the fact that city carriers have capacity to handle new Saturation mailings  
15 as extra-bundles/trays. Other information also supports that view and explains  
16 why many Saturation letters are either DPSed or cased in lieu of being taken out  
17 as an extra-bundle or tray.

18 Finally, Dr. Haldi's proposed modeled delivery cost assumes that there is  
19 no city carrier capacity *ever* to handle a new (marginal) Saturation mailing as an  
20 extra-bundle/tray. This is so far from the truth that he cannot bring himself to  
21 support that assumption (response to ADVO/VP-T2-24). His theory and  
22 proposed modeled costs should be rejected.

23

24

1           **B.     Organization of the Remainder of this Rebuttal Testimony**

2           The remainder of this testimony is organized into three parts. The  
3 first addresses rate structure issues presented by Mr. Mitchell and explains them  
4 in their proper context. The second part discusses some cost issues noted by  
5 Dr. Haldi and explains why they should not have any impact on the rates  
6 proposed by the USPS in this case. And, the final part explains why Dr. Haldi's  
7 radical capacity constraint theory is wrong and his letter-flat cost proposal is  
8 unnecessary.

9           Workpapers supporting the results presented in this rebuttal are included  
10 in ADVO LR-1 (excel spreadsheets) and LR-2 (SAS program and output).

11

1 **II. VP WITNESS MITCHELL'S RATE STRUCTURE PROPOSAL IS**  
2 **INCONSISTENT WITH SOUND RATEMAKING PRINCIPLES**  
3

4 Much of Mr. Mitchell's testimony (pages 37 through 76) addresses the  
5 need to reduce ECR cost coverage. Specifically at page 80 he recommends:

6 (1) A reduction of 10 percentage points in the ECR cost coverage  
7 relative to the coverage proposed by the USPS and 10 additional  
8 points of coverage in each of the next two cases; and  
9

10 (2) ECR rates that remain unchanged from current levels.

11 However, despite his recommendation to leave ECR rates unchanged, Mr.  
12 Mitchell also comments on ECR rate structure issues (pages 81-88). In  
13 particular, he discusses the ECR letter-flat rate differentials, contending that 100  
14 percent or even substantially more of the letter-flat cost differentials should be  
15 passed through to the relevant rate differentials. He believes that ECR letters  
16 and ECR flats are different products whose individual costs need to be  
17 recognized and for which individual cost coverages need to be selected (page  
18 83). Mr. Mitchell claims that, if the passthroughs are less than 100 percent, then  
19 ECR letter cost coverages are excessive compared to ECR flat cost coverages  
20 (page 84).

21 Mr. Mitchell's passthrough treatment is not only incorrect but incorrectly  
22 mixes ratemaking concepts. "Passthroughs" are used in conventional  
23 ratemaking where all rate categories within a subclass are considered to be  
24 worksharing variants of the same basic product. Differences between rate  
25 elements (e.g., the letter and flat piece rates) are based on their worksharing cost  
26 differences. When passthroughs are 100 percent, the unit contribution should be  
27 the same for each rate category. However, to determine the cost coverages for  
28 different *products*, a set of costs different from those used in the conventional  
29 approach must be used, together with total product revenues. The correct

1 treatment of products provides a completely different and more efficient result  
2 than that proposed by Mr. Mitchell.

3 To demonstrate this, I first explain the conventional ratemaking treatment  
4 and then explain the correct ratemaking treatment for two different products:  
5 ECR High-Density/Saturation Flats and ECR High-Density/Saturation Letters.  
6 The quantitative results I present demonstrate that, even at the Postal Service's  
7 proposed rates, High-Density/Saturation Flats provide a greater institutional cost  
8 coverage than High-Density/Saturation Letters and that expanding the rate  
9 differential between them, as Mr. Mitchell advocates, would only exacerbate the  
10 disparity.

11 **A. Conventional ECR Cost and Rate Treatment**

12 **(1) Conventional Treatment of ECR Rate Categories**

13  
14  
15 Because all ECR rate categories are in the same subclass, postal  
16 ratemaking conventionally considers them as worksharing variants of one  
17 product. Thus, all the category costs are adjusted so that they reflect  
18 worksharing-related differences. Under that convention, passthroughs of no  
19 more than 100 percent of cost differentials are applied (with some minor  
20 exceptions) to piece rate differentials. This treatment is appropriate when the  
21 cost difference between two rate categories is considered only the result of  
22 worksharing. The intent is to ensure that (a) all rate categories generate the  
23 same institutional cost contribution and (b) mailers have the correct price signals  
24 so that they may efficiently choose from among the product variants.

25  
26

1           **(2) Letter-Flat Cost Differences Reflect Both Shape**  
2           **and Weight-Related Cost Differences**

3           ECR letter and flat unit costs include all costs caused by all their  
4 individual characteristics – including shape- or piece-related and weight-related  
5 costs. Despite this fact, the cost differentials between those unit costs are used  
6 to determine the supposedly piece-related rate differentials between the letter  
7 and flat piece rates for each density level. Because weight-related costs are  
8 recovered separately through the pound rate, the weight-related portion of costs  
9 captured in the letter-flat unit cost differential must be excluded when setting the  
10 letter-flat rate differential. Stated another way, a 100 percent passthrough of  
11 both the shape-related and weight-related unit cost differential, as Mitchell  
12 advocates, is excessive. Charging flats with a 100 percent passthrough of the  
13 letter-flat cost differential plus the pound rate would produce a clearly improper  
14 double-counting of weight-related flat costs. This fact was recognized by the  
15 Commission in Docket R200-1 and used to support a reduction in the ECR  
16 pound rate in that case:

17  
18           “[5461]       The Commission finds that several considerations,  
19 not directly related to the study, point to the appropriateness of a  
20 modest reduction in the ECR pound rate. [footnote deleted] These  
21 include (1) the demonstration that the current pound rate produces  
22 an illogical postage result, inconsistent with notions of fairness and  
23 equity and efficient postal operations; (2) the recognition that  
24 reclassification has reduced the need for the pound rate to act as a  
25 proxy; and (3) the demonstration that the pound rate “over  
26 recovers” due to shape. The first two points are largely self-  
27 evident; with the respect to the latter point, the Commission notes  
28 that witness Crowder’s contention that the ECR letter/flat cost  
29 differential reflects differences due to shape and weight has merit.”  
30 R2001-1 PRC Opinion 2000-1 at 365

31  
32       The Commission further stated:

33  
34           “However, because the weight of letters and flats varies, the  
35 letter/flat cost differential by density level likely reflects differences  
36 in both weight and shape. As the pound rate is supposed to reflect

1 the effect of weight on cost, passing through a substantial portion of  
2 the ECR letter/flat differential amounts to a double counting of the  
3 effect of weight.” Id., page 365.

4  
5 Indeed, even Dr. Haldi in R97-1 presented testimony that  
6 recognized the letter-flat cost differential included both shape- and weigh-  
7 related costs and he, therefore, made allowances for it in his ECR rate  
8 structure proposal (Tr. 27/15055-56). Despite this, Mr. Mitchell did not  
9 address this inherent and accepted characteristic of the letter-flat cost  
10 differential. At the hearing, he was apparently unaware of the issue. (Tr.  
11 9/5417-20) Yet the inclusion of weight-related costs in the letter-flat cost  
12 differential is, standing alone, sufficient reason to reject his proposal for a  
13 full passthrough.

14 **(3) In Conventional Ratemaking, the Letter-Flat**  
15 **Passthroughs Must Be Far Less Than 100 Percent to**  
16 **Avoid Double-Charging**

17  
18 For the above reasons, the passthrough of the letter-flat cost  
19 differential must be substantially less than 100 percent to avoid double-  
20 charging for weight-related costs. In this section, I calculate the actual  
21 passthroughs at the Postal Service’s proposed rates, using revised cost  
22 estimates under the USPS and PRC versions of delivery costs that take  
23 into account revised estimates of the number of detached address labels  
24 (DALs) in the system.<sup>1</sup> From that information plus other information

---

<sup>1</sup> Development of these costs as well as all the other estimates and calculations described in this text are explained in ADVO LR-1. The revised number of DALs and their treatment is as proposed in ADVO/VP-T2-2 with the exception that the DAL volume distribution between city and rural routes is the actual for the ADVO-reported DAL volumes. In the PRC version, an adjustment was also made to distribute the DAL-related costs only to Saturation flats and to correct for the erroneous rural “crosswalk.”

1 provided by the USPS in its library references, I have calculated the  
 2 USPS- and PRC-versions of ECR delivery plus mail processing costs by  
 3 density-level and shape as set forth in the following tables.

4 **USPS Version of TY 06 ECR Category Costs**

	<b>USPS Adj MP LR K-84</b>	<b>USPS Delivery LR K-67</b>	<b>Total Ratemaking Costs</b>
<b>Letters</b>			
Automation	1.457¢	2.887¢	4.344¢
Basic	3.776	5.334	9.110
High Density	0.967	4.476	5.443
Saturation	0.967	3.629	4.596
<b>Flats</b>			
Basic	2.889	6.143	9.032
High Density	1.225	4.609	5.834
Saturation	1.225	4.358	5.583

5  
 6 This table shows that under the USPS version of costs, because of the  
 7 revised DAL estimate, Saturation flat delivery cost is higher and Saturation letter  
 8 cost is lower than the Postal Service estimate. Even with this change, however,  
 9 the Saturation level letter-flat rate differential of 0.9-cent is 91.2 percent of the  
 10 0.987-cent cost differential. This is an excessively high passthrough given that  
 11 only 65.6 percent of Saturation flat TYAR revenue is from pieces (i.e., given the  
 12 implicit ratemaking assumption that 65.6 percent of Saturation flat cost is shape-  
 13 related).

14 For the PRC version of costs, the passthrough of the Saturation level  
 15 letter-flat rate difference is 60.7 percent of the 1.483-cent cost difference, a  
 16 passthrough quite close to the 65.6 percent of revenue that is piece-related.<sup>2</sup>

<sup>2</sup> In R2001, the PRC approved a 0.8-cent saturation ECR saturation letter-flat rate differential based upon a 1.182-cent cost differential, which represented a passthrough of roughly 68%, quite close to the proportion of Saturation flat piece-rate revenue.

1

**PRC Version of TY06 ECR Category Costs**

	<b>USPS Adj MP K-107</b>	<b>USPS Delivery PRC Vers Est</b>	<b>Total Ratemaking Costs</b>
<b>Letters</b>			
Automation	1.523¢	3.579¢	5.102¢
Basic	3.431	5.584	9.014
HD	1.056	4.064	5.121
Sat	1.056	3.808	4.864
<b>Flats</b>			
Basic	3.115	6.509	9.624
HD	1.466	4.755	6.221
Sat	1.466	4.880	6.347

2

3

The results presented above show that there is no reason to

4

increase the letter-flat differential at the Saturation level and, in the case of

5

the USPS version, even provide a reason to reduce it. Conversely, if the

6

piece rate differential is increased, then the pound rate should be reduced.

7

**B. Appropriate Treatment of Product Costs and Rates**

8

Mr. Mitchell argues that ECR letters and flats are “to a considerable

9

extent” different products and should be priced as different products, each

10

bearing its own costs and meeting its specified institutional cost coverages

11

(pages 82-84 and in response to several interrogatories). To achieve this, he

12

proposes a Basic-Rate letter-flat passthrough percentage that equals the ECR

13

coverage percentage. For all other rate levels, he proposes to increase the

14

passthroughs to 100 percent. Then he apparently proposes to apply the

15

conventional ECR ratemaking algorithm to determine all category piece and

16

pound rates for both products. Apparently he believes that if this is done, it will

1 ensure that ECR letters, as an individual product, will have a contribution equal to  
2 ECR flats, as an individual product.<sup>3</sup>

3 Mr. Mitchell's discussion wrongly mixes the conventional rate-design  
4 concepts as described above with concepts far more appropriate for separate  
5 product costing. If the objective is to design efficient product rates for ECR mail,  
6 one must (1) identify the distinguishable ECR "products" and (2) calculate the  
7 total costs for those products. Differences in worksharing cost features should  
8 not be neutralized, as done in the conventional rate-design approach. Thus,  
9 trying to efficiently price two or more products by manipulating multiple cost  
10 passthroughs within the current ECR subclass structure (using workshare-  
11 adjusted costs), as proposed by Mr. Mitchell, is extremely awkward if not  
12 impossible. It will not generate the efficient rates that Mr. Mitchell professes to  
13 desire.

14 For true product pricing, a different approach must be used that, as  
15 described below, first identifies the real "products" that are included in the ECR  
16 subclass and then estimates their respective costs, revenues, and contribution  
17 percentages.

### 18 **(1) Identification of Products**

19 Mr. Mitchell's discussion leaves one with the impression that there  
20 are only two ECR products: letters and flats. That is not correct. Shape is not  
21 the only determinant of product distinctions. Market and operational  
22 characteristics are important determinants in identifying different products.

---

<sup>3</sup> VP-T-1, pages 81-83 and 87 and responses to ADV0/VP-T1-3 and -8.

1 For ECR flats, there are clearly two separate markets: (1) Basic-Rate flats  
2 and (2) High-Density and Saturation flats. Because the different markets these  
3 products dictate different mailing needs, these two flat products have different  
4 mail and postal cost characteristics and they are very likely to have different own-  
5 price sensitivities and differences in income and cross-price sensitivities. If, as  
6 Mr. Mitchell believes, the costs for each product should be separately identified  
7 and marked-up, then, for flats, this should apply to two separate products: Basic-  
8 Rate and High-Density/Saturation flats. The same is likely true for ECR letters.

9 In fact, the High-Density/Saturation product is consistent with the  
10 Commission's requirements for determining separate subclass treatment (i.e.,  
11 separately determined coverage on total product cost). Those requirements  
12 specify that the product must have market, mail, and cost characteristics that are  
13 distinguishable from those of other products.<sup>4</sup> When that occurs, the subclass for  
14 that product will have unique criteria that minimize undesirable crossovers by  
15 other products that may cause undesirable product cost and contribution  
16 changes.<sup>5</sup> Establishing subclass treatment for such distinguishable products is  
17 the best way to ensure efficient rate recognition of total product costs, market  
18 characteristics, and mark-up considerations.

19 For purposes of addressing Mr. Mitchell's comments concerning product  
20 costs and cost coverages, I accept his comments that letters and flats are

---

<sup>4</sup> See, e.g., Commission Opinion in R87-1, paragraphs 5505 ff (pages 581 ff) and MC-95-1, paragraphs 1004 ff (pages 1-2 ff).

<sup>5</sup>An undesirable cross-over occurs when mail from one subclass shifts to another in order to take advantage of lower price but that mail does not change its cost or market characteristics. Such shifts could affect the subclass cost and price sensitivity characteristics upon which subclass mark-up is based. Unique subclass criteria define the type of product included in the subclass to the exclusion of all other types of products that could change subclass cost and contribution.

1 different products and treat High-Density/Saturation flats as a product that is  
2 different from High-Density/Saturation letters.

3 **(2) Appropriate Product Costs**

4 In conventional ECR rate design, the actual unit mail processing  
5 costs (derived from the IOCS distribution) for the various ECR letter and flat  
6 categories are adjusted so that they all represent mail processing cost with zero  
7 drop-shipment – thus neutralizing the cost effect of differences in drop-shipment  
8 levels. So, despite the fact that Saturation flats actually have a lower unit mail  
9 processing cost because of their greater drop-shipment compared to Saturation  
10 letters, the “drop-shipment” adjustment has the effect of making the adjusted flat  
11 mail processing unit cost greater than that for letters. This conventional  
12 treatment is appropriate if one is attempting to price all ECR shape and density  
13 rate categories as if they are simply workshare variations of one product. But it is  
14 not appropriate when attempting to determine prices for different products within  
15 ECR, each assessed on the basis of its individual cost coverage level, as  
16 envisioned by Mr. Mitchell.

17 **(3) The High-Density/Saturation Flat Product Has a Larger**  
18 **Percentage Coverage Than the High-Density/Saturation Letter**  
19 **Product**

20  
21 I have estimated the USPS- and PRC-versions of unit product costs  
22 for the two products identified above: High-Density and Saturation Flats and  
23 High-Density and Saturation Letters. The costs for these two products include  
24 the estimated actual mail processing, transportation, and delivery costs (with  
25 piggybacks) and are divided by the sum of their corresponding RPW volumes.

1 These are compared to the USPS estimate of ECR High-Density and Saturation  
 2 letter and flat (commercial) revenues under current and proposed rates in order  
 3 to determine their respective cost coverages.

4 The results are as follows:

5 **USPS Version of TY06 Product Costs<sup>6</sup>**

	<b>TY Unit Cost</b>	<b>TYAR Unit Revenue</b>	<b>TYAR % Coverage</b>
High-Density/ Saturation Letters	4.653¢	13.630¢	292.9%
High-Density/ Saturation Flats	4.961	16.144	325.4%

6

7 **PRC Version of TY06 Product Costs<sup>7</sup>**

	<b>TY Unit Cost</b>	<b>TYAR Unit Revenue</b>	<b>TYAR % Coverage</b>
High-Density/ Saturation Letters	4.818¢	13.630¢	282.9%
High- Density/ Saturation Flats	5.558	16.144	290.4%

8

9 It is clear from these results that the High-Density/Saturation flat product  
 10 has a greater markup than does High-Density/Saturation letter product.

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<sup>6</sup> Total unit cost is the sum of unit mail processing cost from LR K-84, unit transportation cost from LR K-84 (with exception that dropship-avoided mail processing costs from LR K-88 were replaced with caused transportation costs), and unit delivery cost from LR K-67, adjusted for Valpak's estimate of DALs. Revenues are for commercial ECR High-Density and Saturation categories from LR K-115 and letter revenues include the revenues from so-called heavy letters. See ADVO LR-1.

<sup>7</sup> Total unit cost is the sum of unit mail processing cost from LR K-107, unit transportation cost from LR K-107 (with exception that dropship-avoided mail processing costs from LR K-112 were replaced with caused transportation costs), and unit delivery cost from a combination of rural costs from LR K-67 and city costs from LR K-101, adjusted for Valpak's estimate of DALs, with all DAL costs attributed to Saturation flats. Revenues are for commercial ECR High-Density and Saturation categories from LR K-115 and letter revenues include the revenues from so-called heavy letters. See ADVO LR-1.

1           **C.     Summary: There Is No Support For Expanding the Letter-Flat**  
2           **Rate Differential**

3  
4           In summary, Mr. Mitchell's concern in this case about equalizing the  
5 percentage contribution of separate letter and flat products is unwarranted in the  
6 case of High-Density/Saturation mail. Under the conventional ratemaking  
7 approach where letters and flats are considered variants of the same product,  
8 the letter-flat cost differential reflects both shape-related and weight-related cost  
9 differences. Only the shape-related cost differences, which are something less  
10 than 100 percent of the total differential, should be "passed-through" to piece  
11 rates. The weight-related cost differences are covered in the pound rate. Thus,  
12 the High-Density/Saturation letter-flat cost differential passthroughs to rate  
13 differentials are appropriately less than 100 percent. If the USPS-proposed  
14 High-Density/Saturation letter-flat rate differentials are increased, then a  
15 concomitant decrease in the pound rate is required in order to prevent High-  
16 Density/Saturation flats from being over-priced relative to letters.

17           Separately, when properly treated as individual products, High-  
18 Density/Saturation flats are shown to have a higher cost coverage than High-  
19 Density/Saturation letters at the USPS-proposed rates. Thus, Mr. Mitchell's  
20 proposal to equalize product cost coverages through manipulating the letter-flat  
21 cost passthrough and rate differential is completely unnecessary. Moreover, his  
22 proposed method of "equalizing" product coverages will not accomplish the  
23 result he claims but will instead produce excessive flats coverage relative to  
24 letters in part because of the double-recovery of weight-related costs in both the  
25 piece and pound rates.

1           Accordingly, Mr. Mitchell's recommendations regarding expanding the  
2 ECR letter-flat rate differentials should be ignored as both uninformed and  
3 causing even more inefficient rates than are now proposed.

4

1 **III. VP WITNESS HALDI’S COSTING ARGUMENTS DO NOT SUPPORT A**  
2 **AN EXPANDED LETTER-FLAT RATE DIFFERENTIAL**

3 Dr. Haldi makes a number of observations concerning what he considers  
4 to be problems with postal cost data and costing studies. These relate to (1) the  
5 detached address labels (DALs) that accompany some Saturation flats and some  
6 parcels and (2) the fact that Saturation “letters” for rate category purposes weigh  
7 3.5 ounces or less while the postal costing systems identify “letters” as all letter-  
8 shapes (even those that weigh more than 3.5 ounces). With respect to the first,  
9 he implies that Saturation letter costs may be overstated due to the presence of  
10 DALs. With respect to the second, he states that these “. . . other possible  
11 inconsistencies and recording errors . . . may have mis-attributed costs  
12 systematically to Saturation letters instead of flats.” (page 25) As discussed  
13 below, now that the delivery costs are adjusted to reflect the revised number of  
14 DALs, there is no evidence that Saturation letter costs are overstated relative to  
15 Saturation flat costs.

16 On the other hand, he also urges the Postal Service to improve the way in  
17 which its data systems collect volume and cost data on DALs. And, I agree with  
18 him on the need for improved data.

19 In the following three subsections, I discuss (1) the impact of DALs on City  
20 Carrier Costing, (2) Dr. Haldi’s concern about DAL automation costs being  
21 attributed to Saturation letters, and (3) Dr. Haldi’s concern about the definition of  
22 “letters” in the USPS cost analyses. None of his concerns warrant an expansion  
23 of the letter-flat rate differential and one strongly argues for the reverse.

24  
25 **A. The Impact of DALs on City Carrier Casing Reduces Flat Costs**  
26 **More than Letter Costs**

27 Dr. Haldi correctly identifies a problem associated with the impact  
28 of DALs on the estimate of cased and sequenced (non-cased) flat volumes used  
29 to distribute ECR city carrier delivery costs. He implies that this causes

1 Saturation flats to be distributed too little city carrier delivery cost (page 19). But  
2 this implication is wrong.

3 **(1) Background**

4 The new USPS city carrier delivery study identifies volume-variable  
5 out-of-office (delivery) cost pools for letters, flats, “sequenced” or non-cased mail,  
6 small and large parcels, accountables and collectibles. By comparison to the old  
7 set of studies, the new study introduces three new cost pools: the “sequenced”  
8 pool, the small parcel pool, and the large parcel pool. The “sequenced” pool is  
9 relevant for this discussion. “Sequenced” mail is non-carrier-cased Saturation  
10 mail that is taken directly to the street by the city carrier as an extra bundle or  
11 tray.<sup>8</sup> The USPS City Carrier Cost System (CCS) collects the delivered rate  
12 category shape-related volumes used to distribute those cost pools.  
13 Unfortunately, the CCS does not yet separate out those volumes by “sequenced”  
14 and non-“sequenced.” So, the CCS Saturation letter and flat volumes that are  
15 “sequenced” and “non-sequenced” must be estimated so that they can be used  
16 as distribution keys relevant to the volume-variable delivery cost pools.

17 USPS witness Kelley (USPS-T-16) does this in three steps:

- 18 - Saturation letter and flat city carrier in-office casing costs are  
19 individually identified from the IOCS data.
- 20 - Saturation letter and flat casing productivities from USPS witness  
21 Shipe (USPS-T-10) in R90-1, together with base-year direct city  
22 carrier workhour cost, are used to estimate unit base-year costs to  
23 case Saturation letters and, separately, Saturation flats.
- 24 - Total Saturation letter and flat in-office casing costs are each then  
25 divided by the respective estimates of unit casing cost to obtain  
26 separate estimates of the number of cased Saturation letters and  
27 flats.  
28  
29  
30

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<sup>8</sup> In Section IV below, sequenced mail is called extra-bundle or extra-tray mail. In these discussions, the term “sequenced” mail should not be confused with delivery-point-sequenced or walk-sequenced mail. The former is a subset of the latter but not all of the latter may be considered “sequenced,” as the term is used here.

1           Then Mr. Kelley’s estimates of sequenced CCS Saturation letters, flats,  
2 and parcels are used to distribute the sequenced mail volume-variable delivery  
3 cost pool to each shape.<sup>9</sup> And, the estimates of non-sequenced CCS Saturation  
4 letters and flats are used in the distribution keys for the letter and flat volume-  
5 variable delivery cost pools. The latter are simply the differences between (a)  
6 total CCS Saturation volumes by shape and (b) estimated CCS Saturation  
7 “sequenced” volumes by shape. In this discussion, it is important to note that  
8 CCS volumes are used as *both* the subclass and intra-subclass distribution keys  
9 for the various delivery cost pools.

10           **(2) The “Problem”**

11           Dr. Haldi points out that Mr. Kelley’s estimate of “sequenced”  
12 Saturation flats is understated. This is because, when a DAL is being handled at  
13 the time an In Office Cost System (IOCS) tally is taken, the USPS attributes that  
14 tally to its host flat or parcel. Thus, the IOCS in-office casing cost for ECR  
15 Saturation flats (used in Mr. Kelley’s Step 1) includes the costs for casing DALs  
16 as well as flats. As a result, his estimate of cased flats is overstated while his  
17 estimate of uncased or sequenced flats is understated.<sup>10</sup> And, understating the  
18 volume of sequenced Saturation flats understates the share of the sequenced  
19 delivery cost distributed to Saturation flats, thereby overstating the share of  
20 sequenced delivery cost distributed to Saturation letters.

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<sup>9</sup> Small Saturation parcels are neither cased nor sequenced.

<sup>10</sup> If some of the IOCS flat casing cost used by Mr. Kelley to estimate is caused by DALs, then only a portion of that cost is caused by flats.

1           However, Dr. Haldi stops his explanation at that point, not taking the  
2 analysis to its ultimate conclusion. If the number of CCS “sequenced” flats is  
3 under-estimated (for purposes of distributing the sequenced or non-cased cost  
4 pool), then the number of CCS “non-sequenced” or cased flats is over-estimated  
5 (for purposes of distributing the cased flat cost pool). If the latter is the case,  
6 then Saturation flats are currently distributed too much of the cased flat delivery  
7 cost pool. And, because sequenced delivery unit cost is less than regular  
8 delivery unit cost, a correction of the total delivery costs for Saturation flats (and  
9 for ECR in total) would make it lower – reducing it even moreso than the  
10 reduction in delivery unit cost for Saturation letters noted by Dr. Haldi.<sup>11</sup>

11           **B.     DALs Do Not Impact Letter Mail Processing Costs**

12           On pages 19 through 21 of his testimony, Dr. Haldi asserts that  
13 some unknown, possibly large, and growing volume of DALs is being sorted on  
14 automation equipment. He then implies that the costs incurred to process DALs  
15 on automation are being wrongly attributed by the IOCS to Saturation letters.<sup>12</sup>  
16 His concerns in this regard are extremely overblown.

17           Dr. Haldi bases his assertion on three points. First, he notes that USPS  
18 witness Lewis (USPS-T-30) stated that “. . . there is field interest in DPSing the  
19 letter-shaped component of a DAL mailing and . . . in some places delivery and

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<sup>11</sup> A larger flat sequenced volume will shift some sequenced delivery cost from Saturation letters back to Saturation flats. For that reason alone, Saturation letter delivery cost will also decline but not to the extent of the decline in Saturation flat costs given that flats would experience a far greater cost reduction as compared to Saturation letters. Depending upon the extent of the correction, this could amount to a substantially lower flat cost and letter-flat cost differential.

<sup>12</sup>Dr. Haldi also implies that any transportation cost to take DALs from the DDU to the plant and back again is wrongly attributed to saturation letters. But, such transportation is through either the Vehicle Delivery Service or Purchased Transportation and neither cost segment uses a shape-related distribution key.

1 plant managers have implemented local procedures to do this” (response to  
2 VP/USPS-T30-14). Second, he points out that costs in the BCS and OCR  
3 MODS cost pool are being attributed to Saturation letters despite the fact that  
4 Saturation letters must be barcoded while DALs are exempt from the barcoding  
5 requirement. And, third, he implies that IOCS tally-takers are unable to identify  
6 DALs at the mail processing plant and would therefore call them Saturation  
7 letters.

8 With respect to USPS automation of DALs, Mr. Lewis simply expressed  
9 the USPS interest in DPSing DALs but he also explained that “. . . it’s got to be a  
10 pretty small number at this point.” (Tr. 6/2433) Further, in response to a Valpak  
11 question during cross, the USPS responded that a review of the FY04 IOCS data  
12 indicated that there were no Standard Mail DAL tallies in the MODS cost pool  
13 BCS/DBCS.<sup>13</sup> Finally, in response to Valpak interrogatories, ADVO data show  
14 that only 0.57% of all DALs it reports (for itself, MMSI, and ANNE) are barcoded  
15 and, despite the miniscule barcoding percentage, it is unlikely that those DALs  
16 were actually automated. The ADVO-provided data also show that there are no  
17 plans to barcode any DALs in the near future.

18 Thus, given the DALs’ physical characteristics, it is highly unlikely that  
19 they could not only be processed on an OCR but also then processed on the  
20 two-pass DBCS/CSBCS (as speculated by Dr. Haldi on page 21). Further,  
21 virtually all Saturation flats with DALs are dropped at the DDU. The DALs’ very

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<sup>13</sup>USPS Response to Valpak request at Tr. 7/27179. Notably, in LR K-67 where unit delivery costs are estimated, Mr. Kelley assumes that no DALs are DPSed but are instead either cased or taken to the street as extra bundles.

1 purpose in accompanying their host flats means that the USPS would have to  
2 ensure unusual coordination between the plant and the DDU before they could  
3 be transported upstream, processed over night, and returned in a such a way as  
4 to ensure their delivery at the same time as their host flats.<sup>14</sup>

5 With respect to the alleged incorrect IOCS attribution of DAL costs to  
6 Saturation letters, Dr. Haldi notes that there are Saturation letter costs in the  
7 OCR/BCS MODS cost pool. Because Saturation letters are already barcoded,  
8 he jumps to the conclusion that they would have no OCR/BCS cost (and  
9 therefore that cost must instead be caused by DALs). However, the amount of  
10 Saturation letter OCR/BCS unit cost is less than a hundredth of a cent and could  
11 easily be caused by Saturation letters requiring OCR/BCS processing because of  
12 inaccurate or unreadable barcodes. Further, USPS Handbook F-45, pages 12-8  
13 to 12-11 (USPS LR-I-14, "Question 22") explains that when a DAL is the subject  
14 of an IOCS tally, that tally is attributed to the host piece. In the event that a host  
15 piece cannot be identified, IOCS editing process attributes them to flats (LR K-9,  
16 Appendix B, page 137).<sup>15</sup>

17 It is clear that there must be extremely few if any DALs processed on  
18 automation equipment. Further, even if there were automated DALs, the vast

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<sup>14</sup>When asked for support for his assertion regarding a large and growing number of DALs being automated, Dr. Haldi responds with cites from Docket R2001-1 where a USPS witness states (1) that running DALs on DPS equipment is inconsistent with keeping DALs matched up with the matching host pieces and (2) it is highly unlikely, if ever, that DALs are run on DPS automation. (Response to ADVO/VP-T2-6.) These simply describe the reality that DALs are very rarely, if ever, run on automation equipment.

<sup>15</sup> USPS Response to Valpak request at Tr. 7/27179.

1 majority of the time, the IOCS would correctly identify them as DALs and attribute  
2 their costs to their host flats or parcels.<sup>16, 17</sup>

3 **C. The Postal Data Systems Are Not Biased Against Letters**

4 Dr. Haldi notes what he considers to be mismatches between  
5 revenues and volumes on one hand and costs on the other (pages 22-24). He  
6 notes that letter-shapes occur in all weight ranges while letter rates apply only to  
7 letter-shapes weighing 3.5 ounces or less. And, he believes that it is more likely  
8 that the postal cost systems will record a letter-shaped piece over 3.5 ounces as  
9 a “letter” than record letter-shaped piece under 3.5 ounces as a “flat.” As a  
10 result, he leads the Commission to believe that there may be a serious bias  
11 against ECR letters, attributing non-letter costs to letters.

12 However, though the postal cost and volume data used to develop unit  
13 cost by shape are not as precise as Dr. Haldi would like them, they do not appear  
14 to be biased or seriously mismatched. The postal cost data are collected on the

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<sup>16</sup>In response to ADVO/VP-T2-7 concerning his hypothesized DAL automation costs, Dr. Haldi claims that the Question 22 DAL instructions cover only single piece tallies. He also speculates that DALs may be handled in non-single-piece mail handling tallies along with other letter-shaped pieces and the tester would consider them Saturation letters and would not have the appropriate instruction on how to identify them as DALs. (Response to ADVO/VP-T2-7) His characterization of the IOCS instructions is a bit misleading. According to USPS Handbook F-45 (pages 12-4 to 12-5, 12-8 to 12-11, 17-2), Question 22 applies to mail that is either a single piece, an identical mailing, or a non-identical mailing (in items or containers) subject to the top piece rule. Question 22 does not apply when the tester finds non-identical or mixed mail (page 17-2 of Handbook F-45). If the mixed mail container can be counted, then, per Question 24 applies and DALs may be counted as “cards.” If the mixed mail container cannot be counted, then either Question 25 (regarding Special Services) or Question 26 (attributing the container by Basic Function) apply. Thus, even if there were some DALs in the automation mailstream, their possible mixed mail tally costs, if any, would be miniscule.

<sup>17</sup> The mixed-mail issue also applies for city carrier in-office costs. But, if any DAL mixed mail cost is attributed to Saturation letters, it should be an extremely minor amount. DALs are not handled as mixed mail in containers except when the carrier is moving, in some sort of rolling container, all his cased and strapped mail to either his truck or relay arrangements. As Dr. Haldi notes, tallies associated with this operation are “minimal” (page 38) and tally costs for each individual mail type counted in that single tally are likely to be miniscule.

1 basis of shape or operation related to shape.<sup>18</sup> So, costs for letter-shape pieces  
2 weighing more than 3.5 ounces are likely included in letter cost. But, the postal  
3 RPW volumes by shape are used with those shape costs to determine unit cost  
4 by shape. Like costs by shape, RPW volumes are also identified on the basis of  
5 shape or operational category and have letter-shape pieces weighing more than  
6 3.5 ounces. The result is that letter-shape costs are divided by RPW letter-shape  
7 volumes to determine unit letter cost, with the letter-shape definition being  
8 roughly the same for both costs and volumes. Thus, the USPS approach  
9 matches up shape-related costs with shape-related volumes and permits rational  
10 data collection procedures.

11           Apparently, to determine the extent of the bias against letters in the In-  
12 Office Cost System (IOCS), Valpak submitted a series of questions to the USPS  
13 on this issue. The USPS responses provide ECR volumes and IOCS costs by  
14 shape and weight increment. For Saturation, those data show the following:

- 15           - Saturation Letter RPW volumes (including those over 3.5 ounces)  
16           exceed Billing Determinant Letter volumes by 7.7 percent.  
17           (VP/USPS-T16-2 and LR K-115)
- 18           - Saturation Letter IOCS costs for letter-shapes at all piece weights  
19           exceed IOCS costs for letter-shapes at or below 3.5 ounces by 6.9  
20           percent. (USPS LR K-146, provided in response to VP/USPS-13)
- 21           - RPW letter-shape volume at or below 3.5 ounces is 5.5 percent  
22           greater than total Billing Determinant volume (letters up to 3.5  
23           ounces). (USPS LR K-146, provided in response to VP/USPS-13)
- 24
- 25
- 26

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<sup>18</sup> See, e.g., Handbook F-45, p. 111ff, and Handbook F-65, pages 110ff, 113ff, and 213ff. Dr. Haldi's concern that a heavy letter may be categorized as a flat because of its piece weight is unfounded. In the USPS costing systems, shape data are based on piece dimensions or operational category, not on piece weight. The IOCS, CCS, and RCS data systems use piece weight principally to identify various subclasses (e.g., First Class vs. Priority) and not to identify shape.

1 - Saturation non-letter RPW volume is only 97.3 percent of total  
2 Billing Determinant non-letter volume. (VP/USPS-T16-2 and LR K-  
3 115)  
4

5 Thus, contrary to Dr. Haldi's contention of bias against letters, it appears  
6 that many more Billing Determinant flats are recorded as RPW letter volume than  
7 the reverse. Based on that information for IOCS costs, one might say that the  
8 Saturation letter volumes in the denominator of the unit cost calculation appear  
9 overstated and therefore Saturation letter unit cost appears understated.

10 Depending on one's bias and choice of data source, it would be easy to argue  
11 either of the following: that unit Saturation letter IOCS cost is too low relative to  
12 Saturation flats or the opposite.

13 Actually, the truth is that, either way, the per-piece IOCS cost variances  
14 appear to be very small – less than one-tenth of a cent. And, although there is  
15 some small imprecision in the estimate of IOCS letter and flat costs and RPW  
16 volumes, it really is not possible to tell whether that imprecision is biased one  
17 way or the other.

18 Moreover, with respect to the city and rural carrier cost systems that are  
19 far more important to Saturation mail costing, their volumes and attributable cost  
20 pools by shape are specifically designed to match precisely. There should be no  
21 "mismatch" problems at all for these systems. In this particular case, however,  
22 there is an exception – the matching of the new city carrier sequenced cost pool  
23 with its estimated CCS volumes. As discussed in Section III.A, there appears to  
24 be a clear bias that lowers Saturation letter cost relative to Saturation flat cost.

1           Hence, the USPS data system results should be considered reasonable  
2 and, if anything, favoring Saturation letters over flats.

3           **D.     Summary: Saturation Letter Costs Are Not Excessive**  
4           **Compared to Saturation Flat Costs**

5  
6           Dr. Haldi, apparently to support Mr. Mitchell's letter-flat rate  
7 passthrough proposal, attempts to provide reasons to believe that the unit cost  
8 difference between Saturation letters and Saturation flats is much greater than  
9 the USPS has estimated. With respect to his revised DAL volume estimate, I  
10 have demonstrated in Section II that the resulting costs from that revision provide  
11 no reason to reject the proposed USPS rates.

12           With respect to his concerns about hypothetical DAL mail processing  
13 costs being attributed to Saturation letters and a potential postal cost systems  
14 bias in favor of non-letters are also unsupported and would likely amount to very  
15 little cost difference in any case. However, his identification of the potential  
16 impact of DALs on city carrier casing and out-of-office delivery costs does  
17 indicate that both Saturation letters and flats may be attributed too much delivery  
18 cost, with Saturation flats being attributed far more than Saturation letters. Of his  
19 expressed data quality and "mismatch" concerns, this latter has the potential for  
20 substantially reducing the disparity between Saturation letter and flat unit costs.

21

1 **IV. VP WITNESS HALDI'S CAPACITY CONSTRAINT THEORY DOES NOT**  
2 **DESCRIBE THE REAL WORLD**

3 In another effort to expand the cost differential between Saturation letters  
4 and flats, Dr. Haldi has introduced a dramatically new theory regarding city  
5 carrier delivery costs. Briefly, he implies that city carrier capacity to handle  
6 Saturation mail in the lowest-cost manner (as a third bundle) is filled and, as a  
7 result, most Saturation letters and some Saturation flats must be handled in a  
8 higher-cost manner. Thus, according to Dr. Haldi, the marginal cost of city  
9 delivery for this mail is much greater than estimated through the USPS cost  
10 systems. To correct for this, he proposes that city delivery costs for Saturation  
11 letters and flats be modeled as if they *all* were handled in the higher-cost way.

12 As discussed below, Dr. Haldi's theory ignores operational realities. City  
13 carriers have considerable capacity to carry out Saturation mail as extra bundles.  
14 However, there are non-capacity-, non-flat-related reasons why more Saturation  
15 letters are not. His proposal to use modeled delivery cost at the Saturation level  
16 is completely unsupported by any facts and should be rejected.

17 **A. The Third Bundle Rule**

18 City carriers usually have only two categories of mail to deliver: (1)  
19 letters that have been DPSed by the postal plant and provided to the carriers as  
20 they leave for their route and (2) non-DPSed letters and flats that have been  
21 cased together in a vertical flat case. However, the mechanism for delivering this  
22 mail differs according to the type of delivery sections the carriers serve. When  
23 delivering to foot and park-and-loop delivery sections where the carriers walk to  
24 multiple delivery points, they carry each category of mail as a bundle while they  
25 walk, pulling mail for each delivery point from the bundles as needed. However,  
26 when delivering to other delivery sections (curbline, dismount, centralized,  
27 NDCBU), the carriers simply pull the mail from trays in their vehicle when they

1 arrive at a delivery point (or set of delivery points). In some cases, they may take  
2 trays into a set of delivery points (e.g., indoor centralized or NDCBU deliveries).  
3 Most carriers have more than one type of delivery point and more than one type  
4 of delivery section on their routes.

5 For foot and park-and-loop delivery sections, carriers may add a third  
6 bundle of “sequenced” or extra-bundle Saturation mail. Due to labor agreement  
7 rules, though, they may not be required to carry more than three bundles of mail  
8 while walking. For other delivery sections, the labor agreement specifies no  
9 constraint on the number of extra trays the carriers may use.

#### 10 **B. Dr. Haldi’s Theory**

11 When city carriers are able to avoid casing Saturation (walk-  
12 sequenced) mail and instead carry it out to the route as separate or extra  
13 bundles and trays, they avoid costs. So, “sequenced” or extra-bundle/tray mail  
14 taken out by carriers as extra bundles or extra trays has the lowest delivery cost.

15 <sup>19</sup> Because of the third-bundle rule for foot and park-and-loop delivery sections  
16 and because there may be an unknown upper limit to the number of “extra trays”  
17 a motorized carrier can access at one time, Dr. Haldi implies that the USPS has  
18 reached or is on the brink of reaching its capacity to handle Saturation mail as  
19 non-cased extra bundles on city carrier routes (pages 28-31).

20 As a consequence of this hypothetical constraint, Dr. Haldi implies that  
21 any marginal (new) Saturation mailing must be cased and thus the marginal cost  
22 of all Saturation must be the unit cased cost. Apparently, the fact that there are  
23 cased Saturation letters and flats leads him to this conclusion (page 33). Further,

---

<sup>19</sup>For purposes of the discussion, this uncased, sequenced mail will be called “extra bundle” mail although it may also be “extra tray” mail, depending upon how the city carriers handle it. The modeled city carrier delivery time for cased and DPS volume is higher than for extra-bundle/extra-tray volume. Extra-bundle volume avoids in-office carrier casing and the out-of-office delivery cost for such mail is also lower than for delivery of cased/DPS mail. Of course, DPSed letters also avoid in-office casing costs.

1 he theorizes that Saturation letters are generally not taken out as extra-bundle  
2 mail because the USPS reserves that capacity for Saturation flats.

3 According to Dr. Haldi, because of the extra-bundle capacity constraint  
4 and the USPS reservation of that capacity for Saturation flats, Saturation letters  
5 must undergo more costly carrier casing and delivery than do Saturation flats  
6 (pages 32-33). He also implies that some Saturation flats are also not accorded  
7 the low-cost extra-bundle treatment because of the capacity constraint (pages  
8 32-33). Because of this capacity constraint, he believes the postal delivery cost  
9 system does not correctly estimate Saturation letter and flat marginal costs. So,  
10 he proposes that the Commission use much-higher, modeled city carrier cased  
11 delivery costs to estimate Saturation letter and flat costs, but *only* for purposes of  
12 developing the Saturation letter-flat cost differential (pages 55-56).

13 **C. There is Real World Carrier Extra-Bundle Capacity**

14 Dr. Haldi's implications are exaggerated and unrealistic. In order  
15 for his analysis and proposed solution to be correct, there would have to be zero  
16 extra-bundle or extra-tray capacity anywhere in the system of city carrier routes  
17 and on all delivery days of the year. But that is clearly ridiculous. He does not  
18 consider how differences in delivery types affect capacity, different ways in which  
19 the USPS can expand its capacity, real evidence of capacity fill, or reasons why  
20 some Saturation mail may not be carried out as an extra bundle.

21 **(1) USPS Techniques to Expand Extra-Bundle Capacity**

22 The USPS appears to have considerable capacity to handle all mail  
23 that, in its opinion, can be most efficiently handled as extra-bundle mail:

- 24  
25 - For the curblines, centralized/cluster box, and dismount deliveries  
26 that account for over 60 percent of all city delivery points,<sup>20</sup> city

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<sup>20</sup>The further response of USPS witness Lewis to oral request from Valpak (Tr. \_\_\_\_\_) identified 55.7 percent from curblines and centralized/cluster box deliveries. The percentage of dismount deliveries was not separately provided in that response. However, if 30 percent of deliveries on

1 carriers can take out multiple extra bundles/trays. This applies to  
2 both Saturation letters and Saturation flats.

- 3
- 4 - For all deliveries, city carriers, if they have too many Saturation  
5 mailings to handle as an extra bundle on one day, may defer some  
6 of those mailings to the next day or two.<sup>21</sup>
  - 7
  - 8 - For park-and-loop and foot deliveries, city carriers can take out  
9 multiple Saturation flat mailings when they collate them into a single  
10 extra bundle. However, they may not carry many Saturation letter  
11 mailings out as extra bundles because, physically, some of them  
12 (depending upon their dimensions and weight) may be difficult to  
13 handle as extra bundles.<sup>22</sup>
  - 14

15 Thus, city carriers have substantially more capacity to handle extra  
16 bundles than recognized by Dr. Haldi.

## 17 **(2) Evidence of Capacity to Handle Extra Bundles**

18 The capacity-expanding techniques listed in the previous  
19 subsection are supported by actual data. In this case, witnesses Stevens  
20 (USPS-T-15) and Bradley (USPS-T-14) sponsor the extensive results of a survey  
21 of city carrier out-of-office time carried out in FY02 – the City Carrier Street Time  
22 Survey (CCSTS) data for use in developing Dr. Bradley’s new econometric  
23 models of city carrier delivery time. Volumes in that data include the number of  
24 extra-bundle or “sequenced” pieces delivered to each sampled route on each  
25 sampled day.

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dismount routes were considered dismount, then another 5 percent of delivery points would be included in the above, making the figure over 60 percent. (See also USPS response to VP/USPS-T30-21.)

<sup>21</sup> See USPS response to ADVO/USPS-8. There is also considerable coordination between the USPS and Saturation mailers, particularly those that mail on a regular, high frequency basis. And, some Saturation mailers accept and account for the fact that there may be not just a two-day delivery window but a three-day window for their mail, depending upon drop time and coordination arrangements.

<sup>22</sup> See, e.g., USPS response to ADVO/USPS-9.

1 With the exception of Saturation DPS letters, the USPS has consistently  
2 stated that city carriers attempt to take out all eligible Saturation mail as extra  
3 bundles or trays.<sup>23</sup> Thus, one would expect that actual data on the number of  
4 extra-bundle mailings handled by city carriers on their routes each day would  
5 provide an accurate measure of the amount of extra-bundle mailings they now  
6 carry out and their capacity to handle more.

7 Of the 32,064 route-days from 3,396 sampled routes surveyed in the  
8 CCSTS, 65.8 percent of route-days had no extra-bundle mail, suggesting that  
9 there are many days where there is no extra-bundle mail but which could be  
10 used either for a new or deferred Saturation mailing, if the latter were  
11 necessary.<sup>24</sup> Of the 34.2 percent of route-days that had extra-bundle mail, 26.1  
12 percent had only one full or a partial extra-bundle mailing while 6.3 percent had  
13 one to two such mailings. (A partial mailing means not all deliveries on the route  
14 received an extra-bundle piece.) Less than 1% of route days had three or more  
15 extra-bundle mailings.

16 Of the 3,396 CCSTS sampled routes, 87.4 percent had some extra-  
17 bundle/tray mail during the sample period.<sup>25</sup> For those routes that had some

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<sup>23</sup>See, e.g., USPS responses to ADV0/USPS-6, 7, 8, 9 and 10. By “eligible,” I mean that it would be more efficient to take that mail out as an extra bundle rather than casing it.

<sup>24</sup>The route and route-day information is based on the sample-weighted data used by Dr. Bradley, adjusted to remove the problem zip-codes that he also deleted in his analysis. An extra-bundle mailing in this data is defined as one “sequenced” piece per possible delivery on the route on a specific day. Thus one mailing means a “sequenced” piece is delivered to every delivery on the route on that day. And, if only a portion of a Saturation mailing is carried out as extra bundles or trays on a particular day, then there is something less than one extra-bundle mailing for that route-day (but not zero). See ADV0 LR-2.

<sup>25</sup>Of interest, the percentage of routes with extra-bundle mail during the sample period was also calculated. The percentages show that more dismount and curblin routes (39.0 percent of all city routes) have extra-bundle mail than do the other route types while foot and other routes (7.6

1 extra-bundle mail during the period, on average, almost 61 percent of their  
2 delivery days had no extra-bundle mail. And, for those same routes, 74.3  
3 percent averaged 0.5 or less extra-bundle pieces per delivery per day during the  
4 survey period and 95.1 percent averaged 1 or fewer extra-bundle pieces per  
5 delivery per day during the survey period.<sup>26</sup>

6 All this together means that, on average, there are many route-days when  
7 there is no extra-bundle mail and therefore a new or deferred “eligible” mailing  
8 can be accommodated very easily as an extra-bundle/tray. And, further, there  
9 are many route-days where there is only one (or a portion of one) extra-  
10 bundle/tray mailing and an additional “eligible” mailing may be either collated into  
11 the extra bundle or carried out as extra trays.

12 Thus, in the vast majority of cases, the USPS has sufficient capacity to  
13 handle additional Saturation mailings as extra bundles either through deferral,  
14 collation, or by carrying them as extra trays (rather than bundles), as long as  
15 those additional mailings have the appropriate physical characteristics. And,  
16 most importantly, in those instances where carriers case or collate Saturation  
17 mail, the postal data systems recognize that situation and record it appropriately.

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percent of all city routes) have the least amount. This is useful to know since the two former route types have more of curblines and dismount type deliveries where extra trays, not subject to the constraint, are used. In other words, it appears that Saturation mail that can be handled as an extra bundle/tray is destined more often for curblines and dismount route types than to any other route type.

<sup>26</sup> For park-and-loop routes alone, which account for 53.4 percent of all city routes, 87.3 percent had extra-bundle mail during the sample period. And, for those routes that had such mail, 63.3 percent of the delivery days had no extra-bundle mail. And, finally, 81.6 percent of those routes averaged 0.5 or less extra-bundle pieces per day during the survey period and 97.7 percent of them averaged one or less.

1           **(3) Actual Levels of DPSed, Cased and Sequenced Saturation Mail**

2           Dr. Haldi relies on the USPS estimated proportions of Saturation  
3 letters and flats that are cased or DPSed to argue that city carriers do not have  
4 sufficient extra-bundle capacity to take them out as extra bundles. For Saturation  
5 letters, he also asserts that they have been deliberately excluded from extra-  
6 bundle treatment because of the more-pressing need to take out Saturation flats  
7 as extra bundles. As noted above, he does not consider any other reasons why  
8 some Saturation letters are not handled as extra bundles or trays.

9           **Saturation Flats**

10          As Dr. Haldi has stated,<sup>27</sup> it is likely that the USPS estimate of the  
11 percentage Saturation flats on city routes that are handled as extra bundles (74.4  
12 percent) is understated. In fact, it is quite likely that virtually all Saturation flat  
13 mail is extra-bundle/tray mail.<sup>28</sup> So, it appears that Saturation flats are  
14 unaffected by the extra bundle constraint.

15          **Saturation Letters**

16          Saturation letters, however, have a different story. One major  
17 reason why fewer Saturation letters are carried out as extra bundles (compared  
18 to flats) is that the USPS tries to DPS all Saturation letters delivered to DPS  
19 zones. Even when the mailer drops the mail at the DDU, the USPS carries those  
20 DDU letters back to the plant to be DPSed.<sup>29</sup> The USPS estimated that 47.5

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<sup>27</sup> See page 19 of VP-T-2 and response to ADVO/VP-T2-4

<sup>28</sup> Based on the information from USPS LR K-67 (Casing04\_Revised.xls), it appears that all of the Saturation flat casing cost could be caused by casing just a portion of the CCS number of DALs alone.

<sup>29</sup> See USPS responses to ADVO/USPS-1-6.

1 percent of CCS Saturation (non-DAL) letters are DPSed.<sup>30</sup> However, given the  
2 revision in the number of actual Saturation non-DAL letters plus the known  
3 amount of CCS DPS (non-DAL) letters, it appears that the proportion of CCS  
4 Saturation (non-DAL) letters that are DPSed is greater – estimated at 56.5  
5 percent. This appears more consistent with postal DPS policy.

6 And, what about the remaining 43.5 percent of Saturation non-DAL letters  
7 delivered by city carriers? They are either delivered in non-DPS zones, or are  
8 not DPSed because of service requirements, or are DPS rejects that the  
9 processing facility sends down to the DDU for carriers to case. Based on the  
10 USPS original proportions, roughly half are cased and the other half are  
11 sequenced – an even lower proportion than that cited by Dr. Haldi.<sup>31</sup>

12 With respect to those that are cased, it is likely that some Saturation  
13 letters do not have the appropriate physical characteristics to make extra-bundle  
14 treatment efficient. Their relatively small dimensions and lightweight make them  
15 difficult for carriers to hold firmly in the crook of their arm, as they do with the  
16 physically larger and heavier Saturation flats. And, holding the extra letter bundle  
17 between the fingers of their hand, along with the DPS bundle, is a much more

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<sup>30</sup> The USPS estimated that the remaining Saturation non-DPS, non-DAL letters on city routes were evenly divided between cased and extra-bundle/tray mail. (FY04.ECRSat.Vols\_Revised.xls in LR K-67)

<sup>31</sup> The USPS estimate of cased letters in LR K-67 was based on the R90-1 witness Shipe walk-sequenced letter productivity. The Shipe productivity, however, has undoubtedly declined over time with the shift from using letter cases to vertical flat cases. So, while there is a lesser number of cased Saturation letters, the total casing cost is the same because the unit casing cost is much higher than the R90 productivity. See USPS-RT-\_\_ (Jeffrey Lewis) in MC95-1.

1 difficult technique.<sup>32</sup> However, the physical characteristics of letters clearly do  
2 not prevent them from being carried as extra trays in the case of curblines,  
3 dismount, and centralized delivery sections. Thus, Saturation letters, when  
4 appropriate, also benefit from the “extra-bundle/tray” cost avoidances, consistent  
5 with USPS statements on this matter.<sup>33</sup>

6 In any case, the fact that Saturation letters are not handled as extra  
7 bundles/trays as often as Dr. Haldi would like has nothing to do with the city  
8 carriers’ capacity to take out extra bundles or the presence of Saturation flat  
9 mailings, but has everything to do with the physical characteristics of Saturation  
10 letters and the USPS DPS policy.

11 **D. Dr. Haldi’s Proposed Modeled Costs Should Be Rejected**

12 Dr. Haldi’s proposed solution to his perceived capacity constraint  
13 and marginal cost estimate problem is to model Saturation letter and flat delivery  
14 costs as though city carriers cased them 100 percent of the time (pages 55-57).  
15 But, under Dr. Haldi’s capacity constraint theory, this solution assumes that, for  
16 *all* carriers on *all* routes on *all* delivery days, there is no further capacity to carry  
17 out an additional extra bundle or tray mailing – in other words, any marginal (but  
18 eligible) Saturation mailing arriving at *any* time for *any* route would have to be  
19 cased rather than carried out as an extra bundle. It assumes that, on all routes  
20 and on all days, the marginal (additional) mailing could not be collated with  
21 another, could not be deferred, and could not be carried out as an extra tray.

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<sup>32</sup> See USPS response to ADVO/USPS-9.

<sup>33</sup> See USPS response to ADVO/USPS-9.

1 This is such an extreme and radical assumption that even Dr. Haldi shies away  
2 from claiming that he believes it.<sup>34</sup>

3 Moreover, contrary to Dr. Haldi's implication, the only instances where the  
4 USPS data systems may incorrectly record the marginal cost of Saturation mail  
5 as being extra-bundle rather than cased is when the carrier is actually handling  
6 the mail as an extra-bundle/tray but has no further capacity to handle another  
7 mailing in the same manner. Given the capacity-expanding technology and the  
8 CCSTS survey data results, such an event would have to be rare.

9 Separately, Dr. Haldi has not quantified the total unit delivery costs his  
10 marginal cost proposal would produce. But, it is clear that the estimates would  
11 be very large relative to those produced by either the USPS or PRC cost  
12 methods. Interestingly, he proposes to use them only for purposes of  
13 establishing the Saturation letter-flat cost differential, which would result in a  
14 lower Saturation letter cost, but not for the density-related cost differentials that,  
15 when included in the rate structure algorithm, would increase the Saturation letter  
16 rate.

17 **E. Summary: There is No Need for Modeled Delivery Costs**

18 There is no evidence that the city carriers have come anywhere  
19 close to reaching their capacity to handle appropriate types of Saturation mail as  
20 extra bundles or extra trays. But, there is evidence that city carriers still have  
21 considerable capacity remaining to handle marginal increases in Saturation  
22 mailings.

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<sup>34</sup> See Dr. Haldi's response to ADVO/VP-T2-24.

1           Moreover, there is also evidence that even more Saturation flats are  
2 treated as extra bundles and more Saturation non-DAL letters are DPSed than  
3 the USPS estimated. And, the reason most Saturation letters are not treated as  
4 extra bundles/trays is due to the USPS DPS policy and the physical  
5 characteristics of the letters that are not DPSed. Finally, the reasons why  
6 Saturation letters are not treated as extra bundles as often as Saturation flats  
7 have nothing to do with either capacity constraints or capacity reserved only for  
8 flats.

9           Finally, Dr. Haldi's proposed solution to his capacity constraint problem is  
10 to model as cased delivery both Saturation letter and flat unit city delivery costs.  
11 This treatment assumes that there is no spare capacity anywhere in the system  
12 at any time in the system – an extreme and completely unrealistic assumption  
13 that even he cannot claim to believe. Moreover, his proposal would have the  
14 effect of radically increasing the unit delivery costs of both Saturation letters and  
15 flats, thus exaggerating the cost differential between them. And, he proposes  
16 only using the modeled costs to develop the letter-flat cost differential (and not  
17 the density-related cost differentials) – a seemingly results-oriented proposal.

18           Both Dr. Haldi's contention that city carriers are at or near their capacity to  
19 take out extra bundles and trays as well as his modeled delivery cost proposal  
20 should be rejected.

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**AUTOBIOGRAPHICAL SKETCH**

My name is Antoinette Crowder and I am a principal with Eagle Analytics LLC, an economic and financial consulting firm located in Alexandria, Virginia. I specialize in regulatory policy, economics, and finance, particular with respect to Postal Services. I have been involved in this type of consulting for over thirty-two years, twenty-seven of them with Transcomm, Inc., an economic and engineering firm. Over all that time, I have been involved in a variety of projects dealing with costing, pricing, market and demand studies, economic and financial analyses, survey design, and research on numerous regulatory and policy issues. These activities have concerned the electric power, gas, communications, and postal/publishing industries. I have prepared or assisted in preparing numerous filings at various federal and state regulatory agencies on behalf of numerous clients. In addition, I have provided overseas consulting activities, providing financial, economic and regulatory assistance to multi-national organizations, international firms, and national governments.

I have been involved in postal ratemaking and policy issues since the beginning of the R77-1 rate case. My work has included analysis of revenue requirement, cost attribution and distribution, subclass rate structure and discounts, institutional cost allocations, service-quality measurement, demand and market assessment, and mail classification issues.

1 I have testified before the Postal Rate Commission in eight proceedings  
2 and have contributed to development of other testimony presented to the  
3 Commission. In Docket R84-1, I contributed to the mail processing peak-load  
4 and second-class intra-SCF discount testimony. In Docket R87-1, I contributed  
5 to testimony on city carrier-out-of-office costs and third-class/fourth-class Bound  
6 Printed Matter drop-ship discounts, and I also prepared and presented rebuttal  
7 testimony on third-class presort discounts. In Dockets C89-3/MC89-1, I helped  
8 prepare and presented direct testimony on the proposed local saturation  
9 subclass. In Docket R90-1, I assisted in preparation of city carrier out-of-office  
10 cost and institutional cost coverage testimony and prepared and presented  
11 rebuttal testimony on third-class rates. In the R90-1 Remand, on behalf of a  
12 third-class mailer's group, I presented two pieces of rebuttal testimony in Docket  
13 R94-1 and rebuttal testimony in MC95-1. In Docket R97-1, I presented testimony  
14 in response to Presiding Officer's Notice of Inquiry No. 3 on city delivery carrier  
15 load time costs and rebuttal testimony on carrier costs and rate design issues. In  
16 Docket R2000-1, on behalf of several mailers and mailing groups, I presented  
17 testimony on city delivery carrier costs. I also presented rebuttal in that docket  
18 concerning ECR rates.

19 Over the course of my 28-year involvement in postal ratemaking matters, I  
20 have had numerous opportunities to observe postal operations and have  
21 analyzed the cost aspects of those operations. I have also become familiar with  
22 economic costing and pricing concepts, both generally and as applied to postal  
23 ratemaking.

1            My education includes a B.S. in Biology from the University of Virginia, an  
2 M.S. in Biology from George Mason University, and additional course work in  
3 economics, mathematics, and statistics.