

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

POSTAL RATE AND FEE CHANGES, 2006

Docket No. R2006-1

RESPONSES OF UNITED STATES POSTAL SERVICE WITNESS TAUFIQUE
TO INTERROGATORIES OF MAJOR MAILERS ASSOCIATION
(MMA/USPS-T32-1 THROUGH 3(A), 4 THROUGH 7(A), 7(C-D))

The United States Postal Service hereby files the responses of witness Altaf H. Taufique to the following interrogatories of Major Mailers Association: MMA/USPS-T32-1 through 3(A), 4 through 7(A), and 7(C-D), filed on June 28, 2006. The interrogatories are stated verbatim and are followed by the responses.

Subpart (B) of MMA/USPS-T32-3 has been redirected to witness Thress for response. Subpart (B) of MMA/USPS-T32-7 has been redirected to the Postal Service for an institutional for response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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

MMA/USPS-T32-1

Please refer to page 8 of your direct testimony where you discuss the proposed additional ounce rates for First Class letters and flats.

- A. Please explain why you propose different additional ounce rates for automation letters (15.5 cents) and single piece letters (20 cents) but propose the same additional ounce rate (20 cents) for both automation and single piece flats.
- B. Did you base your specific additional ounce rate proposals on any considerations, such as, for example, special studies or economic pricing principles, other than “the revenue requirements, pricing criteria, and special circumstances surrounding each rate request?” If yes, please identify such other considerations and explain how each affected your recommendations. If no, please explain why not. Please provide all documents you reviewed in formulating your positions on additional ounce rates.
- C. Please explain your position regarding the relationship between your proposed additional ounce rates and the costs for processing additional ounces for (1) single piece letters, (2) automation letters, (3) single piece flats and (4) automation flats.

RESPONSE

- A. The Postal Service’s proposal in this docket recognizes, to a degree, the role of shape in cost causation and reflects this in the proposed rates. This recognition is consistent with the proposed reductions in additional ounce rates for both single-piece and presort mail pieces. The largest reduction in an additional ounce rate is for Automation Letters: from 23.7 cents to 15.5 cents, a reduction of 34.6 percent. My testimony discusses the specific reason for the lower additional ounce rate for Automation Letters.

(USPS-T32 at 38 and 39.):

As discussed in VI.A.2, I propose the establishment of a First-Class Mail Business Parcels rate category and a separate rate for flat-shaped pieces within the nonautomation presort rate category. These proposals reflect explicit recognition of shape as a cost-driving factor within all workshare First-Class Mail rate categories. Even if the passthroughs are less than 100 percent for shape based additional costs, explicit recognition of shapes in all rate categories relieves the

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RESPONSE to MMA/USPS-T32-1 (continued):

additional ounce rate of the burden of recovering the costs caused by differences in shapes.

Accordingly, I also am proposing to reduce the additional ounce rate for nonautomation presort automation flats and the newly proposed Business Parcels rate categories from the current 23.7 cents to 20 cents, a 15.6 percent reduction. For Automation Letters, where shape is not an issue and all of the proposed Letter dimensions (including aspect ratio and maximum weight requirement of 3.5 ounces) are met, I propose an even lower additional ounce rate of 15.5 cents. This is a 34.6 percent reduction from the current rate of 23.7 cents.

The pricing of First-Class Mail is gradually moving in the direction of recognizing shape related costs in its rates, but the additional ounce rate still serves to recover some of the shape-related costs for nonletters.

- B. Consistent with the approach to rate design in previous dockets, the additional ounce rates are proposed, in part, based on the revenue that must be generated to meet the cost coverage targets established for First-Class Mail Letters and Sealed Parcels. However, as I discuss, the Postal Service's proposal also reflects a movement to more shape-based rates. I did not rely on any special studies in formulating the proposal for additional ounce rate. The guiding principle was to reflect the recognition of shape-related costs in the rates proposed for additional ounces given all the other requirements mentioned in your query such as revenue requirement, pricing criteria and special circumstances surrounding this filing.

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RESPONSE to MMA/USPS-T32-1 (continued):

C. Again, I did not consult specific cost figures by ounce increment by shape.

See my response to subpart A regarding the rate design with respect to additional ounce rates.

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MMA/USPS-T32-2

On pages 15 and 16 of your direct testimony you discuss the Postal Service's decision to take a fresh new look at the manner in which First-Class workshare letter rates are determined. You have proposed to de-link the costs and rates for presort letters from those of single piece letters. As part of your discussion you have proposed a new objective insofar as achieving an appropriate rate design for workshare letters: to obtain similar (but not necessarily equal) unit contributions to institutional costs from an average single piece and an average presort mail piece.

- A. Does the preamble to this interrogatory correctly state your position as to the reasoning and justification for your proposed rates for First Class presort mail? If not, please explain.
- B. Please explain how you decided upon this goal of equal unit contributions to institutional costs for single piece and presort mail.
- C. When you decided to adopt this new rate design goal, did you analyze any historical data to see whether, and the extent to which, such a goal has been met in the past? If so, please provide that data. If not, why not?
- D. Please explain the logic behind the goal of equal unit contributions to institutional costs for single piece and presort mail, in the aggregate.
- E. Is this goal something that the Postal Service would strive to achieve in future rate cases?

RESPONSE

- A. Yes.
- B. The rationale for this methodology has been discussed in my testimony.

See USPS-T-32, page 15, lines 18 through 23 and page 16, lines 1 through 9. This was decided upon after consultation with Postal Service managers familiar with rate design for First-Class Mail.
- C. Yes. The attached spreadsheet provides the historical data. Between FY2000 and FY 2005 the per-unit contribution of presort mail was higher than the single-piece mail for four years, while for one year, FY2002, per-unit contribution of single-piece mail was higher and in one year, FY 2000 the unit contributions for the two mail streams were equal.
- D. Please see my response to subpart B, above.

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RESPONSE to MMA/USPS-T32-2 (continued):

E. I cannot speculate on the nature of future rate filings; however, I would expect that, if it were appropriate given the specific circumstances in a future filing, this might be one of the goals.

Attachment to Response to MMA/USPS-T32-2

	SINGLE-PIECE			PRESORT			Difference SP less Presort
	Average Revenue	Vol. Var. Cost	Per Unit Contribution	Average Revenue	Vol. Var. Cost	Per Unit Contribution	
2000	\$ 0.416	\$ 0.239	\$ 0.177	\$ 0.275	\$ 0.098	\$ 0.177	0.000
2001	\$ 0.421	\$ 0.243	\$ 0.178	\$ 0.280	\$ 0.101	\$ 0.179	(0.001)
2002	\$ 0.436	\$ 0.247	\$ 0.188	\$ 0.288	\$ 0.101	\$ 0.188	0.001
2003	\$ 0.455	\$ 0.252	\$ 0.203	\$ 0.307	\$ 0.098	\$ 0.209	(0.006)
2004	\$ 0.454	\$ 0.252	\$ 0.202	\$ 0.306	\$ 0.095	\$ 0.210	(0.009)
2005	\$ 0.453	\$ 0.264	\$ 0.189	\$ 0.305	\$ 0.101	\$ 0.203	(0.014)

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MMA/USPS-T32-3

Please refer to Question 2 of Presiding Officer's Information Request No. 5, issued June 14, 2006, page 15 of your direct testimony where you state "the Postal Service proposes that the rates for Single-Piece Letters and for Presort Letters be developed independently of each other," and page 16 of your direct testimony where you state "[a]ll of the rates for workshared First-Class Mail would be developed by reference to the CRA rollforward costs for Presort Letters, after establishing a required revenue for Presort Letters such that the unit contribution target is met."

- A. Do you agree that, since MC95-1, in which the Postal Service proposed that First-Class Workshare be classified as a separate subclass, technological advancements have changed significantly both the manner in which First Class workshared mail is prepared by the mailers and the manner in which such workshared mail is processed by the Postal Service? Please explain your answer.
- B. Do you agree that, since MC95-1, the demand characteristics for First-Class workshared mail have changed significantly due in part to increased use of the Internet as a viable, less expensive substitute for many paper transactions, including but not limited to invoice presentation, payment remittance, and delivery of financial statements? Please explain your answer.

RESPONSE

- A. The implementation of Docket No. MC95-1 involved mail preparation changes, and billing determinant information for the intervening years detail changes in presort level and the percentage of automation-rated mail. For a history of the evolution of mail processing since MC95-1, please see the testimonies of operations witnesses in the current and last three omnibus dockets.

Docket Number	Page No. - Letters	Page No. - Flats	Page No. Parcels & Bundles
R2000-1 T-10	8	14	19
R2001-1 T-39	11	17	22
R2005-1 T-29	10	17	20
R2006-1 T-42	12	21	25

- B. Redirected to Thress, USPS-T-7.

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MMA/USPS-T32-4

On page 19 of your direct testimony, you state that, in order to qualify for First-Class single piece letter rates, a letter-shaped piece of mail must weigh 3.5 ounces or less.

- A. If a letter-shaped piece of First-Class mail weighs 4.0 ounces, will it pay the flat rate or the parcel rate? Please explain your answer.
- B. Please explain precisely how the Postal Service determined that the cut-off weight for single piece letters should be 3.5 ounces and provide any studies or other documents relating to that determination.
- C. Did the Postal Service consider increasing the maximum weight for First-Class workshared letters from 3.3 ounces to 3.5 ounces? If not, why not? If so, please explain why the maximum weight for First-Class Single Piece letters should be 3.5 ounces but only 3.3 ounces for First-Class workshare letters.
- D. Please confirm that on average, First-Class single piece letters require more processing on Postal Service automated equipment than do workshared letters. If you cannot confirm, please explain.

RESPONSE

- A. The flat-size rate because the maximum weight of a letter-shaped piece would be 3.5 ounces. A 4.0 ounce letter shaped piece would pay the 4 ounce rate for a flat-shaped piece.
- B. Please refer to MMA/USPS-T42-5.
- C. Yes. Under this proposal, the maximum weight for both presort and single-piece letters is expected to be 3.5 ounces.
- D. It is my understanding that, all else equal, a single piece letter will require more processing than a workshared letter.

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MMA/USPS-T32-5

Please refer to the table shown on pages 29 and 30 of your direct testimony. There you show the unit costs to process automation letters and derive the percent pass-throughs for the rates you propose. Please explain why you didn't include delivery cost differences that the Postal Service has shown to exist in the past among the various presort levels. See, for example, R2005-1 Library Reference USPS-LR-K-67 sponsored by USPS witness Kelley.

RESPONSE

Please see my response to Presiding Officer's Information Request Number 5,

Question 2c.

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MMA/USPS-T32-6

On page 30 of your direct testimony, you describe the general means by which you determined the specific rates for First Class presort letters, encompassing five separate criteria. On pages 34-35 you state that "...the Presort categories are priced on the basis of cost causation attributes (preparation, entry profile, etc.) unrelated to Single-Piece mail." Please explain why the Postal Service does not consider consistently high originating volumes (from one mailer) as a primary and significant cost driver and, therefore, an appropriate cost causation basis to distinguish between Single-Piece mail and presorted mail. Please provide any studies or other documents that you believe support your position.

RESPONSE

My rate design does not establish presorted First-Class Mail Letter rates based on cost differentials between single-piece and presorted mail in the same way that has been done in previous dockets. Instead of using special cost studies, I use the results of the CRA to establish the overall price differences. Within the more general presort grouping, I use the more specialized cost studies to further differentiate the prices. Please see USPS-T-32, pages 12 through 17.

However, I do not use customer-specific data, including the volume of mail originating from any one customer as a cost driver for the First-Class Mail rates I am proposing. Furthermore, I am unaware of any studies that demonstrate that either higher or lower costs result based on the volume of mail originating from any one customer.

Generally, the presort structure does provide incentives for customers who have higher volumes or densities and, therefore, are able to achieve a greater depth of sort, and thus a lower price. Please see USPS-T-32, pages 31 through 33.

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MMA/USPS-T32-7

On page 16 of your direct testimony, you state the following with respect to pricing First-Class workshared mail compared to First-Class single piece:

The goal of similar unit contributions from these two mail categories is not an absolute one; other rate design and rate impact considerations may require the Postal Service and the Commission to deviate from this goal. However, to the extent practicable, the Postal Service's intention going forward is to equalize the unit contribution from the Single-Piece Letter category and from the Presort Letter category.

- A. Please confirm that under the rates you propose, the TYAR unit contributions to institutional costs from First-Class single piece and presort letter mail are \$.2348 and \$.2343, respectively. If you cannot confirm, please provide the correct unit contributions to institutional costs for First-Class single piece and presort letter mail.
- B. Please confirm that, using the Commission's attributable cost methodology, if the rates you propose are adopted the TYAR unit contributions to institutional costs from First-Class single piece and presort letter mail are estimated to be \$.2104 and \$.2294, respectively, a difference of 1.9 cents. If you cannot confirm, please provide the correct unit contributions to institutional costs for First-Class single piece and workshared mail using the Commission's attributable cost methodology.
- C. Do you agree that, using the Commission's attributable cost methodology, the specific rates you propose do not satisfy your stated objective of equal unit contributions to institutional costs for First-Class single piece and presort letters? If no, please explain your answer.
- D. Please confirm that, under the Commission's rate recommendations in R2000-1, R2001-1, and R2005-1, First-Class presort letters have on average contributed 1.7 cents, 1.9 cents, and 1.9 cents, respectively, more to institutional costs than First Class single piece letters. Derivation of these unit cost contribution differences is shown on the following table. If you cannot confirm, please provide the correct unit cost contributions and demonstrate how they are derived.

Docket No.	R2005-1	R2001-1	R2000-1
First-Class Single Piece			
Revenues (000)	20,506,695	21,865,222	22,576,889
Attributable Costs (000)	12,056,748	13,691,814	14,684,352
Contribution (000)	8,449,947	8,173,408	7,892,537
Volume (000)	42,459,296	46,841,145	52,828,895
Unit Contribution (\$)	0.199	0.174	0.149
First-Class Presorted			
Revenues (000)	15,382,831	15,915,988	13,172,716
Attributable Costs (000)	4,929,340	5,985,539	5,305,138
Contribution (000)	10,453,491	9,930,449	7,867,578
Volume (000)	47,962,523	51,353,440	47,320,291

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Unit Contribution (\$)	0.218	0.193	0.166
Presort - S.P. Unit Contrib (\$)	0.019	0.019	0.017

RESPONSE to MMA/USPS-T32-7:

- A. The revised numbers based on the changes in assumption regarding First-Class Mail Business/Presort parcels (See my response to USPS-T32-20) are:
- Single-Piece: \$ 0.2436 Presort: \$ 0.2303
- B. [Redirected to the USPS for institutional response.]
- C. Yes. However, that does not necessarily mean that the proposed rates do not meet the policy goals outlined in my testimony. As I have stated in my testimony, the goal of similar unit contribution is not an absolute one; other policy, rate design and rate impact considerations may require the Postal Service or Commission to deviate from this goal.
- D. Confirmed.