

MPA/ANM-T-2

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

Postal Rate and Fee Changes,
2006

)
)

Docket No. R2006-1

**DIRECT TESTIMONY OF SANDER A. GLICK
ON BEHALF OF
MAGAZINE PUBLISHERS OF AMERICA, INC.,
AND
ALLIANCE OF NONPROFIT MAILERS**

Please address questions about this
testimony to:

David M. Levy
Paul A. Kemnitzer
SIDLEY AUSTIN LLP
1501 K Street, N.W.
Washington, DC 20005-1401
(202) 736-8000

*Counsel for Magazine Publishers of America,
Inc., and Alliance of Nonprofit Mailers*

September 6, 2006

TABLE OF CONTENTS

	Page
I. INTRODUCTION AND SUMMARY	1
A. Qualifications And Background	1
B. Sponsoring Parties.....	2
C. Summary Of Testimony	2
II. GENERAL DESCRIPTION OF PROPOSED RATE DESIGN FOR OUTSIDE COUNTY PERIODICALS MAIL	2
A. Why We Propose To Modify Outside County Periodical Rate Design Proposed By USPS.....	2
B. Elements Of USPS Rate Design That We Accept.....	3
C. Elements of USPS Rate Design That We Propose To Change	4
1. Corrections	4
2. Rate Design Changes	5
D. Side-By-Side Comparison Of Rate Schedules Proposed By MPA-ANM vs. Current Rates	7
E. Evaluation Of Our Proposal With Regard to Incentives For Efficiency.....	9
F. The Rate Increases Produced By Our Proposal	10
III. DERIVATION OF PROPOSED RATE DESIGN AND UNDERLYING COST MODELS.....	11
A. Presort and Automation Discounts.....	12
1. Benchmark for Estimating Carrier Route Discount.....	13
2. Presort and Automation Cost Avoidance Model	16
B. Container-Related Rates and Discounts	24
1. Issues with the Proposed Container Rate	24
2. Pallet discount	25
3. 5-Digit Pallet Discount	28
C. Destination Entry Incentives.....	30

1.	Benchmark for Estimating Nontransportation Destination Entry Cost Avoidance	30
2.	Nontransportation Destination Entry Cost Avoidance Model	32
D.	Editorial Discount	34
E.	Ride-Along Rate.....	35

1 **B. Sponsoring Parties**

2 I submit the present testimony on behalf of MPA and the Alliance of
3 Nonprofit Mailers.

4 **C. Summary Of Testimony**

5 Using the rate design goals explained in the testimony of MPA/ANM
6 witness Rita D. Cohen (MPA/ANM-T-1), I propose an alternative to the rate
7 design proposed by the USPS for the Periodicals Outside County subclass. The
8 purpose of this alternative rate design is to create stronger incentives for efficient
9 mail preparation than the Postal Service's rate design would create, while
10 avoiding very large rate increases for small publications.

11 **II. GENERAL DESCRIPTION OF PROPOSED RATE DESIGN FOR**
12 **OUTSIDE COUNTY PERIODICALS MAIL**

13 **A. Why We Propose To Modify Outside County Periodical Rate**
14 **Design Proposed By USPS**

15 The Postal Service professes to accept in this case the finding of the
16 Postal Rate Commission in Docket No. C2004-1 that "progress towards a more
17 cost-based structure is both possible and necessary to increase efficiencies in
18 the Periodicals rates." 7 Tr. 1690 (Response of USPS witness Tang to
19 MPA/USPS-T35-6) (quoting Order No. 1446 at 6). The progress offered by the
20 Postal Service's actual rate design proposal in this case, however, is limited.

21 Although the USPS rate design would modestly increase worksharing
22 incentives, the percentage rate increase faced by many mailers who engage in
23 efficient practices (such as co-mailing and co-palletization) would be similar to or
24 higher than if they had not engaged in these practices at all. Major reasons for
25 this perverse result are:

- 1 • The Postal Service proposes to increase the rate difference between 5-Digit
2 Automation and Carrier Route Basic rate, a rate difference critical for
3 encouraging co-mailing, by only 4.5 percent.
- 4 • The Postal Service does propose new rate elements – a container rate and
5 destination entry rates for editorial pounds – designed to encourage
6 palletization and dropshipping. The incentives that these discounts provide,
7 however, are largely offset by the elimination of per-piece pallet and
8 experimental co-pallet discounts.
- 9 • The Postal Service continues to base its destination entry discounts on
10 understated cost avoidance estimates.

11 While MPA and ANM accept many elements of the Postal Service's
12 proposal, we propose focused changes to the rate design to create stronger
13 incentives for efficient mail preparation. At the same time, my proposed rate
14 design avoids very large rate increases for small publications, even if they do not
15 respond to the rate changes by engaging in more co-mailing and co-palletization.
16 We also propose an increase in the Ride-Along rate that is in line with the
17 subclass average (rather than the disproportionate increase proposed by USPS).

18 **B. Elements Of USPS Rate Design That We Accept**

19 Consistent with the Postal Rate Commission's recognition in Docket No.
20 C2004-1 that "it is initially the responsibility of the Postal Service to review the
21 materials provided herein and choose a path for improving the efficiency of
22 Periodicals consistent with rates that do not unreasonably impact any segment of
23 that class" (Order No. 1446, ¶ 1019, Point 3), we have accepted many aspects of
24 the Postal Service's proposed rate design.

1 These include the Postal Service's proposed revenue requirement for the
2 Periodicals Outside County subclass; almost all of the USPS-proposed rate
3 design elements, including destination entry rates for editorial pounds; the Postal
4 Service's proposal to significantly increase the discount given to editorial content;
5 and the Postal Service's desire to encourage palletization (albeit with a different
6 rate design than we propose).

7 **C. Elements of USPS Rate Design That We Propose To Change**

8 We ask the Commission to accept our proposed rate design as an
9 alternative to the Postal Service proposal. Our proposal improves on the rate
10 design presented by Witness Tang by correcting mistakes in the Postal Service's
11 spreadsheets and increasing the incentive to commingle and dropship
12 publications.

13 **1. Corrections**

14 My rate design spreadsheet (Library Reference MPA/ANM-LR-1)
15 documents all of the corrections that we have made. The most important
16 corrections relating to rate design involve the calculation of advertising pound
17 rates. Because air transportation costs for Periodicals will be nearly eliminated
18 by the Test Year, I excluded air transportation costs in calculating the proportion
19 of transportation costs that are distance-related. Responses of Waterbury and
20 Kelley to MPA/USPS-T35-21.

21 I also have corrected an intermediate step in determining the DSCF
22 advertising pound rate – subtracting the per-pound portion of the DSCF container
23 handling cost avoidance from DSCF transportation costs. In performing its
24 calculations, the Postal Service incorrectly subtracted the DSCF container

1 handling cost avoidance (net of the Destination Area Distribution Center
2 (“DADC”) container handling cost avoidance). I correctly subtract the entire per-
3 pound portion of the DSCF container handling cost avoidance in this step.¹

4 **2. Rate Design Changes**

5 I have also made focused changes in the Postal Service rate design
6 proposal to provide stronger incentives for co-mailing, co-palletization, and
7 dropshipping. The following are the most important differences between the rate
8 designs proposed by Postal Service witness Tang and by me. My proposed rate
9 design:

- 10 • Replaces the proposed container rate with a deeper pallet discount;
- 11 • Reduces automation discounts to provide additional incentive to
12 achieve Carrier Route presortation through co-mailing;
- 13 • Increases the dropship incentive by basing it on a more accurate
14 (albeit still conservative) estimate of the costs avoided by
15 dropshipping;
- 16 • Introduces a discount for pieces that are entered on 5-Digit pallets,
17 which, according to USPS witness McCrery, “most plant
18 managers...welcome”²; and

¹ In response to MPA/USPS-T35-27, USPS witness Tang suggests that my approach “may...double count” the 0.3-cent DADC container handling cost avoidance. 7 Tr. 1715. She is mistaken. Her mistake can readily be seen in USPS-LR-L-126. The advertising pound rate difference between Zones 1 & 2 and DSCF is 4.9 cents, while the cost difference is 5.2 cents (3.7 cents in distance-related transportation costs and 1.5 cents in container-handling costs).

² 11 Tr. 3038 (response of USPS witness McCrery to TW/USPS-T42-8(a)).

- 1 • Reduces the proposed Ride-Along rate so that the percentage
2 increase in this rate is in line with the subclass average.

3 At the same time, the MPA/ANM rate design seeks to ensure that these
4 changes do not result in very large rate increases for the smallest publications,
5 even if they do not respond to the rate changes by co-mailing or co-palletizing.
6 First, I propose to reduce significantly the 3-Digit presort discount (which flows
7 through to 5-Digit and Carrier Route rates) proposed by the Postal Service. This
8 change will substantially lower the Basic Presort rate, which will apply to many
9 pieces mailed by very small non-local publications.

10 As discussed by MPA-ANM witness Rita Cohen (MPA/ANM-T-1), we are
11 replacing the Postal Service's proposed container rate with a deepened pallet
12 discount. This pallet discount will provide an increased incentive (which reflects
13 more of the cost differences) for palletization. At the same time the pallet
14 discount will avoid imposing disproportionate impacts on any publications that
15 are entered in smaller-than-average sacks or alternative containers and eliminate
16 disincentives to comailing of mixed-class mail.

17 Further, to increase the incentive to co-mail, I reduced automation
18 discounts (which are based upon passthroughs greater than 100%), rather than
19 increasing the Carrier Route discount relative to nonautomation rates. While
20 increasing the incentive to co-mail, this change reduces the rate increase that
21 mailers of nonautomation flats will face.

22 Finally, to limit the rate increase in the unzoned editorial pound rate
23 resulting from the larger destination entry discounts that we propose, we shift a
24 portion of the editorial benefit from the piece rates to the pound rates. This

1 change results in a larger downward adjustment in the editorial pound rate than
2 proposed by the Postal Service.

3 **D. Side-By-Side Comparison Of Rate Schedules Proposed By**
4 **MPA-ANM vs. Current Rates**

5 Table 1 provides a side-by-side comparison of our rate proposal with
6 current (R2005-1) rates:

Table 1

**CURRENT OUTSIDE COUNTY RATES vs.
RATES PROPOSED BY MPA AND ANM**

Regular Rate	R2005-1 Rate (\$)	MPA-ANM Proposed Rate (\$)	Percent Change
Advertising Pounds			
Destinating Delivery Unit	0.167	0.184	10.18%
Destinating SCF	0.214	0.230	7.48%
Destinating ADC	0.235	0.254	8.09%
Zones 1&2	0.261	0.294	12.64%
Zone 3	0.281	0.315	12.10%
Zone 4	0.332	0.372	12.05%
Zone 5	0.410	0.458	11.71%
Zone 6	0.491	0.549	11.81%
Zone 7	0.589	0.658	11.71%
Zone 8	0.672	0.751	11.76%
Editorial Pounds			
Destinating Delivery Unit	0.203	0.148	-27.09%
Destinating SCF	0.203	0.185	-8.87%
Destinating ADC	0.203	0.204	0.49%
Editorial Pound Rate (All other Zones)	0.203	0.236	16.26%
Science of Agriculture			
Advertising Pounds			
Destinating DDU	0.125	0.138	10.40%
Destinating SCF	0.160	0.172	7.50%
Destinating ADC	0.176	0.190	7.95%
Zones 1 & 2	0.196	0.220	12.24%
Nonadvertising			
Destinating DDU	0.203	0.111	-45.32%
Destinating SCF	0.203	0.139	-31.53%
Destinating ADC	0.203	0.153	-24.63%
Zones 1 & 2	0.203	0.177	-12.81%
Presort Rate Pieces			
BASIC NON-AUTOMATION	0.393	0.446	13.49%
BASIC AUTOMATION LETTER	0.296	0.342	15.54%
BASIC AUTOMATION FLAT	0.343	0.412	20.12%
3-DIGIT NON-AUTOMATION	0.341	0.388	13.78%
3-DIGIT AUTOMATION LETTER	0.262	0.302	15.27%
3-DIGIT AUTOMATION FLAT	0.298	0.356	19.46%
5-DIGIT NON-AUTOMATION	0.270	0.307	13.70%
5-DIGIT AUTOMATION LETTER	0.206	0.238	15.53%
5-DIGIT AUTOMATION FLAT	0.238	0.284	19.33%
CARRIER ROUTE BASIC	0.172	0.210	22.09%
CARRIER ROUTE HIGH DENSITY	0.138	0.186	34.78%
CARRIER ROUTE SATURATION	0.118	0.155	31.36%
PERCENTAGE EDITORIAL DISCOUNT	(0.078)	(0.086)	10.26%
WKSHARING DISCNTDELIVERY OFFICE ENTRY	(0.019)	(0.019)	0.00%
WKSHARING DISCNT SCF ENTRY	(0.008)	(0.012)	50.00%
WKSHARING DISCNT ADC ENTRY	(0.002)	(0.007)	250.00%
WKSHARING DISCNT 5-DIGIT PALLET	N/A	(0.015)	N/A
WKSHARING DISCNT PALLET	(0.005) & (0.016)	(0.027)	N/A
RIDE-ALONG PIECE	0.131	0.146	11.45%
CONTAINER RATE	N/A	N/A	N/A

* Nonprofit and Classroom mailers pay the same rates, subject to a 5% discount on postage.
Discount is not applicable to advertising pound or Ride-Along postage

1
2
3

Table 3
Percentage Increase in Postage Incentive
to Commingle Publication

Publication	Number of Pieces/Issue	USPS	MPA
<i>Farm Collector</i>	38,036	8.6%	19.3%
<i>Gas Engine</i>	15,192	13.7%	21.7%
<i>Harper's</i>	155,472	11.8%	25.9%
<i>Herb Companion</i>	23,632	12.7%	22.4%
<i>Interweave Knits</i>	33,637	14.7%	24.2%
<i>Mother Earth News</i>	217,676	9.1%	20.2%
<i>Natural Home and Garden</i>	27,760	13.1%	25.2%

4 Source: Library Reference MPA/ANM-LR-4

5 **F. The Rate Increases Produced By Our Proposal**

6 Although our rate proposal will not produce uniform rate increases for all
7 publications, the largest increases under our proposal are dramatically less than
8 the increases the Commission was concerned about in C2004-1. Table 4 shows
9 that our proposal would produce, for the sample of 101 small publications in the
10 C2004-1 database, an average rate increase that is approximately five percent
11 above the subclass average.³ Further, none of the publications would receive
12 increases of more than 10.5 percent above the average.

³ The sample of 101 small publications in C2004-1 was randomly drawn. See Docket No. C2004-1, Order No. 1446, App. A, ¶¶ 261-263; *id.*, App. F, ¶ 3; Docket No. C2004-1, Tang Rebuttal (USPS-RT-2) at 3-4; Docket No. C2004-1, Response of USPS Witness Tang to Presiding Officer's Information Request No. 2, Item 2 (revised Oct. 28, 2004).

1
2
3
4

Table 4
Rate Increases Produced By MPA/ANM Proposal
for 101 Small Publications In C2004-1 Sample

	Increase Over R2005-1 Rates	Deviation From Average Increase For All Outside- County Periodicals
Publication In Sample With Smallest Increase	7.1%	(4.6%)
Average for All Outside- County Mail	11.7%	--
Average for 101-Publication Sample	17.1%	5.4%
Publication In Sample With Largest Increase	22.2%	10.5%

5 Source: Library Reference MPA/ANM-LR-3.

6 Further, by replacing the container rate proposed by the Postal Service
7 with a per-piece pallet discount, our rate design provides a significant incentive to
8 palletize, while eliminating the risk that some publications could be saddled with
9 much larger container-based charges. The 24-piece sack minimum rule should
10 eliminate most instances of publications entered in very small containers.
11 However, in the infrequent exceptions (e.g., if uncontainerized bundles
12 containing ten pieces are entered at a DDU), a container rate could result in
13 much larger increases. Response of USPS Witness Tang to Questions Posed
14 by Chairman Omas at the August 10 Hearing (August 17, 2006).

15

16 **III. DERIVATION OF PROPOSED RATE DESIGN AND UNDERLYING**
17 **COST MODELS.**

18 The remainder of my testimony discusses my proposed rate design and
19 the cost avoidance models that I used to develop it. My library references
20 provide further detail.

- 1 • Section III.A covers our proposed presort and automation discounts
2 and the underlying cost avoidances.
- 3 • Section III.B discusses rate design elements related to
4 containerization.
- 5 • Section III.C explains the basis of our proposed destination entry
6 discounts.
- 7 • Section III.D explains the shifting of the editorial benefit from the piece
8 side to the pound side.
- 9 • Section III.E explains why a rate increase in line with the subclass
10 average is reasonable for the Ride-Along rate.

11 MPA/ANM-LR-1 is a revised version of the Postal Service's Periodicals
12 Outside County rate design spreadsheet (USPS-LR-L-126). MPA/ANM-LR-2 is a
13 revised version of the Postal Service's flats presort cost avoidance model
14 (USPS-LR-L-43). Both library references contain a new worksheet entitled
15 "Documentation of Changes" that highlights the changes I have made.

16 **A. Presort and Automation Discounts**

17 I propose two changes to the USPS-proposed presort and automation
18 discounts: (1) reducing the proposed 3-Digit presort discount by 1.5 cents per
19 piece, and (2) reducing the proposed automation discounts by 0.5 cents per
20 piece. As mentioned earlier, the purpose of reducing the 3-Digit presort discount
21 is to moderate the financial impact on small publications of the increased
22 incentives to commingle and dropship periodicals.

1 The second proposed modification – reducing automation discounts by 0.5
2 cents – has two major benefits. First, it lowers the very large passthroughs that
3 underlie the automation discounts. Second, it provides additional incentive to co-
4 mail without pushing up the rates for nonautomation flats.

5 I have also modified the Postal Service’s methods for estimating the
6 underlying cost avoidances. These changes include the use of a different and
7 more appropriate benchmark rate category, and several adjustments to USPS
8 models and assumptions. In combination, these improvements provide a more
9 accurate accounting of these cost avoidances.

10 **1. Benchmark for Estimating Carrier Route Discount**

11 On numerous occasions, the Commission has endorsed setting
12 worksharing discounts according to the efficient component pricing (“ECP”) rule –
13 the principle that worksharing discounts should be set equal to the unit costs
14 avoided by the worksharing activity. In other words, discounts should be based
15 on a 100 percent passthrough of avoided costs.

16 As discussed by the Commission, ECP enhances efficiency because it
17 encourages mailers to workshare only if they can perform work less expensively
18 than the Postal Service. See, e.g., MC95-1 Op. & Rec. Decis. ¶ 3074. ECP also
19 promotes equity because, under this rule, worksharing neither increases nor
20 decreases the contribution that a worksharing mailer makes to institutional costs.
21 R2000-1 Op. & Rec. Decis. ¶ 5060.

22 Critical to the success of ECP is the choice of an appropriate benchmark
23 mail category from which to estimate cost avoidances and apply discounts. As
24 described by the Commission, the benchmark should represent the category of

1 mail most likely to convert to worksharing or revert from the worksharing
2 category. R2000-1 Op. & Rec. Dec. ¶ 5089. The Postal Service's benchmark for
3 estimating the Carrier Route cost avoidance does not conform to these criteria. I
4 thus propose a change so that the Carrier Route cost avoidance can be
5 calculated accurately.

6 The benchmark category of mail from which USPS calculates the Carrier
7 Route Basic cost avoidance is 5-Digit Nonautomation flats. 7 Tr. 1687
8 (Response of USPS witness Tang to MPA/USPS-T35-4(f)). Although using a
9 nonautomation rate category as the benchmark has intuitive appeal because
10 there is no requirement to barcode Carrier Route Basic flats, nonautomation flats
11 are not the category of mail most likely to convert to the Carrier Route Basic rate
12 category, or the category of mail to which Carrier Route mail is most likely to
13 revert. That category of mail is automation flats. Thus, my rate design uses 5-
14 Digit Automation flats as the benchmark from which to measure the Carrier
15 Route cost avoidance.⁴ Likewise, my rate design calculates the Carrier Route
16 rate by deducting the Carrier Route discount from the 5-Digit Automation rate.⁵
17 Below, I discuss why automation flats are the correct benchmark.

⁴ Note that even if 5-Digit Nonautomation flats is used as the benchmark, the passthrough does not significantly exceed 100%.

⁵ USPS witness Tang expresses two concerns about using 5-Digit Automation flats as the benchmark: (1) that the passthrough of the 5-Digit Automation discount is large; and (2) that Carrier Route preparation may have less value in the future. 7 Tr. 1687-88 (Response of USPS witness Tang to MPA/USPS-T35-4(f)). I deal with her first concern by reducing the 5-Digit Automation discount and passing through only 80 percent of the Carrier Route cost avoidance. I disagree that the second concern justifies limiting the Carrier Route discount in this case. Although Carrier Route presort may not have value for some locations in the future flat sequencing environment, McCrery Direct (USPS-T-42) at 22, having a large number of pieces per ZIP Code still will. 11 Tr. 2865-66 (response of USPS witness McCrery to MPA/USPS-T42-5(b)-(c)). In other words, FSS may change the *method* of preparing large mailings (e.g., from preparing these

1 Two major requirements must be fulfilled to qualify a piece for the Carrier
2 Route Basic rate. *First*, the piece must be in a bundle that includes at least six
3 pieces for the particular carrier. For publications that do lack sufficient address
4 density to generate six pieces per carrier, the primary way to achieve the
5 required density is through comailing. My understanding is that mailers of both
6 automation and nonautomation flats can and do participate in comailing.
7 *Second*, the piece must meet the following address hygiene requirement:

8 Carrier route rates require the accuracy of the carrier route codes
9 and sequence of mailpieces within the carrier route be updated
10 within 90 days of the date of mailing using a CASS certified
11 address matching software program.

12 11 Tr. 2880-81 (response of USPS witness McCrery to MPA/USPS-T42-
13 13(a)(ii)).

14 Only pieces that currently qualify for automation rates are likely to meet
15 this address hygiene requirement. Apart from an inability to place barcodes on a
16 publication (11 Tr. 2880-81 (response of USPS witness McCrery to MPA/USPS-
17 T42-13(b))), the major reason for entering a periodical at nonautomation, non-
18 carrier route rates is an inability to meet the CASS address hygiene requirement
19 for automation rates:

20 Automation rates require that the accuracy of the ZIP+4 code and
21 delivery point code information be updated within six months of the
22 date (sic) of mailing using a Coding Accuracy Support System
23 (CASS) certified address matching software program.

24 11 Tr. 2880-81 (response of USPS witness McCrery to MPA/USPS-T42-
25 13(a)(iii)).

mailings in Carrier Route bundles to preparing them in much larger 5-Digit groupings) without reducing the costs that these mailings avoid for the USPS.

1 A piece that does not meet the address hygiene requirement to qualify for
2 automation rates is also unlikely to be able to meet the higher standard to qualify
3 for carrier route rates. 11 Tr. 2880-81 (response of USPS witness McCrery to
4 MPA/USPS-T42-13(c)).

5 Recent discussions with providers of co-mail services have confirmed that
6 comailing, while an effective means of upgrading Basic and 3-Digit
7 nonautomation flats to 3-Digit and 5-Digit presort, does not upgrade these pieces
8 to carrier route for the address hygiene reason discussed above.

9 Further, automation flats are the most likely to convert to Carrier Route as
10 a matter of basic math. In FY 2005, automation flats represented more than 80%
11 of Periodicals Outside County non-carrier route pieces.

12 **2. Presort and Automation Cost Avoidance Model**

13 The Postal Service uses a hybrid method to estimate mail processing
14 costs by rate category (and thus to determine cost avoidances between rate
15 categories). With this method, the Postal Service first estimates costs by rate
16 category using an engineering mail flow model. The Postal Service then adjusts
17 the modeled costs to be consistent with Cost and Revenue Analysis (“CRA”)
18 costs through a “CRA adjustment” process.

19 While I have generally accepted the Postal Service’s model (USPS-LR-L-
20 43) for estimating these cost avoidances, I propose adjustments to both the mail
21 flow model and the CRA adjustment. I have filed a revision to the Postal

1 Service's model as MPA/ANM-LR-2.⁶ I discuss the adjustments I made to the
2 Postal Service's model below.

3 **a. Adjustments to USPS Mail Flow Model**

4 Despite the increased automation of the flat mailstream that has occurred
5 over the last few years, only 59 percent of incoming secondary distribution (i.e.,
6 sortation of flats from one or multiple 5-Digit ZIP Codes to Carrier Route) in FY
7 2005 occurred at plants. McCrery Direct (USPS-T-42) at 21. The remainder of
8 incoming secondary flat sortations occurred at delivery units, which generally
9 lack flat sorting machines. *Id.* at 20. As a result, 44.7% of incoming secondary
10 flat sorts in FY 2005 were manual. 11 Tr. 2853 (response of USPS witness
11 McCrery to MPA/USPS-T42-1(a)). While no Periodicals-specific data are
12 available, USPS witness McCrery believes that the FY 2005 figure may have
13 been even higher for Periodicals. 11 Tr. 2875 (response of USPS witness
14 McCrery to MPA/USPS-T42-9)).

15 According to USPS witness McCrery, the primary operational reason why
16 nearly fifty percent of incoming secondary sorts are manual is that "small
17 volumes of flats for a particular destination are processed manually when the
18 volume is insufficient to justify the fixed costs of setting-up and sweeping a
19 scheme for such a small volume." McCrery Direct (USPS-T-42) at 19.

20 Previous versions (through Docket No. R2001-1) of the model used to
21 estimate flats cost avoidances reflected this operational reality through the use of
22 "Incoming Secondary Machinable Flats" coverage factors. 3 Tr. 256 (response of

⁶ I have not made any changes to the Postal Service's estimates of unit delivery costs by rate category from USPS-LR-L-67.

1 USPS witness Miller to MPA/USPS-T20-1(c)). These factors sent a percentage
2 of machinable flats destined for ZIP Codes with FSMs to manual operations for
3 their incoming secondary sort.

4 Between Docket No. R2001-1 and Docket No. R2005-1, however, USPS
5 witness Miller decided to remove these factors. 3 Tr. 256 (response of USPS
6 witness Miller to MPA/USPS-T20-1(e)). Their removal has caused the cost
7 avoidance model to understate significantly the proportion of Periodicals Outside
8 County incoming secondary flats that are finalized in manual operations. In
9 contrast to McCrery's 44.7% estimate, the cost avoidance model estimates that
10 only 20% of these sorts will be manual in the Test Year. 3 Tr. 261 (Response of
11 USPS witness Miller to MPA/USPS-T20-4).

12 While the USPS cost reduction efforts described by Mr. McCrery are likely
13 to cause a decrease in the proportion of incoming secondary sorts for Periodicals
14 that are manual by the Test Year (see USPS-T-42 at 20-21), it seems unlikely
15 that the proportion will drop to less than half of the FY 2005 average for all flats.

16 The understatement of the proportion of flats that receive manual
17 incoming secondary sorts is of particular importance from a rate design
18 perspective because this value has a large effect on the estimated cost
19 avoidance between the two largest categories of Periodicals Outside County
20 mail: 5-Digit Automation and Carrier Route flats. This is because 5-Digit
21 Automation flats require incoming secondary piece sortations, while Carrier
22 Route flats generally do not.⁷

⁷ Carrier Route flats only receive incoming secondary piece sorts when the bundles containing these pieces break.

1 To model actual operations more realistically, MPA/ANM-LR-2 includes
2 “Incoming Secondary Machinable Flats” coverage factors.⁸ I have set the
3 Incoming Secondary factors to 80% machine and 20% manual. This ratio means
4 that 80% of the flats that the model flows to an FSM for incoming secondary
5 sortation will be sorted on the FSM, and the remaining 20% will instead be sorted
6 manually. Combined with other factors in the model (e.g., accept rates, coverage
7 factors), these values result in approximately 36% of incoming secondary sorts
8 for Periodicals Outside County flats being manual in the Test Year. This allows
9 for the likelihood that USPS efforts will reduce the volume of Periodicals Outside
10 County flats that are sorted manually by the Test Year, but by a more reasonable
11 magnitude than implicitly assumed by the Postal Service.

12 **b. Changes to the CRA Adjustment**

13 To tie the mail processing costs from the mail flow model back to mail
14 processing costs generated by the CRA, witness Miller (USPS-T-20 at 6)
15 performs a CRA adjustment. The first step in this process is to classify each
16 CRA cost pool as either proportional or fixed. As described by Miller (USPS-T-
17 20 at 6):

18 The proportional cost pools contain the costs for piece or bundle
19 distribution operations that have actually been modeled. The flat
20 sorting machine cost pool is an example of a proportional cost pool.
21 The fixed cost pools contain the costs for activities that have not
22 actually been modeled.

23 The second step is to develop a ratio of (1) the CRA unit cost for
24 Periodicals Outside County flats in proportional cost pools to (2) the weighted

⁸ Note that while the formulae that I use to implement these factors in MPA/ANM-LR-2 differ from the formulae used by the Postal Service in past cases, the results of the calculations are the same.

1 average modeled cost from the mail flow models. The ratio is then multiplied by
2 the modeled costs by rate category. Finally, the unit cost in the fixed CRA cost
3 pools is added to the cost for each rate category. See USPS-LR-L-43,
4 worksheet "CRA ADJ UNIT COSTS."

5 MPA/ANM-LR-2 follows this same general CRA Adjustment procedure,
6 but ties the modeled costs back to the CRA cost for all Periodicals Outside
7 County nonletters. The cost pool classifications in MPA/ANM-LR-2 also differ
8 from those in USPS-LR-L-43. These modifications are discussed below.

9 In his testimony, witness Smith (USPS-T-13) estimates that the unit mail
10 processing cost of Periodicals Outside County parcels is more than \$26. USPS-
11 T-13, Attachment 14. While he has not studied this particular anomalous result,
12 he confirms in response to an MPA interrogatory that this could "quite possibly"
13 be due to the erroneous recording of some costs of flats as parcel costs.

14 **Question** – "Do you believe that the most likely explanation of the
15 \$26 unit cost estimate for Periodicals Outside County parcels is that
16 some Periodicals 'show as flats on mailing statements and parcels
17 in [IOCS]?"

18 **Response** – "Quite possibly, but I can not say for sure."

19 Response of USPS witness Smith to MPA/USPS-T4-1.

20 The reason why this is "quite possible" is because IOCS records the costs
21 for automation flats that are more than ¾" thick as parcel costs, while RPW
22 records these pieces as flats. Smith Direct (USPS-T-13) at 34; 13 Tr. 2635-36
23 (response of USPS witness Harahush to PSA/USPS-T4-1); 13 Tr. 3629-31
24 (response of USPS witness Harahush to POIR NO. 5, Question 16(b)). Because
25 unit costs are computed by dividing the IOCS-generated costs by the RPW-
26 generated volume data, this mismatch overstates the unit cost for Periodicals

1 Outside County parcels and understates the unit cost of Periodicals Outside
2 County flats.

3 Because (according to RPW) flats comprise 99.98% of all Periodicals
4 Outside County Nonletters,⁹ the simplest way to correct for the inconsistency is
5 to use the CRA mail processing cost for all Periodicals Outside County nonletters
6 in the CRA adjustment. MPA/ANM-LR-2 includes this correction.

7 MPA/ANM-LR-2 also classifies the costs in letter, parcel, Priority Mail, and
8 Express Mail sorting cost pools as proportional. As defined by Miller, “[t]he
9 proportional cost pools contain the costs for piece or bundle distribution
10 operations that have actually been modeled.” Miller Direct (USPS-T-20) at 6. As
11 confirmed by McCrery, the costs of Periodicals Outside County flats in letter,
12 parcel, Priority Mail and Express Mail sorting cost pools arise when “the Postal
13 Service does (albeit infrequently) handle flat-shaped mail in non-flat operations”
14 and when “Postal Service clerks and mail handlers do (albeit infrequently) work
15 in operations that are different than the operation into which those employees are
16 clocked.” 11 Tr. 2885 (response of USPS witness McCrery to MPA/USPS-T42-
17 17(a)-(c)). He further confirms that costs in these pools for flats are likely
18 incurred sorting flats. 11 Tr. 2885 (Response of USPS witness McCrery to
19 MPA/USPS-T42-17(d)-(f)). Given that the activity being performed in these cost
20 pools is flat sorting, an activity that Mr. Miller has modeled, these cost pools
21 should be classified as proportional.

22 Further, even if the sorting activities in these cost pools were somehow
23 regarded as materially different than the sorting activities included in the mail flow

⁹ $8,207,322/(8,207,322+1,713)$. Source: 14 Tr. 4270-71 (attachment to response of USPS witness Smith to PSA/USPS-T13-3).

1 model, it would still be appropriate to classify these pools as proportional
2 because they achieve “the same end” as the sorting activities modeled. Miller
3 himself makes this point.

4 While mechanized sack sorting at non-BMCs is not explicitly
5 included in the mail flow models, it achieves the same end as the
6 manual sorting operation, which is explicitly included in the model
7 (typically a sortation to the 5-digit level). I am therefore relying on
8 the CRA adjustment factor to compensate for any cost differences
9 related to these processing methods.

10 3 Tr. 303 (response of USPS witness Miller to UPS/USPS-T21-1).

11 Similarly, I treat a portion of the costs in the non-MODS allied operation as
12 proportional because 37 percent of the costs in this pool are for sorting bundles.

13 10 Tr. 2747-75 (response of USPS witness Van-Ty-Smith to TW/USPS-T20-13).

14 Consistent with the Postal Service’s “piggyback” distribution approach for
15 the 1SUPPF1 cost pool – the Function 1 support cost pool – in which USPS
16 distributed the costs for this pool to subclass “in proportion to the distribution of
17 volume-variable costs of subclasses in the cost pools [it] support[s],”¹⁰
18 MPA/ANM-LR-2 distributes the costs for the 1SUPPF1 cost pool to “fixed” and
19 “proportional” in the same proportions as the distribution between “fixed” and
20 “proportional” in the supported cost pools.

21 Finally, while I, like the Postal Service, treat the 1FLATPRP (flat mail
22 preparation) cost pool as fixed, I attribute half of these costs only to non-carrier
23 route mail. This cost pool includes the cost of flat preparation activities, which
24 “consist of unloading containers, separating bundles for subsequent operations,
25 removing the packaging material, orienting, and stacking the flats in postal

¹⁰ Van-Ty-Smith Direct (USPS-T-11) at 19; 10 Tr. 2454-55 (response of USPS witness Van-Ty-Smith to MPA/USPS-T11-1).

1 containers or on ledges of distribution equipment.” McCrery Direct (USPS-T-42)
2 at 14. I propose this change because the mail processing costs in this cost pool
3 are primarily incurred for non-carrier route flats. While all flats must be prepped
4 for piece distribution, mailhandlers (whose costs are included in mail processing
5 costs) generally perform these preparation activities for non-carrier route flats
6 while carriers (whose costs are not included in mail processing costs) generally
7 perform these preparation activities for carrier route flats. 11 Tr. 2877, 2886
8 (responses of USPS witness McCrery to MPA/USPS-T42-11 and 18).¹¹

9 Because all carrier costs (including the costs for performing flat
10 preparation activities for carrier route flats) are already reflected in the unit
11 delivery costs in USPS-LR-L-67,¹² distributing exactly the same amount of the
12 mail processing costs for these activities to carrier route flats as to non-carrier
13 route flats (which the Postal Service’s treatment does) amounts to charging
14 carrier route flats twice for these activities.

15 On the other hand, it would be inappropriate not to attribute any flat
16 preparation costs to carrier route flats because these activities are sometimes
17 performed by mailhandlers. As a compromise, MPA/ANM-LR-2 attributes half of
18 the costs in this pool to all flats and the other half only to non-carrier route flats.

¹¹ While some of the flat preparation activities for carrier route flats—such as distributing bundles to carriers—are performed by clerks, most of the flat preparation costs are incurred for activities – breaking open bundles and the subsequent activities of removing the packaging material, orienting, and stacking the flats in postal containers and ledges of distribution equipment – that carriers perform for carrier route flats (in the absence of bundle breakage). 11 Tr. 2886 (response of USPS witness McCrery to MPA/USPS-T42-18).

¹² Response of USPS witness Kelley to MPA/USPS-T30-1.

1 **B. Container-Related Rates and Discounts**

2 I recommend two changes to the Postal Service rate design regarding
3 containerization. First, I propose to encourage palletization by expanding the
4 existing per-piece pallet discount to 2.7 cents per piece, rather than replacing it
5 with a container rate. I also recommend an additional 1.5-cent discount for
6 pieces entered on 5-Digit pallets. This reflects the cost savings from avoiding a
7 bundle sort.

8 Below, I discuss specific issues with the Postal Service-proposed
9 container rate. I then describe the basis for the 2.7-cent pallet discount. Finally,
10 I discuss our proposed per-piece 5-Digit pallet discount. These points are
11 discussed further in the testimony of MPA/ANM witness Cohen (MPA/ANM-T-1).

12 **1. Issues with the Proposed Container Rate**

13 In addition to the reasons discussed in Ms. Cohen's testimony and in
14 Section II.F. above, I am also concerned with the Postal Service's proposed
15 application of the container rate. The Postal Service proposes to apply the entire
16 container charge to any container with even a single piece of Periodicals Outside
17 County mail. 7 Tr. 1678-79 (response of USPS witness Tang to MPA/USPS-
18 T35-1). In most instances, this will not be problematic, because most Periodicals
19 Outside County container only contain Periodicals Outside County mail. The rule
20 may cause problems, however, in at least two circumstances.

21 First, the Postal Service expects to allow Periodicals and Standard Mail to
22 be prepared in the same containers by mid-2007. 11 Tr. 2884 (response of
23 USPS witness McCrery to MPA/USPS-T42-16). The Postal Service's application
24 of the container rate may discourage this efficiency-enhancing practice,

1 particularly when a mailer would otherwise seek to merge a small volume of
2 Periodicals with a large volume of Standard Mail pieces.

3 For example, merging 50 pieces from an existing Periodicals Outside
4 County sack onto an existing Standard Mail pallet will save the Postal Service all
5 of the sack handlings for the pieces from that sack. However, the container rate
6 postage would be unchanged, because the entire container charge will now have
7 to be paid for the (primarily Standard Mail) pallet.

8 In some instances, the Postal Service's approach could actually provide a
9 postage disincentive to comailing of mixed-class mail. What if the contents of
10 that 50-piece sack were divided onto 5 different Standard Mail pallets? In this
11 scenario, five full container charges would need be paid

12 Second, based upon Periodicals eligibility requirements, some within-
13 county publications mail some of their pieces at within-county rates and others at
14 outside-county rates. For these publications, within-county and outside-county
15 pieces are often combined in the same containers. The Postal Service's
16 approach will effectively apply the container charge to a portion of these
17 publications' within-county pieces. This seems inappropriate because within-
18 county rates (without any container charge) are designed to cover the entire
19 within-county revenue requirement.

20 **2. Pallet discount**

21 The primary goal of the proposed pallet discount is to encourage
22 publishers to shift mail from sacks onto pallets. To put this discount into context,
23 this section first explains the magnitude of costs incurred by mail that is entered

1 in sacks. Then, I discuss the per-piece cost difference between sacks and
2 pallets.

3 As estimated by the Postal Service, the cost for handling a sack at the
4 destination facility is \$1.16. USPS-LR-L-85. This cost, however, represents only
5 a portion of total sack handling costs because only a small portion (about 10-20
6 percent) of sacks are entered at the destination facility. 7 Tr. 1488-92 (response
7 of USPS witness Loetscher to MPA/USPS-T28-1).

8 The vast majority (80-90 percent) of sacks incur additional sack-handling
9 costs at “origin” and “intermediate” facilities as the sacks flow from entry point to
10 destination facility. In fact, the average sack is handled at approximately 2.2 to
11 2.4 facilities before ever reaching the destination facility.¹³ At a cost of
12 approximately 75 cents to handle a sack at a non-destination facility,¹⁴ sack
13 handling costs at non-destination facilities average about \$1.65 to \$1.80 (\$0.75
14 times 2.2 and 2.4). As table 5 shows, total sack-handling costs at both
15 destination and non-destination facilities total nearly \$3.

16 **Table 5.**
17 **Average Sack Handling Costs**

Facility Type	Lower Bound	Upper Bound
Destination	\$1.16	\$1.16
Non-Destination	\$1.65	\$1.80
Total	\$2.81	\$2.96

¹³ Institutional response of USPS to MPA/USPS-4.

¹⁴ 75 cents is the simple average of the cost of a BMC sack handling (79 cents) and an SCF sack handling (71 cents). 5 Tr. 869-70 (response of USPS witness Mayes to MPA/USPS-T25-1).

1 Furthermore, bundles of periodicals mail entered in sacks are much more
2 likely to break than bundles entered on pallets. Bundle breakage is highly costly:

3
4 Bundle integrity can have a significant impact on the productivity of
5 any bundle sorting operation. If and when a bundle breaks
6 prematurely, the value of the bundle presort can be partially or
7 completely lost, and the bundle may require distribution in a
8 residual distribution operation. Also, productivity can suffer when,
9 for example, a mailhandler attempts to capture and repair a
10 ruptured bundle within the bundle sorting operation.

11 McCrery Direct (USPS-T-42) at 26.

12 The 2.7-cent pallet discount is an appropriate discount in light of the
13 significant costs of handling periodical sacks and the significant savings offered
14 by pallets. For example, the container-handling cost difference between sacks
15 and pallets that pass through two facilities¹⁵ (an SCF and a BMC) on their way to
16 the destination facility exceeds this discount.

17 • According to the Postal Service's cost model (which assumes 45.11
18 pieces per sack), the per-piece container-handling cost difference
19 between sacked and palletized mail at the destination facility is
20 approximately 1.38 cents. USPS-LR-L-85.¹⁶

21 • Again assuming 45.11 pieces per sack, the per-piece crossdocking
22 cost difference between sacked and palletized periodicals that pass

¹⁵ The average sack is handled at 2.2 to 2.4 facilities before reaching the destination facility. Institutional Response of USPS to MPA/USPS-4.

¹⁶ Substituting 41.64 pieces per sack (the average pieces per sack figure used by Tang) into USPS-LR-L-85 produces a larger cost difference between sacks and pallets at destination facilities -- 1.59 cents per piece.

1 through a BMC and an SCF is another 1.39 cents per piece.
2 Response of USPS witness Mayes to MPA/USPS-T25-1.¹⁷

3 While I have not attempted to quantify the cost savings from improved
4 bundle integrity that McCrery describes, the presence of these additional savings
5 make the proposed 2.7 cent discount conservative.

6 **3. 5-Digit Pallet Discount**

7 My rate design also includes one new rate design element – a 5-Digit
8 pallet discount – to encourage the preparation of these efficient pallets that “most
9 plant managers would welcome.” 11 Tr. 2871-72 (response of USPS witness
10 McCrery to TW/USPS-T42-8(a)). This new rate design element will be both
11 beneficial and administratively feasible.

- 12 • The Postal Service has indicated that it could use the same
13 procedures that it uses to administer the existing per-piece pallet
14 discounts to administer a 5-Digit pallet discount. Institutional response
15 of USPS to MPA/USPS-1.
- 16 • Not only would “most plant managers...welcome” 5-Digit pallets in
17 today’s environment, this preparation will continue to be valuable in the
18 future flat sequencing environment because “[t]hese pallets will enable
19 the contents to be directly prepped and inducted into the FSS
20 operation without first sorting the contents to the appropriate FSS
21 scheme.” 11 Tr. 2865-66 (response of USPS witness McCrery to
22 MPA/USPS-T42-5(c)).

¹⁷ Assuming 41.64 pieces per sack, the crossdocking cost difference increases to 1.67 cents per piece. Calculated from USPS-LR-L-88, Appendix F.

1 I am proposing a 1.5-cent per-piece 5-Digit pallet discount based upon a
2 100% passthrough of the cost avoidance from avoiding one bundle sort (as
3 compared to pieces entered on 3-Digit pallets). 11 Tr. 2855-56 (response of
4 USPS witness McCrery to MPA/USPS-T42-3(a)-(b)). My calculations are
5 detailed in MPA/ANM-LR-1, worksheet “5-Digit Pallet.”

6 While I am proposing a 100% passthrough of this cost savings, my
7 proposal is still conservative because I have included no savings from avoided
8 container handlings. Consider, for example, the difference in how USPS handles
9 DSCF-entered, Carrier Route mail, depending on whether it is entered on 3-Digit
10 or 5-Digit pallets.¹⁸ For 5-Digit pallets, the “pallets are staged and then cross-
11 docked onto transportation to the appropriate delivery unit.”¹⁹ On the other hand,
12 container handlings are required before and after the bundle sort for Carrier
13 Route bundles on 3-Digit pallets.

14 After entry, the pallets are staged then moved to an automated,
15 mechanized, or manual bundle distribution operation where the
16 contents will be dumped and the Periodicals Outside County
17 Carrier Route bundles distributed to the appropriate delivery unit
18 containers. These containers will be staged then transferred onto
19 the appropriate delivery unit transportation.

20 11 Tr. 2855-56 (response of USPS witness McCrery to MPA/USPS-T42-3(b)).

¹⁸ This is a typical scenario because almost 90 percent of 5-Digit pallets are entered at the DSCF and almost all pieces on 5-Digit pallets are presorted to Carrier Route. Response of USPS witness Loetscher to MPA/USPS-T28-1; MPA/ANM-LR-2, worksheets “BY 2005 VOLUME – NONAUTO” and “BY 2005 VOLUM – AUTO”.

¹⁹ 11 Tr. 2855 (response of USPS witness McCrery to MPA/USPS-T42-3(a)). As noted by Mr. McCrery, there may be some instances where an additional activity – “consolidat[ing the pallet] into another container” – is required for 5-Digit pallets. 11 Tr. 2855-57 (response to MPA/USPS-T42-3).

1 These container handling costs are not insignificant. USPS-LR-L-85
2 estimates that the per-piece cost of a pallet movement is nearly 0.4 cents and the
3 per-piece cost for dumping a pallet is more than 0.5 cents.

4 **C. Destination Entry Incentives**

5 I propose increases in both the per-piece and per-pound discounts for
6 entering periodicals at destination facilities. In addition to providing stronger
7 incentives to dropship periodicals, these changes will better align these discounts
8 with the underlying costs avoided. While the Postal Service based its destination
9 entry discounts on a greater-than-100% passthrough of an understated cost
10 avoidance, I base my proposed discounts on the traditional 100% passthrough
11 (50% on the piece side/50% on the pound side) of a more accurate estimate of
12 the nontransportation destination entry cost avoidance. The remainder of this
13 section discusses the changes I have made to the Postal Service's method for
14 estimating the nontransportation destination entry cost avoidance

15 **1. Benchmark for Estimating Nontransportation**
16 **Destination Entry Cost Avoidance**

17 Consistent with past practice, the Postal Service proposes to calculate the
18 nontransportation (i.e., cross docking) costs avoided by entering Periodicals at
19 destination facilities (i.e., DADC, DSCF, and DDU) relative to non-dropshipped
20 Zones 1 & 2 Periodicals. Mayes Direct (USPS-T-25) at 7; 5 Tr. 872 (response of
21 USPS witness Mayes to MPA/USPS-T25-3). As discussed below, this choice of
22 benchmark understates the nontransportation cost savings from destination
23 entry.

1 This is because most non-dropshipped Periodicals are entered in higher
2 zones²⁰ and require more container handlings than the USPS cost avoidance
3 model assumes. Further, not only are non-destination-entered publications
4 entered in all of the zones, they “convert” to destination entry from higher zones
5 as well. For example, as Table 6 shows, participation in a co-mailing and
6 dropshipping program converts mail from higher zones to destination entry.

7 **Table 6.**
8 **Zone Distribution of *Herb Companion***

Zone	Co-mail	Solo Mailing
DDU	0.4%	0.0%
DSCF	83.2%	0.0%
DADC	13.7%	0.0%
1&2	0.3%	2.1%
3	1.4%	3.1%
4	0.2%	16.2%
5	0.1%	33.3%
6	0.1%	33.8%
7	0.0%	10.8%
8	0.7%	0.7%

9 Based upon the non-dropshipped Zones 1&2 benchmark, the USPS cost
10 avoidance methodology amounts to estimating the cost savings from entering
11 Periodicals containers at the DDU, DSCF, and DADC relative to containers
12 entered at the DBMC.²¹ As Table 7 shows, the vast majority of Zones 1-8
13 containers are entered at Origin ADCs, SCFs, and AOs. Based upon this entry

²⁰ More than 70 percent of Periodicals Outside County Zones 1-8 advertising pounds are entered in Zones 3-8. USPS-LR-L-126, R2006-1 REV 7-13-2006 LR 126 Outside County Revised.xls, worksheet, "Editorial Lb Dist."

²¹ 5 Tr. 872 (response of USPS witness Mayes to MPA/USPS-T25-3). Given that such a small percentage of containers are entered at the DBMC, the use of what amounts to a “DBMC” benchmark may even understate the costs avoided relative to Zones 1 and 2.

1 profile, Zones 1-8 containers are typically handled at one or more facilities before
2 ever reaching the DBMC (or equivalent facility). 11 Tr. 2878-79 (response of
3 USPS witness McCrery to MPA/USPS-T42-12(a)-(b)).

4
5 **Table 7.**

6
7 **Percentage of Zones 1-8 Containers by Entry Point**

8

Entry Point Type	Pallets	Sacks	Total
DBMC	2.2%	0.3%	0.4%
OBMC	1.5%	10.6%	10.5%
OADC	49.4%	46.3%	46.3%
OAO/OSCF	47.0%	42.8%	42.8%
Total	100%	100%	100%

Calculated from 7 Tr. 1488-1492 (response of USPS witness Loetscher to MPA/USPS-T28-1, Table 1). Figures may not add to exactly 100% because of independent rounding.

9 To match better the entry profile of Zones 1-8 containers, I propose
10 changing the benchmark for estimating the nontransportation destination entry
11 cost avoidance to Periodicals Outside County mail entered at Origin ADCs and
12 SCFs.

13 **2. Nontransportation Destination Entry Cost Avoidance**
14 **Model**

15 With one modification, I use the Postal Service's model (USPS-LR-L-88,
16 Appendix F) to estimate the nontransportation destination entry cost avoidance
17 from dropshipping. As mentioned above, the Postal Service's model effectively
18 estimates the cost savings from dropshipping relative to Periodicals entered at
19 destination bulk mail centers ("DBMCs"). Relative to this benchmark, the Postal

1 Service estimates that containers entered at destination SCFs (“DSCFs”) avoid
2 container handlings at 1.194 facilities and containers entered at destination Area
3 Distribution Centers (“DADCs”) avoid handlings at 0.194 facilities.

4 I, on the other hand, calculate this nontransportation destination entry cost
5 avoidance relative to Origin ADC and Origin SCF-entered containers. USPS
6 witness McCrery testifies that these containers will likely be handled once at the
7 origin SCF and possibly again at an Origin BMC before reaching the DBMC.²²
8 To be conservative, I assume that these containers are handled just once – at
9 the origin SCF – before reaching the DBMC.²³ Thus, I simply add the cost of one
10 additional SCF handling to the Postal Service’s cost avoidance estimates.
11 Table 8 shows my calculations.

²² 11 Tr. 2878-79 (response of USPS witness McCrery to MPA/USPS-T42-12(b)). Data provided in response to MPA/USPS-2 provide further support for McCrery’s estimate that OSCF and OADC-entered containers are handled once or twice before reaching the DBMC. For almost all container types, OSCF and OADC-entered containers are estimated to be handled at between 1 and 2 more facilities than the same type of container if entered at the DBMC.

²³ To illustrate how conservative this assumption is, McCrery estimates that these containers will be handled an average of approximately 1.5 times (2.5 times minus one handling at the DBMC) before arriving at the DBMC. 11 Tr. 2878-79 (response of USPS witness McCrery to MPA/USPS-T42-12(b)).

1
2
3

Table 8.

**Calculation of Nontransportation
Destination Entry Cost Avoidance**

Entry Point	Per Piece			Per Pound		
	USPS	SCF Handling	MPA/ANM	USPS	SCF Handling	MPA/ANM
	[1]	[2]	[3]=[1]+[2]	[4]	[5]	[6]=[4]+[5]
DADC	\$0.0030	\$0.0106	\$0.0136	\$0.0065	\$0.0234	\$0.0299
DSCF	\$0.0136	\$0.0106	\$0.0242	\$0.0300	\$0.0234	\$0.0533
DDU	\$0.0274	\$0.0106	\$0.0381	\$0.0618	\$0.0234	\$0.0852

Source: USPS-LR-L-88, Appendix F, Table 6

4

D. Editorial Discount

5 In this case, the Postal Service proposes a significant increase in the
6 discount given to editorial content. The Service proposes to increase the per-
7 piece editorial discount by 14.1 percent (from 7.8 cents to 8.9 cents). Tang
8 Direct (USPS-T-35) at 13. It also proposes to make a 1.3-cent downward
9 adjustment to all of the editorial pound rates to mitigate the increase in the
10 unzoned editorial pound rate. *Id.* at 9.

11 MPA and ANM propose to maintain the aggregate editorial discount, but to
12 shift some of the discount from the piece side to the pound side. As discussed
13 above, we propose larger dropship discounts than does the Postal Service. This
14 is based upon a more accurate estimate of the destination entry
15 nontransportation cost avoidance.

16 These larger discounts result in a higher unzoned editorial pound rate than
17 proposed by USPS. To mitigate some of this increase, we adjust the editorial
18 pound rates downward by two cents, 0.7 cents more than the Postal Service's
19 1.3-cent downward adjustment. To maintain the aggregate editorial discount

1 proposed by the Postal Service, we propose a slightly lower per-piece editorial
2 discount (8.6 cents as compared to the Postal Service's proposed 8.9 cents).

3 **E. Ride-Along Rate**

4 The Postal Service is proposing to increase the Periodicals Ride-Along
5 rate from 13.1 cents to 15.5 cents. Its justification for this increase is that 15.5
6 cents is close to 15.2 cents, which is the Zone 8 Advertising Pound rate for a 3.3-
7 ounce piece. Tang Direct (USPS-T-35) at 14. While I understand that the Ride-
8 Along rate was originally developed using this formula, it is important to
9 recognize that the formula provides no insight into the actual cost of Ride-Along
10 pieces (or the pound rate that would be paid if these pieces could be mailed as
11 advertising) because only about 3% of Ride Along pieces are mailed to Zone 8.

12 I see no reason for a disproportionate rate increase in the Ride-Along rate
13 and thus propose increasing it by the subclass average increase. The resulting
14 rate, 14.6 cents per piece, is sufficient to cover the advertising pound rate based
15 upon a more realistic zone distribution while leaving plenty of room to cover any
16 other potential costs of Ride-Along pieces.

17 According to FY 2005 PostalOne Mailing Statement data, the average
18 weight of a Ride-Along piece in FY 2005 was only 1.45 ounces and, as shown in
19 Table 9, most Ride-Along pieces were dropshipped to the DSCF or DADC, not
20 mailed to Zone 8. See 7 Tr. 1680-82 (response of USPS witness Tang to
21 MPA/USPS-T35-2).

1
2

Table 9.

Zone Distribution of Ride-Along Pieces

Zone	Percent
DDU	0.31
DSCF	45.16
DADC	11.91
1 & 2	7.16
3	5.01
4	8.92
5	10.16
6	4.80
7	3.15
8	3.42

3 Based on this zone distribution, the per-piece pound rate for 1.45 ounces
4 of advertising is only 2.9 cents (11.7 cents less than my proposed rate). If
5 analyzed at 3.3 ounces (the maximum weight for a Ride-Along piece), the per-
6 piece advertising pound rate is still only 6.7 cents (7.9 cents less than my
7 proposed rate).²⁴

²⁴ In response to MPA/USPS-T35-11, Ms. Tang raises the following concerns about this calculation:

The table provided in my response to MPA/USPS-T35-2(b) refers to the zone distribution by piece of ride-along pieces, not zone distribution by weight. I do not think the advertising pound rate can be accurately assessed by applying the pound rate to a piece distribution based on average piece weight.

7 Tr. 1697-98. While it would be preferable to perform this calculation using a zone distribution by weight, my calculation makes clear that the Ride-Along rate far exceeds the rate that these pieces would pay if mailed at the advertising pound rate.

1 USPS witness Tang mentions ways that the addition of Ride-Along pieces
2 may increase delivery and mail processing costs in ways that additional
3 advertising pounds may not. Given how significantly my proposed Ride-Along
4 rate exceeds the per-piece advertising pound rates calculated above, I believe
5 that a 14.6-cent Ride-Along rate leaves plenty of room to cover any such costs
6 and still make a reasonable contribution.

7 Further, at least one of the issues raised by Tang is likely to be resolved
8 by the test year. She states, “[i]t is my understanding that a piece containing a
9 ride-along is more likely to use polywrap. Publications with polywrap tend to be
10 less desirable than bound publications without polywrap, since polywrap reflects
11 light and tends to make addresses difficult to read.” 7 Tr. 1699 (response of
12 USPS witness Tang to MPA/USPS-T35-12). The Postal Service appears
13 headed for a resolution of the issue by the test year, however. On August 22, the
14 Postal Service proposed a new polywrap standard in the Federal Register.
15 Notice of Proposed Rule, *New Polywrap Standards for Automation-Rate Flat-*
16 *Size Mail*, 71 Fed. Reg. 48868 (2006). The new standard was based upon
17 extensive testing:

18
19 In 2001, we ran extensive tests of flat-size mailpieces on our AFSM
20 100 machines. As a result, we added a specification for “blocking”
21 -- the chemical bonding of films to themselves -- to our polywrap
22 specifications to help prevent polywrapped pieces from sticking
23 together during processing. But this simple change did not result in
24 a noticeable improvement in the performance of polywrapped
25 mailpieces.

26
27 Therefore, we initiated a test program to more accurately define the
28 polywrap characteristics best suited to automated processing of
29 flat-size mail. We performed complete testing on over 100 types of
30 polywrap submitted by polywrap manufacturers. We then selected
31 46 films (polyethylene, polypropylene, and shrinkwrap) to test on
32 the AFSM 100. We processed 500-piece test decks and collected

1 extensive data to evaluate performance. Again, blocking was the
2 physical attribute that most influenced processing compatibility.

3 *Id.* at 48869.

4 The new standard appears likely to be in place in the test year. The
5 standard, given the extensive testing undertaken by the USPS in developing it,
6 should substantially reduce any readability problems with polywrap.