

USPS/PB-T2-5 Please refer to your testimony at page 2 and page 4 where you discuss the Efficient Component Pricing Rule (ECPR).

- a. Does ECPR provide any guidance as to which characteristics of mail should be distinguished for pricing purposes? Please explain.
- b. Does ECPR provide any guidance regarding whether there is a distinction between cost avoidance and cost difference? Please explain.
- c. Please confirm that the de-linking proposal permits the consideration of cost differences between First-Class Mail single-piece and First-Class Mail presort letters, even when such differences were not caused by presorting, per se. If you do not confirm, please explain.
- d. Which of the rate-setting factors of the Postal Reorganization Act refer to efficiency?
- e. For each rate-setting factor of the Postal Reorganization Act, Sec. 3622 (b), please indicate whether the factor supports setting of prices not necessarily consistent with efficiency goals, and explain your conclusion

RESPONSE

- a. ECPR says that rate differences should equal cost differences.
- b. The principles supporting ECPR make no distinction between cost differences and cost avoidances and, therefore it, should be applied not just to worksharing but also to other cost causative characteristics of a mail piece like shape, weight, distance-related costs, address quality, and sales channel.
- c. Confirmed.

- d. None of the nine factors of the Act explicitly reference “efficiency;” nor do any of the factors require the development of inefficient rates.
- e. Please see my response to (d) above.

USPS/PB-T2-6 Please refer to your testimony at pages 4 and 5 where you discuss ECPR and the Commission's embrace of the concept. Please confirm that setting a discount at more than the cost avoided would be an inefficient result. If you do not confirm, please explain.

RESPONSE

Confirmed that setting discounts either higher or lower than cost differences or cost avoidances leads to productive inefficiency. Also please note that costs must be properly measured for ECPR to produce its beneficial effects.

USPS/PB-T2-7 Please refer to your testimony at page 13, lines 7-17, where you discuss the exclusion of the delivery cost differences associated with DPS percentages previously provided in the letter models.

- a. Please provide a methodological approach to identifying the presort level of a letter that is rejected from a piece of letter-sorting equipment.
- b. Please provide a methodological approach for identifying the presort level(s) of letters that are not contained in the DPS bundle provided to the carrier.

RESPONSE

(a. and b.) As I explain in my testimony, delivery unit cost differences are a natural consequence of USPS witness Abdirahman's cost model so I did not have to develop a method for identifying either the presort level of a letter that is rejected from a piece of letter-sorting equipment or the presort level(s) of letters that are not contained in the DPS bundle provided to the carrier.

USPS/PB-T2-8 Please confirm that classifying cost pools as “proportional” does not, in and of itself, establish the degree to which or the way in which the costs in those cost pools vary with presort levels. If you do not confirm, please explain.

RESPONSE

Confirmed that calling a cost pool proportional (or fixed) does not make it so. As I explain in my testimony, I rely on several methods to determine whether a pool is truly proportional rather than just declaring that it is. Calling a pool proportional also does not, in and of itself, establish the degree to which or the way in which costs in proportional pools vary with presort level.

USPS/PB-T2-9 Please refer to your testimony at page 14, line 6, where you state that most of the costs in the cost pools classified as fixed “actually vary with the presort level.”

- a. Please confirm that once you have re-classified the cost pools as proportional, you performed no study to determine the degree to which any of the costs in any of the re-classified cost pools actually varied with presort level. If you do not confirm, please explain and provide the analysis demonstrating the degree to which and way in which the re-classified costs vary with presort level.
- b. If you do not confirm part a above, please provide the functional form of the equation used by you to determine the degree to which each cost pool varied with presort level.

RESPONSE

- a. As I explain in my testimony, I assume that the pools I have classified as proportional vary with presort level in the same way as those proportional pools that the Postal Service has modeled. In fact, this is the same assumption that the Postal Service makes for the three cost pools – 1OPBULK, 1OPREF, and 1POUCHNG - newly classified as proportional for automation mail in this case. Assumptions of this sort are fairly common in postal costing and are used to distribute very large amounts of costs. In mail processing cost pools, the Postal Service assumes that non-handling tallies can be distributed to class and sub-class on the basis of the direct and mixed mail tallies. Logic also supports this. For piggyback costs, the Postal Service assumes that the piggybacked costs are distributed to class and subclass in the same way as are the costs on which they

are piggybacked. I have made the same sort of assumption because it is logical and because it is clearly superior to assuming that all of these costs are fixed.

b. Not applicable.

USPS/PB-T2-10 Please refer to your Tables 4 and 5.

- a. Please confirm that, of the 38 cost pools you examined, the ratios of the single-piece letter unit cost to the automation letter unit cost range from less than 1 to over 5. If you do not confirm, please explain.
- b. Please confirm that 20 of the cost pools had a ratio of single-piece unit cost to automation letter cost of between 2 and 5. If you do not confirm, please explain.
- c. Please confirm that simple examination of these ratios does not suggest that a single ratio exists for the ratio of single-piece unit costs to automation unit costs. If you do not confirm, please explain.

RESPONSE

- a. Confirmed for Table 4. Note that Table 4 explores only the ratios in the fixed pools. Table 5 examines costs in the 13 pools classified as proportional by the Postal Service.
- b. Confirmed for Table 4. Note that Table 4 explores only the ratios in the fixed pools. Table 5 examines costs in the 13 pools classified as proportional by the Postal Service.
- c. Confirmed that different pools displayed different ratios as shown in Table 4. Note that Table 4 explores only the ratios in the fixed pools.

USPS/PB-T2-11 Please refer to your testimony at page 16, lines 11-17 and page 17, lines 1-3 where you discuss the reasons for cost differences between single-piece and automation letters.

- a. Please confirm that the proportion of single-piece letters that are forwarded or returned is lower than the proportion of presort or automation letters that are forwarded or returned. If you do not confirm, please explain.
- b. Please confirm that, as shown in the testimonies provided in support of the Negotiated Service Agreements for Capital One and other companies using First-Class Mail for advertising purposes, the costs of forwarding and returning letters are significantly more than the costs of providing mail processing service to an automation letter that is not forwarded or returned. If you do not confirm, please explain.
- c. Please confirm that, independent of the depth of presort, automation mail is more likely to be entered by large, relatively sophisticated mailers and single-piece letters is (sic) less likely to be entered by large, relatively sophisticated mailers. If you do not confirm, please explain.

RESPONSE

- a. Confirmed for FY 2004. Please see Table 2.3 of USPS LR-L-61, Final Disposition of Volume of UAA Mail by Class of Mail/Rate Category –FY 2004.
- b. Not confirmed. The NSAs do not show that Capital One and other companies use First-Class Mail for advertising purposes. Total mail processing costs for First - Class Mail letters are larger, by definition, than the total mail processing costs of forwarding and returning these letters.

- c. Large, sophisticated mailers will likely almost always enter some single-piece letter mail with their mailings. It also seems likely that large relatively sophisticated mailers are responsible for a larger percentage of the presort letter mail than of the single-piece letter mail.

USPS/PB-T2-12 Please confirm that the distribution keys you describe in your testimony at pages 19 and 20 as being used by witnesses Van-Ty Smith and Smith and Bozzo have been developed as a result of analysis. If you do not confirm, please identify how you believe those keys were developed.

RESPONSE

As a clarification, pages 17 – 20 of my testimony discuss why witness Bozzo’s attribution methods (and not distribution methods) show that cost pools are proportional. Witness Smith is not mentioned at all on pages 19 and 20, the only reference to him is on page 29. Confirmed that the distribution keys I describe on pages 19 and 20 that witness Van-Ty-Smith develops and applies have a logical, rather than an empirical basis. Given that logic is a form of analysis, they have been developed as a result of analysis, but are without empirical basis.

USPS/PB-T2-13 Please refer to your testimony at page 21, lines 12-14 where you describe the activity of sorting letters in a manual flat sorting operation and state that these costs “like all other piece handling costs, vary with the amount of worksharing performed.”

- a. Please provide an empirical basis for this statement.
- b. Please confirm that the pieces found in manual flat sorting operations may have been damaged or for some other reason, such as a floppy leading edge, rejected from letter-sorting operations. If you do not confirm, please explain.

RESPONSE

- a. Witness Abdirahman’s mail flow models show that piece handling costs for letters in letter cost pools vary with the amount of worksharing performed. This statement is a logical extension of that.
- b. Confirmed that pieces found in a manual flat sorting operation do appear there for some reason.

USPS/PB-T2-14 Please refer to your Table 6 listing the number of cost pools you consider to be anomalous.

- a. Is it your testimony that the more finely presorted a letter is, the less likely it is to wind up in an “unexpected facility”? If so, please provide the basis, empirical or otherwise for that position. If not, then please explain how and why one would divide these anomalous cost pools by presort level.
- b. Is it your testimony that the more finely presorted a letter is, the less likely it is to wind up mixed in with “unexpected shapes” or “unexpected classes”? If so, please provide the basis for that position. If not, then please explain how and why one would divide these anomalous cost pools by presort level.

RESPONSE

- a. Yes. The more finely presorted a piece is, the fewer operations it goes through; thus, it has a smaller chance of winding up in an “unexpected facility.”
- b. Yes. The more finely presorted a piece is, the fewer operations it goes through and the smaller chance it has of winding up mixed in with “unexpected shapes” or “unexpected classes.”

USPS/PB-T2-15 Please refer to your testimony at page 23 where you discuss preparation of pallets as it relates to the presort level of the mail.

- a. Please refer to lines 6-7 where you state that the “size of the mailing is generally related to the presort level of the letter trays: the larger the mailing, the greater the depth of presort.” Please confirm that the geographic dispersion of the mailing also has an effect on the depth of presort and the preparation of pallets. If you do not confirm, please explain.
- b. Please explain the difference between the operational activities associated with handling a pallet with 5-digit trays of letters and a pallet with Carrier Route trays of letters.

RESPONSE

- a. Confirmed.
- b. Assuming that the pallet with 5-digit trays has trays all of which destinate at the same ADC (a reasonable assumption because mailers make pallet separations), the mail flows for the pallet with 5-digit trays of letters and a pallet with Carrier Route trays of letters both destinating in the same 5-digit zip would be identical until the incoming secondary sort operations. At the incoming secondary sort operations Carrier Route trays will usually go into different schemes than 5-digit trays.

USPS/PB-T2-16 Please see lines 14-15 of page 23 that state, “when mailers use PostalOne! the Postal Service avoids transportation and mail processing costs.”

- a. Please explain how use of PostalOne! reduces transportation costs.
- b. Please explain how the use of PostalOne! varies by presort level.
- c. Please explain how the use of PostalOne! by varying presort level will avoid transportation cost *by presort level*.

RESPONSE

- a. In its response to MMA/USPS-T21-33 in R2005-1, which the Postal Service confirmed is still valid in this case in response to PB/USPS-T22-11, the Postal Service explained how the use of Postal One! saves costs, as follows, “[b]ecause mailers assign and separate letter trays in their production facilities, Postal service savings come from reduced tray processing, reduced tray handlings, and diversion of mail for air transportation to surface transportation.”
- b. Mailers with small amounts of mail are much more likely to make MAADC and AADC trays while mailers with more mail are more likely to make 3-Digit and 5-Digit trays. Given that PostalOne! is cost effective only for larger amounts of mail, mailers making more finely sorted trays are more likely to use PostalOne! than those making less finely sorted trays.
- c. My testimony does not discuss presort levels and avoided transportation costs.

USPS/PB-T2-17 Please refer to lines 18-19 of page 24 of your testimony where you state that “letters in 5-digit trays on pallet separations could bypass the tray sorting costs at the origin plant.” Please provide an estimate of how often this happens, and the basis of your estimate.

RESPONSE

I do not have an estimate.

USPS/PB-T2-18 Please refer to lines 5-6 of page 25 of your testimony where you state that “Originating letters in mixed AADC trays can be processed in four sort schemes and require two or three strapping and/or sleeving activities.”

- a. Please provide an estimate of how often originating letters in mixed AADC trays are processed in four sort schemes, and the source of your estimate.
- b. Please provide an estimate of how often two strapping and/or sleeving activities are required for this mail, and provide the source of your estimate.
- c. Please provide an estimate of how often three strapping and/or sleeving activities are required for this mail, and provide the source of your estimate.

RESPONSE

(a. – c.) I do not have an estimate.

USPS/PB-T2-19 Many of the examples provided in your testimony, for example on page 25, refer to the difference between mixed AADC letters and 5-digit letters.

- a. Please confirm that the cost analysis and ratesetting activities involve distinguishing among all levels of presort.
- b. Please explain how the examples provided, for example on page 25 of your testimony, would permit distinction among all of the presort levels.

RESPONSE

- a. Confirmed.
- b. I provided examples referring to the differences between mixed AADC letters and 5-digit letters for ease of exposition and to establish the general principle that costs vary by presort level. The examples show the differences between the presort level. My Library Reference provides the details of how I calculated the cost avoidances between the presort level.

USPS/PB-T2-20 Please refer to page 26, lines 22-23 of your testimony where you state that “originating letters in 5-digit trays could bypass the platform at the destinating AADC altogether.” Please provide an estimate of how often this occurs, and provide the basis for your estimate.

RESPONSE

I do not have an estimate.

USPS/PB-T2-21 Please refer to page 27, line 21 of your testimony where you state, “the costs of allied labor activities vary to some degree with presort level.” To what degree do they vary? Please provide the basis for this estimate.

RESPONSE

I do not have an estimate.

USPS/PB-T2-22 Please refer to page 28, line 9 of your testimony where you state that “it is intuitive that some miscellaneous and support operations are proportional to distribution operations.”

- a. Is it your testimony that the Commission should develop cost avoidance estimates based solely on intuition?
- b. Please specify the “some” miscellaneous and support operations.
- c. Please provide the proportional factor to which those support activities relate to distribution operations and provide the basis for that estimate.

RESPONSE

- a. The Commission should review any cost or cost avoidance estimates using the best information, data, and analysis available. More data and more analysis is always preferable, yet the Commission does approve cost methods that are not grounded in data but are grounded in logic. As an example, there is no data showing that the distribution of the cost of non-handling tallies follows the distribution of the cost of handling and non-handling tallies, yet the Commission accepts the general proposition.
- b. Please see page 28, line 15 of my testimony.
- c. I used a factor of 1 based on the attribution and distribution of these pools.

USPS/PB-T2-23 Please refer to page 29 of your testimony at lines 11-14 where you quote witness Smith as saying that “it would be better to be able to model the non-modeled activities in order to accurately relate these costs to categories.” Please confirm that you have not modeled the costs for the cost pools that you propose to shift to the “proportional” classification.

RESPONSE

I have not modeled them but I have provided multiple reasons why they are proportional.

USPS/PB-T2-24 Please refer to your testimony at page 33, lines 3-4 where you state that setting discounts appropriately induces "the optimal amount and mix of worksharing activity provided by mailers and third-party service providers."

- a. Is it your testimony that the cost estimates and rates proposed in your testimony do a superior job of "inducing the optimal amount and mix of worksharing activity provided by mailers and third-party service providers"? If not, please explain why the Commission should adopt your proposals.
- b. If your response to part a is affirmative, please describe the shifts in mail mix which will result from the impact of your proposals on mailers behavior.
- c. If you did not develop estimates of the shifted mail volumes, please explain how you developed your revenue leakage and financial impact analysis.

RESPONSE

- a. Yes.
- b. Although I have not developed quantitative estimates of the shift in mail mix that will occur as compared to after rates volumes estimated by the Postal Service, it will be small. I have proposed exactly the same 3-Digit rate as the Postal Service, my proposed 5-digit rate is .4 cents smaller than that proposed by the Service, my AADC proposed rate is .3 cents higher, and my proposed AADC rate is 1.2 cents higher.
- c. For simplicity of calculations, I assumed that the volumes would not shift or change in response to my proposed rates. Given the small differences between

my proposed rates and those of the Service, I would assume that the changes in revenue leakage would not be material.

USPS/PB-T2-25 Please refer to section IV.D of your testimony concerning cost pool classifications.

- a. Please confirm that in Docket Nos. R2000-1, R2001-1, R2005-1 and Docket No. R2006-1, the Postal Service First-Class Mail presort cards/letters cost witnesses classified cost pools as proportional if those cost pools represented tasks that were actually included in the mail flow models. If not confirmed, please explain.
- b. Please confirm that the Commission relied on the same general proportional cost pool classification methodology as the Postal Service in Docket Nos, R2000-1, R2001-1, and R2005-1. If not confirmed, please explain. (Please note that even though Docket Nos. R2001-1 and R2005-1 involved settlement agreements, the Commission did place cost models on the record that were used for final adjustments.)

RESPONSE

- a. Not confirmed. In R2006-1, it does not appear that costs are explicitly modeled for 1OPBULK, 1OPPREF, and 1POUCHNG. Nonetheless, the modeling method used implicitly distributes the costs of these activities to presort levels in exactly the same ratio as the costs for the modeled activities. This is the same approach I have used for the activities that were not explicitly modeled.
- b. I do not know what is meant by “the same general proportional cost pool classification methodology.” Even assuming the methodology is the same, it does not follow that further improvements are impossible. For example, the Service has improved its estimate by classifying three pools as proportional and then

distributing them on the basis of the modeled costs. The Commission accepts changes in cost methods if they are supported on the record.