

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268

Annual Compliance Report, 2008

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Docket No. ACR2008

INITIAL COMMENTS OF TIME WARNER INC.
ON ACR2008 IN RESPONSE TO ORDER NO. 161
(January 30, 2009)

Time Warner Inc. (Time Warner) respectfully submits these initial comments in response to Order No. 161, Notice of Filing of Annual Compliance Report by the Postal Service and Solicitation of Public Comment (issued December 31, 2008).

At the technical conference in this docket sponsored by the Commission and held at Commission Headquarters on January 26, 2009, Time Warner consultant Halstein Stralberg raised three points that he said “need to be addressed in the estimates of the FY08 cost avoidances produced by various worksharing activities for Periodicals flats, as presented in USPS FY08-3 of the ACR2008 filing” and distributed a written statement summarizing those points. Appended hereto is a copy of Mr. Stralberg’s statement, which he has revised in order to add an additional table (Table 2), which shows the passthrough percentages that result from different methodologies. In particular, Table 2 shows that the passthrough percentage for the carrier route discount was lower in FY 2008 than is indicated by the Postal Service's FY 2008 Annual Compliance Report.

Time Warner adopts Mr. Stralberg’s appended statement as its initial comments in this docket.

As in our comments on ACR2007, Time Warner wishes to express appreciation for the openness and flexibility of the process adopted by the Commission and for the openness and responsiveness of the Postal Service in addressing questions and criticisms regarding its annual compliance report.

Respectfully submitted,

s/

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ESTIMATES OF WORKSHARING RELATED COST AVOIDANCES FOR PERIODICALS FLATS IN ACR2008

The following points out issues I believe need to be addressed in the estimates of the FY08 cost avoidances produced by various worksharing activities for Periodicals flats, as presented in USPS FY08-3 of the ACR2008 filing. At the end is an alternative set of cost avoidance estimates that I believe are more consistent with the established methodology and the cost results in USPS FY08-11 and FY08-19.

ISSUES THAT NEED TO BE ADDRESSED

There appear to be at least three issues that need to be addressed regarding cost avoidances in the Outside County piece rates portion of the FY08-3 spreadsheet:

(1) In estimating the delivery cost component of the cost difference between (a) 5-digit machinable non-auto flats and (b) carrier route presorted flats, the Postal Service appears to have repeated a mistake that appeared in the ACR2007 filing and that the Commission, in its FY2007 annual compliance determination (ACD), agreed should be corrected.

According to USPS FY08-19, the delivery costs for ECR flats with basic carrier route presort are 9.058 cents per piece, versus 12.796 for Standard non-carrier route flats. The difference between these two costs, which was equal to 3.738 cents in FY08, has traditionally been used as a proxy for the delivery cost differential between carrier route and non-carrier route Periodicals flats. Unfortunately, in R2006-1, and again in the initial ACR2007 filing, the ECR basic carrier route delivery cost per piece was instead compared with the cost for all Periodicals flats. This is clearly inappropriate, given that well over half of Periodicals flats are carrier route presorted, so that the Periodicals delivery cost estimate cannot be used to represent non-carrier route flats.

In its FY2007 compliance determination the Commission, at page 76, agreed that the pre-R2006-1 methodology, based on comparing Standard regular flats with Standard Carrier route flats, should be restored. However, this has not been done in the Postal Service's ACR2008 filing.

(2) For the flats worksharing activities whose cost avoidances are measured on a per-piece basis, the Periodicals flats model in USPS FY08-11 provides estimates of both "direct" and "allied" per-piece unit costs. In ACR2007, mail processing related cost

avoidance estimates presented by the Postal Service were based on the “direct” piece costs only. The Commission determined that the decision on whether or not to include “allied” costs should be deferred until the issue could be addressed in a separate rulemaking. Nevertheless, the Postal Service appears to have included them in its ACR2008 filing.¹

“Allied” piece costs are incurred in moving flats between piece sorting operations, and from the final piece sorting operation to carriers who sequence the flats for delivery. In my R2006-1 testimony they were referred to as “weight related” piece costs. In ACR2007 the Postal Service renamed them as “allied” piece costs. But it did not include “allied” piece costs in its ACR2007 estimates of worksharing cost avoidances

In their ACR2007 comments, Time Warner and MPA argued that the allied piece costs should be included in estimates of worksharing cost savings, since they are marginal costs, and that if they are not included the cost avoidances from flats presorting would be understated. However, on page 82 of its FY2007 compliance determination the Commission said, regarding the inclusion of allied piece costs:

The appropriate treatment of allied costs in cost avoidance models is an issue that should be resolved in a more deliberative manner than is possible in the context of this docket. It is better dealt with in the context of the joint Postal Service/Postal Regulatory Commission study of Periodicals costs that section 708 of the PAEA requires.

Since I believe the allied piece costs should be included in order to account for all costs avoided by the presorting of flats, I do not object to the fact that the Postal Service now has included them. But I believe that, in view of the Commission’s FY2007 determination, the inclusion of these costs should be done transparently, with explicit agreement from the Commission.²

¹ In the FY08-11 Periodicals flats model, the piece costs per presort level and piece characteristic appear at the ‘SUMMARY’ worksheet. The “direct” costs are in cells d26:g30, and the combined “direct” and “allied” costs are in cells d11:g16.

² The labeling of these costs as “allied” has the potential to cause some confusion, since the term “allied” also is often used in postal costing terminology to refer to a much larger pool of costs, namely all platform and container or bundle handling operations performed on a given category of mail. In fact, the Standard and First Class flats models, which do not compute bundle or container unit costs, do instead distribute those much larger “allied” costs proportionately over the true piece related costs, resulting in substantially larger worksharing cost avoidance estimates.

(3) The FY08-3 estimates of cost avoidances that result from pre-barcoding machinable and non-machinable flats with MADC presort are incorrect. I have not been able to determine how the numbers presented in FY08-3 were derived. The table in the next section contains the values I believe are correct.

ALTERNATIVE ESTIMATES OF WORKSHARING COST AVOIDANCE

Table 1 below illustrates how I inferred which methodology the Postal Service must have used in deriving the cost avoidance estimates in USPS FY08-3, and presents the results I believe would be consistent with the Commission's established methodology.

The table shows the results of alternative ways to determine worksharing related cost avoidances for Outside County flats, and compares with the avoidances indicated in FY08-3. Column 1 describes the various worksharing activities and column 2 the benchmarks against which cost avoidances are measured. Column 3 shows the per-piece cost avoidance according to FY08-3. The last four columns show alternative ways to derive the cost avoidances based on the mail processing results for Periodicals in USPS FY08-11 and the delivery costs in USPS FY08-19.

Column 4 shows results identical to those from USPS FY08-3, except for the last two rows in the table, which reflect the costs avoided by pre-barcoding flats with MADC presort.³ In order to produce results identical to the Postal Service's results in all the other rows I had to:

- (1) Incorrectly and contrary to the Commission's ACR2007 determination, compute the delivery cost differential between flats with 5-digit and carrier route presort as the difference in USPS FY08-19 between: (a) all Periodicals flats and (b) ECR basic carrier route flats.
- (2) Contrary to the Commission's ACR2007 determination, include "allied" piece costs from USPS FY08-11 in the estimates of mail processing cost avoidances.

Column 5 shows the cost avoidance results obtained by using mail processing cost

³ I have not found any way to replicate the Postal Service's results for these last two cost avoidance estimates. Nor do I know why the rows containing these estimates are "hidden" in the FY08-3 Excel spreadsheet.

differences for “direct” piece costs only.

Column 6 shows the results when both direct and allied mail processing costs are used, and the delivery cost avoidance from basic carrier route presorting is determined as the FY08-19 difference between (a) regular (non-carrier route) Standard flats; and (b) ECR basic carrier route flats. I believe these results are the most accurate reflection of the marginal cost avoidances for the various worksharing activities.

Finally, Column 7 shows the results of including only “direct” mail processing costs while computing the carrier route delivery cost avoidance as in column 6. I believe this column most accurately reflects the methodology that the Commission approved in ACR2007.

Table 2 is similar to Table 1 but compares passthrough percentages (i.e., current discount divided by the FY2008 cost avoidance) for each worksharing activity, calculated according to the different methodologies described above.⁴ For example, according to FY08-3, the discount for carrier route presorted flats, relative to non-auto flats with 5-digit presort, is shown as 89%. But if the delivery cost component of the cost differential is calculated correctly, the passthrough becomes only 74% (column 6). If, however, the allied mail processing piece costs are excluded from the cost differential (column 7) the passthrough goes up to 82%.

To summarize:

Column 7 in Table 1 shows worksharing cost avoidances calculated according to the Commission’s current methodology. Column 6 shows the avoidances that most accurately reflect the marginal cost differences between the mail preparation categories that the table compares. Regarding the estimates from FY08-3, shown in Column 3, at least some of them are incorrect and should be replaced. The corresponding passthrough percentages in FY08-3 are similarly wrong and should also be replaced.

⁴ For the last two worksharing activities in Tables 1 and 2, the discounts indicated in USPS FY08-3 are also wrong, reflecting the discounts from R2006-1 rather than those currently in effect.

Table 1: Alternative Estimates of Worksharing Cost Avoidance (\$/piece) for Periodicals flats						
1	2	3	4	5	6	7
Type Worksharing	Benchmark	FY08-3	ECR basic C-Route Vs All Periodicals		ECR basic C-Route Vs Standard Non C-Route	
			Direct & Allied Piece Costs	Direct Piece Costs Only	Direct & Allied Piece Costs	Direct Piece Costs Only
Mach Nonauto ADC	Mach Nonauto MADC	\$0.046	\$0.046	\$0.035	\$0.046	\$0.035
Mach Nonauto 3-D	Mach Nonauto ADC	\$0.024	\$0.024	\$0.017	\$0.024	\$0.017
Mach Nonauto 5-D	Mach Nonauto 3-D	\$0.114	\$0.114	\$0.097	\$0.114	\$0.097
CR Basic	Mach Nonauto 5-D	\$0.124	\$0.124	\$0.109	\$0.149	\$0.134
High Density	CR Basic	\$0.027	\$0.027	\$0.027	\$0.027	\$0.027
Saturation	High Density	\$0.019	\$0.019	\$0.019	\$0.019	\$0.019
Mach Auto ADC	Mach Auto MADC	\$0.037	\$0.037	\$0.026	\$0.037	\$0.026
Mach Auto 3-D	Mach Auto ADC	\$0.023	\$0.022	\$0.015	\$0.022	\$0.015
Mach Auto 5-D	Mach Auto 3-D	\$0.104	\$0.104	\$0.086	\$0.104	\$0.086
NonMach Nonauto ADC	NonMach Nonauto MADC	\$0.125	\$0.125	\$0.111	\$0.125	\$0.111
NonMach Nonauto 3-D	NonMach Nonauto ADC	\$0.103	\$0.103	\$0.095	\$0.103	\$0.095
NonMach Nonauto 5-D	NonMach Nonauto 3-D	\$0.225	\$0.225	\$0.194	\$0.225	\$0.194
NonMach Auto ADC	NonMach Auto MADC	\$0.103	\$0.103	\$0.089	\$0.103	\$0.089
NonMach Auto 3-D	NonMach Auto ADC	\$0.074	\$0.074	\$0.065	\$0.074	\$0.065
NonMach Auto 5-D	NonMach Auto 3-D	\$0.180	\$0.180	\$0.148	\$0.180	\$0.148
Mach Auto MADC	Mach Nonauto MADC	\$0.028	\$0.032	\$0.023	\$0.032	\$0.023
Nonmach Auto MADC	Nonmach Nonauto MADC	\$0.056	\$0.104	\$0.082	\$0.104	\$0.082

Table 2: Alternative Estimates of Passthrough (Discount/Cost Avoidance) for Worksharing Activities On Periodicals Flats						
1	2	3	4	5	6	7
Type Worksharing	Benchmark	FY08-3	ECR basic C-Route Vs All Periodicals		ECR basic C-Route Vs Standard Non C-Route	
			Direct & Allied Piece Costs	Direct Piece Costs Only	Direct & Allied Piece Costs	Direct Piece Costs Only
Mach Nonauto ADC	Mach Nonauto MADC	136.1%	136.2%	180.1%	136.2%	180.1%
Mach Nonauto 3-D	Mach Nonauto ADC	97.0%	97.1%	136.7%	97.1%	136.7%
Mach Nonauto 5-D	Mach Nonauto 3-D	64.8%	64.8%	76.2%	64.8%	76.2%
CR Basic	Mach Nonauto 5-D	89.0%	88.9%	101.1%	73.9%	82.2%
High Density	CR Basic	77.5%	77.5%	77.5%	77.5%	77.5%
Saturation	High Density	96.3%	96.5%	96.5%	96.5%	96.5%
Mach Auto ADC	Mach Auto MADC	150.5%	150.7%	214.5%	150.7%	214.5%
Mach Auto 3-D	Mach Auto ADC	84.4%	84.5%	123.9%	84.5%	123.9%
Mach Auto 5-D	Mach Auto 3-D	62.7%	62.8%	75.7%	62.8%	75.7%
NonMach Nonauto ADC	NonMach Nonauto MADC	84.1%	84.1%	94.3%	84.1%	94.3%
NonMach Nonauto 3-D	NonMach Nonauto ADC	59.0%	59.0%	64.3%	59.0%	64.3%
NonMach Nonauto 5-D	NonMach Nonauto 3-D	38.3%	38.3%	44.4%	38.3%	44.4%
NonMach Auto ADC	NonMach Auto MADC	92.0%	91.9%	106.2%	91.9%	106.2%
NonMach Auto 3-D	NonMach Auto ADC	69.2%	69.2%	78.0%	69.2%	78.0%
NonMach Auto 5-D	NonMach Auto 3-D	44.4%	44.4%	54.0%	44.4%	54.0%
Mach Auto MADC	Mach Nonauto MADC	94.8%	87.1%	120.6%	87.1%	120.6%
Nonmach Auto MADC	Nonmach Nonauto MADC	53.9%	29.9%	37.9%	29.9%	37.9%