



## POSTAL REGULATORY COMMISSION

In the Matter of: )  
 )  
 RATE ADJUSTMENT DUE TO ) Docket No. R2010-4  
 EXTRAORDINARY OR )  
 EXCEPTIONAL CIRCUMSTANCES )

Hearing Room  
 Postal Regulatory Commission  
 901 New York Avenue, N.W.  
 Washington, D.C.

Volume 3  
 Thursday, August 12, 2010

The above-entitled matter came on for hearing  
 pursuant to notice, at 9:32 a.m.

## BEFORE:

HON. RUTH Y. GOLDWAY, CHAIRMAN  
 HON. TONY HAMMOND, VICE-CHAIRMAN  
 HON. DAN G. BLAIR, COMMISSIONER  
 HON. NANCI E. LANGLEY, COMMISSIONER  
 HON. MARK ACTON, COMMISSIONER

## APPEARANCES:

On behalf of the United States Postal Service:

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APPEARANCES: (cont'd.)

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On behalf of Greeting Card Association:

(No Appearance.)

On behalf of National Association of Postmasters of the United States:

(No Appearance.)

On behalf of National Association of Letter Carriers:

(No Appearance.)

On behalf of David B. Popkin:

(No Appearance.)

On Behalf of National Rural Letter Carriers Association:

(No Appearance.)

C O N T E N T S

## WITNESSES APPEARING:

Frank Neri  
James M. Kiefer

<u>WITNESSES:</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RE CROSS</u>	<u>VOIR DIRE</u>	<u>COMMISSION</u>
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1 will ask questions of these postal representatives.

2           Nevertheless, interested parties have been  
3 given the opportunity to suggest questions to the  
4 Commission, and a number of groups and entities have  
5 filed suggested questions. The Commission appreciates  
6 the effort that has gone into the preparation of these  
7 questions.

8           As previously discussed, some of these  
9 questions will be asked today while others may appear  
10 in additional Presiding Officer Information Requests  
11 that include some of the suggested questions, as well  
12 as followup questions from these hearings.

13           At this point I would like to give my  
14 colleagues an opportunity to make any opening remarks  
15 they would wish. Vice Chairman Hammond?

16           VICE CHAIRMAN HAMMOND: No thank you, Madam  
17 Chairman.

18           CHAIRMAN GOLDWAY: Commissioner Acton?

19           COMMISSIONER ACTON: Thank you, Madam  
20 Chairman. I just want to thank the witnesses for  
21 their time and testimony.

22           CHAIRMAN GOLDWAY: And Commissioner Langley?

23           COMMISSIONER LANGLEY: I have no response  
24 right now. Thanks.

25           CHAIRMAN GOLDWAY: Okay. Does any

1 participant have a procedural matter to discuss before  
2 we begin?

3 (No response.)

4 CHAIRMAN GOLDWAY: If not, our first order  
5 of business is introducing into the record certain  
6 information previously provided by the Postal Service.

7 That information was provided in the form of  
8 written responses to several questions raised during  
9 our July 2010 technical conferences and written  
10 responses to Presiding Officer Information Requests  
11 that were answered by the Postal Service as an  
12 institution.

13 (The documents referred to  
14 were marked for  
15 identification.)

16 CHAIRMAN GOLDWAY: Mr. Koetting, have you  
17 had a chance to review the packets containing these  
18 Postal Service responses to determine if they remain  
19 accurate?

20 MR. KOETTING: They were, Madam Chairman.  
21 We did take the opportunity to correct one typo. I  
22 neglected to add the final E in the word service in  
23 the header of one question. We penciled that in.

24 CHAIRMAN GOLDWAY: Thank you. Will you  
25 please provide the reporter with two copies of the

1 corrected packet? Those responses are received into  
2 evidence and are to be transcribed.

3 (The documents referred to,  
4 previously identified, were  
5 received in evidence.)

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**DOCKET NO. R2010-4**  
**INSTITUTIONAL RESPONSES TO**  
**QUESTIONS POSED AT THE TECHNICAL CONFERENCE**

**July 19, 2010 Technical Conference**

- Responses of the United States Postal Service to Informal Questions Regarding Forecasting Matters Posed At the Technical Conference, filed July 26, 2010
- Response of the United States Postal Service to Informal Question Regarding Cost Reduction Programs Posed at the Technical Conference on July 19, 2010, filed July 27, 2010

**July 27, 2010 Technical Conference**

- Response of the United States Postal Service to Informal Question Regarding Cost Reduction Programs Posed at the Technical Conference on July 27, 2010, filed August 2, 2010
- Response of the United States Postal Service to Informal Question Regarding Flats Strategy Programs Posed at the Technical Conference on July 27, 2010, filed August 3, 2010

**Response of United States Postal Service to Request for Additional  
Information  
Related to Volume Forecasting from Technical Conference on July 19, 2010**

1. **Volume-Adjustment Multipliers**

At the July 19, 2010, Technical Conference, the Postal Service was asked to document the volume-adjustment multipliers found at row 83 of sheet 'Comp. Mult' of the volume forecasting spreadsheets filed in USPS-R2010-4/8.

As explained at the conference, the purpose of the volume-adjustment multipliers is to adjust base-year volumes for factors which may have influenced only portions of the base year. If, for example, a rule which served to reduce mail volume was in effect for only the last two quarters of the base year, a volume-adjustment multiplier would be introduced by lowering the observed volume for the first two quarters of the base year based on the expected impact of such a rule. In this way, the base volume, adjusted by the volume-adjustment multiplier, would fully reflect the expected impact of such a rule going forward through the forecast period.

Almost all of the volume-adjustment multipliers used in the present case are constructed based on shifting some base-period volume between the Negotiated Service Agreement (NSA) portion of a particular mail subclass and the non-NSA mail categories of the same subclass.

The one exception to this is with respect to Market-Dominant Parcel Post volume. In this case, the volume-adjustment multiplier is included to adjust the base-year volume to account for a significant decline in this volume beginning around the time of the Postal Service's May, 2009, rate increase. The demand equation for Market-Dominant Parcel Post includes a dummy variable equal to one since the introduction of May, 2009, rates (D\_R09). This variable has an estimated coefficient of -0.445 (t-statistic of -6.897).

Over the four quarters of the base period used in this case, this variable, D\_R09, was equal to 0 in 2009Q2, had a value of (51/91) in 2009Q3, and was equal to 1 in 2009Q4 and 2010Q1. Market-Dominant Parcel Post volumes in 2009Q2 and 2009Q3 were adjusted based on what they would have been expected to be had D\_R09 had a value of 1 in each of those quarters.

The mathematics of how this is done can be explained briefly as follows.

$$(1) \text{ Actual Volume} = X * e^{(D\_R09 \text{ Value} * D\_R09 \text{ Coefficient})}$$

$$(2) \text{ Adjusted Volume} = X * e^{(1 * D\_R09 \text{ Coefficient})}$$

Re-writing (1) as a function of X and plugging it into (2), then, yields

$$(3) \text{ Adjusted Volume} = \text{Actual Volume} * [e^{(1 * D\_R09 \text{ Coefficient})} / e^{(D\_R09 \text{ Value} * D\_R09 \text{ Coefficient})}]$$

Adjustments were made separately for inter-BMC and intra-BMC market-dominant Parcel Post. The specific adjustments made are shown in the Table below.

	<u>Volume</u>	<u>Value of D_R09</u>	<u>Coefficient</u>	<u>Adjusted Volume</u>
<u>2009Q2</u>		0	-0.444522	
Inter-BMC	17.826			11.429
Intra-BMC	5.379			3.448
<u>2009Q3</u>		(51/91)	-0.444522	
Inter-BMC	9.074			7.463
Intra-BMC	8.320			6.843
<u>2009Q4</u>		1	-0.444522	
Inter-BMC	0.000			0.000
Intra-BMC	13.045			13.045
<u>2010Q1</u>		1	-0.444522	
Inter-BMC	0.000			0.000
Intra-BMC	16.712			16.712
<u>Base Year</u>				
Inter-BMC	26.900			18.892
Intra-BMC	43.455			40.048
<u>Volume-Adjustment Multipliers</u>				
Inter-BMC				0.7023
Intra-BMC				0.9216

**Response of United States Postal Service to Request for Additional  
Information  
Related to Volume Forecasting from Technical Conference on July 19, 2010**

2. Hodrick-Prescott Filters

At the July 19, 2010, Technical Conference, the Postal Service was asked to provide the spreadsheet used to apply Hodrick-Prescott filters to the macro-economic data used in the volume forecasting spreadsheets filed in USPS-R2010-4/8.

The attached spreadsheet, 1st.TC.FilteredData.xlsx, calculates Trend components for Retail Sales (STRR), Employment (EMPLOY), and Investment (INVR), using the Hodrick-Prescott filter. Note that because of the complexity of the calculations here, this spreadsheet requires Excel 2007 or a later version.

The Cyclical component of these variables is calculated by subtracting the Trend component from the unadjusted data. The cumulative negative trend variables, EMPL\_TN\_L and INVR\_TN\_L, are constructed as described at pages 9 – 11 of the document "Narrative Explanation of Econometric Demand Equations for Market Dominant Products filed with the Postal Regulatory Commission on January 20, 2010", which was filed with the Commission on July 1, 2010.

**Response of United States Postal Service to Request for Additional  
Information  
Related to Volume Forecasting from Technical Conference on July 19, 2010**

3. Workshare Equations

At the July 19, 2010, Technical Conference, the Postal Service was asked to provide a version of the 'Shares' sheet of the volume forecasting spreadsheets filed in USPS-R2010-4/8 which would allow one to update the share forecasts given changes to the worksharing discounts.

Unfortunately, in preparing this spreadsheet, it was discovered that the discounts used in constructing the volume forecasts originally filed with USPS-R2010-4/8 were the same in all three forecasts and that, moreover, these discounts were not entirely correct for any of the three forecasts. These errors have been corrected in the revised versions of USPS-R2010-4/8 and USPS-R2010-4/NP3 filed on July 26, 2010. The revised versions also allow one to update the share forecasts given changes to the worksharing discounts.

**Response of United States Postal Service to Request for Additional  
Information  
Related to Volume Forecasting from Technical Conference on July 23, 2010**

1. Lag Effects

At the technical conference on July 23, 2010, despite the fact that the same topic had been covered at the Technical Conference on July 19, 2010, a question was posed regarding the period of time over which the lagged price effects in the equation affect the forecasts. As a practical matter, a forecast through Quarter 2 of FY2012 would be sufficient to allow all of the lag effects to play out in the price variables. Technically speaking, with new rates scheduled to take effect on Sunday, January 2, 2011, there is a very small fraction of Quarter 2 of FY11 in which the "old" rates are still effective. Therefore, a minute portion of the lag effect would not show up until Quarter 3 of FY2012 but, again, as a practical matter, that can reasonably be ignored.

**Response of United States Postal Service to Request for Additional  
Information Related to Cost Reduction Programs from  
Technical Conference on July 19, 2010**

At the Technical Conference on July 19, 2010, interest was expressed in a description of the various cost reduction programs reflected in financial estimates provided by Mr. Masse for FY2011, akin to the types of descriptions provided in Docket No. R2006-1 as a part of Library Reference USPS-LR-L-49. The requested descriptions are attached to this response electronically as a pdf file (Ist.TC.Cost.Red.Prog.Descriptions).

Postal Regulatory Commission  
Submitted 7/27/2010 4:13:20 PM  
Filing ID: 69337  
Accepted 7/27/2010

**EXIGENT RATE CASE**

**Rate Adjustment Due to Extraordinary or Exceptional Circumstances**

**Docket No. R2010-4**

**EXPLANATION OF COST REDUCTIONS,  
OTHER PROGRAMS,  
AND CORPORATEWIDE ACTIVITIES**

## INTRODUCTION

This document summarizes the major programs and management initiatives expected to be active during fiscal years 2010 and 2011. It performs a similar role to the corresponding parts of Library Reference USPS-LR-L-49 in Docket No. R2006-1. The discussion of the programs and activities is organized into the three groupings briefly described below. Personnel-related and non-personnel related expenses are identified by cost component.

Cost Reduction Programs are Postal Service initiated-programs that result in cost savings. The Cost Reduction Programs are organized into two sections: cost savings programs addressing operational and other cost reductions in Section 1A, and Breakthrough Productivity Initiatives to achieve savings in addition to specific operational and other programs in Section 1B.

Other Programs add costs for initiatives related to operational and service improvement as well as security. Cost increases associated with cost reduction programs are also included. The Other Programs are identified in Section 2.

Corporatewide Activities reflect national costs initiatives affecting Headquarters and field service units. These activities are generally non-discretionary and ongoing, as opposed to programs which have a life cycle.

Each of the major programs and initiatives is subjected to an intensive review and validation by our investment review and approval process. During the formulation phase of the budget process, an additional check is performed on all major program assumptions. This step involves field and Headquarters executives who review the program savings/cost targets and resolve issues with the program managers or sponsors. These steps ensure the planning assumptions used in formulating program expectations are reasonable and accurately portray the impact a program will have on the Postal Service's financial position.

Program savings/costs reflect both new programs initiated in the current fiscal year and partial year savings/costs which carryover from the previous fiscal year.

Workhour savings/costs are estimated using the most appropriate methodology for each particular program. For major mail sortation equipment deployments, site-specific data and information concerning equipment and mail flows are used.

Feed rates, read rates, reject rates, densities, flows, etc., for the affected sortation operations are estimated to derive net workhour savings/costs.

Equipment field test data are also used in estimating program expectations.

Some types of program savings/costs are calculated using additional engineering methods studies and management's judgment from past experience. Some programs show lag times ranging from one to several months between the date

of the equipment deployment and the realization of full workhour savings/costs. Individual site savings/costs estimates are aggregated to calculate the total national program costs/savings estimate.

This means that most calculations of savings/costs takes into account local, and generally unique, conditions at each site where the program (or equipment) is going to be deployed. However, for some programs, local factors do not materially impact program expectations and average savings/costs per program (or equipment) calculations are utilized. For these programs, savings/cost projections are generally based on national averages rather than being site specific.

## **Section 1A**

### **Cost Reduction Programs**

#### **739 ADDITIONAL DELIVERY BARCODE SORTERS STACKER MODULES**

##### **(EN-61)**

This program provides 739 additional stacker modules and 1,478 supporting tray carts for existing DBCS Phase 2 – 6 machines at 110 postal processing facilities.

Each module consists of 16 additional sort bins that help expedite the distribution of letter mail by providing a greater depth-of-sort to existing letter mail processing operations, thereby reducing the number of handlings required to sort letter mail to its final destination.

#### **POSTAL AUTOMATED REDIRECTION SYSTEM (PARS) - PHASE 2 (EN-105)**

The Postal Automated Redirection System (PARS) handles Undeliverable-As-Addressed (UAA) letter mail more efficiently than today's process. The UAA mail is intercepted earlier in the sorting process, resulting in a reduction in total handlings.

The initial phase of the PARS program, Phase I, covered comprehensive implementation of the PARS program in 50 Postal Processing & Distribution Centers (P&DCs), all of our Remote Encoding Centers (RECs), and the delivery

units they serve. Additionally, scanners were deployed into Computerized Forwarding System (CFS) units, as appropriate, to allow a PARS database with nationwide coverage to be constructed immediately. Phase II of the program was implemented into 233 additional P&DCs and the delivery units they serve. Some CFS units lost their mechanized letter terminals; others were reconfigured as their automated letter mail workload was redirected to a nearby processing plant. The IMS version 4.0 incentive software, released in July/August 2007 has increased the weighted intercept and AFR finalization rates, and COA REC productivities resulting in additional workhour savings.

#### **POSTAL AUTOMATED REDIRECTION SYSTEM (PARS - 3) – LETTER INCENTIVE PROGRAM (EN-88)**

The PARS Letter Incentive Program provided a single PARS software release that was deployed in May 2009 and provided the following PARS performance improvements:

- 1.87% increase in Undeliverable-as-Addressed (UAA) intercept rate
- 12.33% increase in Advanced Forwarding Reader (AFR) intercept finalization rate
- 5.72% increase in AFR Carrier Identified Forward finalization rate
- 12.77% increase in AFR Return-to-Sender (RTS) finalization rate
- 48 images per hour increase in Remote Encoding Center (REC) keying productivity for UAA images

- 34 images per hour increase in REC keying for Change-of-Address (COA) form images
- 1.03% reduction in non-UAA mail intercepted incorrectly

Other benefits of this software release included:

- Supports Intelligent Mail Barcode (IMB) requirements by increasing the limits for Mailer Identification (ID) numbers from 6- to 9-digits
- Supports the national COA address database by consolidating multiple Computerized Forwarding Site (CFS) site-specific databases into a single national database
- Provides the capability to implement future rate changes via a loadable table instead of requiring a software release

Deployment of the software upgrade began on May 01, 2009 and ended May 18, 2009.

#### **ADVANCED FACER CANCELLER SYSTEM (AFCS) IMPROVEMENTS (EN-84)**

This program improves the performance of letter mail cancellation equipment by providing double feed detection and cancellation upgrades for all 1,086 Advanced Facer Cancellation System (AFCS) machines. The double feed detector will recognize double feeds as they occur and create a more efficient mail handling process. The inkjet printer will automate the AFCS cancellation process from the current manual method.

These enhancements will increase the efficiency of letter mail processing operations by reducing remote keying requirements, decreasing the amount of mail that has to be rehandled manually due to miscoding by the AFCS, and eliminating the manual effort required to update the AFCS machine's cancellation date stamp. Maintenance costs will also be reduced.

### **AUTOMATED LETTER MOVEMENT SYSTEM**

The Automated Letter Movement System (ALMS) will connect multiple Advanced Facer Canceller Systems (AFCS) to multiple Delivery Bar Code Sorters (DBCS). It will allow mail processed by multiple AFCS/ISSs to be routed directly to multiple DBCS/OSSs.

The ALMS will eliminate manual sweeping of the AFCS stackers and movement of mail in trays from the AFCS to downstream operations by mail handlers (LDC-17), as well as significantly reduce the manual feeding of mail into the DBCS/OSS by mail processors (LDC 11). This program will also improve customer service by increasing mail quality and reducing mail processing time through implementation of a continuous flow (from AFCS to DBCS) process.

### **DISTRIBUTION QUALITY IMPROVEMENT – PHASE 1 PROGRAM (EN-102)**

The Distribution Quality Improvement (DQI) Program is enhancing the address

recognition technology used in letter mail automation equipment. This program is encoding much of the letter mail that cannot be barcoded or can only be partially barcoded to a finer depth of code, and sorted to delivery points. Increases in acceptance and finest depth of sort rates reduce keying workhours required at Remote Encoding Centers (RECs) and manual distribution workhours at plants and delivery units. Lower RCR error rates produce workhour savings in manual distribution and carrier casing.

#### **DISTRIBUTION QUALITY IMPROVEMENT (DQI) – PHASE 2 (EN-86)**

The DQI Phase 2 Program is enhancing the address recognition technology used in letter mail automation equipment. This is the second phase of an incentive-based program that is improving Remote Computer Reader (RCR) encode rates and reducing error rates through the use of a commercially available name and address database. The following improvements are targeted under this program:

- 0.20 percentage point increase in the RCR accept rate
- 1.65 percentage point increase in RCR finest depth of sort rate
- 0.50 percentage point reduction in RCR error rates

The plan included four incremental software releases from April 2009 – August 2011.

**110 ADDITIONAL DELIVERY BARCODE SORTERS PHASE 6 (DBCS 6) AND 394 ADDITIONAL STACKER MODULES (EN-50)**

This program provides 110 new Delivery Barcode Sorter Phase 6 machines (DBCS-6) and 394 additional stacker modules for existing DBCS Phase 2 – 5 machines. The new DBCS equipment is used to increase the amount of letter mail that can be processed in automated operations. It provides additional capacity needed to increase delivery point sequenced volumes. The number of sort bins provided for each new machine is specific to the respective facility's requirements.

Each stacker module consists of 16 additional sort bins that help expedite the distribution of letter mail by providing a greater depth-of-sort and a reduction in the number of total piece handlings. The additional stacker modules increase the number of firm holdouts available during DPS operations.

**DELIVERY BAR CODE SORTER (DBCS) CENTRAL VACUUM SYSTEMS (EN-101)**

The DBCS Central Vacuum System program is installing 1,307 centralized vacuum systems to maintain 4,427 DBCS machines (Phase 2 through 5) at 480 postal facilities. Each central system consists of a heavy duty vacuum unit and a network of steel tubing connected to a group of up to four DBCSs. Debris is deposited at a central location. The central vacuum unit is mounted on heavy-duty wheels and can be easily moved and re-located within the plant. This

program will reduce the maintenance workhours required to service the DBCSs. This program will also provide parts savings due to elimination of the multiple bags and filters used in the existing portable systems and longer motor life expectations in the central vacuum systems.

#### **CENTRAL VACUUM SYSTEMS FOR PHASE 1 DELIVERY BAR CODE SORTER (DBCS) MACHINES (EN-51)**

The Central Vacuum Systems for Phase 1 Delivery Bar Code Sorter (DBCS) Machines program will install 227 centralized vacuum systems to maintain 676 existing Phase 1 DBCS machines located at 129 postal facilities. Each system consists of a heavy duty vacuum unit and a network of steel tubing connected to a group of up to four DBCSs. Debris is deposited at a central location. The central vacuum unit is mounted on heavy-duty wheels and can be easily moved and re-located within the plant. This program will reduce the maintenance workhours required to service the DBCS Phase 1 machines.

#### **DBCS 7 MACHINES**

Currently under further review. This program would provide new Delivery Barcode Sorter machines.

#### **AFSM 100 CANCELLATION UPGRADE PROGRAM (EN-87)**

This program purchased 230 AFSM 100 cancellation upgrade kits (227

operational and 3 training/support systems) that allowed cancellation of First-Class flat mail on the AFSM 100. The program reduced flat mail processing costs by significantly reducing the need to process flats on stand-alone cancellation machines or via hand cancellations.

### **FUTURE FLAT SEQUENCING SYSTEM**

This program is currently undergoing further evaluation. The Flats Sequencing System (FSS) will be used to walk sequence flat mail pieces that are to be delivered within one or more 5-digit delivery zones. The FSS machine will have 360 sortation bins and flat mail pieces will be passed through it twice, resulting in flats in walk sequence for each letter carrier.

The first 100 FSS machines are being deployed under the BOG approved FSS Phase 1 Program. This program would cover additional deployments beyond Phase 1.

### **FLAT RECOGNITION IMPROVEMENT PROGRAM (FRIP) PHASE 2 (EN-103)**

Phase 2 of the Flat Recognition Improvement Program (FRIP) will provide additional enhancements to the address recognition technology used in flat mail automation equipment. This program will improve optical character reader (OCR) accept rates and reduce OCR error rates on all AFSM 100 and UFSM

1000 equipment.

Increases in the AFSM 100 OCR accept rate will reduce keying workhours at Remote Encoding Centers, while a higher UFSM 1000 OCR accept rate will decrease UFSM 1000 keying or manual flat sorting workhours in our plants. Lower OCR error rates will produce workhour savings in manual flat sorting and carrier operations.

#### **FLATS SEQUENCING SYSTEM (FSS) RESEARCH & DEVELOPMENT ENGINEERING(EN-107)**

The Flats Sequencing System (FSS) will be used to walk sequence flat mail pieces that are to be delivered within one or more 5-digit delivery zones.

Under this R&D project, one PreProduction FSS machine will be installed in the Dulles VA P&DC. It will be a full-sized FSS that is expected to have 360 sortation bins and all of the functionality of the FSSs that subsequently will be deployed. Flat mail pieces will be passed through it twice, resulting in flats in walk sequence for each letter carrier.

Following the completion of the Postal Service's field acceptance test, a one year operational test will be conducted, frequently with live mail, with postal employees staffing the machine.

## **FLATS SEQUENCING SYSTEM (FSS) – PHASE 1 (EN-108)**

The Flats Sequencing System (FSS) will sort flat-sized mail into delivery sequence at high speeds and at a much higher productivity than today's manual process. The FSS will process flats from the AFSM 100 and UFSM 1000 mail streams along with a significant amount of carrier presorted mail that is not handled on our automation equipment today.

The production FSS machine will have 360 sortation bins and flat mail pieces will be passed through it twice, resulting in flats sorted to walk sequence for each letter carrier. The FSS Phase 1 program will deploy 100 FSS machines.

Savings are expected to result in a reduction in carrier workhours , carrier supervisor hours , and delivery unit clerk hours as a portion of our flat mail arrives at the delivery units in walk sequence order. For the portion of flats that can be processed on the FSS, the manual casing and pull-down activities will no longer be necessary.

## **FIELD MATERIAL HANDLING SYSTEMS(EN-75)**

Material Handling Systems are being deployed to support material handling operations in our plants, Bulk Mail Centers (BMCs), and Air Mail Centers (AMCs). The primary goal is to reduce LDC-17 labor hours associated with the

handling of all types of mail by providing better material handling solutions and system modifications to the facilities.

This program is being implemented through a series of individual, site-specific projects initiated by requests from the plants, or identified through proactive site staff.

### **PACKAGE RECOGNITION IMPROVEMENT PROGRAM – PRIP (EN-106)**

The Package Recognition Improvement Program (PRIP) will upgrade the address recognition capabilities of the 76 Phase 1 Automated Package Processing System (APPS) machines that have been purchased. This program will improve the efficiency of parcel and bundle sorting operations by reducing the amount of mail that requires remote keying support at the Remote Encoding Centers (RECs) that process APPS images.

The upgrades consist of three incremental software releases over a three-year period. All of the savings expected from this program are at the Remote Encode Centers. The savings are based on incremental improvements in OCR recognition capabilities for the Phase 1 APPS machines.

### **CENTRAL VACUUM SYSTEMS FOR AUTOMATED FLAT SORTING MACHINE (AFSM) 100s (EN-85)**

This program deployed centralized vacuum systems for all Automated Flat

Sorting Machine (AFSM) 100 equipment. A total of 534 centralized central vacuum systems, one for each AFSM, were purchased as replacements for the costly portable vacuums previously used. A total of 530 of the 534 systems purchased were deployed and installed. The remaining systems are being held at Topeka. Deployment began in February 2009 and was completed in November 2009.

#### **PHILADELPHIA NETWORK DISTRIBUTION CENTER (NDC) – (EN89)**

This program cover the work required to allow the Philadelphia NDC to process the originating Priority Mail flats and parcels being relocated from the P & DC due to its planned closure when the lease expires in March 2010. The project includes demolishing two Parcel Sorter Machines and two Sack Sorter Machines and relocating the control room and computer room. In addition, a 200 bin Automated Package Processing System (APPS) will be transferred from another site and a Small Parcel and Bundle Sorter (SPBS) and SPBS feed system will be removed.

#### **SURFACE VISIBILITY (NO-01)**

The Surface Visibility system collects information and reports on asset tracking, providing visibility into the movement of each sack, tray, container, and trailer within the USPS supply chain. This kind of real-time visibility affords the Postal Service the opportunity to identify problems such as:

-Mail that was processed late, resulting in a container missing its assigned dispatch.

-Handling units that were loaded into the wrong containers and containers loaded onto the wrong trailers.

### **AUTOMATED PACKAGE PROCESSING SYSTEM (APPS) – SORT ACCURACY IMPROVEMENT (SAI) PROGRAM**

The APPS Sort Accuracy Improvement Program (SAI) upgraded all 74 existing Automated Package Processing System (APPS) machines with Sort Accuracy Improvement kits. This enhancement reduces sorting errors resulting in improved service for mail processed on the APPS.

Deployment of all 129 operational kits and 2 training/support kits began on June 30, 2009 and ended November 18, 2009. Each of the 55 dual induction APPS machines received two (2) SAI kits (one per induction station); and each of the 19 single induction machines received one (1) SAI kit.

### **REMOTE ENCODING CENTER (REC) CONSOLIDATIONS**

As the technology for computerized resolution of addresses improves, the percentage of mail requiring manual keying at the RECs is reduced. Currently, the reduction of keying requirements due to improvements in computerized encoding is being offset by additional keying requirements for other products such as flat mail, Automated Package Processing Systems (APPS) and the

Postal Automated Redirection System (PARS). Although the keying requirements for each are different, and they are handled in separate operations, the Postal Service is pursuing their integration.

### **MULTI-CHANNEL CUSTOMER EXPERIENCE IMPROVEMENT PROJECT (HR03) -- PROJECT PHOENIX**

Project Phoenix will address increasing competitive and technological challenges by improving the underlying information technology (IT) that supports three key revenue generating channels within USPS: the website (USPS.com), the contact center, and retail. Project Phoenix will also fund enhancements to USPS.com and the contact centers. These improvements will support a more positive and consistent customer experience across channels by offering more products and services, and will positively impact customer satisfaction, retention, and revenue growth. The improvements will also reduce IT maintenance and integration costs over time.

Project Phoenix will be implemented in two phases and multiple releases. Revenue growth is anticipated due to Project Phoenix. This project will generate an increase in revenue primarily by enhancing the customer experience through the Internet channel and contact centers. Enhancements to the website will make it easier for customers to find the products they need by creating a more streamlined and intuitive user interface. Customer data integration between the

contact center and Internet channels will promote customer satisfaction by enabling agents to provide consistent personal service.

The redirection of Shipping and Stamps revenue from the retail channel to USPS.com will result in cost savings and cost avoidance due to a reduction in retail staffing hours.

### **LEARNING MANAGEMENT SYSTEM (HR-02)**

The Learning Management System is a comprehensive learning solution that will enable the Postal

Service to manage and integrate a full range of its training, administration, delivery, and talent management processes. Currently, these processes are managed using multiple legacy systems that lack interoperability and are inefficient and costly to maintain.

The LMS system includes an intuitive learning portal and learning management software, as well as test authoring, content structuring, content management, and collaboration functionality. The system offers back-office functionality for competency management and comprehensive support of performance management. It provides strong analytical functionality that includes support for ad hoc reporting. The LMS tailors learning paths to an individual's educational

needs and personal learning style. This personalized learning that is based on job requirement, tasks preferences, and existing knowledge improves learning efficiency for employees by providing the training needed for their development.

## **Section 1B**

### **Breakthrough Productivity Initiatives (BPI)**

Breakthrough Productivity Initiatives (BPI) refer to various initiatives and actions by the Field and Headquarters to achieve savings in addition to specific operational programs. The savings are achieved through implementation of standardized field operations procedures and information systems resulting in increased efficiencies in operational functions, reductions in administrative functional areas, and more efficient transportation utilization. The improved processes enable the Postal Service to develop specific measures of performance and national targets, and support the Transformation Plan goal of better aligning workhours to workload.

In Fiscal Year 1999, efforts were underway to develop and establish a mechanism that would fairly measure the performance for plant and delivery Operations. From this effort, the Breakthrough Productivity Initiative (BPI) was developed and implemented.

The Breakthrough Productivity Initiatives for Mail Processing, Customer Service, and Delivery Services are a tool used to measure production efficiency. This is accomplished by collecting data (volume and actual hours) by processing category type, (e.g. automation or manual, office or street delivery).

The Performance Achievement measure is the computed value that corresponds to the production efficiency for a unique operation and is represented as a percent value, 0% to 100%, with 100% representing the highest. The Performance Achievement Percent is computed as follows:

- Total Mail Volume by unique category - Actual
- Total Work Hours by unique category - Actual
- Predefined Target Productivity – Computed yearly based on actual productivity by category
- Earned Hours – Computed value based on Total Mail Volume divided by Predefined Target Productivity
- Opportunity Hours – Computed value based on Total Work Hours minus Earned Hours

Although opportunity hours are calculated for each type of operation, it is unlikely that field initiatives will result in the same percentage reduction in opportunity hours for each type of operation. Since savings estimates are more predictable for larger groups of operations, BPI savings are assumed distributed to each of the following groups in direct proportion to the opportunity hours in each group.

- Letter Distribution such as the Delivery Barcode Sorter (DBCS) and manual letter casing.
- Flats Distribution such as the Advanced Flats Sorting Machine 100 (AFSM 100) and manual flats casing.
- Bulk Mail Centers

- Manual Priority and Parcels
- Other Mechanized operations such as the Small Parcel and Bundle Sorter (SPBS) and the Tray Sorter

The Breakthrough Productivity Initiative for Maintenance currently encompasses two efforts. The first initiative focuses on improving the performance of the custodial staffs and monitoring performance using workhours per 1,000 square feet of interior and exterior space. The second initiative focuses on reducing the replenishment costs of maintenance spare parts and supplies in field maintenance stockrooms by comparing actual inventory value with the inventory value that would exist at two inventory turns per year.

## **Section 2**

### **Other Programs**

Most programs add costs as well as generate savings. The cost portion is called and labeled "Other Programs". The following programs include identified costs, as well as cost savings, during the period. For program descriptions, see Section 1A, Cost Reduction Programs.

- AUTOMATED LETTER MOVEMENT SYSTEM (ALMS)
- DELIVERY BAR CODE SORTER CENTRAL VACUUM SYSTEMS
- CENTRAL VACUUM SYSTEMS FOR PHASE 1 DBCS'S
- DBCS 7 MACHINES
- CENTRAL VACUUM SYSTEMS FOR AFSM 100 MACHINES
- AFSM 100 CANCELLATION UPGRADE
- PHILADELPHIA NETWORK DISTRIBUTION CENTER
- FUTURE FLAT SEQUENCING SYSTEM (FSS)
- FLATS SEQUENCING SYSTEM PHASE 1
- FIELD FIXED MECHANIZATION /FIELD MATERIAL HANDLING SYSTEM (CURRENT&FUTURE)
- APPS SORT ACCURACY IMPROVEMENT

### **Section 3**

#### **Corporatewide Activities**

##### **EXPEDITED MAIL SUPPLIES & SERVICES**

This activity is intended to cover printing of Express Mail and Priority Mail envelopes, boxes, labels, forms, and tags.

##### **ADVERTISING**

The advertising program provides information on our products and services using the following media: television, radio, outdoor, transit, magazines, newspapers, direct mail and newsletters, film and video, yellow pages, post office lobby posters and displays, and promotional materials such as posters, brochures, and point-of-purchase items.

##### **RESEARCH & DEVELOPMENT**

Corporatewide activities include research and development which have the objectives of improving service, reducing costs, and providing an adequate working environment by implementing new and improved technology-based

systems. These systems affect practically all areas of the postal system, including mail processing, transportation, delivery, retail services, administrative services, and new postal products. Many cost reduction program savings are based on new and improved technology-based systems resulting from Research and Development.

#### **ALL OTHER CORPORATEWIDE ACTIVITIES**

This item reflects the estimated change in expenses for corporatewide activities that have not been listed separately (i.e., activities that are centrally funded and managed, such as debit/credit card, mail transport equipment and postage stock).

**Response of United States Postal Service to Request for Additional  
Information Related to Cost Reduction Programs from  
Technical Conference on July 27, 2010**

At the Technical Conference on July 27, 2010, further interest was expressed in a presentation breaking out estimated cost savings by program as the product of workhour savings and productive hourly rates, also akin to part of USPS-LR-L-49. That breakout is attached to this response electronically as 3<sup>rd</sup>.TC.Cost.Redctn.Attach.xls.

With regard to the source of the workhour savings estimates, those estimates generally start with the estimates in the Decision Analysis Report (DAR), if a DAR has been completed. If not, estimates would need to be developed separately. After a program is implemented, as events unfold, DAR estimates may be adjusted for variances, primarily due to schedule changes. For example, estimates used in the budget for a subsequent year may not necessarily match initial estimates in the DAR for that subsequent year.

Thus, the workhour savings estimates upon which the cost reduction program portion of Mr. Masse's presentation is premised may involve both the original workhour estimates in the DAR, plus ongoing consultations between program managers, Operations, and Finance.

Response of United States Postal Service to Request During  
Technical Conference on July 27, 2010  
for Additional Information Related to Flats Strategy Programs

At the Technical Conference on July 27, 2010, interest was expressed on when the 30 operational strategies might be implemented, and the firmness of our expectations that any particular item might be among those implemented. Responsive information is provided in the following chart.

	<b>OPERATIONS</b>	<b>Size of Opportunity</b>	<b>Development Stage [a]</b>	<b>Savings Expected [b]</b>
	<b>Transportation</b>			
1	Improving Handling Unit/Container Density	Large	Concept	2011
2	Eliminate Periodical and Standard Mail Flown	Small	Concept	2011
3	Transportation Utilization (all products)	Large	Development	2011
4	Network Optimization (all products)	Medium	Development	2011
	<b>Mail Processing</b>			
5	Facility Optimization	Large	Development	Ongoing
6	Equipment optimization	Medium	Development	2012
7	Future FSS enhancements and processing modes	Medium	Concept	2012 or later
8	Automated Flats Preparation (AFP)	Medium	Concept	2013 or later
9	Automated Package and Bundle Sorter	Medium	Planning	Ongoing
10	Material Handling	Large	Planning	2011 or later
11	Flat Recognition Improvements	Small	Development	2011
12	Automated Flats Forwarding	Small	Concept	2013 or later
13	Using IMb data to determine letters processed on flat sorting equipment	Small	Concept	2011 or later
14	Electronic Condition-Based Maintenance	Small	Development	2011
15	Utilize a single Incoming Secondary run for all flats	Small	Concept	2011 or later
16	Monthly Periodicals – merge with Standard Mail service standards	Sm/Med	Concept	2011 or later
17	Distribution compression (all products)	Large	Planning	2011
18	Reduce mixed-states consolidation processing locations (L009) and optimize mixed states flow	Medium	Development	Ongoing
19	Realign operating and transportation plan to improve utilization	Medium	Concept	Ongoing
20	Periodicals Lean Six Sigma (LSS) end-to-end value stream mapping project	Undefined	Concept	Ongoing

Response of United States Postal Service to Request During  
 Technical Conference on July 27, 2010  
 for Additional Information Related to Flats Strategy Programs

21	Refine work methods to improve Business Mail Entry Unit (BMEU) / Plant load handoff to mail processing	Large	Concept	Ongoing
22	Sort Plan Optimization (SPO) for flats	Small	Development	Ongoing
23	Continuous Improvement	Undefined	Concept	Ongoing
<b>Post Office and Delivery Operations</b>				
24	Business Plan Staffing and Scheduling Reviews	Large	Planning	Ongoing
25	Shifting distribution from Post Office Operations (Function 4) to Mail Processing Operations (Function 1)	Medium	Planning	Ongoing
26	Customer Service Unit Optimization	Medium	Concept	2011 or later
27	FSS work methods	Large	Development	Ongoing
28	Route Adjustments - Joint Alternate Route Assessment Process (JARAP) / Carrier Optimal Routing (COR) (all products)	Medium	Development	Ongoing
29	Route Optimization 100 Percent Street routes	Large	Concept	2011
30	Facility Optimization (all products)	Small	Development	Ongoing

- [a] *Concept* indicates that an opportunity has been identified, but no plan has yet been developed to take advantage of it.  
*Development* indicates that a plan is being identified to take advantage of an opportunity.  
*Planning* indicates that planning for implementation of a plan is taking place.
- [b] This is the earliest date that savings from an opportunity can be expected.

**DOCKET NO. R2010-4**  
**INSTITUTIONAL RESPONSES TO**  
**PRESIDING OFFICER'S INFORMATION REQUESTS**

<b><u>POIR</u></b>	<b><u>Question</u></b>
POIR No. 1	1
POIR No. 3	20-23
POIR No. 4	5, 9

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

1. Please refer to Library Reference USPS-LR-9, Operations Plans for Flats. The Postal Service discusses 29 strategies for improving transportation, mail processing, and Post Office operations and delivery. Also, please refer to the attached Excel worksheet "Flats strategy.xlsx" as an example of the level of detail being sought in the following questions.

- a. For each of these strategies, please provide a quantitative estimate of each program's overall impact on cost. Please utilize the most recent existing information (such as Decision Analysis Reports or Return on Investment calculations) in responding and identifying the sources relied on.
- b. Please provide the unit cost savings from each strategy for Periodicals and Standard Mail Flats for FY 2010 through FY 2013.
- c. For each unit cost savings in subpart a., please provide detailed information for each affected cost segment or cost pool to support the estimate of unit cost savings. Details should be as specific as possible (e.g., percent increase in productivity and/or changes in machine throughput.)
- d. Please calculate an estimated unit cost based on the savings from subpart b. for Standard Mail Flats and Periodicals for FY 2010 through FY 2013.
- e. Please provide the estimated cost coverage for Standard Mail Flats and Periodicals for FY 2010 through FY 2013 using the projected unit cost calculated in subpart d.
- f. If the cost coverage does not exceed 100 percent for Standard Mail Flats or Periodicals by FY 2013, please explain when the product in question is estimated to cover its cost and describe additional steps to be taken to achieve profitability.

**RESPONSE:**

All programs for which cost savings have been planned or budgeted are contained in Mr. Masse's statement and associated materials. Beyond these programs, cost savings are more speculative; they are based on the size of the opportunity, but detailed plans for addressing each issue have not all been developed yet. Additional savings from the strategies in USPS-R2010-4/9 are part of the Postal Service's productivity goals, and are recognized in the BPI provisions of Mr. Masse's estimates.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

20. The following questions concern potential transportation savings identified in the Flats Strategy, USPS-R2010-4-LR-9. These improvements are estimated to be implemented during the test year

- a. Please provide the percentage of Flats that currently utilize the NDC network.
- b. When will the Redesign of NDC Mail Transportation Equipment (MTE) be completed?
- c. Please provide the estimated ROI for this project.
- d. When will the NDC/Surface Transportation Center Integration be completed?
- e. Please provide the estimated ROI for this project.

**RESPONSE:**

- a. No estimate of this percentage has been identified.
- b. 2011
- c. No ROI for this project is currently available because cost estimates for new equipment associated with it have not been finalized
- d. 2012
- e. Expected savings for all mail is \$125 million; no additional investment is expected.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

21. The following questions concern the estimated savings from the implementation of the FSS provided in USPS-LR-R2010-4-NP-2:

- a. Please provide the total amount of cost savings estimated for the FSS in FY 2010 and FY 2011.
- b. Please provide the source and methodology for that estimate.
- c. USPS OIG Audit DA-AR-10-007, concerning the performance projection of the FSS in the FY 2010 Q1 *Investment Highlights*, states that the estimated savings from the FSS machines do not comport with the DAR methodology or current performance. How does the methodology described in subpart b. differ from the methodology used in the Q1 FY 2010 *Investment Highlights*.

**RESPONSE:**

- a. Savings related to FSS are detailed in the attachment to the Response of the United States Postal Service to Informal Question Regarding Cost Reduction Programs Posed at the Technical Conference on July 27, 2010 (3rd.TC.Cost.Redctn.Attach.xls, filed August 2, 2010). The information requested can be found in rows 24-27 of the first four worksheets contained in the file.
- b. The cost savings estimate is based on internal Postal Service projections of machine performance, which are in turn driven by flat mail volume projections and the FSS deployment schedule.
- c. The methodology described in subpart b is essentially the same as the Investment Highlights methodology. The range of expectations contained in the Q1 FY 2010 Investment Highlights projects a range of possibilities which varies machine throughput, and also includes benefits from the use of Transitional Employees during the implementation period.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

22. According to the Flats Strategy, USPS-R2010-4-LR-9, the estimated date of implementation for the programs listed below is after FY 2011. For each program, as available, please provide the following: (1) a description of the concept; (2) when the decision to implement the concept will be made; and (3) any available additional detail concerning cost savings estimates for:

- a. Automated Flats Preparation;
- b. Automated Package and Bundle Sorter;
- c. Material Handling;
- d. Utilize a single Incoming Secondary run for all flats;
- e. Route Optimization 100 Percent Street Routes; and
- f. Facility Optimization.

**RESPONSE:**

Beyond the description in the original document, details on the practical scope or implementation of these concepts relies on a number of factors, including feasibility, the cost and effectiveness of new equipment, and negotiations with the unions. Any decision to develop a program will be dependent on evaluations of these factors, which do not themselves have timelines for completion.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

23. According to the Flats Strategy, USPS-R2010-4-LR-9, the estimated date of implementation for the programs identified below occurs before or during FY 2011.

- a. Equipment Optimization
  - i. Please provide the percentage of bundles currently processed in a non-optimal fashion on the SPBS or manually.
  - ii. Please provide the FY 2009 APPS operational run-time availability, excluding maintenance time.
  - iii. Please provide the FY 2009 APPS run-time.
  - iv. Please provide the percentage of pieces currently processed in a non-optimal fashion by manual sort.
  - v. Please provide the FY 2009 AFSM operational run-time availability, excluding maintenance time.
  - vi. Please provide the FY 2009 AFSM run-time.
- b. Reduce mixed-states consolidation processing locations (L009) and optimize mixed-states flow
  - i. Please provide the current cost of the L009 operation.
  - ii. When will consolidation be completed?
  - iii. What will be the effect on service of consolidation?
  - iv. Please provide the savings from consolidation.
- c. Realign operating and transportation plan to improve utilization
  - i. Please provide the current nationwide standard for Critical Entry Times.
  - ii. Please provide the percentage of mail tendered after the Critical Entry Time.
- d. Shifting distribution from Post Office Operations (Function 4) to Mail processing Operations (Function 1)
  - i. Please provide the percentage of mail currently processed in Function 4.
  - ii. Please provide or discuss the Postal Service's plan for centralizing the processing of flats to Function 1.

**RESPONSE:**

- a. i. Unknown. The Postal Service does not track bundle mail that is processed annually.
- ii. 371,287 hours
- iii. 309,512 hours

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

- iv. 30 percent of volume was handled manually in FY 2009.
  - v. 2,484,195 hours
  - vi. 1,669,821 hours
- b. i. The annual cost of single-piece processing of outgoing mixed states residue flat volumes entered under the L009 labeling list is estimated at \$8.4 million
- ii. The consolidation of mixed states residue flat distribution is expected to be complete in Quarter 2 of FY 2011
- iii. The Postal Service expects that service for these volumes will improve through a combination of streamlined mail flows and reduced cycle time for origin processing.
- iv. The savings associated with this consolidation effort is estimated for the next ten years at \$28 million each year.
- c. i. The only current nationwide standard CET is 4:00 p.m. for destinating Standard Mail
- ii. This data to provide an estimate are not recorded.
- d. i. Approximately 25.5 percent
- ii. The Postal Service is continuously researching the centralizing of flat mail distribution to locations where automated equipment capacity currently exists or redeploying excess automated equipment to locations where opportunity volume is identified. This would include mail from Function 4 distribution operations being moved to Function 1 when there is available capacity within service responsive operational windows.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

5. Please refer to the Flats Strategies described in USPS-LR-9. Please confirm that in addition to reducing costs for flat-shaped mail, the USPS-LR-9 strategies in the areas listed below will, if implemented, reduce the costs of parcels in general and the costs of Standard Mail NFM/Parcels in particular. If not confirmed, please identify which of the listed strategies will, if implemented, reduce parcel costs.
- a. Transportation
    - i. Improve Handling Unit/Container Density
    - ii. Eliminate Periodical and Standard Mail Flown
    - iii. Transportation Utilization
    - iv. Network Optimization
  - b. Mail Processing
    - i. Facility Optimization
    - ii. Equipment Optimization – APPS Utilization
    - iii. Automated Package and Bundle Sorter
    - iv. Material Handling
    - v. Electronic Condition-Based Maintenance
    - vi. Distribution Compression
    - vii. Realign Operating and Transportation Plan to Improve Utilization
    - viii. Refine Work Methods to Improve Business Mail Entry Unit (BMEU)/Plant Load Handoff to Mail Processing
    - ix. Continuous Improvement
  - c. Post Office and Delivery Operations
    - i. Business Plan Staffing and Scheduling Reviews;
    - ii. Shifting distribution from Post Office Operations (Function 4) to Mail Processing Operations (Function 1);
    - iii. Customer Service Unit Optimization
    - iv. Route Adjustments Joint Alternate Route Assessment Process (JARAP) / Carrier Optimal Routing (COR)
    - v. Route Optimization 100 Percent Street Routes
    - vi. Facility Optimization

**RESPONSE:**

Confirmed. The strategies listed above would be expected to generate savings for parcels. Most of them, with the exception of APPS utilization and the automated package and bundle sorter, would be expected to generate savings for letters as well.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO 4**

9. Please provide the number of post offices (excluding stations and branches) that were supervised by an employee other than a permanently assigned postmaster as of the beginning of FY 2008, FY 2009 and FY 2010.

**RESPONSE:**

At the beginning of FY09, our best estimate is that 1,679 out of 26,928 post offices reporting workhours did not have a permanent postmaster, while at the beginning of FY10, we estimate that 3,248 out of 26,872 post offices did not have a permanent postmaster. Analysis to develop a similar estimate for the beginning of FY08 is ongoing, and an updated response will be filed if the information can be estimated using available information.

1 CHAIRMAN GOLDWAY: Is there any additional  
2 information that you have for us?

3 (No response.)

4 CHAIRMAN GOLDWAY: If not, Mr. Koetting,  
5 will you identify the next Postal Service witness?

6 MR. RUBIN: I'm David Rubin. I'll be  
7 representing the Postal Service today, along with Mr.  
8 Koetting.

9 CHAIRMAN GOLDWAY: Welcome, Mr. Rubin.

10 MR. RUBIN: Presiding Officer's Ruling No. 3  
11 requested that the Postal Service make available an  
12 individual to respond to questions on the Postal  
13 Service's flat strategy, and in response to that  
14 ruling the Postal Service calls Frank Neri to the  
15 stand.

16 CHAIRMAN GOLDWAY: Mr. Neri, will you rise?  
17 Whereupon,

18 FRANK NERI

19 having been duly sworn, was called as a  
20 witness and was examined and testified as follows:

21 EXAMINATION BY THE COMMISSION

22 CHAIRMAN GOLDWAY: Thank you. Mr. Neri,  
23 you've been offered by the Postal Service as someone  
24 with knowledge to answer Commission questions relating  
25 to the Postal Service's flat strategy.

1           As a foundation for your testimony here  
2           today, would you please discuss your role in putting  
3           together the various programs identified as being part  
4           of the flat strategy?

5           THE WITNESS: Madam Chairman, as one of the  
6           operations managers of Postal Service Headquarters I  
7           was involved in the development of the strategies, the  
8           document including the strategies. It was a  
9           collective effort of various departments within  
10          Operations, and collectively we assembled the document  
11          for submission.

12          CHAIRMAN GOLDWAY: How many people were on  
13          the team that you worked with to develop it?

14          THE WITNESS: Various managers from various  
15          departments in Headquarters Operations.

16          CHAIRMAN GOLDWAY: How many is various?

17          THE WITNESS: Engineering, Delivery  
18          Operations, Processing Operations are among those that  
19          provided information for the document.

20          CHAIRMAN GOLDWAY: So three people  
21          participated with you?

22          THE WITNESS: And their collective staff.

23          CHAIRMAN GOLDWAY: So those three  
24          departments and their collective staff.

25          THE WITNESS: And Operations support

1 functions.

2 CHAIRMAN GOLDWAY: Did anyone from the field  
3 attend these meetings?

4 THE WITNESS: Not that I'm aware of.

5 CHAIRMAN GOLDWAY: Did you visit the field  
6 at all to see the flat sorting operations in action  
7 while you were considering the --

8 THE WITNESS: Madam Chairman, yes. From my  
9 perspective over many years of experience and also  
10 observing our operations, I visit the field quite  
11 frequently and visit with operations managers and  
12 interact with operations managers on a regular basis.

13 CHAIRMAN GOLDWAY: I have several questions  
14 here that have been submitted by outside parties.  
15 I'll begin with some of those. This is from Valpak to  
16 Masse Question 6.

17 In response to POIR No. 1, Question 1,  
18 concerning cost savings from the programs in the flat  
19 strategy, the Postal Service stated: All programs for  
20 which cost savings have been planned or budgeted are  
21 contained in Mr. Masse's statement and associated  
22 materials.

23 For which programs contained in the flat  
24 strategy did you provide information for Witness  
25 Masse's workpapers?

1 THE WITNESS: Madam Chairman, are you  
2 referring to the roll forward document, the programs  
3 included in the roll forward document?

4 CHAIRMAN GOLDWAY: I believe I am.

5 THE WITNESS: Madam Chairman, the best way  
6 for me to answer that question is to describe our  
7 process for program development within the Postal  
8 Service.

9 There's a process whenever there is a  
10 decision analysis prepared and circulated, it's  
11 circulated within the various functions in Postal  
12 Service Headquarters and we do have input. Many of  
13 these programs, the actual documents may be prepared  
14 by Engineering and processed through the various  
15 functions for review and input and the assumptions  
16 that are made within the opportunities that are  
17 described for the various programs.

18 So we have input on an ongoing basis as they  
19 are developed for many of those programs and also  
20 there is a process for review before it goes to our  
21 funding committees within the organization for  
22 approval of funding. So I would say that a number of  
23 these programs -- many, if not most or all -- we do  
24 have input of review and/or direct input of the  
25 assumptions that are made for opportunities.

1           CHAIRMAN GOLDWAY: So not necessarily all of  
2 them. You can't identify which one?

3           THE WITNESS: Many of these are over a long  
4 period of time, so I would say that all of the  
5 programs that are associated with decision analysis  
6 are circulated through my department for review.

7           CHAIRMAN GOLDWAY: The flat strategy does  
8 not contain programs that were included as line items  
9 in the Masse workpapers?

10          THE WITNESS: The flat strategy does include  
11 line item programs, two line item programs that are in  
12 the Masse document, and they are the FSS Program and  
13 the Flat Recognition Improvement Program.

14          CHAIRMAN GOLDWAY: Do you have a dedicated  
15 team for a long-term flat strategy and some  
16 designation of areas so that those decision analyses  
17 that are circulated related to flats come to you and a  
18 particular group of people?

19          THE WITNESS: It would be the responsibility  
20 of my functional managers within the various  
21 departments of my organization to review. They all  
22 are responsible for reviewing decision analysis  
23 reports, various areas of --

24          CHAIRMAN GOLDWAY: And the flat strategy is  
25 not separated out into some --

1 THE WITNESS: No.

2 CHAIRMAN GOLDWAY: -- group of people?

3 THE WITNESS: No. I have a Manager of  
4 Processing Operations, Processing Center Operations,  
5 that's responsible for all processing center policies  
6 and activities. I have a Manager of Network  
7 Distribution Center Operations that has areas of  
8 responsibility with respect to any initiatives that  
9 are identified or developed. I have a Manager of  
10 Technical Systems and Systems Integration with similar  
11 responsibilities.

12 So the opportunities and initiatives are  
13 circulated and/or developed through the various  
14 managers.

15 CHAIRMAN GOLDWAY: Okay. I'll go back to  
16 ValPak now. The question was:

17 The program automated package and bundle  
18 sorter would upgrade the small parcel and bundle  
19 sorter with a bar code reader, saving keyer work  
20 hours. This program is defined as "in planning," the  
21 furthest along stage. When will this piece of  
22 equipment begin deployment, and how many SPBS will be  
23 upgraded?

24 THE WITNESS: Madam Chairman, this  
25 particular program is in the development stage and

1 evaluation, and that's in fact what is part of the  
2 determination is based on the opportunity that has  
3 been identified.

4 First, the valuation of the costs associated  
5 with that conversion of the equipment and the analysis  
6 on the work hour savings opportunity related to that  
7 would all determine the extent of the investment and  
8 the amount of equipment.

9 CHAIRMAN GOLDWAY: So in the development  
10 stage you are analyzing the initial cost savings, but  
11 there is no plan yet to begin deployment?

12 THE WITNESS: It is in the development  
13 stage. Based on the equipment that exists we  
14 anticipate that there may be an opportunity, if  
15 funding is approved with the limited capital that is  
16 available and estimated, that maybe as many as 180  
17 small parcel and bundle sorters that are converted.

18 CHAIRMAN GOLDWAY: The July 27, 2010,  
19 technical conference response that you provided said  
20 this project was in the planning stage. So are you  
21 saying it is not in the planning stage?

22 THE WITNESS: It is in the planning stage of  
23 determining the extent of the opportunity and the  
24 investment and the extent of the deployment.

25 CHAIRMAN GOLDWAY: So you don't have any

1 information on what the projected savings will be yet  
2 for 2011?

3 THE WITNESS: Not yet.

4 CHAIRMAN GOLDWAY: You don't have a  
5 timeline?

6 THE WITNESS: No.

7 CHAIRMAN GOLDWAY: Maybe you could, because  
8 this was a question among ourselves. Could you  
9 clarify the different stages in this flat strategy  
10 plan? What does planning mean? What does development  
11 mean? There was a third stage as well.

12 We could not by the words themselves  
13 determine what the differences were, and the word you  
14 used in the report that you provided to us in July was  
15 planning, and now you're saying the word is  
16 development.

17 So could you help us to understand those  
18 three different levels, three different stages of  
19 projects?

20 THE WITNESS: The planning stage within our  
21 Engineering function, the planning stage is where an  
22 opportunity has been identified, the concept is  
23 initiated, and the opportunities that the initiative  
24 may afford are evaluated.

25 I would describe this initiative as being at

1 that stage. The concept of being tested within  
2 Engineering and as a result of that initial testing,  
3 developing the initiative for review and approval for  
4 funding within the Postal Service.

5 CHAIRMAN GOLDWAY: So this concept is being  
6 tested within Engineering at the moment?

7 THE WITNESS: That's how I would describe  
8 it.

9 CHAIRMAN GOLDWAY: Okay. That's planning.  
10 And then what's development?

11 THE WITNESS: Development would be the  
12 initial testing, and if it's proven that this will be  
13 an effective initiative we would likely test at a  
14 number of locations, identifying the number of  
15 locations that we would test the initiative, and  
16 deploy an initial set of equipment for the testing of  
17 the concept.

18 CHAIRMAN GOLDWAY: And what's the last  
19 stage?

20 THE WITNESS: Once the decision is made for  
21 deployment, deploying the equipment.

22 CHAIRMAN GOLDWAY: So we have planning,  
23 development and deployment, right?

24 THE WITNESS: Yes.

25 CHAIRMAN GOLDWAY: The concept is before

1 planning, the concept stage? The concept is within  
2 the planning stage?

3 THE WITNESS: I would describe it as within  
4 the planning stage.

5 CHAIRMAN GOLDWAY: We had understood the  
6 concept was sort of the beginning, but you're saying  
7 the planning stage identifies opportunities and  
8 concepts and then the concepts are tested and that's  
9 all within the planning stage? Yes?

10 We're trying to clarify what's not very  
11 clear to us. So we've got a planning stage, a  
12 development stage and a deployment stage, and within  
13 planning there's a concept stage. Is that the way you  
14 want to say it now?

15 THE WITNESS: Well, initially an opportunity  
16 is identified as a concept, and planning begins once  
17 that concept, once that opportunity, is identified.

18 CHAIRMAN GOLDWAY: Okay. But you listed in  
19 your report several things that were in the concept,  
20 others that were in the planning stage, others that  
21 were in the development stage. Now you're sort of  
22 muddying concept and planning here so that we can't  
23 really distinguish where they are.

24 I think I'll ask my staff to go back and  
25 look at what you submitted and see if they can't get

1 you to clarify where some of those projects are that  
2 you've identified as concepts and to maybe clarify  
3 where they are in the planning stage.

4 COMMISSIONER LANGLEY: Madam Chairman, could  
5 I just ask for a moment that we also add where the  
6 cost savings associated with these proposals, at what  
7 point they are assigned?

8 CHAIRMAN GOLDWAY: That's a good question,  
9 but my understanding is -- well, you tell us. Where  
10 are the cost savings?

11 COMMISSIONER LANGLEY: I mean, are there  
12 discrete --

13 CHAIRMAN GOLDWAY: Right.

14 COMMISSIONER LANGLEY: -- cost savings  
15 embedded in each of these steps? I don't want to take  
16 away from the Chairman's time, but I think --

17 CHAIRMAN GOLDWAY: Yes.

18 COMMISSIONER LANGLEY: -- how all this is  
19 melded together.

20 THE WITNESS: In the development of any  
21 initiative, as that initiative is being pursued the  
22 opportunities are identified for where there could be  
23 work hour savings associated with whatever the  
24 initiative is.

25 As the initiative progresses and we identify

1 those opportunities, those are developed into a  
2 decision analysis for investment purposes, so once  
3 that decision analysis is completed and we are all in  
4 agreement on where the savings opportunities are the  
5 funding is approved for the initiative.

6 CHAIRMAN GOLDWAY: So you wouldn't begin  
7 what you've just called development, which is initial  
8 testing, unless you had had a decision analysis that  
9 showed that there were savings?

10 THE WITNESS: And if savings opportunities  
11 are identified, there could also be testing on a  
12 limited basis with limited funding prior to full  
13 deployment or approval for funding for full  
14 deployment.

15 COMMISSIONER LANGLEY: So a plan to  
16 implement a plan doesn't come after the testing?

17 THE WITNESS: I'm sorry. A plan to  
18 implement?

19 COMMISSIONER LANGLEY: When would a decision  
20 be made to go full bore with a new program?

21 THE WITNESS: Once the decision analysis is  
22 completed and presented to the funding committees  
23 within the Postal Service for approval, senior  
24 management approval, depending on the funding level  
25 and the amount of the investment. Then once that

1 decision is made with the approval of the funding then  
2 it would go forward.

3 COMMISSIONER LANGLEY: But you mentioned  
4 limited funds could be released for limited testing?

5 THE WITNESS: Correct.

6 CHAIRMAN GOLDWAY: Do you have DARs for the  
7 programs in development and in planning?

8 THE WITNESS: The program that you referred  
9 to?

10 CHAIRMAN GOLDWAY: Yes.

11 THE WITNESS: We do not at this point have a  
12 DAR completed for that program.

13 CHAIRMAN GOLDWAY: So there's no DAR for the  
14 automated package and bundle sorter yet?

15 THE WITNESS: Not at this time.

16 CHAIRMAN GOLDWAY: Do you have a timeline  
17 when you think you'll make a decision on them?

18 THE WITNESS: I could reach out to  
19 Engineering and determine what that timeline is.

20 CHAIRMAN GOLDWAY: We'd appreciate that  
21 information. Any other questions along this line?

22 (No response.)

23 CHAIRMAN GOLDWAY: Time-Warner has a  
24 question that they wanted us to ask. What is the  
25 standard operating procedure for processing periodical

1 flats with a manual incoming secondary sort when the  
2 mailing arrived after the published critical entry  
3 time?

4 THE WITNESS: Madam Chairman, we operate  
5 within a processing window described within our  
6 operating plans. Our operating plans define critical  
7 entry times and clearance times for operations.

8 Our expectation is that the field process  
9 mail in the most efficient manner and at their  
10 discretion make a decision in what manner that mail is  
11 processed. We expect and monitor performance to  
12 ensure that the most efficient manner of processing is  
13 being utilized.

14 It's our expectation that mail that arrives  
15 prior to the critical entry time is processed within  
16 the most efficient manner. We recognize that at the  
17 local level decisions are made, and it's been  
18 identified that decisions have been made at some  
19 locations to work mail manually.

20 And where that is occurring, if it is  
21 occurring for mail that's received after the critical  
22 entry time, we are very interested in that information  
23 as to where it may be occurring so that we could  
24 encourage the correct decisions by local managers to  
25 work that mail efficiency on automated processing

1 equipment, mechanized processing equipment, as opposed  
2 to manually.

3 CHAIRMAN GOLDWAY: Well, what policies are  
4 currently in effect to maximize the amount of  
5 periodical mail processed on automated piece sorting  
6 equipment when the mailing arrives after the  
7 automation bundle sorting equipment has finished the  
8 run for the day or to encourage the local operators,  
9 the local processing center, to use automation  
10 equipment at any time?

11 THE WITNESS: It's our expectation that mail  
12 is processed on automated and mechanized equipment  
13 where it is available and when it is available.  
14 Ultimately the decision that local management --  
15 decisions are at their discretion. If in fact they're  
16 facing variables that may be impacting their  
17 operations, other influences on their operations, that  
18 may force them to make other decisions.

19 The discretion exists at the local level for  
20 managers to make decisions, but overall we monitor the  
21 performance of operations to drive the correct  
22 behavior and to drive work on the most efficient  
23 processing manner that is available.

24 CHAIRMAN GOLDWAY: Well, how do you monitor  
25 it at the same time that you give full discretion to

1 the local decision maker?

2 THE WITNESS: There's indicators,  
3 performance indicators that we monitor, utilization of  
4 equipment, the workload that's worked, the processing  
5 window analysis, the number of hours that the  
6 equipment is processing mail, the windows of operation  
7 compared to when the mail is available.

8 Typically within our processing facilities  
9 there are planned windows of operation, and we compare  
10 the actual windows of operation -- performance  
11 indicators such as throughput, run hours -- to those  
12 windows of operation to ensure that mail is being run  
13 in the most efficient manner, but we have managers in  
14 the field with the discretion to make decisions where  
15 it's necessary.

16 CHAIRMAN GOLDWAY: What is the standard  
17 operating procedure for processing standard mail flats  
18 with a manual income secondary sort when the mailing  
19 arrived after the published critical entry time?

20 THE WITNESS: If I understand the question  
21 correctly, if the operation is a manual incoming  
22 secondary then the standard operating procedure would  
23 be to process that mail manually.

24 But if you're describing an operation that  
25 has mechanized equipment the expectation is that if

1 that equipment, based on the schedule of that  
2 equipment for the various operations that are  
3 processed on that equipment, if that operation is  
4 scheduled for that equipment that that mail be worked  
5 on automated and mechanized equipment.

6 CHAIRMAN GOLDWAY: Do you process standard  
7 mail bundles manually when they could be processed on  
8 automation?

9 THE WITNESS: Our expectation is that our  
10 field managers make the decision to process it on  
11 automated and mechanized equipment and not process it  
12 manually when it's available.

13 CHAIRMAN GOLDWAY: And what are the policies  
14 currently in effect to maximize the amount of standard  
15 mail flats processed on automation piece sorting  
16 equipment when the mailing arrives after the  
17 automation bundle sorting equipment has finished the  
18 run for the day?

19 THE WITNESS: I would describe it as an  
20 expectation, and as we identify performance results we  
21 identify where there may be opportunities for the  
22 field to improve their performance. If in fact they  
23 are not taking full advantage of those opportunities  
24 we provide that direction in identifying those  
25 opportunities with the field.

1           The expectation is they are in the field.  
2           What I'm trying to describe is an environment where  
3           the expectation is there to work the mail in the most  
4           efficient manner possible.

5           If the equipment is available, the  
6           expectation is there that mail is worked on the  
7           equipment. Are there instances where that might not  
8           be happening? Yes, and we address those issues when  
9           we identify them.

10           CHAIRMAN GOLDWAY: Can you say affirmatively  
11           that this manual processing is happening less  
12           frequently than it has happened in the past?

13           THE WITNESS: I can't say that there is a  
14           great deal of attention on the utilization of our  
15           equipment and that we are driving behavior to in fact  
16           utilize that equipment to the maximum extent possible.

17           CHAIRMAN GOLDWAY: This is a Hot 2C  
18           question. Has the Postal Service performed any  
19           studies concerning the extent and cost of manual  
20           bundle and piece processing of automation compatible  
21           mail, especially in regard to Hot 2C and Hot 3C  
22           procedures?

23           THE WITNESS: No specific study that I'm  
24           aware of.

25           CHAIRMAN GOLDWAY: Are you aware of the

1 conclusion in the recent OIG report, EAAR10-007, that  
2 the FSS may not be a profitable venture for the Postal  
3 Service?

4 THE WITNESS: I am aware that the report was  
5 issued recently, but I have not reviewed the report,  
6 no.

7 CHAIRMAN GOLDWAY: The report indicates that  
8 the return on investment will not be able to be  
9 captured. There will be not enough savings, if  
10 savings at all, from the FSS machines.

11 Has the AFSM been successful at reducing  
12 flat processing costs? Enough to make flats  
13 processing profitable?

14 THE WITNESS: I can't speak to the  
15 profitability, but I can say that the AFSM introduced  
16 an improved level of productivity to the operations.

17 CHAIRMAN GOLDWAY: Do you have a measurement  
18 of what that improved productivity is?

19 THE WITNESS: Prior to the AFSM-100s when we  
20 had flat sorter 881s, the throughput was approximately  
21 5,500 pieces per hour at a per activity rate of 919  
22 pieces. With the AFSM-100, our throughput is  
23 approximately 13,800 with a productivity rate of  
24 approximately 1,700 pieces per hour.

25 CHAIRMAN GOLDWAY: We don't know whether

1 that increase in profitability, however, is enough to  
2 eliminate the below water impact of the flats?

3 THE WITNESS: I cannot speak to that.

4 CHAIRMAN GOLDWAY: This next question refers  
5 to the honest, efficient, economical management  
6 requirements of the PAEA for the Postal Service. When  
7 did the Postal Service begin to lose money on standard  
8 mail noncarrier route flats?

9 THE WITNESS: Madam Chairman, respectfully  
10 my knowledge is in Operations, and I cannot answer  
11 questions related to --

12 CHAIRMAN GOLDWAY: How long have you worked  
13 in Operations, which included flats? How many years?

14 THE WITNESS: Madam Chairman, I've worked in  
15 Operations in the Postal Service my entire career, for  
16 26 years.

17 CHAIRMAN GOLDWAY: Was there any expression  
18 ever given to you by other people on your team or  
19 above you that said we have a problem with standard  
20 mail noncarrier route flats?

21 THE WITNESS: My knowledge and the extent of  
22 my responsibility includes identifying the  
23 opportunities to operate more efficiently and  
24 identifying the opportunities for reducing work hours.

25 That is my responsibilities within the

1 Postal Service and driving the policies within  
2 Operations to --

3 CHAIRMAN GOLDWAY: I take it you were given  
4 some direction to specifically pay attention to flats,  
5 standards flats, at some time, at some point in your  
6 career? After all, you're here representing --

7 THE WITNESS: Yes.

8 CHAIRMAN GOLDWAY: -- the flat strategy. Do  
9 you have a date when that occurred?

10 THE WITNESS: Well, in my various roles in  
11 the Postal Service as an operations manager, as a  
12 plant manager -- I was a plant manager in three  
13 various locations -- in the field, in that role I  
14 managed operations so that we can operate efficiently  
15 and improve our performance.

16 In my role here at Headquarters I drive  
17 policies in the field and I develop policies for the  
18 field that are related to operating efficiently.

19 CHAIRMAN GOLDWAY: Are you aware that  
20 standard mail and periodicals --

21 THE WITNESS: Yes, I am.

22 CHAIRMAN GOLDWAY: When did you become aware  
23 of that?

24 THE WITNESS: I've been aware for many years  
25 that that's been the case.

1 CHAIRMAN GOLDWAY: How many? Five? Ten?

2 THE WITNESS: Ten.

3 CHAIRMAN GOLDWAY: Ten. Ten years. And  
4 that's for both periodicals and flats?

5 THE WITNESS: I am aware, yes.

6 CHAIRMAN GOLDWAY: And do you know when the  
7 AFSM rollout was completed?

8 THE WITNESS: Madam Chairman, I believe it  
9 was in 2002.

10 CHAIRMAN GOLDWAY: 2002.

11 THE WITNESS: I would have to verify that  
12 information.

13 CHAIRMAN GOLDWAY: And does the document,  
14 Flat Strategy, contain the Postal Service's plan to  
15 improve the cost coverage of standard flats and  
16 periodicals?

17 THE WITNESS: The document, Flat Strategy,  
18 was intended to improve efficiencies and reduce costs.

19 CHAIRMAN GOLDWAY: There's no relationship  
20 of the cost reduction to the actual cost of flats and  
21 periodicals to be sure that the cost reductions end up  
22 by providing some measure of profitability for those  
23 two products?

24 THE WITNESS: I believe the opportunities  
25 for reducing work hours is the relationship.

1                   CHAIRMAN GOLDWAY: But there's no  
2 documentation that defines the number of work hours  
3 that are going to be reduced and relates it to  
4 specific numbers of cost savings so that periodicals  
5 and flats would in fact cover their costs?

6                   THE WITNESS: Not that I'm aware of.

7                   CHAIRMAN GOLDWAY: Nothing in the plan that  
8 does that?

9                   THE WITNESS: Not in the flat strategy.

10                  CHAIRMAN GOLDWAY: How many of the programs  
11 have planned implementation dates in the flat  
12 strategy?

13                  (Pause.)

14                  THE WITNESS: Quickly going through this,  
15 Madam Chairman, and I would like the opportunity to  
16 provide a more accurate answer. I would say four or  
17 five of these programs have implementation dates or  
18 implementation plans.

19                  CHAIRMAN GOLDWAY: Only four or five have.  
20 And when you go back over that and report to us, could  
21 you give us the planned implementation dates? How  
22 many of these programs will require a DAR before  
23 implementation?

24                  THE WITNESS: I would have to provide that  
25 information.

1                   CHAIRMAN GOLDWAY: And how many programs  
2 currently have a DAR, and how many of the programs  
3 having DARs are in the development stage?

4                   Why do you think these clearly largely  
5 hypothetical strategies that you've listed in this  
6 document will lead to cost reductions for flats where  
7 other programs in the past have failed?

8                   THE WITNESS: I believe just as other  
9 programs, any initiative starts with a concept and  
10 starts with an idea. We begin planning and developing  
11 that idea, and I don't know whether or not any of  
12 these programs will lead to savings.

13                   The development of those ideas will answer  
14 that question. The development of the DARs will  
15 answer that question.

16                   CHAIRMAN GOLDWAY: Has the Postal Service  
17 learned anything in the attempts thus far with regard  
18 to AFSM or other projects that it could use in the  
19 future where it's failed? Has it learned anything  
20 from where it's failed that it could apply to the  
21 future?

22                   THE WITNESS: I believe that we, as any  
23 organization, do learn from our experiences. I'm not  
24 sure that I would describe any of our initiatives  
25 specifically from a general description as having

1 failed, but I will state that we do learn from our  
2 experiences and build on those experiences for future  
3 opportunities as we develop them.

4 COMMISSIONER ACTON: Mr. Neri, could you  
5 talk a bit about what you regard the measure of  
6 failure or success? What's the goal when you're  
7 testing or implementing these concepts or plans?

8 THE WITNESS: My description of failure or  
9 success is whether or not the initiative proves true  
10 to the expectations, whether or not the savings  
11 opportunities that were identified with that  
12 initiative are achieved.

13 COMMISSIONER ACTON: Okay. That's key  
14 because you know, of course, that it's a compliance  
15 issue for the regulator covering these costs. That's  
16 our driver for our interest in this concern.

17 So if you understand that the plan you're  
18 conceiving and developing and implementing is in the  
19 end supposed to achieve a goal which will cover those  
20 cost gaps then that's what we're looking for.

21 CHAIRMAN GOLDWAY: It doesn't appear that  
22 you've got any direct relationship, though, between  
23 your plans and actual cost savings.

24 This document that you prepared that's in  
25 response to the PRC's directive is providing a

1 description of the strategies the Postal Service has  
2 implemented and intends to implement in the future to  
3 address these issues.

4 But if this isn't a strategy to improve cost  
5 coverage, just a general idea of what will gain some  
6 general efficiencies, where is that strategy?

7 THE WITNESS: Madam Chairman, these are  
8 strategies that we are pursuing in order to identify  
9 where we can reduce costs.

10 COMMISSIONER ACTON: Mr. Neri? I'm sorry,  
11 Madam Chair.

12 CHAIRMAN GOLDWAY: Go ahead. Go ahead.

13 COMMISSIONER ACTON: Mr. Neri, can you  
14 outline for me the new programs that have been  
15 developed for flat processing during the past 12  
16 months? Which are those?

17 THE WITNESS: FSS is one that is in the  
18 deployment stage. We are deploying equipment for flat  
19 sequenced sorting. That's one program.

20 And along with that is the integration of  
21 that operation within our processing facilities, so  
22 there's been a great deal of resources focused on the  
23 success integration of the flat sequencers within our  
24 operations.

25 COMMISSIONER ACTON: Okay. And I think the

1 Chairman referenced earlier a report by the Office of  
2 Inspector General to the Postal Service that addresses  
3 some of his concerns about the FSS.

4 I would encourage you to review it because  
5 it may provide you some guidance on how to target some  
6 of your resource since I believe you indicated that  
7 you're not familiar with those findings.

8 CHAIRMAN GOLDWAY: If your strategy was  
9 meant to improve cost coverage and you are not  
10 familiar with the way the OIG has evaluated cost  
11 coverage I think you'd better review that document to  
12 be informed of how cost coverage is evaluated for  
13 efficiencies.

14 In the AFSM, for instance, or any of the  
15 other implemented changes from stacks to bundles or  
16 co-palletization, et cetera, have you found any  
17 unintended consequences of your efficiencies that have  
18 resulted in additional cost?

19 THE WITNESS: I'm sorry. With regard to the  
20 AFSM?

21 CHAIRMAN GOLDWAY: Over the years with the  
22 AFSM or with any of the other strategies or procedures  
23 that have been implemented in the last 10 years to  
24 deal with flats to try to make them more efficient,  
25 have you discovered any unintended consequences that

1 have raised costs?

2 I've been on the Commission for 12 years,  
3 and for 12 years I've heard about projects that are  
4 going to save costs within flat handling. If you add  
5 up all of those projects and ideas, one would think  
6 that flats would cost zero because of all of those  
7 brilliant ideas, and yet we're still here with costs  
8 even greater than what the prices are that we can  
9 charge for periodicals.

10 The difference between the cost and the  
11 coverage is expanding all the time, so there must be  
12 some problems in the last 10 or 12 years. Have you  
13 identified any of those problems?

14 THE WITNESS: In answer to your question,  
15 Madam Chairman, I am not aware of any unintended  
16 consequences for any particular program.

17 CHAIRMAN GOLDWAY: And you're not aware of  
18 any areas that have developed in the last 10 years  
19 that increased costs for periodicals?

20 THE WITNESS: No, I am not.

21 CHAIRMAN GOLDWAY: Well, this is a  
22 frustrating exercise. I will ask my other Commission  
23 colleagues if they'd like to take a stab at this.  
24 Commissioner Blair?

25 COMMISSIONER BLAIR: Thank you, and I

1 apologize for coming in late. The storms this morning  
2 blocked my access, so I appreciate your patience with  
3 me.

4 I think the discussion we're having right  
5 now about flats and the frustration of the Commission  
6 reflects the frustration in the community. It's all  
7 about how to bring these costs down.

8 One thing I wanted to ask you just as more  
9 of a big picture question is that it seemed to me in  
10 reviewing the Postal Service's submission this time  
11 that with the rates that were proposed it seemed to be  
12 moving closer to covering costs for those products  
13 that were currently under water.

14 I want to know what kind of priority is it  
15 for the Postal Service, or is it a priority, that  
16 rates cover costs under this new PAEA environment? Is  
17 it a priority for the Postal Service to have prices  
18 that cover rates, that cover costs?

19 THE WITNESS: Commissioner, I would not be  
20 the best individual from the Postal Service to answer  
21 that question with my operational responsibilities,  
22 not pricing responsibilities, so I'm not in a position  
23 to be able to answer that question.

24 CHAIRMAN GOLDWAY: You're not given any  
25 targets in your operations to say okay, we need to

1 save this amount of money in order to --

2 THE WITNESS: Yes, Madam Chairman.

3 CHAIRMAN GOLDWAY: -- make this product  
4 profitable?

5 THE WITNESS: In fact, Madam Chairman, I am  
6 given targets, performance targets for budgets,  
7 achieving our budget. Operations has a budget that  
8 are issued, and we develop strategies and initiatives  
9 within Operations in order to achieve our budget.

10 COMMISSIONER BLAIR: Do those budgets have a  
11 relationship to the prices that are charged? If so,  
12 what is that relationship?

13 THE WITNESS: Our budgets have a  
14 relationship to the revenue that the Postal Service  
15 generates.

16 COMMISSIONER BLAIR: What's that  
17 relationship? Is it one-for-one? I'm just trying to  
18 get a better sense of how budgets -- you said that you  
19 can't answer the initial question, but you're involved  
20 in the operations.

21 I think it would be interesting to better  
22 know how the budgets that you receive are related to  
23 the revenues that the Postal Service is bringing in.

24 THE WITNESS: Respectfully, I believe that  
25 that would be a better question for Finance.

1                   CHAIRMAN GOLDWAY: Are you asked to meet a  
2 certain budget by product? In other words, what I'm  
3 imagining is that you have to demonstrate that you  
4 provided a certain amount of total savings.

5                   THE WITNESS: Yes.

6                   CHAIRMAN GOLDWAY: Do you have to do that by  
7 product?

8                   THE WITNESS: We have to accomplish budget  
9 performance, and we monitor performance by operation  
10 so we set expectations for individual operations  
11 within the capabilities of those individual  
12 operations.

13                   CHAIRMAN GOLDWAY: So the operations would  
14 be what?

15                   THE WITNESS: Letter processing, flat  
16 processing. So individual operations have performance  
17 measures, and the results of those individual  
18 operations are collectively measured and bottom line  
19 assessed as to whether or not we're achieving the  
20 budget.

21                   CHAIRMAN GOLDWAY: But not by product?

22                   THE WITNESS: Not within Operations, no.

23                   CHAIRMAN GOLDWAY: How has the flats  
24 processing operation been performing in relationship  
25 to its budget?

1 THE WITNESS: I would have to provide that  
2 detailed information.

3 CHAIRMAN GOLDWAY: Could you do that for us?

4 THE WITNESS: Yes.

5 CHAIRMAN GOLDWAY: Thank you.

6 COMMISSIONER LANGLEY: At what point would  
7 the flats processing performance in relation to its  
8 budget be integrated with other parts of the operation  
9 so that there is this review of meeting performance  
10 levels?

11 THE WITNESS: For our individual operations  
12 we have performance indicators for activity  
13 performance, and those are established.

14 Targets are established, and based on the  
15 performance compared to those targets the  
16 opportunities are identified where in fact we set  
17 expectations for improved performance from the field,  
18 from field managers.

19 COMMISSIONER LANGLEY: And then how are the  
20 times that there is manual processing of flats rather  
21 than going through automation? How is that brought  
22 in? How is that factored in, if at all?

23 THE WITNESS: We do evaluate the utilization  
24 of equipment and drive behavior to improve that  
25 utilization if the opportunity exists.

1           In fact, there is work being performed  
2 manually during the same processing windows that may  
3 reflect an opportunity of capacity that exists on  
4 equipment. Then the expectation is that that capacity  
5 is utilized and the mail is processed in the most  
6 efficient manner possible on the mechanized and  
7 automated equipment.

8           COMMISSIONER LANGLEY: Is there any weight  
9 given to meeting the target?

10          THE WITNESS: Absolutely. Within our  
11 operating plans we balance our cost initiatives with  
12 meeting service expectations.

13          COMMISSIONER LANGLEY: Thank you. Sorry,  
14 Commissioner Blair.

15          COMMISSIONER BLAIR: That's okay. I think  
16 that's an important point that you just brought out,  
17 Commissioner Langley, that there are service standards  
18 incorporated in there, but I'm still not seeing where  
19 an overall budget strategy is involved in the  
20 implementation or establishment of these expectations  
21 from true performance. If performance isn't improved,  
22 what happens? Do budgets increase? Decrease?

23          THE WITNESS: We do not reward poor  
24 performance with lower expectations. No, we do not.  
25 There's an accountability.

1                   COMMISSIONER BLAIR: But it seems that your  
2 intent has been frustrated over the past few years in  
3 trying to make the FSS and the other flats processing  
4 programs more efficient.

5                   I'm trying to reconcile what I see as a  
6 continuing frustration in not being able to achieve --  
7 or are you achieving? I think Commissioner Acton  
8 asked this question. Are you meeting expectations  
9 with your flats processing?

10                  THE WITNESS: I would have to review some  
11 indicators to answer that question, sir.

12                  COMMISSIONER BLAIR: What would be those  
13 indicators?

14                  THE WITNESS: Productivity, performance.

15                  COMMISSIONER BLAIR: If you could provide  
16 that for us, I think that would be helpful as we go  
17 down this difficult path.

18                  CHAIRMAN GOLDWAY: Is it possible that flats  
19 are brought in, or periodicals let's say. Periodicals  
20 are brought into a plant and the automation equipment  
21 has been shut off for one reason or another and the  
22 plant manager determines that given service standard  
23 requirements and the small volume of periodicals that  
24 are presented to him that for that particular instance  
25 it's just simpler to sort them manually?

1                   THE WITNESS:  It's possible that that  
2 occurs.

3                   CHAIRMAN GOLDWAY:  And will that plant  
4 manager then be asked to justify why he's done that  
5 for you, or will it just be part of the noise of the  
6 report because overall his service performance is fine  
7 and overall his cost reductions, hourly reductions,  
8 are fine?  How would you be able to track that  
9 decision?

10                  THE WITNESS:  Madam Chairman, we have  
11 specifically identified that in fact there are  
12 instances and there are locations where what you've  
13 described does occur, mail arriving after the critical  
14 entry time and being worked less efficiently.

15                  We are communicating -- monitoring and  
16 communicating -- that that in fact is not an  
17 expectation that we hold within our responsibilities.  
18 You know, my responsibility is to drive the  
19 expectations.  That is not a behavior that we support,  
20 and we in fact are addressing that and recognizing  
21 that it does occur out there in the field.

22                  CHAIRMAN GOLDWAY:  Have you ever given any  
23 thought to the fact that you invested all this money  
24 and are investing even more in these highly automated  
25 machines but that the volume flows are such that it

1 may not be worth the investment?

2           That seems to be what the OIG is saying;  
3 that you might be better off figuring out some other  
4 low tech ways to deal with this. Has that ever  
5 crossed your mind since there doesn't seem to be  
6 enough volume in the FSS at the moment to justify its  
7 investment? The throughput isn't as fast as you  
8 expected it to be, and there's not enough volume even  
9 if the throughput were faster.

10           THE WITNESS: To generally answer your  
11 question, I would state that we consider all  
12 opportunities when considering how we can improve the  
13 efficiency of our operations.

14           Specifically for the FSS, again I can't  
15 comment on the OIG report and their findings and  
16 whether or not we're in agreement with those findings.  
17 At this time I can't answer to that. The report was  
18 not directed to me, but I will become familiar with  
19 the report.

20           With regard to the drop in volume which you  
21 described, we are redeploying and have modified our  
22 deployment plans for the FSS by redirecting a number  
23 of machines to additional sites to expand the coverage  
24 because of the drop in volume in the original sites  
25 that they were scheduled to be deployed to.

1                   Originally the 100 machines which are in the  
2                   process of being deployed were scheduled for 34  
3                   locations. That's now been increased to 47 locations,  
4                   so the same 100 machines will now be spread to 47  
5                   locations, providing the opportunity for deeper  
6                   penetration in more locations so that the lost  
7                   opportunity from the top in volume from the original  
8                   locations will now be replaced by being able to expand  
9                   it to additional zones and carrier routes to be  
10                  processed on the FSS.

11                  CHAIRMAN GOLDWAY: You didn't think about  
12                  perhaps not taking all 100 machines?

13                  THE WITNESS: It's a contractual issue with  
14                  the investment which was made.

15                  CHAIRMAN GOLDWAY: Do you know if in plants  
16                  currently there are bundles that are being processed  
17                  manually even if the automation bundle sorter  
18                  equipment is running? What would make a plant manager  
19                  choose to do that?

20                  THE WITNESS: Well, one situation may be if  
21                  it is running what operation is running on that  
22                  equipment. Is the operation the same operation that  
23                  may be performed manually simultaneous?

24                  Again, operations. There are prescribed,  
25                  defined processing windows for each operation in order

1 to meet the expectations of the network, the dispatch  
2 schedules for the network, and if there is an  
3 operation scheduled on the equipment there may be  
4 other operations that are performed simultaneous to  
5 that operation so that those dispatches can be met in  
6 order to meet service standards.

7 Now, that doesn't eliminate the possibility  
8 that there may be the wrong decision being made out  
9 there or the wrong behavior out there and mail could  
10 be worked manually. If that's identified, it's  
11 addressed.

12 VICE CHAIRMAN HAMMOND: Madam Chairman,  
13 along with your line of questioning could I ask a  
14 question right now?

15 CHAIRMAN GOLDWAY: By all means. That's  
16 where we're here for.

17 VICE CHAIRMAN HAMMOND: Okay. Mr. Neri,  
18 you've been discussing with the Chairman especially on  
19 this question of manual processing instead of  
20 automation, being on automation equipment, and you  
21 talk about the most efficient processing way.

22 You leave that up to the local plant manager  
23 is basically what I understand your answer to the  
24 Chairman is. I've heard this discussed before that  
25 that's what the Postal Service does is leave it up to

1 the local plant manager, who is supposed to follow the  
2 most efficient processing. That's essentially what  
3 you've said, isn't it?

4 THE WITNESS: The expectation is that the  
5 most efficient processes are utilized within the  
6 operations, and the plant manager is making those  
7 decisions that result in the performance levels that  
8 we expect, but in fact local managers have the  
9 discretion to make the decision when necessary.

10 VICE CHAIRMAN HAMMOND: Okay. So would you  
11 say when you find that they're not following this most  
12 efficient processing way generally it's when they're  
13 manually processing mail that ought to be automated  
14 more likely than not from my understanding, but you  
15 say you deal with it when it comes to your attention.

16 I was wondering. Well, how do you deal with  
17 it? I mean, what's the penalty for getting caught? I  
18 mean, is there training to correct it, or is there a  
19 memo to file? I mean, you say you deal with it. What  
20 do you do to correct the problem?

21 THE WITNESS: Commissioner, it's not my  
22 intent to portray an environment that we don't have  
23 efficient processes out there or managers making the  
24 correct decisions.

25 In fact, the performance level that our

1 managers out there are achieving are exceptional. We  
2 continue to improve productivities across the country.  
3 We continue to operate with fewer employees and match  
4 our work hours, reduce our work hours to the workload  
5 reductions that we've been experiencing since 2006.

6 I described that since 2006 the Postal  
7 Service is operating with about 111,000 fewer  
8 employees, so we are driving efficiencies and our  
9 managers are performing.

10 I was asked specific questions about whether  
11 or not these instances occur. They do occur. I  
12 believe they occur on a very limited basis. Some have  
13 been behavior that have occurred over years in  
14 managers and supervisors within Operations believing  
15 that they were doing the right thing for service in  
16 working this mail within the processing windows, mail  
17 that arrives late.

18 We are educating our managers in fact that  
19 we have operating plans to meet. We want to process  
20 all the mail in the most efficient manner and that in  
21 fact the mail that arrives after critical entry times  
22 we are still meeting service expectations by holding  
23 that mail to work on the automated systems, so it's a  
24 matter of educating and it's a matter of changing  
25 behavior that may occur in some isolated locations.

1           VICE CHAIRMAN HAMMOND: So you don't really  
2 have a problem?

3           CHAIRMAN GOLDWAY: Well, we got an answer to  
4 an interrogatory that said that 30 percent of mail is  
5 handled manually.

6           VICE CHAIRMAN HAMMOND: Yes, but that's not  
7 being incorrectly handled. There's no problem with  
8 that.

9           I mean, I do hear once again that when you  
10 talk about mail arriving late, et cetera, et cetera,  
11 it's usually the mailer's fault. It's not anyone at  
12 the U.S. Postal Service's fault. It's usually the  
13 mailer's fault. Is that correct?

14          THE WITNESS: Commissioner and Madam  
15 Chairman, the statement about 30 percent of the mail  
16 being worked manually, without knowing the specifics  
17 of that interrogatory I do believe that it includes  
18 our manual operations at every post office across the  
19 country so it's not the manual percentages.

20          It's not the manual workload or mail that's  
21 being worked manually within our processing centers.  
22 I believe that that's all of the processes and  
23 accumulated percentage of all of the processes not  
24 only in processing center facilities, but also local  
25 post offices.

1                   VICE CHAIRMAN HAMMOND: So back to my  
2 original question on this. Are you saying that it is  
3 the fault of the mailer or the Postal Service?

4                   THE WITNESS: I don't believe it's anyone's  
5 fault. I believe that it's the result of a practice  
6 that has been occurring over the years, and I believe  
7 that requires both a re-education of -- a continuous  
8 education of -- our employees, our managers and the  
9 education of our mailers as well.

10                  VICE CHAIRMAN HAMMOND: So it's not really  
11 that big of a problem and when it does occur you  
12 re-educate them. That's how you specifically deal  
13 with it. Is that what you're saying?

14                  THE WITNESS: I would say that's accurate.

15                  VICE CHAIRMAN HAMMOND: Okay. Thank you.

16                  CHAIRMAN GOLDWAY: But again, there's no  
17 direction with regard to cost savings specifically  
18 directed by product, so when you have a flat strategy  
19 that you presented to us it doesn't include any  
20 relationship between savings and cost coverage?

21                  THE WITNESS: I believe I described it as  
22 our initiatives identifying cost savings by operation,  
23 and that would be the link to the product.

24                  CHAIRMAN GOLDWAY: To the extent it's linked  
25 to a product.

1 COMMISSIONER BLAIR: Madam Chair?

2 CHAIRMAN GOLDWAY: I think I've gotten as  
3 much information as I can, but if there are more  
4 questions?

5 COMMISSIONER BLAIR: Just a followup on  
6 this. I was looking at a GAO report that came out in  
7 July of 2009, and the GAO report recognized that there  
8 was progress being made with the FSS, but stated that  
9 the future savings may be limited by the Postal  
10 Service's lack of specific cost saving targets, which  
11 we've been discussing up here, and results, which  
12 again we've been discussing, for most of these  
13 actions.

14 Without such information, the Postal Service  
15 is unable to assess the contribution and performance  
16 of each action and focus on those with the greatest  
17 savings potentials. While we were encouraged by the  
18 Postal Service's effort to coordinate with employees,  
19 unions and mailers for more efficient delivery,  
20 continued focus will be needed to help address ongoing  
21 challenges related to declining volumes, technical  
22 issues and financial and operational issues.

23 GAO recommended that cost saving targets and  
24 tracking results for each of the major initiatives,  
25 including FSS, be developed. Did you follow up on

1 those GAO recommendations?

2 THE WITNESS: Yes, Commissioner. In the  
3 last year we have established targets for our FSS  
4 operations, and we are monitoring those targets on a  
5 continuous basis. We communicate through webinars and  
6 teleconferences with our field managers at the  
7 locations where that equipment has been deployed.

8 As we continue to deploy that equipment,  
9 targets such as pieces sent, run time, throughput,  
10 accept rates, DPS percentage for the flat sequence,  
11 sir, have been put in place and are tracked and  
12 reported on and are being utilized as indicators to  
13 drive performance.

14 CHAIRMAN GOLDWAY: But they drive  
15 performance of the machine. They don't drive  
16 performance of the reduced cost of the product on the  
17 machine. There seems to be a disconnect.

18 COMMISSIONER BLAIR: Right. I mean, are  
19 they again tied to any kind of budget?

20 THE WITNESS: Well, they're tied to the  
21 operating budget of our processing operations and the  
22 performance of the machine and cost savings that the  
23 machine is intended on achieving is, in my opinion,  
24 how it's tied to the product.

25 Now, Finance would have to better answer the

1 specific ties there, but I drive operational  
2 performance. I drive cost reduction initiatives in  
3 order to reduce our costs.

4 CHAIRMAN GOLDWAY: It's not a cost reduction  
5 initiative for the operation of the product.

6 COMMISSIONER BLAIR: We're getting just part  
7 of the picture.

8 CHAIRMAN GOLDWAY: Yes, yes.

9 COMMISSIONER BLAIR: And that you are  
10 unable, unwilling but unable to answer the fuller  
11 broader picture that we're asking.

12 COMMISSIONER LANGLEY: But also, if there is  
13 a disconnect and we're looking pretty much just at the  
14 operation of the machine, how does the Postal Service  
15 even develop incentives within its pricing structure  
16 to incentivize action on the part of the mailer when  
17 the focus is really the machine?

18 THE WITNESS: I believe the focus is also  
19 with the mailer, and working with the mailer on they  
20 introducing the product for processing on our  
21 machines. We just issued an optional FSS prep  
22 opportunity through the Federal Register notice, an  
23 opportunity for mailers to make up their mail into  
24 bundles and pallets through the sorts meet level for  
25 the FFS machine which allows mailers to create larger

1 bundles and qualify for carrier route pricing, and be  
2 able to make more pallets that qualify for that  
3 pricing.

4 So, I do believe that we do have initiatives  
5 that provide those opportunities for the mailers, and  
6 that's one example.

7 COMMISSIONER LANGLEY: But if we're looking  
8 at problems and fully utilizing even the AFSM, and  
9 we're not on the FFS, I think what my colleagues have  
10 said is there needs to be more of a retrenchment maybe  
11 so that you're looking at a much broader picture than  
12 just the operation of the machines.

13 THE WITNESS: And our initiatives include  
14 looking at opportunities such as that. AFSM  
15 utilization is an area that we are currently analyzing  
16 based on volumes of funds are our current locations  
17 the best locations for all of our equipment. We are  
18 evaluating the opportunity for redeploying equipment  
19 from one location to another in order to increase our  
20 utilization of that equipment.

21 Examples are sites that may have multiple  
22 pieces of equipment, that we reduce the number at one  
23 site and introduce the equipment at new sites in order  
24 to have that coverage. So we are in fact looking at  
25 those opportunities to increase utilization.

1                   COMMISSIONER LANGLEY: Okay, I appreciate  
2 that response. That actually helps me go into a  
3 question that I have that is very non-contiguous state  
4 and territory-related.

5                   In a response to POIR-3, question 23,  
6 regarding the LOO9, or L009, these are mixed states'  
7 consolidation centers for mixed ADC flats. In the  
8 flat strategy it's mentioned that the numbers would be  
9 reduced from 40 sites to 18, and my understanding is  
10 there is a site in Honolulu as well as Anchorage,  
11 Alaska.

12                   Are there sites in the Virgin Islands and  
13 Puerto Rico as well?

14                   THE WITNESS: Yes. Yes, Commissioner.

15                   COMMISSIONER LANGLEY: Will these sites  
16 continue to have an LOO9, will they continue to be  
17 LOO9 processing sites after consolidation is completed  
18 if it were approved?

19                   THE WITNESS: Yes, they will.

20                   COMMISSIONER LANGLEY: Okay, and will that  
21 impact the consolidation on the U.S. mainland? Will  
22 the consolidation on the U.S. mainland impact delivery  
23 to Hawaii and other non-contiguous areas if there is a  
24 consolidation?

25                   THE WITNESS: The consolidation would have

1 no service impact.

2 COMMISSIONER LANGLEY: So there would be no  
3 service impact --

4 THE WITNESS: Right.

5 COMMISSIONER LANGLEY: -- that the  
6 residents --

7 THE WITNESS: Resulting from the  
8 consolidation, correct.

9 COMMISSIONER LANGLEY: And at what stage is  
10 it? Is there a DAR on this?

11 THE WITNESS: There is no DAR with this  
12 initiative. This initiative is relocating operations  
13 in consolidated locations, and we are -- within the  
14 initiative we have established it at 15 locations of  
15 the 18.

16 COMMISSIONER LANGLEY: Thank you very much.

17 COMMISSIONER ACTON: Mr. Neri, from some of  
18 your discussion it seems like you're dealing with a  
19 couple of important competing priorities. One would  
20 be delivering the mail in a good and timely fashion  
21 that meets service measure requirements, and the other  
22 is trying to cut cost, and sometimes that may be at  
23 odds. Is that a fair characterization of part of your  
24 challenge?

25 THE WITNESS: I would describe it as -- that

1 in fact over time that's been a challenge, and that we  
2 are developing more definitive lines within our  
3 operating environment with critical entry times in our  
4 operating plans and sharing those critical entry time  
5 with mailers so that they have an expectation what is  
6 the time that they must have the mail within our  
7 operations, arriving at our operations so that we can  
8 in fact meet those operating plans, and in fact meet  
9 those service standards.

10 So, I believe that we are evolving and we  
11 are educating both internally and externally so that  
12 those guidelines provide us an opportunity to achieve  
13 both.

14 COMMISSIONER ACTON: Okay. From what I can  
15 glean from it, it seems as if you are trying to  
16 implement some needed standardization of operations  
17 and that part of the problem is that when you have  
18 your local managers working to deliver mail in a  
19 timely way, and occasionally they may be choosing to  
20 deviate from some of those standard operations that  
21 are designed to lower cost, and instead they are doing  
22 what they need to do to move the mail in an  
23 expeditious fashion. Am I grasping that properly?

24 THE WITNESS: There are times where that may  
25 occur.

1                   CHAIRMAN GOLDWAY: You know, I think the  
2 point is that it may be for the individual plant that  
3 the handling of the mail manually turns out for the  
4 plant's operation to be more cost effective for the  
5 plant because of the volumes and the various things  
6 that are on the machine that are running that may not  
7 be compatible with what comes in, and I think there is  
8 a contradiction between the needs of the machine and  
9 the needs of the plant in terms of where the cost  
10 savings are, and I don't think that we have gotten the  
11 nexus to solve that problem.

12                   That seems to me as I have been watching  
13 this problem with standard flats develop over the last  
14 12 years that we haven't -- we haven't quite gotten to  
15 what the real problem is.

16                   COMMISSIONER ACTON: I suppose, Mr. Neri, I  
17 just would like to leave you with the impression that  
18 the reason we have so many questions about this is  
19 that we rarely -- we very rarely have an opportunity  
20 to have this kind of a candid exchange with someone  
21 who is as close to what's happening as this. So we  
22 have a lot of interest in knowing how the Postal  
23 Service is managing the regulatory priorities of  
24 meeting service measures which we've helped or had a  
25 role in establishing as well as the compliance

1 concerns that we have expressed in our annual  
2 determinations with respect to these cost coverages.  
3 So we appreciate your input.

4 I have one last question, and that is, your  
5 flat strategy document indicate that a Lean 6 Sigma  
6 value stream map for periodicals is going to be  
7 complete by August of this year. Is that accurate and  
8 this is on schedule?

9 THE WITNESS: Yes, sir. We expect by the  
10 end of this month to have the periodical process  
11 within the Postal Service mapped, value stream map  
12 from end to end, and if I could describe that it  
13 identifies all of the steps of the process, and then  
14 presents us the opportunity to identify projects that  
15 we could launch for leaving out activities or steps of  
16 that process.

17 COMMISSIONER ACTON: So you anticipate that  
18 that steam map will be developed and available on  
19 schedule later this year, and that it will likely  
20 provide you some hopefully helpful insight on how to  
21 target these concerns more effectively?

22 THE WITNESS: Yes.

23 COMMISSIONER ACTON: Thank you.

24 CHAIRMAN GOLDWAY: But there is no actual  
25 cost saving target with the Lean 6 sigma, no dollar

1 amount, is there, or are there?

2 THE WITNESS: I'm sorry, Madam Chairman.

3 CHAIRMAN GOLDWAY: Are there --

4 THE WITNESS: The initiative which I  
5 described is the first step to identifying  
6 opportunities. It's mapping out the process from end  
7 to end so that then projects could be developed for  
8 leaving out steps of the process.

9 CHAIRMAN GOLDWAY: And the projects would go  
10 through the same development stages, these three  
11 development stages that you described earlier?

12 THE WITNESS: No, it's a different process.  
13 It's a Lean 6 Sigma process which follows a prescribed  
14 process of steps. It's called the Domaic process  
15 where you define the problem. Once the process is  
16 mapped from end to end, and following the steps you  
17 define a potential problem that you want to solve.  
18 Then you measure by collecting data on that process,  
19 you analyze the data, you determine and implement  
20 improvements, and then you put the controls in place  
21 to sustain those improvements.

22 COMMISSIONER ACTON: I think it's well  
23 established that the 6 Sigma approach is a very proven  
24 tool for doing what you're outlining, and we have a  
25 great interest in what you're trying to achieve, so

1 I'm hopeful that you will keep in mind that down the  
2 road we'd like to learn more about this, and in fact  
3 sometime after October 4th we will plan to remind the  
4 Chairman that we might ask the senior management to  
5 come and brief us on how that is progressing.

6 CHAIRMAN GOLDWAY: And it may well be that  
7 that should be something that's submitted in the  
8 annual report to meet our annual compliance  
9 determination.

10 COMMISSIONER LANGLEY: May I ask Mr. Neri on  
11 this Lean 6 Sigma initiative that you're undertaking  
12 now?

13 At what point, if at all, are field  
14 personnel brought into the discussion?

15 THE WITNESS: Commissioner, we have field  
16 personnel involved today with the -- and mapping the  
17 process having input. At this time I would estimate  
18 about 20 individuals across the country at various  
19 locations spread randomly around the country that have  
20 input into effort, and as we identify opportunities  
21 for projects we will also include field individuals on  
22 those project teams.

23 COMMISSIONER LANGLEY: So are these 20  
24 people managers, operations managers or are they at a  
25 different level?

1 THE WITNESS: Support staff, operation  
2 specialists, supervisors within operations.

3 COMMISSIONER LANGLEY: So some of them are  
4 actually within plants?

5 THE WITNESS: Yes, most of them are within  
6 plants.

7 COMMISSIONER LANGLEY: So their  
8 understanding of whether things are going through an  
9 automated process or manual processing is --

10 THE WITNESS: Correct.

11 COMMISSIONER LANGLEY: They are well versed  
12 in that?

13 THE WITNESS: Correct.

14 COMMISSIONER LANGLEY: Thank you.

15 CHAIRMAN GOLDWAY: Vice Chairman Hammond.

16 VICE CHAIRMAN HAMMOND: Thank you. I had  
17 just one more question.

18 Mr. Neri, have you ever designed on your own  
19 or been asked to design by others at the Postal  
20 Service under the managerial processing operation, a  
21 very difficulty position, I understand?

22 When you have worked on such things have you  
23 ever been asked to come up with anything in  
24 consideration of a class or subclass of mail that  
25 could end up driving that mail out of the system

1 because the Postal Service consider it unprofitable,  
2 and it would be much better if the mail were to -- if  
3 that type of mail was simply gone? Have you ever done  
4 anything toward that end?

5 THE WITNESS: No, sir.

6 VICE CHAIRMAN HAMMOND: Okay, thank you.

7 CHAIRMAN GOLDWAY: I think that concludes  
8 the questioning that we have for Witness Neri. There  
9 is nothing further so I would like to reiterate my  
10 fellow Commissioners' comments of appreciating your  
11 testimony here today, and giving you the good news  
12 that you are excused. Thank you very much.

13 THE WITNESS: Thank you.

14 (Witness excused.)

15 CHAIRMAN GOLDWAY: What I would like to do  
16 is take a 10-minute break before we begin with our  
17 next witness, and before I do that I did want to  
18 acknowledge a couple of special guests who are in our  
19 audience today. We are pleased and honored to have  
20 with us today two guests from the National Postal  
21 Agency of Ecuador, which is the postal regulator for  
22 that country. Dr. William Said Reich, and Dr. Byron  
23 Manchilauro. I'm not sure. I'm not pronouncing it,  
24 Manchilauro, Deputy Director, Executive Director and  
25 Deputy Director. Dr. Said and Dr. Lauro are visiting

1 the Commission for three days this week to learn more  
2 about the role of our Commission and the U.S. Postal  
3 System. They represent a regulator that is only two  
4 years old, and one of the only independent postal  
5 regulators in Latin America. Please join me in  
6 welcoming them here today. They have been able to  
7 witness our hearings firsthand and I hope they will be  
8 able to stay for some more of the hearings later this  
9 morning. Thank you very much for coming.

10 And with that we will reconvene at 11:10.

11 (Whereupon, a short recess was taken.)

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1                   CHAIRMAN GOLDWAY: We will try and  
2 reconvene. Before we begin with our witness, I'd like  
3 to make a comment here. This inaugural Exigent Rate  
4 case has required adaptability by all participants,  
5 and this hearing is a prime example.

6                   As I noted previously, we appreciate the  
7 questions that parties have submitted in this  
8 proceeding, and we intend to issue additional CHIRs as  
9 the hearings conclude.

10                   We also appreciate the Postal Service's  
11 prompt responses to prior CHIRs, and the candor of  
12 witnesses in responding to our questions.

13                   Following yesterday's hearing, parties to  
14 this proceeding filed pleadings requesting the  
15 Commission to address two questions to the Postal  
16 Service concerning statements made by witness Masse  
17 during the hearing. The request, filed by the Parcel  
18 Shippers Association, and jointly by the Alliance of  
19 Nonprofit Mailers and the Magazine Publishers of  
20 America, are in the nature of follow-ups and seek  
21 clarification of witness Masse's statements.

22                   One request seeks details of the projected  
23 \$115 billion deficit for the period Fiscal 2009 to  
24 Fiscal 2020. The other seeks data concerning the May  
25 2009 price increase for non-flat machinable parcels.



1 DIRECT EXAMINATION

2 BY MR. RUBIN:

3 Q Was this document prepared by you or under  
4 your supervision?

5 A It was.

6 Q Does it contain the errata that were filed  
7 on August 10, 2010?

8 A Yes, it does.

9 Q If you were to present this statement orally  
10 here today, would this be your statement?

11 A Yes, it would.

12 Q There are also, associated with your  
13 statement, five sets of pricing worksheets?

14 A Yes.

15 Q Are you prepared to sponsor those  
16 worksheets?

17 A I am.

18 MR. RUBIN: So we will present the two  
19 copies of your statement to the reporter, and we ask  
20 that the statement and its associated worksheet be  
21 entered into the record of this proceeding.

22 CHAIRMAN GOLDWAY: Thank you. Counsel,  
23 please provide the reporter with two copies of the  
24 statement of James M. Kiefer. The statement and its  
25 associated library references are received into

Heritage Reporting Corporation  
(202) 628-4888

1 evidence. However, as is our practice, it will not be  
2 transcribed.

3 (The document referred to was  
4 marked for identification and  
5 was received in evidence.)

6 Dr. Kiefer has been identified as a Postal  
7 Service representative prepared to attest to the  
8 accuracy of answers to certain Presiding Officer  
9 Information Requests; and, if necessary, to respond to  
10 questions about those answers. A packet has been  
11 prepared that includes Dr. Kiefer's answers.

12 Dr. Kiefer, can you confirm that the answers  
13 contained in that packet are accurate, to the best of  
14 your knowledge?

15 THE WITNESS: Yes, I can.

16 CHAIRMAN GOLDWAY: Counsel, will you please  
17 provide the reporter with two copies of the answers of  
18 Dr. Kiefer to Presiding Officer Information Request?

19 MR. RUBIN: Yes, we will.

20 CHAIRMAN GOLDWAY: His answers are received  
21 into evidence, and are to be transcribed.

22 (The documents referred to,  
23 previously identified, were  
24 received in evidence.)

25 //

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pgs-

**DOCKET NO. R2010-4**  
**JAMES KIEFER RESPONSES TO**  
**PRESIDING OFFICER'S INFORMATION REQUESTS**

RECEIVED

2010 AUG 13 A 11:34

POSTAL REGULATORY  
COMMISSION  
OFFICE OF THE SECRETARY

<u>POIR</u>	<u>Question</u>
POIR No. 1	2, 3a, 3b, 6-10, 12
POIR No. 2	1-14
POIR No. 3	1-19
POIR No. 4	1, 6-8

Case No. Official Exhibit No.

R2010-4

Disposition: Identified   
Rejected  Received

IN THE MATTER OF:

Exigent Request 2010

Date: Witness: Reporter:

Kiefer

No. Pages:

77

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

2. Please refer to the Exigent Request of the United States Postal Service, Tables 1 and 2, at page 13.

a. In Table 1, Available Unused Price Adjustment Authority, By Mail Class, please confirm that for First-Class Mail, the "Unused Authority (%)" of 0.030 should be 0.044 (0.030 [R2009-2] + 0.014 [R2008-1]). If not confirmed, please explain.

b. In Table 2, Price Adjustment Authority By Mail Class, please confirm that for First-Class Mail, the "Price Adjustment Authority (%)" of 0.608 should be 0.622 (0.578 + 0.044). If not confirmed, please explain.

**RESPONSE:**

a.-b. Confirmed, as correctly reflected in Table 1 on page 9 of the Statement of James M. Kiefer.

**RESPONSE OF JAMES KIEFER  
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3. Please refer to Library Reference USPS-R2010-4/1, Excel file Inbound FCMI Worksheets R2010-4.xls, and worksheet tab Inbound FCMI Rates, which references the following terminal dues rates:

<b>Base Terminal Dues in SDRs - UPU</b>			
<b>(Inbound First-Class Mail International/Surface and Air Letters)</b>			
	<b>CY</b>	<b>CY</b>	<b>Percent</b>
	<b>2010</b>	<b>2011</b>	<b>Change</b>
<b>Per Item</b>	0.171	0.169	-1.17%
<b>Per Kilogram</b>	1.731	1.709	-1.27%

The Postal Service cites UPU Circular 155 (July 6, 2009) and UPU Circular 142 (July 5, 2010) for these CY 2010 and CY 2011 inbound terminal dues "base" rates for target system countries, respectively.

- a. For CY 2010 and CY 2011, please explain why the Postal Service only used the UPU inbound terminal dues "base" rates for target system countries, rather than the CY 2010 and CY 2011 "provisional" terminal dues rates referenced in the circulars of 0.174 SDR per item and 1.760 SDR per kilogram, and 0.173 SDR per item and 1.747 SDR per kilogram, respectively, that include the quality of service link.
- b. For CY 2010 and CY 2011, please explain why the Postal Service only used the UPU inbound terminal dues rates paid by target system countries rather than calculating a weighted average rate reflecting the terminal dues rates paid by countries in the target system that include the quality of service link and the CY 2010 and CY 2011 terminal dues rates paid by countries in the transition system of 0.155 SDR per item and 1.562 SDR per kilogram and 0.159 SDR per item and 1.610 SDR per kilogram, respectively.
- c. For FY 2011, please provide the estimated volumes and revenues for inbound letter post from Canada. Please show all calculations used to derive the estimated volumes and revenues in electronic form.

**RESPONSE:**

- a) The Postal Service used the Universal Postal Union (UPU) base terminal dues rates in Inbound FCMI Worksheet R2010-4.xls because the applicable UPU base terminal dues rates were used in analogous worksheets for USPS-R2008-1/NP1 and USPS-R2009-2/1. As the final

**RESPONSE OF JAMES KIEFER  
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2009 quality results have not yet been published by the UPU, no reliable assumptions are available to use for the actual FY 2009 baseline and subsequent roll forwards for FY 2011.

- b) The Postal Service used the UPU target system terminal dues to be consistent with the methodology used in the analogous worksheets for USPS-R2008-1/NP1 and USPS-R2009-2/1.
- c. Answered by Mr. Masse.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

6. Please refer to "Standard\_Mail\_Worksheets\_R2010-4.xls" which contains the price increase calculations for Standard Mail. Cells I8 and I9 in Tab "HDSatCR IM & Move Update Adj" calculate Full Year IM Full Service Volume for Commercial Former ECR Flats and Nonprofit Former ECR Flats.

- a. Please confirm that Saturation Flats were excluded from these calculations. If confirmed, please provide an explanation and a revised version, if necessary.
- b. Do the IM Penetration rates in cells G8 and G9 apply to Saturation flats? If not, please provide the appropriate penetration rates.

**RESPONSE:**

- a. The Postal Service confirms that Saturation Flats were excluded from the above mentioned calculations. Saturation Flats are not eligible to participate in the Full Service IMb program (see MCS section 1210.4). Saturation flats are typically prepared in walk-sequenced bundles and are dropshipped either to the DSCF or DDU. They therefore are ready to be taken directly to the street without any Postal Service machine processing. It is also expected that Saturation flats will not be placed on the Flats Sequencing System (FSS) even in FSS zones. For these reasons, participating in the Full Service IMb program was deemed to be of little advantage to the Postal Service or to mailers of Saturation flats.
- b. The IM Penetration rates in cells G8 and G9 do not apply to Saturation flats. See the explanation in part (a), above.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

7. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service at page 34 line 13, which states "the discount for 5-digit parcels produces a passthrough of 104.4 percent." Please confirm that the passthrough referred to in the above statement should be 88.1 percent (36.4/41.3).

**RESPONSE:**

Confirmed.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

8. Please confirm that the discount in the request for 5-digit irregular parcels exceeds avoided cost. If confirmed, please discuss how the proposed discount complies with the workshare discount requirements in section 3622(e) of title 39.

**RESPONSE:**

The Postal Service confirms that the discount for 5-digit irregular parcels (\$0.270) exceeds avoided cost (\$0.182). The resulting passthrough is 148.4 percent ( $0.270/0.182$ ). There are two factors that contribute to this passthrough, which can be justified under Section 3622(e)(2)(D).

First, we set the 5-digit irregular parcel price equal to the price of 5-digit machinable parcels because parcels sorted to 5-digit ZIP Codes have the same costs and follow the same mail processing and delivery path, regardless of their classification as machinable or irregular. Equal prices better align the pricing with cost causation, and encourage mailers of irregular parcels to sort to 5 digits, reducing the amount of costly manual handling these parcels may receive. (See Statement of James M. Kiefer on Behalf of the United States Postal Service, page 61, lines 10-16.)

Second, we gave larger increases to SCF-presorted irregular parcels to discourage inefficient mailer behavior. The Postal Service has observed that some mailers have been entering potentially machinable parcels as irregular parcels at destination Sectional Center Facilities (DSCFs). As pointed out in the Statement of Mr. Kiefer (at p. 34), the Postal Service believes that the most efficient path for machinable Standard Mail parcels is to get mailers to enter them in Network Distribution Center (NDC) containers at the destination NDCs, where they can be processed to 5-digits using efficient parcel sorting machines.

**RESPONSE OF JAMES KIEFER  
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Entering them as SCF-presorted irregular parcels at DSCFs would require these parcels to undergo less efficient manual or machine sorting. To encourage all potentially machinable parcels to be sorted at the NDCs, larger increases were given to the prices of SCF-presorted irregular parcels. These reasons show that the larger passthrough is needed to ensure efficient mail processing, consistent with section 3622(e)(2)(D).

**RESPONSE OF JAMES KIEFER  
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9. Please refer to Excel file, [http://pe.usps.gov/prices/Prices\\_Jan2011.xls](http://pe.usps.gov/prices/Prices_Jan2011.xls), worksheet AMS where the Postal Service lists proposed prices for the Address Management Services and Customized Postage products. For three mail categories, Address Sequencing Service (line 5), 99 Percent Accuracy Method (lines 124-126), and Customized Postage (lines 153-157), the Postal Service identifies proposed prices, but does not include the mail categories in its Special Services price adjustment worksheets. See Library Reference USPS-R2010-4/5, Excel file "Special Services Worksheets R2010-4." Please file a revised Excel file "Special Services Worksheets R2010-4" that includes the above three mail categories.

**RESPONSE:**

See the file POIR1.Qu9.10.xls associated with this response. In that file new worksheets have been added for Address Sequencing service, 99 Percent Accuracy Method, and Customized Postage. Second, the "Other Income" worksheet has been revised to remove the reference to Sequencing of Mailing Lists, since Address Sequencing now has its own worksheet. Third, the CDS worksheet has been revised to remove numbers reflecting the electronic portion of Address Sequencing, which had been erroneously included with CDS. Fourth, POIR1.Qu9.10.xls contains updated volume and revenue data for all of the AMS products, and the correction of an error in the volumes presented on the "Other Income" worksheet for Correction of Mailing Lists and Address Changes to Election Boards. Finally, for the AMS products (starting with worksheet "AIS Viewer," the volumes and revenues presented cover the period from the 3<sup>rd</sup> quarter of FY 2009 through the 2<sup>nd</sup> quarter of FY 2010 (replacing the data originally filed, which covered the period from the 2<sup>nd</sup> quarter of FY 2009 through the 1<sup>st</sup> quarter of FY 2010).

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

10. Please refer to Library Reference USPS-R2010-4/5, Excel file "Special Services Worksheets R2010-4," worksheet "Stamped Envelopes," which provides the price percentage increase calculations for Stamped Envelopes. In Docket No. MC2010-23, the Commission approved the Postal Service's request to add shipping charges for Personalized Stamped Envelopes to the Mail Classification Schedule as a part of the Stamped Envelope service. However, the Postal Service's price adjustment Special Services worksheets do not include shipping charges for Personalized Stamped Envelopes. Please file a revised Excel file that includes shipping charges for Personalized Stamped Envelopes.

**RESPONSE:**

See the file "POIR1.Qu9.10.xls. The shipping charges for Personalized Stamped Envelopes have been added to the "Stamped Envelopes" worksheet.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

12. Please refer to Attachments 10-11 to the Statement of Stephen J. Masse on Behalf of the United States Postal Service, which estimate the contribution for each mail class for FY 2011 Before Rates and FY 2011 After Rates (January 2, 2011 Implementation). For the Stamped Cards service, the attachments project cost coverages of 21.58 percent and 21.87 percent, respectively. Please also refer to the FY 2009 ACD at 104, which discusses the cost coverage for Stamped Cards. Please explain why the Postal Service did not propose to increase prices for Stamped Cards.

**RESPONSE:**

See the Statement of James M. Kiefer at 51. Additional explanation will be provided in response to POIR No. 2, Question 14.

**RESPONSE OF JAMES M. KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 2**

1. Refer to USPS-R2010-4/1, "FirstClassMail\_Worksheets\_R2010-4.xls" tab 'Single-Piece'. Please confirm that the 0.917 value entered as the new price for Flats First-Ounces (cell G22) should be 0.92 instead. Please revise the worksheet and all other materials that reference the resulting calculated percentage change in rates.

**RESPONSE:**

Confirmed. The number in Cell G22 in the above referenced worksheet should be \$0.92 instead of \$0.917. Please see the spreadsheet POIR.2.Q.1..8.10.xls filed with this response which includes the revisions reflecting the responses to this question and questions 8 and 10. The changes are highlighted in yellow . As a result of these changes the Pricing Statement filed by James M. Kiefer should also change in the following areas.

Page 9, Table 1, row titled "First-Class Mail", Exigent Adjustment changes from 4.795 to 4.901 and Total Price Adjustment changes from 5.417 to 5.523.

Page 10, Table 2, First-Class Mail Price Change (percent), changes from 5.417 to 5.523 and Flats Price Change (percent), changes from 6.079 to 6.256.

Page 12, Table 3, Percent Changes: Single-Piece Letters/Postcards changes from 4.7 to 4.8, Presort Letters/Postcards changes from 5.9 to 6.0, Flats, changes from 6.1 to 6.3.

Page 14, Line 6, 5.423 percent changes to 5.523 percent.

Page 21, Line 3, 6.1 percent changes to 6.3 percent.

Finally, in Table 3 of the Request, 5.417 changes to 5.523.

Formal errata to Dr. Kiefer's Statement will be filed shortly.

Revised July 29, 2010

**RESPONSE OF JAMES M. KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 2**

2. In the calculation of the percentage changes in rates for each class, the Postal Service indicates that it uses billing determinants for a hybrid year consisting of the last two quarters of FY 2009 and the first two quarters of FY 2010.
- a. For each class of mail, please provide spreadsheets containing the hybrid year billing determinants. The spreadsheets should show the quarterly billing determinants used as inputs and the calculation of the total volumes for the hybrid year as the sum of the inputs. The inputs should refer to (and be consistent with) documents previously filed with the Commission. If adjustments are made, please explain them fully.
  - b. Please also provide the source (e.g., Mail Characteristics Study) of the data underlying the First-Class Mail parcel volumes by presort level, ounce increment and indicia ("Retail" vs. "Commercial" single-piece) presented in USPS-R2010-4/1, "FirstClassMail\_Worksheets\_R2010-4.xls" tab "Hybrid Billing Determinants" rows 53-96.
  - c. Please confirm that the volume of QBRM letters first ounces used in the percentage change calculations reflects the revised FY2010 Quarter 2 Billing Determinants filed by the Postal Service on July 16, 2010. If not, please incorporate the revision into the responses.

**RESPONSE:**

(a) The spreadsheets for each class of mail are filed with this response as a zip file, POIR.2.Q.2.zip. Any adjustments are described below.

**First-Class Mail**

There were no adjustments made to First-Class Mail hybrid year billing determinants.

**Standard Mail**

The workbook Standard Mail BD Data—2009Q3-2010Q2.xls shows the billing determinants of the four quarters as filed. The billing determinants of these four quarters were summed to get the data used for the hybrid year billing

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**RESPONSE OF JAMES M. KIEFER  
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determinants. This workbook also shows the allocation of the NSA volumes into the billing determinants for each of the four quarters. The NSA volumes for each of the four quarters were summed to get the total NSA volumes for the hybrid year. The NSA total volumes were then added to the hybrid year billing determinants data.

The workbook Master Standard BDs 2009Q3-2010Q2—MCS—WP.xls shows the hybrid year billing determinants using the data in workbook Standard Mail BD Data – 2009Q3-2010Q2.xls. The workbook also shows the hybrid year billing determinants split between “before rate change” and “after rate change.”

The workbook STD BD-LFP Crosswalk-FY09Q3-FY10Q2.xls, as filed July 6, 2010, shows the hybrid year billing determinants for Regular Letters, Flats, and Parcels from workbook Master Standard BDs 2009Q3-2010Q2—MCS—WP.xls, but in a different format. The workbook also shows the adjustments for parcel migration distributions; these adjustments are explained in the Preface, filed July 6, 2010.

The workbook STD BD-HDSatCR Crosswalk-FY09Q3-FY10Q2.xls shows the hybrid year billing determinants for High Density, Saturation, and Carrier Route Letters, Flats, and Parcels from workbook Master Standard BDs 2009Q3-2010Q2—MCS—WP.xls, but in a different format.

The workbook Standard Mail Worksheets R2010-4.xls, filed July 6, 2010, shows the hybrid year billing determinants from the workbooks STD BD-LFP Crosswalk-FY09Q3-FY10Q2.xls and STD BD-HDSatCR Crosswalk-FY09Q3-FY10Q2.xls. IM Program Incentive adjustments and Move Update adjustments

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**RESPONSE OF JAMES M. KIEFER  
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were made, as explained in the Preface. NFM migration adjustments were also made in this workbook; these adjustments are explained in the Preface.

**Periodicals**

There were no adjustments made to the Periodicals hybrid year billing determinants. The hybrid year total volume was calculated by summing Q3 2009, Q4 2009, Q1 2010 and Q2 2010 volumes.

**Package Services**

i. **Single-Piece Parcel Post**

There were no adjustments made to Single-Piece Parcel Post hybrid year billing determinants.

ii. **Single-Piece Bound Printed Matter Flats**

File 09Q3-10Q2 Billing Determinants—Single-Piece Bound Printed Matter Flats sums included in each cell from E43 through K41 are not correct. The cells in row 23 were excluded in error. However, this sum is not used elsewhere in the workpaper. The numbers that have changed are highlighted in yellow.

There were no adjustments made to Bound Printed Matter hybrid year billing determinants for presort flats.

iii. **Single-Piece Bound Printed Matter Parcels**

File 09Q3-10Q2 Billing Determinants—Single-Piece Bound Printed Matter Parcels sums included in each cell from E43 through K41 are not correct. The

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cells in row 23 were excluded in error. However, this sum is not used elsewhere in the workpaper. The numbers that have changed are highlighted in yellow.

There were no adjustments made to Bound Printed Matter hybrid year billing determinants for presort parcels.

**iv. Media Mail and Library Mail**

There were no adjustments made to Media Mail and Library Mail hybrid year billing determinants.

**Special Services**

The original Special Services Billing Determinants used to develop USPS-R2010-4/5 were derived by taking the 2009 annual billing determinants and subtracting the first and second quarters of FY 2009, then adding the first and second quarters from FY 2010. The workbook filed with this response, adding the four quarters together as requested, produced four types of products and services: (1) those that had no change in total volumes and revenues included in the original USPS-R2010-4/5, (2) those that had a very small change due to rounding, (3) those that corrected an incorrect average revenue so that volume could be accurately derived from a total revenue, and (4) those that corrected a service-specific error.

The following worksheets have no changes:

"Certificates of Mailing"

"Certified Mail"

"Insurance"

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**"Merchandise Return" (Merchandise Return Service Volumes)**

**"PAL" Parcel Airlift**

**"Premium Stamped Stationery"**

**"Premium Stamped Cards"**

**"Registered Mail"**

**"Return Receipts"**

**"Scheduled Pickup"**

**"Shipper-Paid Forwarding"**

**"Other Income"**

**"Per Mailing App" (Periodicals Applications)**

**The following worksheets have changes due to rounding:**

**"Bulk Parcel Return Service"**

**"Bulk Parcel Accounting Fee"**

**"Business Reply Mail"**

**"Media Mail Presort Permits"**

**"Restricted Delivery"**

**"Standard Mail Weighted Fee"**

**"Signature Confirmation"**

**The following worksheets have changes in the volume because an incorrect average unit revenue had originally been used to calculate the volume.**

**"Bulk Parcel Return Permits"**

**"First Class Presort Permits"**

**"Merchandise Return Acctg Fee"**

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**RESPONSE OF JAMES M. KIEFER  
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"Merchandise Return Permits"

"Parcel Return Serv Permits"

"Parcel Return Serv Acct Fee"

"Parcel Select Permits"

"Std Bulk Permit"

The following worksheets corrected service-specific issues:

"Address Correction Service" – corrects transactions for Electronic ACS for First-Class Mail.

"ICOA" (Change of Address Credit Card Authentication) – corrects an understated volume and revenue that were reported in the Hybrid Billing Determinants that were originally submitted.

"COD" – Corrects an error in the calculation of the "Revenues from the Fees", which increases the revenue by \$38,649.

"Delivery Confirmation" – Corrects USPS volume, USPS volume is not used to calculate price increases so there is no impact.

"Stamped Cards" – Due to data errors for three of the 4 quarters in the hybrid billing determinants, the Postal Service believes that the best data to report for this product is the corrected FY 2009 annual billing determinant for Stamped Cards. The rationale for why the Postal Service believes these values to be correct is presented in the responses to POIR 1, Question 12 and POIR 2, Question 14.

"Confirm" – Corrects the quarterly billing determinants to reflect a revision that was provided at the end of the year.

Revised July 29, 2010

**RESPONSE OF JAMES M. KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 2**

**"Money Orders" – The Billing Determinants for the first quarter of 2009 were derived with a formula that contained an error that caused the revenue and volume for that quarter to be incorrect for all three types of Money Orders and the inquiry fees. This error is corrected.**

**"PO Boxes" – The only adjustment made for PO Boxes was subtracting out the box volumes that were moved from Market Dominant to Competitive in Docket No. MC2010-20. This adjustment is shown starting on line 105 in tab "PO Boxes."**

**"Stamped Envelopes" – Corrects double counting for FY10, quarter 1 for volumes and revenues from the premium features for the personalized stamped envelopes.**

**"Special Handling" – corrects volumes for Package Services lines that were based on unintentionally hard coded volumes in the Quarterly Billing Determinants that have been filed with the Commission.**

**(b) Hybrid Billing Determinants for First-Class Mail include two additional worksheets in the end: 'SP Parcels by Ind, Wt. Qtr' and 'Presort Parcels by Wt Incr.' These two sheets provide the additional data and the source for this data.**

**(c) Confirmed.**

RESPONSE OF JAMES M. KIEFER TO QUESTION 3 OF  
PRESIDING OFFICER'S INFORMATION REQUEST NO. 2,  
AS REVISED AUGUST 10, 2010

3. Refer to USPS-R2010-4/1, "First-Class Mail Preface R2010-4.doc" at pages 2-3, "Standard Mail Preface R2010-4.doc" and "Periodicals Preface R2010-4.doc" at pages 2-3, which state that the percentage usage of Full-Service IMb for March 2010 is used as a proxy for the annual percentage. The rationale given is that the upward trend in the percentage usage would cause the actual average percentage usage to underestimate the full-year percentage. Please define the conditions (e.g., the length of time after implementation and/or the slowing of initial growth) that will determine when the Postal Service believes it will be appropriate to use the actual previous four quarters of billing Determinants Volume for Full-Service IMb to calculate percentage changes in rates.

**RESPONSE:**

At the present time, it is challenging to project Full Service IMb usage in the mail classes in which the Full Service IMb program is available. The Postal Service's approach in this docket is discussed in the prefaces to the worksheets as follows: on pages 2-3 of the First-Class Mail preface (USPS-R2010-4/1), pages 5-6 of the Standard Mail preface (USPS-R2010-4/2), and pages 2-3 of the Periodicals preface (USPS-R2010-4/3). Given that the discounts for use of the Full Service IMb option became effective only on November 29, 2009, and taking into consideration that usage requires up-front planning and investment, it is not surprising that the actual usage figures are trending upward and have not leveled off. Adoption of new technologies takes time, especially in the current economic environment.

The Postal Service expects the upward trend in usage to continue at least until May 2011, when the use of either the Basic or Full Service IMb option will be required to receive automation prices. The possibility of using a full year of data to project future Full Service IMb usage will be considered then. On the other hand, as mailer adoption of the Full Service IMb option is likely to continue its upward trend, the Postal Service

RESPONSE OF JAMES M. KIEFER TO QUESTION 3 OF  
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may determine not to use a full year, fixed percentage of volume to calculate future usage until later in the adoption curve, when usage is more predictable and has leveled off.

**RESPONSE OF JAMES KIEFER TO  
PRESIDING OFFICER'S INFORMATION REQUEST NO. 2, QUESTION 4**

4. Refer to USPS-R2010-4/1, "First-Class Mail Preface R2010-4.doc" at page 3 and "FirstClassMail\_Worksheets\_R2010-4.xls" tab 'Move Update Adjustment'. The number of First-Class mailings paying the Move Update Assessment Charge in FY 2010 Q2 is divided by the Presort First-Class Mail (letters and cards) volume for the same period, producing a ratio of mailings to volume. This percentage is then multiplied by the hybrid year Presort First-Class Mail volume (letters, flats, and cards) "to estimate total First-Class Mail volume that would pay the assessment charge for the full-year period."
- a. Multiplying the quarterly ratio of mailings to volume (cell C7) by annual volume (cell C8) produces an estimate of the annual number of mailings subject to the Move Update Assessment Charge, not the number of pieces. Please revise the calculations to incorporate the factor (assessed pieces per assessed mailing) necessary to estimate the volume of assessed pieces, as opposed to the volume of assessed mailings.
  - b. Please provide the source data for the Q2 First-Class mailings that were tested for PBV Move Update Compliance Assessment. The data should provide sufficient details about each PBV-tested mailing to enable the reproduction of the number of assessed pieces given the current (30 percent) and proposed (25 percent) tolerance levels. At the minimum, for each tested mailing, the data should include the number of pieces, the number of pieces sampled, the number of addresses in the sample with address changes on file, and the number of such addresses in the sample that were not updated. Please also provide the same data for Standard Mail.
  - c. Using the actual volumes and failure rates of Move Update PBV Assessments, please revise the calculation of percentage changes in rates for First-Class Mail and Standard Mail. The calculations should reflect two categories of volumes for Move Update Assessment Charges, (1) pieces subject to the charge at the current tolerance level; and (2) the pieces that are not subject to the charge at the current tolerance level, but are subject to the charge at the proposed tolerance level. As with other rate change calculations (e.g., parcel classification changes), no assumptions should be made about changes in mailer behavior in response to the proposed classification changes.

**RESPONSE:**

- a. Please see POIR2.Q.4ab.xls, filed with this response. The volume of assessed pieces is shown in worksheet "Summary", cell I10.

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- b. The source data for both First-Class Mail and Standard Mail are provided in POIR2.Q.4ab.xls, worksheets "Detail< 70%" and "Detail >=70% but <75%". Note that the Postal Service does not have the number of pieces, the number of pieces sampled, the number of addresses in the sample with address changes on file, and the number of such addresses in the sample for mailings in the 70 to 75 percent category. Instead the spreadsheet calculates the average assessment for mailings in the 65 to 70 percent category, and assumes that assessment amount would apply to the mailings in the 70 to 75 percent category. See cells P1 through T6 in worksheet "Detail >=70% but <=75%".
- c. Please see POIR2.Q.4c.FCM70.xls, POIR2.Q.4c.FCM75.xls, POIR2.Q.4c.STD70.xls, and POIR2.Q.4c.STD75.xls, filed with this response. The first two workbooks calculate the percent changes for First-Class Mail using the 70 and 75 percent thresholds, respectively. These two workbooks supplement the file POIR.2.Q.1.8.10.xls filed on July 28, 2010. They also add a new row 34 in "Presort Ltrs & Crds", to include the previously omitted move update assessment in the calculation of revenue and percent changes for Presort Letters and Cards. The last two workbooks calculate the percent changes for Standard Mail using the 70 and 75 percent thresholds, respectively.

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5. Refer to the Statement of James M. Kiefer at 22-23, where he states that First-Class Mail single-piece parcels that are the residual of a presorted mailing or that use permit imprint, IBI meter, or PC Postage would be eligible for the proposed commercial single-piece prices.

- a. Please confirm that the use of one of the three named payment methods is the only requirement for eligibility for commercial single-piece rates (assuming the parcel in question would otherwise qualify for retail single-piece parcel rates). If not, please explain.
- b. Please describe the market differences and similarities between the parcels that would qualify for (1) retail single-piece parcel rates; (2) commercial single-piece parcel rates; and (3) presorted parcel rates. Please provide citations to qualitative and quantitative support, where available.
- c. Please describe the cost differences and similarities between the parcels that would qualify for (1) retail single-piece parcel rates; (2) commercial single-piece parcel rates; and (3) presorted parcel rates. Please provide citations to qualitative and quantitative support, where available.
- d. Please provide a discussion of how the proposed classification change helps to achieve the Objectives of § 3622(b) and properly takes into consideration the Factors of § 3622(c).

**RESPONSE:**

As requested, the Postal Service is providing information about market and cost characteristics (as well as the different payment methods used by customers) for retail single-piece parcels, presort parcels, and the proposed commercial single piece parcels categories. The following response is not intended to imply that the differences described below are statutory prerequisites guiding the decision of the Postal Service to create separate price categories for retail and commercial parcels.

- a. Confirmed.
- b. First-Class Mail parcel mailers who do not use permit imprint, IBI meter, or PC postage are mostly individual mailers. These mailers typically use

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stamps and postage validation imprinter (PVI) indicia because they only occasionally mail a parcel-shaped piece. They also typically use the Post Office window to weigh, price, and pay for the mail piece. IBI and PC postage mailers are typically small to large business customers, and permit imprint customers typically are large fulfillment mailers. These mailers weigh, price, and pay postage without the assistance of postal personnel. Presort parcel mailers are typically large fulfillment mailers: 95 percent of Presort parcels were submitted with a permit imprint in FY2009; the other 5 percent were metered and stamped. Presort mailers are required to meet the minimum of 500 pieces per mailing.

- c. The cost differences between First-Class Mail single-piece and presorted parcels are routinely filed as part of the Annual Compliance Report. The attributable cost per piece for Single-Piece parcels was \$1.89 in FY2009 while the attributable cost for presorted parcels was approximately \$1.60. While the Postal Service has not studied the cost differences between Retail and Commercial single-piece parcels, cost differences are likely because retail parcels, unlike commercial parcels, are typically weighed and priced at the retail window where the postage is affixed. Almost 75 percent of retail parcels have PVI indicia that are affixed by the retail clerk. Source: "First Class and Standard Mail WGTI 2009.xls" in USPS-FY09-14 in Docket No. ACR2009. Stamped parcels in many cases are brought to the window for weight and pricing verification.

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- d. This classification change promotes the Postal Service's pricing flexibility (objective 4) and allows it to maximize the incentives to reduce costs and increase efficiency (objective 1). The change helps maintain a just and reasonable schedule for rates and classifications (Objective 8). This classification change meets the requirement laid out in factor 5 to take into account the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service. Also, pricing flexibility to encourage increased mail volume and operational efficiency (factor 7) and the need to increase efficiency and reduce costs to maintain high quality postal services (factor 12) are both supported by this classification change. Having a separate commercial pricing option can further influence customers' choices regarding the entry channel that is most convenient and efficient for the customers and the Postal Service (factor 7 and objective 1).

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6. In explaining its proposal for above average increases in First-Class Mail presort flats rates, the Postal Service cites the October 2008 correction of an error in the flats model. It asserts that the correction "caused the Postal Service and the Commission to realize that presort flats were underpriced compared to single-piece flats. Since that time, the Postal Service has been raising the presort flats prices at above average rates to restore the appropriate pricing relationship. This price adjustment continues that practice." Statement of James M. Kiefer at 21. The table below presents information about single-piece flats, nonautomation presort flats, and automation Mixed ADC flats. As the two least-workshared categories of presort flats, each represents the closest presorted rate to the single-piece rate. The table presents the changes in avoidable unit costs for these categories that resulted from the correction in question (Docket No. RM2008-2, Proposal 8), and the effects of both the Docket No. R2009-2 and instant rate adjustments on the differences between the single-piece flats rate and the first tier of presort flats rates.

	Effect of Correction on <u>Unit Cost</u> (1)	R2008-1 <u>Price</u> (2)	R2009-2 <u>Price</u> (3)	Proposed <u>Price</u> (4)
Single-Piece	0.00	83.0	88.0	92.0
Nonauto Presort	-7.38	72.7	75.7	86.6
Difference from SP	7.38	10.3	12.3	5.4
Mixed ADC Auto Presort	-3.26	70.2	72.5	80.0
Difference from SP	3.26	12.8	15.5	12.0

Sources: Docket No. RM2008-2 Order No. 115 at 41 (Table IX-1), PRC-R2009-2-LR1, and USPS-R2010-4/1.

The Docket No. RM2008-2 correction altered the modeled unit costs of presort flats resulting in changes to the intra-presort cost differences. However, it did not affect the overall cost difference between total single-piece flats and total presort flats. The effect that the correction did have on the relationship between presort and single-piece flats was to increase the cost differences between single-piece flats and the least-workshared categories of presort flats.

Given the absence of a change in the average costs and the increase in cost differences at the margin between single-piece and presort flats, the supposition that presort flats are underpriced compared to single-piece flats may be problematic. In the only price adjustment that occurred after the correction (Docket No. R2009-2), the Postal Service reflected the increased cost difference by increasing the discount (from the single-piece flats rate) for each of the two least-workshared categories of presort flats. The current proposal to reduce

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each of these discounts below pre-correction levels reverses, rather than continues, this practice. The Postal Service identifies the effects of the correction as "one contributing factor" in the decision to propose above average increases for presort flats. Please describe all other contributing factors.

**RESPONSE:**

The Postal Service agrees with the assertion made in the question that the Docket No. RM2008-2 correction altered the modeled unit costs of presort flats, resulting in changes to the intra-presort cost differences, but not resulting in any changes to the overall cost difference between total single-piece flats and total presort flats. Perhaps looking at the relative volumes in the various categories of First-Class Mail flats and a brief history of pricing presort flats would clarify the Postal Service's perspective on pricing of Presort flats.

First-Class Mail Flat Shaped Pieces - Hybrid Year FY2009 Q3 & 4, FY2010 Q1 & 2		
Single-Piece	1,949,673	74%
Nonautomation Presort	60,970	2%
Automation		
Mixed ADC	55,209	2%
ADC	101,273	4%
3-Digit	295,143	11%
5-Digit	175,766	7%
Total Automation	627,391	24%
Total Flat Shaped Pieces	2,638,033	

In Docket No. R2008-1 (which was before the Docket No. RM2008-2 correction), the Automation Presort Flats price decreased by 1.14 percent. Most of this decrease resulted from a reduction in the prices for 3-Digit and 5-Digit Automation. As can be seen from the above table, most of the 26 percent of the volume that is in the presort category is in the ADC, 3-Digit, and 5-Digit price categories.

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The most significant change in cost avoidances after the Docket No. RM2008-2 correction was in the cost avoidance between the Mixed ADC and ADC price categories. This particular cost avoidance was 8.4 cents in Docket No. ACR2008, and dropped to 4.5 cents in Docket No. ACR2009. In Docket No. R2009-2, even with passthroughs of over 100 percent, the increase for Automation Flats was 5.1 percent, compared to 3.7 percent for single-piece flats. This trend continues in R2010-4, in which the overall single-piece flats increase is 4.8 percent, while Automation Flats increases by 11.9 percent.

Even though the correction resulting from Docket No. RM2008-2 did not change the overall cost difference between total single-piece and total presort, it did lead to higher increases for finer presort Automation Flats, causing the increase for presort flats to be higher than single-piece flats. Another contributing factor is the desire of the Postal Service to improve the cost coverage for flats.

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7. Refer to Attachment A to the Postal Service Request at 14 of 84, where the proposed rates for First-Class Mail Keys and Identification Devices are listed. Please provide a discussion of the proposed changes to these rates, including how the proposed changes relate to the Objectives and Factors of § 3622(b) and (c). Please also revise the calculation of percentage changes in rates to incorporate the effect of the proposed changes.

**RESPONSE:**

Before the PAEA, Keys and Identification Devices were priced using First-Class Mail single-piece parcel prices plus the highest Business Reply Mail (BRM) fee and, when appropriate, a nonmachinable surcharge (until shape-based pricing introduced in Docket No. R2006-1 eliminated the need for the nonmachinable surcharge). DMCS § 272. This pricing design has continued under the PAEA. The general price changes under the PAEA (Docket Nos. R2008-1 and R2009-2) did not present a separate price schedule or MCS language for Keys and Identification Devices. In this docket, a separate price schedule is presented in Attachment A to the Request (the MCS changes) for clarity. But the prices still are just a combination of the First-Class Mail Retail Parcel prices and the BRM fee.

These prices therefore conform to the objectives and factors in the same ways as these other prices relate to the objectives and factors of Section 3622(b). In addition, objective 2 requires the Postal Service to create predictability and stability in rates. Pricing for keys and identification device is predictable because it is linked to two existing pricing schedules. Also, factor 6 requires the Postal Service to take into account the simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees

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charged the various classes of mail for postal services. A separate price schedule based on two other price schedules makes the structure simple for these particular users of the postal services.

There is no reason to recalculate the revenue or percent changes for First-Class Mail or Special Services because volumes for Keys and Identification Devices are already included in the hybrid year billing determinants.

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8. The Postal Service states that the First-Class Mail workpapers report the expected revenue impacts of the "Reply Rides Free" initiative as a separate line item. Statement of James M. Kiefer at 27, n.23.

- a. Please identify where this is presented.
- b. Please also provide an estimate of the effect of the proposed initiative on Postal Service contribution, showing all calculations and explaining all assumptions.
- c. Please discuss the expected impact of the initiative on the relevant marketplace.

**RESPONSE:**

a-b. The worksheet for Reply Rides Free was inadvertently excluded from the First-Class Mail work papers. The revised First-Class Mail workpapers POIR.2.Q.1.8.10.xls include a worksheet "Reply Rides Free". This worksheet provides all the assumptions, calculations and the effect the effect of the proposed initiative on First-Class Mail contribution. In addition, the additional revenue is incorporated in the appropriate mail categories.

c. The goal of the Reply Rides Free program is to allow mailers to generate additional value from their operational mail by giving them more space to include revenue-generating materials. The Postal Service hopes this additional value will help slow the erosion of First-Class Mail volume. Because the program is available to all customers who include reply envelopes in their First-Class Mail, there is an equal opportunity to take advantage of the program, which should maximize benefit to the mailers.

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- 9. Refer to the Statement of James M. Kiefer, Appendix A, at 1-3. Please provide additional details about the implementation of the proposed "Reply Rides Free" initiative.**
- a. Please confirm that the initiative is not a one-year program, but will continue indefinitely. If confirmed, please identify any changes necessary to volume threshold calculations for use in subsequent years. Please also describe the data that the Postal Service plans to collect to measure the performance of the program and how that data will be utilized to evaluate its success.
  - b. The scenarios presented in the description refer to a "program year." Will program years align with calendar years? If not, will all participating mailers have concurrent program years, or will each have its own unique program year?
  - c. For mailers that may not immediately qualify for the initiative (e.g., they do not use Full-Service IMb), what will be the process for subsequent enrollment? Will the beginning of a mailer's enrollment be timed to coincide with a fiscal year, calendar year, or other common program year?

**RESPONSE:**

- a. The Postal Service will make a decision as to whether the program will continue based on the results of the first year. The Postal Service will evaluate the program based on participation and estimates of participant growth, profitability, and increase in the use of ancillary materials and reply envelopes. Any changes to program parameters will depend on the results of this evaluation and on projections of mail use.
- b. The program year is equivalent to calendar year 2011, and any future program years would presumably also coincide with calendar years. Participants must participate on a program-year basis.
- c. Assuming the program continues, a mailer would be able to enroll at the beginning of a program year.

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**10.** Refer to Attachment A to the Postal Service Request at 10 of 84. The proposed MCS language for the First-Class Parcel Nonmachinable surcharge deletes the phrase "Weighs less than 2 ounces" from the description of the price category.

- a. Please provide the rationale for this apparent proposed classification change.
- b. Please provide an estimate of the portion of nonmachinable parcel surcharge volumes that are due to the 2 ounce requirement, as opposed to the remainder that are due to the lack of a barcode or noncompliance with machinability requirements.
- c. Please revise the calculation of the percentage changes in rates for First-Class Mail to reflect the two categories of nonmachinable parcel surcharge volume: (1) those subject to the surcharge under the current classification that will remain so; and (2) those currently subject to the surcharge that are not subject to the redefined surcharge.

**RESPONSE:**

- a. Generally speaking, pieces weighing less than two ounces fall into the nonmachinable category and are subject to the nonmachinable surcharge. In the current filing the Postal Service is proposing to charge a single price for parcels weighing up to 3 ounces, which leads to a significant increase in the prices for parcels weighing less than 2 ounces. This increase should cover the cost caused by the nonmachinable nature of these parcels.
- b. Approximately 688 thousand pieces (of the total 6.6 million pieces that were subject to the surcharge) may not be subject to the surcharge as a result of deleting the "Weighs less than 2 ounces" condition for the surcharge. See tab "Hybrid Billing Determinants," cells H45 and D102. This estimate is based on the assumption that only 0-1 ounce parcels reported in the Mail Characteristics Study were subject to the surcharge. The assumption is that all 1-2 ounce pieces have added enough

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advertising to reach, but not exceed, the 2 ounce threshold. It is possible that some parcels that weigh between 1 and 2 ounces were subject to the nonmachinable surcharge, but data are not available to provide an estimate.

- c. Please see the spreadsheet POIR.2.Q.1.8.10.xls filed with this response which includes the revisions reflecting the responses to questions 1, 8 and this question.

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- 11.** Please refer to Library Reference USPS-R2010-4/1, Excel file "FirstClassMailIntl Worksheets R2010-4.xls," and worksheet tab "FY 2009 Q3 - FY 2010 Q2 FCMI."
- a. Please show the quarterly volumes by Rate Group and Ounce increment used to derive the "FCMI Letter Volume" shown in Table 1. Please show all calculations in electronic form and provide citations to sources used.
  - b. Please show the quarterly volumes by Rate Group and Ounce increment used to derive the "FCMI Flats Volume" shown in Table 2. Please show all calculations in electronic form and provide citations to sources used.
  - c. Please show the quarterly volumes by Rate Group and Ounce increment used to derive the "FCMI Parcels Volume" shown in Table 5. Please show all calculations in electronic form and provide citations to sources used.

**RESPONSE:**

- a. Please see the POIR No. 2 - 11a FCMI LETTERS tab of the Excel file ("POIR.2.Q.11.12.Attach.xls") attached to this response electronically for the quarterly and hybrid year volume totals.
- b. Please see the POIR No. 2 - 11a FCMI FLATS tab of the Excel file ("POIR.2.Q.11.12.Attach.xls") attached to this response electronically for the quarterly and hybrid year volume totals.
- c. Please see the POIR No. 2 - 11a FCMI PACKAGES tab of the Excel file ("POIR.2.Q.11.12.Attach.xls") attached to this response electronically for the quarterly and hybrid year volume totals.

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12. Please refer to Library Reference USPS-R2010-4/1, Excel file "FirstClassMailIntl Worksheets R2010-4.xls," and worksheet tab "FY 2009 Q3 - FY 2010 Q2 CARDS." Please show the quarterly volumes by Rate Group used to derive the "FCMI Cards Volume." Please show all calculations in electronic form and provide citations to sources used.

**RESPONSE:**

Please see the POIR NO. 2 - 11a FCMI CARDS tab of the Excel file

("POIR.2.Q.11.12.Attach.xls") attached to this response electronically for the

quarterly and hybrid year volume totals.

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13. Please provide the rationale for the following rate decreases.
- a. The per pound rate for High Density and Saturation letters and flats (Commercial and Nonprofit).
  - b. The DDU per pound rate for Carrier Route, High Density, and Saturation parcels (Commercial and Nonprofit).
  - c. The price per piece for pound-rated 3-digit presort flats.
  - d. The per piece rates for pound-rated Nonprofit automation letters.
  - e. The per piece rates for piece-rated and pound-rated 5-digit Nonprofit nonmachinable parcels.
  - f. the DDU per pound rate for Nonprofit 5-digit machinable parcels.

**RESPONSE:**

a. The Postal Service assumes that the question refers to the per-pound price elements for dropshipped mail pieces. Lower per-pound prices for dropshipped flats and heavy letters result from the higher dropship discounts for flats, which followed the Commission's approval of shape-based dropship avoided costs for Standard Mail. The per-pound prices for Saturation heavy letters and High Density and Saturation flats actually increase in the proposed prices, compared to the current prices.

While the per-pound price for High Density heavy letters does decrease in the price tables, this just reflects the correction of an anomaly that arose when this price was not reduced in Docket No. R2009-4, which reduced the prices for High Density flats. For as long as heavy (pound-rated) automation letters have been permitted in Standard Mail, they have been priced at the comparable automation flats prices, less a discount off the per-piece price element (but not off the per-pound element) equal to the difference between the minimum-per-piece prices for automation letters and automation flats. Therefore, when the pound price for High

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Density flats was reduced in Docket No. R2009-4, the pound price for heavy High Density letters should have been reduced in the price charts, but was inadvertently not changed. The proposed pricing simply restores the identical per-pound pricing for High Density flats and heavy letters as specified in the MCS.

b. The current DDU discount for parcels is \$0.625 per pound. The Postal Service's proposal in this docket raises this discount to \$0.834 per pound. This proposal reflects the Commission's approval of a costing methodology that produces separate dropship avoided costs by shape. The avoided cost for DDU parcels is \$1.159. While the DDU discount passes through only a part of that, the resulting expanded DDU discount causes the DDU dropship per-pound price element to decrease when compared to the current prices. The dropship discounts for Standard Mail parcels are set with non-carrier-route presorted parcels in mind. As can be seen in the Postal Service's Standard Mail workpapers (USPS-R2010-4/2), there are only about a half-million Carrier Route, High Density, and Saturation parcels, compared to well over 600 million non-carrier-route presorted parcels. For this reason the size of the discount was determined by the needs of the regular (non-carrier-route presorted) parcels and NFMs. The DDU discount was expanded to provide increased incentives for mailers to dropship mainly regular parcels deeper into system.

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c. The avoided cost for 3-digit nonautomation (presort) flats increased from \$0.045 to \$0.070 (a \$0.025 increase), based on the 2009 ACD compared to the 2008 ACD. Had the Postal Service not imposed an underlying increase of \$0.023 to the per-piece element, the per-piece element would have decreased by the full \$0.025 change in avoided costs (all else being equal). The \$0.023 increase offset all but \$0.002 of the change in avoided costs, so the per-piece element shows a reduction of \$0.002.

d. Please see the response to part (a), above. The price for nonprofit heavy letters, and all heavy (pound-rated) Standard Mail letters, is determined as specified in the Mail Classification Schedule. Heavy letters pay flats prices, but receive a discount based on the difference between the minimum-per-piece prices for automation flats and automation letters. If the minimum-per-piece price for automation flats increases relative to the minimum-per-piece price for automation letters, the discount for heavy letters off the flats per-piece price will increase. The per-piece price element for nonprofit heavy letters decreases because the difference between the minimum-per-piece prices for nonprofit automation flats and letters increased faster than the per-piece pricing element for pound-rated automation flats. These price elements are determined to help achieve the overall pricing goals for piece-rated letters, piece-rated flats and pound-rated flats, and the price for heavy letters is primarily determined as

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a result of these other pricing decisions. There are very few heavy automation letters, so the effect of these pricing decisions on heavy letters is of secondary importance when the decisions are made.

e. As explained in my pricing Statement, the Postal Service set the price for 5-digit presorted nonmachinable (irregular) parcels (both commercial and nonprofit) equal to the per piece rate for machinable parcels. There is no reason for separate prices. Parcels presorted to 5-digit ZIP Codes have the same costs and follow the same mail processing and delivery path, regardless of their classification as machinable or irregular. This pricing change better aligns the pricing with cost causation and encourages mailers of irregular parcels to sort to 5 digits, reducing the amount of costly manual handling these parcels may receive.

f. Please see the response to (b), above. There are relatively few nonprofit machinable parcels, and the DDU discount is set based on the need to send the appropriate signals to mailers of commercial regular parcels. Following past practice, the Postal Service offers the same dropship discounts to nonprofit parcels as commercial parcels.

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**14.** Please refer to the Statement of James M. Kiefer at 51, which states the following:

Stamped Cards in actuality did cover its costs. The FY 2009 ACR included an error in the volume reported in the Revenue Pieces Weight (RPW) report. The reported volume was 22 million, while the actual volume was 85 million. Correcting this error raises the revenue to well above costs.

With the corrected volume, for FY 2009, Stamped Cards cost coverage would be 238.3 percent. Also, please refer to the Statement of Stephen J. Masse, Attachments 9-11, which show the projected contribution for Stamped Cards for FY 2010, FY 2011 Before Rates, and FY 2011 After Rates. For the Stamped Cards service, the attachments project a cost coverage of 22.36 percent, 22.58 percent, and 21.87 percent, respectively. Please explain the significant decrease in cost coverage.

**RESPONSE:**

The information provided in Mr. Masse's attachments results from an error in the RPW in FY 2009, which greatly understated the volume for Stamped Cards. (The FY 2010 RPW will use correct volumes.) Please see the Postal Service's responses to ChIR No. 4, Questions 18 and 20, Docket No. ACR2009 (Feb. 24, 2010). As stated in the question, using the correct volumes results in a much higher cost coverage than in Mr. Masse's attachments. However, Mr. Masse's attachments used the "official" results in the 2009 ACD, which reflect adoption of a volume of 22 million pieces for the derivation of revenue, and of 85 million pieces for the cost analysis. Similarly, the roll forward used an accurate cost (based on the higher, accurate Stamped Cards volume) for the forecasted cost because that was the "official" cost from the ACD. This resulted in erroneously low cost coverage figures.

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Review of unit revenues and costs supports the fact that Stamped Cards has a healthy cost coverage. USPS-FY09-28, filed with the 2009 ACR, presented the unit costs for stamped cards as shown below:

**Stamped Cards FY 2009**

<i>Stamped Card Style</i>	<i>Cost per Thousand</i>	<i>Cost per Card</i>
<b>Single Cut</b>	\$ 12.380	\$ 0.012
<b>Single Sheet (40)</b>	\$ 10.290	\$ 0.010
<b>Reply Card</b>	\$ 18.370	\$ 0.018

Clearly the unit costs presented above do not exceed the unit revenue of \$0.03 cents from the Stamped Cards price. Additionally the 2009 ACD (TableVII-20) adopted a total cost of \$1,071,572, consistent with the Postal Service assertion that the actual volume of Stamped Cards in FY 2009 was 85 million. Dividing the \$1,071,572 in costs by a volume of 85,301,000 cards results in a unit cost of \$0.0126, which is well with in the range of the unit costs presented in the table above.

While the price of a stamped card more than covers its cost, the price would have been increased had the minimum possible price increase, given whole cent rounding, not required a 33 percent increase (\$0.04/\$0.03). It is not appropriate to give a product with a 239 percent cost coverage a 33 percent price increase, when the overall goal is a 5.6 percent increase.

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TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

1. The discussion of the proposed price changes for First-Class Mail states that "the Postal Service does not believe that the erosion of single-piece mail through electronic diversion can be materially affected by limiting the growth of the stamp price." Statement of James M. Kiefer at 15. It then goes on to assert that "many presort First-Class Mail customers may respond to large price increases, not by simply sending fewer pieces (the traditional elasticity effect), but by abandoning hard copy mail altogether." *Id.* at 17.

a. Please provide all studies and analyses underlying the conclusion that electronic diversion of single-piece mail is essentially unaffected by price, while the electronic diversion of presort First-Class Mail is likely to exhibit a response to price beyond that anticipated by price elasticity.

b. Please confirm that the Postal Service believes that First-Class presort flats (11.9 percent proposed increase) are not as susceptible to price-driven electronic diversion as presort letters (5.9 percent proposed increase). If confirmed, please provide all studies and analysis underlying this conclusion. If not, please explain.

**RESPONSE:**

a. No specific study underlies this conclusion. Rather, the context of the argument on pages 17 through 20 is essentially that the diversion of transaction and statement mail is initiated and driven by the businesses that generate this mail. See pages 9-10 ("Key Drivers" section) of "Projecting U.S. Mail Volumes to 2020", prepared by the Boston Consulting Group, March 2, 2010.<sup>1</sup> Individuals who receive this mail and send remittances are driven to shift by convenience and incentives provided by the businesses. The price of the stamp is a relatively minor consideration in this regard. See, e.g., Testimony of Claude R. Martin on Behalf of the Greeting Card Association, GCA-T-2, Docket No. R2006-1. at 22, 26, 30, and 47. In this context, the single-piece price elasticity is less than half the price elasticity of Presort mail, in absolute terms. Please see USPS-R2010-

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<sup>1</sup> Please see: [http://www.usps.com/strategicplanning/pdf/BCG\\_Narrative.pdf](http://www.usps.com/strategicplanning/pdf/BCG_Narrative.pdf)

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4/8, workbook "vf-Oct'10 implementation md.xls", tab "Elasts". The reported price elasticities are -0.400383 for Presort Mail and -0.183752 for single-piece mail.

b. Pages 15 and 17 of my statement do not discuss flat-shaped mail at all. Postal Service demand models do not estimate separate equations for various shapes, such as flats and parcels. The Postal Service does not have sufficient information to confirm or reject the proposition that "First-Class Mail presort flats . . . . are not as susceptible to price-driven electronic diversion as presort letters . . . ."

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2. The response to CHIR No. 2 question 6, states that one reason for proposing an 11.9 percent increase for First-Class Mail presort flats "is the desire of the Postal Service to improve cost coverage for flats." While acknowledging the "unprecedented challenges" facing the periodicals industry, the Postal Service proposes an 8 percent increase for Periodicals Mail to improve its cost coverage. Statement of James M. Kiefer at 39. In contrast, the Postal Service proposes a much smaller 5.1 percent increase for Standard Mail Flats, due to concern for the delicate financial position of the catalogue industry. *Id.* at 28-30. Please provide all studies and analyses relied upon to evaluate and compare the relative financial health of the periodicals industry, the catalogue industry, and industries that use First-Class presort flats. Please also provide all other studies and analyses underlying the Postal Service's evaluation of the relative ability of each industry to withstand postal rate increases of various sizes.

**RESPONSE:**

The Postal Service did not conduct studies or analyses to evaluate and compare the relative financial health of the periodicals industry, the catalogue industry and industries that use First-Class Mail presort flats. Also, the Postal Service did not conduct studies or analyses to evaluate the relative ability of each industry to withstand postal rate increases of various sizes.

Instead, the Postal Service used its business judgment to determine the relative price increases each category should be asked to bear. This judgment was informed by knowledge of the industries that use these products, and our customers for these products. This knowledge was gained by regular contact with customers and industry representatives, as well as information gathered through meetings, conferences, consultation with experts, and the media that cover these industries and customers. Using this knowledge the Postal Service made an informed judgment as to the appropriate prices for these and other price categories.

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3. The response to POIR No. 2, question 3 states that, "[t]he Postal Service expects the upward trend in usage [of Full-Service IMb] to continue at least until the use of the Full Service IMb option is required to receive automation discounts."

- a. Please describe the Postal Service's plans to require the use of Full-Service IMb to qualify for automation discounts, including the timing of such a requirement and plans to address the potential difficulties for smaller mailers in adopting Full-Service IMb (as opposed to Basic IMb).
- b. Please confirm that when Full-Service IMb is required to qualify for automation discounts, the percentage of automation pieces using Full-Service IMb will be 100 percent. If not, please explain.

**RESPONSE:**

- a. The Postal Service does not currently plan to require the use of Full-Service IMb to qualify for automation discounts. Instead, use of the Intelligent Mail Barcode (IMb) (Basic or Full Service) will be required for automation discounts. Please see the revised response to Presiding Officer's Information Request No. 2, Question 3, also filed today.
- b. Not applicable.

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4. Please refer to the response to POIR No. 2, questions 8 and 9, including the spreadsheet "POIR.2.Q.1.8.10.xls" provided with the response.
- a. Please refer to tab 'Reply Rides Free' cells C20-C24. While labeled as assumptions, some of these data appear to be taken from other sources (e.g., current volume between 1 oz. and 1.2 oz. = 1.34388220786953%). Please explain the rationale and provide the source for each of the assumptions.
  - b. Please refer to tabs 'SP Ltrs & Crds' and 'Presort Ltrs & Crds.' The revised calculations incorporate the anticipated additional volume into the percentage rate increase by multiplying the estimated incremental volumes by new and current prices, with zero used as the current price. This has the effect of increasing the percentage rate change, which implies that the discount initiative is effectively a rate increase. A possible alternative treatment would be to isolate the additional ounces that would be subject to the discount, and apply the current (12.5 cents) and proposed (0 cents) prices to the estimated volume of discounted additional ounces. This would have the effect of showing the discount as reducing the percentage change in rates. Another alternative, given the limited scope of the proposal, the unique and unusual requirements for eligibility, and its intended purpose of retaining marginal volumes through targeted discounts, would be to treat the initiative like NSAs and other special classifications by excluding it from the price change calculations. Please explain the rationale for the method of incorporating the initiative into the price change calculations used by the Postal Service, including a discussion of why other alternatives were not used.
  - c. See response to POIR No. 2, question 9.a. Please identify the data sources and methods of recording participants:
    - i. volumes,
    - ii. profitability,
    - iii. use of ancillary materials and reply envelopes.

**RESPONSE:**

- a. The "current volume between 1 oz. and 1.2 oz." is an estimate of the amount of exposure for the program, based on an analysis of ODIS/RPW data. "Program participants" is an estimate of the amount of volume that will participate in the program. The estimate is based on experience with past incentive programs, discussions with mailers, and management judgment.

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"Cost of additional weight" is an estimate of the additional cost of a 1.2-ounce piece, compared to the systemwide average. The estimate is based on previous analyses of cost by weight increment.

"Transaction and Statement Volume" is an estimate of the total size of the likely pool of qualifying volume. It is based on management's estimate of the current amount of transaction and statement volume and the likely growth of that volume.

"Retained Presort Volume" is an estimate of the amount of volume that will stay in the mail as a result of the program, and is based on management judgment.

- b. The Postal Service accepts the second alternative provided in the question, i.e., given the limited scope of the proposal, the unique and unusual requirements for eligibility, and its intended purpose of retaining marginal volumes through targeted discounts, the estimated revenue from this incentive program will be excluded from price change calculations. Please see POIR3.Q.4.xls. This workbook incorporates the analysis from POIR2.Q.4c.FCM75.xls, filed on August 3, 2010.
- c. In general, customer data will be captured via PostalOne! mailing statements, which also feed into the Corporate Business Customer Information System (CBCIS). Analysis will be performed by extracting data from these source systems into an external database where those data can be manipulated and calculations performed.

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- i. CBCIS and mailing statements will be used to determine both total participant volume and change in volume over the base period.
- ii. Contribution will be calculated by using CBCIS data for volume and revenue, and using unit costs estimated from CRA and cost models. Total cost will be estimated by multiplying volumes by unit costs, and contribution will be determined by subtracting this amount from total revenue.
- iii. CBCIS and mailing statement weight and volume data will be used to calculate changes in weight per piece, reflecting changes in use of ancillary materials and reply envelopes.

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5. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service commencing at page 28, line 23 which states, "[t]hese volume declines have helped to drive the Flats cost coverage down to only 82 percent." Please explain how the decline in volume drove down cost coverage.

**RESPONSE:**

In general, the Postal Service would agree that volume increases or decreases within the relatively narrow range over which postal volumes have routinely varied for the last four decades would not be expected to have much, if any, effect on unit attributable cost or, consequently, on cost coverage. But as discussed on page 28 of the statement, the volume of Flats declined by over 20 percent over a short period of time. Despite substantial efforts to trim costs in line with volume declines, it was not possible to reduce costs by the same percentage as the massive mail volume declines that occurred within a relatively short period of time. This issue is given a more thorough discussion in the Response of the United States Postal Service to Motion of the Affordable Mail Alliance to Dismiss Request (filed August 2, 2010) on pages 51-56, including footnote 47. If attributable costs do not shrink proportionately with volumes within a specific time window, the cost coverage (the ratio of revenues -- which do tend to shrink in line with volumes -- to attributable costs) must, of mathematical necessity, also shrink.

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6. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service at page 32, footnote 28 which states “[c]atalog advertising often leads to sales of shipping services for fulfillment, as well as additional follow-on advertising using the Standard Mail Flats product as well as other Mailing Services products.”

a. Please provide the percentage of all catalog advertising that leads to sales of shipping services for fulfillment.

b. Please provide the percentage of shipping services for fulfillment (taken from your answer to subpart a.) that is provided by the Postal Service.

c. Please provide a list of Postal Service products used by catalogers for fulfillment and the proportionate use of each product by catalogers.

**RESPONSE:**

a. The average response rate varies among catalog companies, but according to statistics from the Direct Marketing Association, in 2009 the average response rate for the industry was 1.5 percent. This 1.5 percent response rate equates to 1.9 shipments per 100 catalogs, which includes the original order, plus any backorders, split orders, and returns.

b. It is believed that the Postal Service has a small percentage of the total of fulfillment shipments from catalogers. No exact data are available.

c. Based on an analysis of the top 600 catalog companies by Postal Service spending, the catalog industry uses for shipping the following Postal Service products (with each product's approximate share of the total combined postal revenue from these shipments in parentheses): Express Mail (3 percent), Priority Mail (43 percent), Parcel Post (3 percent), BPM Parcels (30 percent), First-Class Mail Parcels (10 percent), and Standard Mail NFMs and Parcels (12 percent). It is also believed that catalog mailers generate significant amounts of Parcel Select mail, but usage data by mailer for this product are not available to the Postal Service.

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7. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service and the discussion of pricing of the Standard Mail Flats product. Reference is made commencing at page 32, line 12 to the "contribution that catalog advertising makes to the health of other Postal Service products." Please provide an estimate of the contribution from other Postal Service products specifically generated by catalogs in FY 2009. Please provide all inputs and assumptions used to derive this estimate and any studies or analyses that identify or that quantify this additional contribution.

**RESPONSE:**

The Postal Service has not prepared any estimates of the contribution from other products generated by catalogs for FY 2009. But it has produced an estimate of cost coverage of mail sent by catalog mailers based on FY 2010-Q2 data. A public version of that analysis, from which information about competitive products has been redacted, is attached. An unredacted version is filed under seal as USPS-R2010-4/NP7. Based on this analysis the catalog industry generates mail with a total cost coverage of approximately 132 percent. This analysis includes contribution for all mail generated by catalog mailers, with the exception of Parcel Select mail, for which data at the customer level were not available.

## Total Revenue/Volume - By Product - Top 600 Catalogers

Attachment to Response to POIR No. 3, Q. 7

	[1]	[2]	[3]	[4]	[5]	[6]	[7]	[8]
	Revenue	Volume	% Total Volume	Revenue/ Pc	Cost/Pc ***	Contribution/ Pc	Cost Coverage	Weighted Cost/Pc
<b>Total Of VOLUME Q2 FY2010</b>	4,818,654,711	18,213,902,099	100.00%	\$0.265	0.20	\$0.064	132%	0.201
<b>CARRIER ROUTE FLATS</b>	1,749,314,114	7,203,478,767	39.55%	\$0.243	0.16	\$0.083	152%	0.063
<b>CARRIER ROUTE LETTERS</b>	21,770,978	109,947,735	0.60%	\$0.198	0.16	\$0.038	124%	0.001
<b>FLATS</b>	1,213,877,912	3,406,392,146	18.70%	\$0.356	0.448	(\$0.092)	80%	0.084
<b>LETTERS</b>	996,422,130	5,040,054,308	27.67%	\$0.198	0.109	\$0.089	181%	0.030
<b>NFM</b>	2,522,168	2,868,892	0.02%	\$0.879	1.237	(\$0.358)	71%	0.000
<b>PARCELS</b>	41,400,753	30,601,040	0.17%	\$1.353	1.237	\$0.116	109%	0.002
<b>SAT HD FLATS &amp; PAR</b>	144,186,163	845,931,505	4.64%	\$0.170	0.063	\$0.107	271%	0.003
<b>SAT HD LETTERS</b>	99,076,053	680,822,509	3.74%	\$0.146	0.067	\$0.079	217%	0.003
<b>FIRST CLASS MAIL FLATS</b>	10,907,024	11,999,545	0.07%	\$0.909	0.753	\$0.156	121%	0.000
<b>FIRST CLASS MAIL PARCELS</b>	34,074,589	16,979,232	0.09%	\$2.007	1.886	\$0.121	106%	0.002
<b>FIRST CLASS MAIL PRESORT CARD</b>	47,375,264	225,826,165	1.24%	\$0.210	0.077	\$0.133	272%	0.001
<b>FIRST CLASS MAIL PRESORT LETTERS</b>	169,909,477	480,994,187	2.64%	\$0.353	0.120	\$0.233	295%	0.003
<b>FIRST CLASS MAIL SINGLE PIECE CARD</b>	2,108,159	7,651,852	0.04%	\$0.276	0.272	\$0.003	101%	0.000
<b>FIRST CLASS MAIL SINGLE PIECE LETTERS</b>	7,119,037	15,408,943	0.08%	\$0.462	\$0.263	\$0.199	175%	0.000
<b>PRIORITY (EXCLUDING CUSTOMIZED)</b>								
<b>PARCEL POST</b>	9,321,617	869,263	0.00%	\$10.724	9.432	\$1.292	114%	0.000
<b>PACKAGE PARCEL RETURN SERVICE</b>								
<b>BPM</b>	106,670,548	116,790,993	0.64%	\$0.913	0.498	\$0.416	184%	0.003
<b>EXPRESS</b>								

## Notes

Revenue (Col [1]): Revenue by product for top 600 catalog mailers

Volume (Col [2]): Volume by product for top 600 catalog mailers

Col [3]: Volume in column [2] divided by total volume (cell C6)

Col [4]: Column [1] / Column [2]

Cost / Piece (Col [5]): Cells E7-E25: FY2009 CRA data; Cell E6 = Cell I6

Col [6]: Column [4] - Column [5]

Col [7]: Column [4] / Column [5]

Weighted Cost / Piece (Col [8]): Cells I7-I25: Col [5] \* Col [3]; Cell I6 = Sum of Cells I7 to I25

\*\*\* Cost per piece data is average data for the product as a whole and may not precisely represent the unit costs of catalog mailers' mail mixes.

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8. Has the Postal Service determined the own-price elasticity for Standard Mail Flats? If yes, please provide the elasticity and all backup documentation.

**RESPONSE:**

The Postal Service has not yet been able to produce own-price elasticity estimates for Standard Mail Flats.

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9. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service commencing at page 28, line 21, where it states that volume declines exceeding 20 percent of the Flats product were driven by reductions in catalog mailings.

- a. Has the Postal Service conducted any studies to determine what percentage of the loss in Flats volume is due to conversion to letter-shaped catalogs?
- b. Has the Postal Service conducted any studies to determine what percentage of the loss in Flats is due to co-mailing to qualify for Carrier Route?

**RESPONSE:**

- a. No.
- b. No. Some Standard Mail Flats mailers engage in co-palletization and other combining activities (such as combining automation and Carrier Route flats in sacks). These programs have been around for some time and it is unlikely that the recent Flats volume declines are due to these kinds of activities.

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10. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service commencing at page 7, line 1, where it states that, “[w]e cannot afford to be short-sighted and take actions that will “fix” a coverage problem by permanently driving mail—mail that we believe will become profitable as the Postal Service and the mailing community adjust to operational and marketplace realities—or mail that is valued in the mailbox—out of the system.”

- a. Please confirm that the Postal Service's position is that the value of the mail in the mailbox, especially for flat-shaped products, offsets the negative contribution. If confirmed, please discuss the short- and long-run ramifications of this position.
- b. Please quantify the financial benefit to the Postal Service of each mail product or service that is valued in the mailbox. Please provide all supporting documentation.

**RESPONSE:**

- a. Not confirmed. It is not the position of the Postal Service that “the value of the mail in the mailbox” offsets negative contribution. The Postal Service's position is that all classes of mail should cover their costs and make a reasonable contribution toward the Postal Service's institutional costs.
- b. While the Postal Service believes that all mail has value in the mailbox, the portion of the Statement quoted in the preamble to the question was intended primarily to refer to Periodicals, which has long been recognized as having particularly high value in the mailbox. While the Postal Service does not have any studies that precisely quantify the external contribution (contribution from products other than Periodicals) generated by Periodicals mailers, a recent examination of the top 100 Periodicals mailers show (1) that less than half of all revenue paid by Periodicals mailers comes from products in the Periodicals class, and (2) the bulk of non-Periodicals revenues generated by Periodicals mailers is in the First-Class Mail and Standard Mail classes, both high contribution classes. Please see the Power Point slides illustrating the value of

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Periodicals to customers, attached to this response set as part of  
the zip file POIR.3.Q.10.11.14.ATTACHS.zip.

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11. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service at page 8, line 20, discussing the wide range of considerations in developing these prices, including "vulnerable customer segments."

- a. What customer segments are considered vulnerable? Please provide any available studies used to support these conclusions.
- b. How does the Postal Service determine which customer segments are vulnerable in areas where no independent studies exist?

**RESPONSE:**

- a. Many customer segments are vulnerable for a variety of reasons, but the Postal Service considers the following segments to be especially vulnerable: First-Class Mail Presort Letters mailers, First-Class Mail Single Piece Letters mailers, Standard Mail Letters and Standard Mail Flats mailers, and Periodicals mailers. As discussed in the Statement, the Postal Service does not believe that the vulnerability for every one of these categories of mail can necessarily be effectively addressed through pricing. The Postal Service has not conducted its own studies but has relied on analyses of the mail market that are reported by groups that monitor the mailing industry, together with information from its own customer contacts to develop its views as to the vulnerability of specific categories of mail. See the response to part (b) for further details.
- b. Aside from direct contact with customers, the Postal Service constantly monitors the trade media and reports and other communications prepared by industry organizations. Attached to this response set as part of the zip file POIR.3.Q.10.11.14.ATTACHS.zip are some examples of articles and presentations that the Postal Service has seen that are germane to the issue of vulnerability, particularly with respect to the catalog industry. See "Outlook 2010: The Maturation of Email in a Continuously Evolving Market," Bruce Biegel, The

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Winterberry Group, presentation April 19, 2010, slide #11, on the shift from direct mail to email. See "Postage Increase Brings a New Prospecting Breakeven," Jim Coogan, published in Multichannel Merchant Magazine, 7/2/07, for a perspective on how postage increases must lead to the cutting of catalog prospecting. See "Search To Grow As Marketers Express ROI Concerns," published in DIRECT Magazine, 3/27/10 for a recent survey showing that merchants are shifting direct mail dollars to Internet-based search engine advertising. See the testimony of Allen Abbott of the American Catalog Mailers Association to Senate and House subcommittees on 7/2/10, particularly the section entitled "Elasticity" on pp. 4-5 for ACMA's view of the responsiveness of catalog volume to price. See also the "2009 Channel Preference Study," prepared by ExactTarget, page 4 in particular, which shows how consumers' preferred channels for permission-based promotional messages are changing.

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12. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service, commencing at page 30, line 7, regarding closing the cost coverage gap for Standard Mail Flats. Mr. Kiefer argues that because "postage accounts for approximately half the cost of mailing a catalog", a large postal price increase would "put serious additional pressures on catalog mailers, thereby reducing postal volumes even further than they have already fallen."

- a. Please explain what costs are included in "the cost of mailing a catalog" as used in the quotation above.
- b. Please provide the approximate percentage of a catalog mailer's total operating expenses that is postage for mailing catalogs? Please provide the source of this estimate.

**RESPONSE:**

- a.- b. Although the costs vary by market segment, the cost components of mailing a catalog can be divided into five distinct categories. Estimates of cost shares for each component, based on industry input, are given after each component.

Creativity – 12%

Marketing – 5%

Paper – 30%

Print – 12%

Postage – 41%

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13. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service commencing at page 32, line 15. With regard to Standard Mail Flats, it states that the Postal Service "is seriously concerned that taking aggressive action to close the gap through pricing alone in the early days of the expected recovery period might endanger the long-run health of the catalog industry and ultimately destroy this important segment of its business." Please also refer to USPS-R2010-4/9—Operations Plans for Flats. On page 11, it states, "[t]he Postal Service believes that Standard Mail volumes are potentially sensitive to large price increases, which may precipitate 'rate shock,' given that this mail is primarily composed of marketing material and other discretionary activities."

- a. When determining the rate increase for Flats, did the Postal Service determine the effect on a typical cataloger that uses both Standard Mail Flats and Carrier Route flats?
- b. If yes, what effects were determined?
- c. Please provide the average percentage increase in rates for a typical cataloger?
- d. Could the effect of a greater increase in rates for Flats be tempered by a smaller increase for Carrier Route flats? Please explain.

**RESPONSE:**

- a-c. The Postal Service is aware that many of its catalog customers use both its Flats and Carrier Route products. Nevertheless the Postal Service has not attempted to define a "typical cataloger" in terms of what percentage of each product such a mailer would use, much less what distribution of presort categories the "typical cataloger" would use within the Flats product and what pattern of entry points the customer would use for each product and presort level. Consequently the Postal Service has not quantified the impact of its pricing on the "typical cataloger." Since both the Flats product and Carrier Route flats category received approximately the same percentage increase (5.1 percent for Flats and 4.9 percent for Carrier Route flats), a mailer whose mailing resembles the volume pattern within each product's pricing categories is likely to see an increase of approximately five percent.

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- d. Possibly. But it is also possible that giving Carrier Route flats a lower increase to "offset" a higher increase for non-carrier-route presorted flats could lead to a much higher average increase for the catalog mailer. Alternatively, it could lead to lower average prices. Any pricing design aimed at offsetting higher Flats price increases with lower Carrier Route flats price increases would necessarily have to pick a fixed mail mix for each product around which the offsetting pricing design would be built. Mailers whose mail mix mirrored the mail mix chosen for the design could potentially offset higher increases in one product with lower increases in the other. But those whose mail mixes are different from the "breakeven" patterns would likely experience either higher or lower increases than those designed for the assumed "typical cataloger." Given the fact that the Postal Service does not know how typical the "typical cataloger" is, without further information such a pricing strategy would have unknown and, possibly, unintended consequences while providing no clear assurance that most, or even many, catalogers would actually break even in the process.

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14. Please refer to the Statement of James M. Kiefer on Behalf of the United States Postal Service at page 30, footnote 25, which cites research from Comscore regarding online purchases by catalog recipients.

- a. Please provide this research.
- b. Who commissioned this research?
- c. What were the objectives of this research?

**RESPONSE:**

- a. Please see the research reports from ComScore, which are attached to this response set as part of the zip file POIR.3.Q.10.11.14.ATTACHS.zip.
- b. The Postal Service commissioned this research.
- c. The objective was to provide a comprehensive overview of the relationship between direct mail and its impact on subsequent online consumer behavior.

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15. In FY 2009, Confirm Service had a negative contribution. Further, in response to POIR No. 1, question 11, the Postal Service stated that "it will ultimately be the level of Product Specific costs in any given year which will have the most significant impact on the performance of [Confirm Service]." In Docket No. ACR2009, the Postal Service explained that Confirm Service's fixed cost increased because of "an IT hardware upgrade (coding) and application development, so that Confirm could provide Full Service IMb data, and use updated technology."

- a. For FY 2010, has the Postal Service undergone any similar Confirm projects that would increase the attributable costs for Confirm Service?
- b. For FY 2011, does the Postal Service anticipate undertaking any similar Confirm projects?

**RESPONSE:**

- a. No.
- b. The Postal Service has not fully determined plans for FY 2011, so attributable cost increases over FY 2010 cannot be ruled out.

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TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

16. Please refer to the Postal Service's response to POIR No. 1, questions 9-10, Excel file, "POIR1Q9.xls," worksheet, 'Change Calc,' lines 42-44. The Change Calc worksheet includes revenue indices for the three International Special Services products. However, for International Ancillary Services and International Business Reply Mail, the indices differ with the Postal Service's original filing (July 6, 2010). See the table below.

<b>July 6, 2010 Filing</b>			
	<b>Revenue Index</b>		<b>Percent</b>
	<b>Transactions Multiplied by</b>		<b>Change</b>
	<b>Current Fees</b>	<b>Planned Fees</b>	<b>in Fees</b>
Intl Ancillary Services	\$17,276,689	\$19,305,230	11.741%
Intl Reply Coupon Service	\$24,644	\$25,817	4.760%
Intl Business Reply Mail	\$132,223	\$136,855	3.503%
<b>July 23, 2010 Revised Filing</b>			
	<b>Revenue Index</b>		<b>Percent</b>
	<b>Transactions Multiplied by</b>		<b>Change</b>
	<b>Current Fees</b>	<b>Planned Fees</b>	<b>in Fees</b>
Intl Ancillary Services	\$17,127,119	\$19,148,671	11.803%
Intl Reply Coupon Service	\$24,644	\$25,817	4.760%
Intl Business Reply Mail	\$189,725	\$196,336	3.485%

- a. Please explain the difference in revenue indices for International Ancillary Services and International Business Reply Mail.
- b. Did the Postal Service revise the billing determinants for International Ancillary Services and International Business Reply Mail? If yes, please provide the revised billing determinants.

**RESPONSE:**

- a. The correct revenue calculations and percent changes were filed on July 6, 2010, in INTL Special Services Worksheets R2010-4.xls. The International Ancillary Services and International Business Reply Mail revenue totals given in the July 23, 2010, filing were taken from a preliminary worksheet.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

b. No.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

17. Please refer to the Exigent Request of the United States Postal Service, Attachment A, and the prices for outbound Single-Piece First-Class Mail International postcards (1125.6 Prices). In Docket No. R2009-2, the proposed postcard price to Canada and Mexico was \$0.75 and \$0.79, respectively. For the Exigent Request, the Postal Service proposes a uniform price for postcards to Canada and Mexico of \$0.80. Please explain the rationale for proposing a uniform price for postcards to Canada and Mexico in the Exigent Request.

**RESPONSE:**

The price for postcards has been equal to the one-ounce price for FCMI letters since 2007, when there was one price for Canada and Mexico and another price for all other countries. In Docket No. R2009-2, the postcard prices for Canada and Mexico were differentiated to align with the one-ounce prices for First-Class Mail International (FCMI) Letters to Canada and Mexico. For the Exigent Request, there are three one-ounce prices for FCMI Letters, but management decided to return to the uniform price for postcards to Canada and Mexico in order to simplify the price structure for outbound Single-Piece First-Class Mail International postcards.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

18. Please refer to the responses to POIR No. 2, questions 11 and 12. For First-Class Mail International letters, flats, parcels, and cards, please explain the adjustment(s) made in the quarterly billing determinants for the hybrid year provided in the responses to questions 11 and 12, compared to the quarterly billing determinants reported in documents previously filed with the Commission.

**RESPONSE:**

In the Exigent Request, Israel will be moved from FCMI price group 8 to price group 5. The quarterly billing determinants for FCMI letters, flats and packages provided for question 11 include the migration of the volumes destined to Israel from price group 8 to price group 5.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

**19.** Please refer to the response to POIR No. 1, question 3(a) and (b). Also, please refer to the UPU Convention, Article RL 215, paragraphs 5 and 6 (quoted below) concerning Quality of Service linked terminal dues:

**Article RL 215.5**

Provisional quality of service linked terminal dues rates shall be calculated by the International Bureau and notified by circular no later than 1 July of each year. The provisional rates shall come into effect on 1 January of the following year and shall remain in force for the entire calendar year. The provisional terminal dues rates shall...include an incentive and an adjustment based on the quality of service results of the previous calendar year.

**Article RL 215.6**

Final quality of service linked terminal dues rates shall be calculated by the International Bureau following the publication of the final quality of service results relating to the calendar year in question. The final quality of service linked terminal dues rates shall be notified by International Bureau circular no later than 1 May of the year following the calendar year in question and shall replace the provisional terminal dues rate previously issued for that calendar year.

a. According to the above referenced articles, the International Bureau has already published the provisional terminal dues rates that will be in effect for CY 2010 and CY 2011. Please provide a rationale for not using the known and certain provisional terminal dues rates for CY2010 and CY 2011 in calculating the percentage change in price for inbound First-Class Mail International in Library Reference USPS-R2010-4/1, Excel file, Inbound FCMI Worksheets R2010-4.xls.

b. Please discuss the merits of using a weighted average rate reflecting the CY2010 and CY2011 "provisional" terminal dues rates paid by countries in the target system *and* the CY2010 and CY2011 terminal dues rates paid by countries in the transition system in calculating the percentage change in price for inbound First-Class Mail International in Library Reference USPS-R2010-4/1, Excel file, Inbound FCMI Worksheets R2010-4.xls.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

**RESPONSE:**

- a. While the provisional terminal dues are published, they are not certain.

Between CY2006 and CY2009, a comparison of the provisional terminal dues per piece component with the final CY final terminal dues per piece component shows only one revision (CY 2009). But a comparison of the provisional terminal dues per kilogram component with the final CY final terminal dues per kilogram component shows revisions for each year between CY 2006 and CY 2009. The Postal Service used the UPU base terminal dues rates in Inbound FCMI Worksheet R2010-4.xls as it did with the analogous worksheets for USPS-R2008-1/NP1 and USPS-R2009-2/1.

- b. The approach suggested in the question should be a more accurate representation to the extent that the FY 2009 inbound volume and weight distributions used in the calculations approximate the FY 2010 distributions. It should yield lower total revenue estimates that result in a small percentage increase in the price for inbound First-Class Mail International, but would have little impact on the overall percentage increase for First-Class Mail.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

1. Please refer to the Statement of James M. Kiefer at 53, which states the "offering of Stamped Envelopes bearing a Standard Mail stamp will be eliminated." Please provide the FY 2009 volume of Stamped Envelopes bearing a Standard Mail stamp.

**RESPONSE:**

13,500 stamped envelopes bore a Standard Mail stamp in FY 2009.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

6. Please refer to page 7 of USPS-LR-2, Standard Mail Preface R2010-4.doc where it states, "[b]ased on its experience and judgment, Postal Service management has estimated that 61 percent of NFM volume will migrate to Fulfillment Parcels." Please explain in detail the rationale underlying the judgment of Postal Service management that 61 percent of NFMs will migrate to Fulfillment Parcels and the remaining 39 percent will be Marketing Parcels.

**RESPONSE:**

The Postal Service examined volume data for the top 200 customers of its NFMs/Parcels product and assigned the volume of each customer to either the Marketing Parcels or Fulfillment Parcels category. The decision as to which category a customer was to be assigned was based upon the Postal Service's knowledge and understanding of the type of business each customer engages in and the kind of parcels it mails. The volumes in each category were summed and the resulting 61-39 percent split was based on the relative proportions of the volumes assigned to each category. In performing this analysis, the Postal Service assumed that if a customer currently mailed fulfillment parcels, it would continue to mail fulfillment parcels and if a customer currently mailed marketing parcels, it would continue to mail marketing parcels.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

7. Please confirm that the Postal Service proposal in this proceeding will result in rate increases as large as 79 percent for Standard Mail NFMs—the proposed rate increase for 3.3-ounce SCF presorted, DSCF-entered irregular NFMs that will fall into the fulfillment parcel category under the proposed classification—and as large as 35 percent for Standard Mail Parcels (the proposed rate increase for 3.3-ounce SCF presorted, DNDC-entered irregular parcels). If not confirmed, please provide the correct figures.

**RESPONSE:**

Confirmed. After the proposed price adjustments, the DSCF-entered former NFM would pay 98.0 cents and the DNDC-entered irregular parcel would pay 105.7 cents per piece.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

8. In the file "SPParcelPost Worksheets R2010-4.xls," The Alaska Bypass Volume for the Hybrid year FY2009 Q3 – FY2010 Q2 is calculated to be 1,391,219 in the tab "Inputs" at cell c22. The Revenue for the hybrid year is calculated to be \$30,203,196 in the tab "New SPP Prices" at cell AA87. These values are used in the file "Package\_Services\_Worksheets\_R2010-4.xls," which contains the calculation of the R2010-4 proposed price increase for Package Services. On July 28, 2010, the Postal Service filed Quarterly Billing Determinants for the Hybrid year. The following questions concern Alaska Bypass Volume and Revenue in the file "Parcel Post Hybrid BD Q309-Q210 R2010-4.xls."

- a. Please confirm that the Alaska Bypass Volume in file "Parcel Post Hybrid BD Q309-Q210 R2010-4.xls" tab "BD Total Q3FY09-Q2FY10" cell L87 is 1,482,963.
- b. Please confirm the following Alaska Bypass Volumes match the volume listed in a text note at the bottom of each quarterly Billing Determinant page in the file "Parcel Post Hybrid BD Q309-Q210 R2010-4.xls."

Tab	Volume
BD Q309	433,440
BD Q409	335,432
BD Q110	307,571
BD Q210	314,776
<b>Total</b>	<b>1,391,219</b>

- c. Please reconcile the discrepancy between the volume figures in "Parcel Post Hybrid BD Q309-Q210 R2010-4.xls" and the file "SPParcelPost Worksheets R2010-4.xls."
- d. Please Confirm that the Alaska Bypass Revenue in tab "BD Total Q3FY09-Q2FY10" cell L87 is \$27,931,604.
- e. Please confirm the following Alaska Bypass Revenues match the revenue listed in a text note at the bottom of each quarterly Billing Determinant page in the file "Parcel Post Hybrid BD Q309-Q210 R2010-4.xls."

Tab	Revenue
BD Q309	\$ 6,901,597
BD Q409	\$ 7,863,038
BD Q110	\$ 7,439,562
BD Q210	\$ 7,297,697
<b>Total</b>	<b>\$ 29,501,894</b>

- f. Please reconcile the discrepancy between the revenue figures in "Parcel Post Hybrid BD Q309-Q210 R2010-4.xls" and the file "SPParcelPost Worksheets R2010-4.xls."

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**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

**RESPONSE:**

- a. The text note reference in cell L87 is in error, and 1,482,963 should read 1,391,219. The entire text note reference should read, "*Excludes 1,391,219 Alaska Bypass Pieces (\$29,501,894).*" This correction does not affect any of the computations in the spreadsheet.
- b. Confirmed. The text notes at the bottom of each quarterly Billing Determinant page in the file "*Parcel Post Hybrid BD Q309-Q210 R2010-4.xls*" correctly match the referenced Alaska Bypass volumes.
- c. The volume figures in "*Parcel Post Hybrid BD Q309-Q210 R2010-4.xls*" and the file "*SPParcelPost Worksheets R2010-4.xls*" match. The only volume discrepancy is in the file "*Parcel Post Hybrid BD Q309-Q210 R2010-4.xls*" in the tab "*BD Total Q3FY09-Q2FY10*" at cell L87. The text note at cell L87 should read, "*Excludes 1,391,219 Alaska Bypass Pieces (\$29,501,894),*" not "*Excludes 1,482,963 Alaska Bypass Pieces (\$27,931,604).*" Additionally, the text note at cell B87 in this tab should read, "*Excludes 1,391,219 Alaska Bypass Pieces.*" These corrections do not affect any of the computations in the spreadsheet.
- d. The text note reference in cell L87 is in error, and \$27,931,604 should read 29,501,894. The entire text note reference should read, "*Excludes 1,391,219 Alaska Bypass Pieces (\$29,501,894).*" This correction does not affect any of the computations in the spreadsheet.
- e. Confirmed. The text notes at the bottom of each quarterly Billing Determinant page in the file "*Parcel Post Hybrid BD Q309-Q210 R2010-4.xls*" correctly match the referenced Alaska Bypass revenues.

**RESPONSE OF JAMES KIEFER  
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

- f. The revenue figures in "Parcel Post Hybrid BD Q309-Q210 R2010-4.xls" and the file "*SPParcelPost Worksheets R2010-4.xls*" differ because of the following methodology, which was used for the "Before Rates" computations associated with the file "*SPParcelPost Worksheets R2010-4.xls*" in tab "New SPPP Prices," in columns "T" through "AA" (the Before Rates part of the "*Fixed-Weight Average Price Change Calculation*" matrix).

The "Before Rates" computations apply current prices (May 2009) to the hybrid billing determinant volumes, and the "After Rates" (proposed prices) apply the proposed prices to the same (fixed) hybrid billing determinant volumes, creating a fixed-weight (by volume) methodology. This controls for factors other than the change in prices.

Hybrid billing determinant volumes are used in the before and after price change computation, but hybrid billing determinant revenues are not. Using hybrid billing determinant revenues introduces bias, because factors other than the change in price are not controlled. Additionally, the percentage price change computation is overstated if hybrid billing determinant revenues are used, because of the integration with the May 2008 price change associated with Q3 FY 2009. Using the fixed weight average price change calculation methodology correctly determines total revenue to be \$631,205,279.

1           CHAIRMAN GOLDWAY: We're now ready for  
2 questions from the Commission. Dr. Kiefer, your  
3 statement covers a lot of ground. And to help  
4 maintain an orderly record, the Commission will start  
5 with some general questions, and then it will take up  
6 questions related to each of the classes and the  
7 proposed rates for each of those classes.

8           We've already had some discussion with other  
9 Postal Service representatives about how the size of  
10 the requested increase was decided. Would you please  
11 describe your role in determining the overall size of  
12 the increase?

13           THE WITNESS: In this particular price  
14 adjustment, as it was laid out in the Postal Service's  
15 action plan issued in March, Postal Service management  
16 determined that it would be appropriate to request a  
17 moderate price increase, above CPI, so therefore  
18 requiring the use of the exigent price change  
19 mechanism.

20           And we were told that, in general, we were  
21 asked to provide prices that, for most of the products  
22 that covered their costs in the four- to six-percent  
23 range.

24           If your question was whether the pricing  
25 function was the origin or was, directed this level of

1 price change, the answer is we received this as a  
2 directive.

3 CHAIRMAN GOLDWAY: So you received direction  
4 from management --

5 THE WITNESS: Yes.

6 CHAIRMAN GOLDWAY: -- to establish prices  
7 within a range.

8 THE WITNESS: Yes.

9 CHAIRMAN GOLDWAY: In your testimony,  
10 throughout your testimony you say that there is a  
11 general knowledge and expertise in the community and  
12 within management about prices. How did you get that  
13 information? Top management told you a range, but  
14 isn't it -- you said there were a lot of people who  
15 work in the field, who are familiar with their clients  
16 and familiar with mailers. And somehow that  
17 information got to you? How did you get information  
18 from the lower level up to your decision level?

19 THE WITNESS: I would say that much of this  
20 knowledge, when you use the term in your question "in  
21 the field," I think that really what we're talking  
22 about is not so much the field as it's used in  
23 standard postal discussions, meaning people out there  
24 in the various plants. Although there is constant  
25 communication between the plants and headquarters.

1                   But we're talking mainly with the functions  
2                   in headquarters, many of the people who work there  
3                   have come from the field, but the people who,  
4                   especially those who work with our product and our  
5                   product management area, they have just continuous  
6                   contact with, with our customers. They are, they are  
7                   very well informed about the trends and what's going  
8                   on in the various industries.

9                   And I would point out that the, the head of  
10                  our Product Management Group is a member of the  
11                  Executive Committee. He's top management. So these  
12                  ideas flow horizontally, but they also flow up. And  
13                  so there's continuous information exchange and  
14                  discussions that go on, so that upper management,  
15                  middle management, and other levels are kept apprised  
16                  of some of these factors that it was discussing in the  
17                  statement.

18                 CHAIRMAN GOLDWAY: Could you better describe  
19                 the role of product managers? You said product  
20                 managers.

21                 THE WITNESS: Yeah, well, product, when we  
22                 say product management, we have, we have individuals  
23                 and functions which are tasked with the  
24                 responsibilities of managing the various postal  
25                 products. And I should say also maybe more than

1 postal products; some of our products, some of our --  
2 some of the mail we handle may be better addressed by  
3 the mail shape.

4 So we may have product managers who focus on  
5 products that are let's say predominantly letters or  
6 predominantly flats. And so they, they may cover more  
7 than one particular product, in a sense that they may  
8 focus on flats. And it is their responsibility to see  
9 what can be done to manage the profitability of these  
10 particular product lines that we have.

11 They're not tasked with operational  
12 responsibilities, or necessarily with the financial  
13 responsibilities, but they communicate with different  
14 functions. Their goal is to try to improve mail  
15 volume and profitability, and they communicate with  
16 the pricing function. They communicate with other  
17 areas to try to see what kind of initiatives we can,  
18 we can put forth in order to increase the  
19 profitability of the Postal Service, actually within  
20 their areas.

21 CHAIRMAN GOLDWAY: So these people who let's  
22 say manage flats are charged with dealing with mailers  
23 who mail flats, and encouraging increased volume.

24 THE WITNESS: Yes.

25 CHAIRMAN GOLDWAY: But they, then, relate to

1 you what the mailers feel is their price sensitivity?

2 THE WITNESS: They communicated within the  
3 Postal Service, yes, they communicated that. They  
4 have communicated to me. But I, what I wanted to say  
5 is that they communicated within the Postal Service,  
6 to senior management, their concerns about the price  
7 sensitivity of different mailer groups. And that was  
8 what informed the decision by management to request  
9 this moderate increase, and to keep it within the  
10 range specified.

11 CHAIRMAN GOLDWAY: And after the overall  
12 size of the rate increase was determined by top  
13 management, you went, as I understand it, you went  
14 through the different classes of mail. And the exact  
15 amount, the 5.6 percent, was then something that was  
16 your discretion, based on advice you got about price  
17 sensitivity for different classes of mail, to come up  
18 to the 5.6 percent?

19 THE WITNESS: The 5.6 percent was an end  
20 result. We were not, we were generally given guidance  
21 to develop prices that fell within the four- to six-  
22 percent range.

23 Also, for certain products and categories  
24 that were, recently haven't been covering their costs,  
25 we were given guidance on above, I want to say price

1 increases above the range, or outside of the range.

2 We developed prices that we understood were  
3 responsive to, to this particular set of directions.  
4 And when we sort of totaled it all up, it came to 5.6  
5 percent. So that's where the 5.6-percent number came  
6 from. We weren't specifically given that number.

7 Of course, this was communicated with senior  
8 management, you know, and it was found to be  
9 acceptable.

10 CHAIRMAN GOLDWAY: So if I get it right,  
11 then you went sort of class by class, or maybe product  
12 by product, and within that range figured out how you  
13 were going to allocate the paying.

14 And what factors did you use to shape your  
15 decision for each of the classes of mail? We'll go  
16 through class by class, but kind of in a general way,  
17 how did you use the factors? And how did you use one  
18 factor in one class, and another factor in another  
19 class?

20 THE WITNESS: Well, we look at, we had some  
21 fairly -- we had some fairly tight guidance on that.  
22 For example, four to six percent is not a broad range,  
23 but it does allow a little bit of leeway. There are  
24 some constraints.

25 When we do our pricing, we are required by,

1 required to observe a number of constraints. Some of  
2 these are, come out of some of the, let's see, the  
3 work-sharing requirements. Some come from the, some  
4 of the Commission's directives. For example, in the  
5 last annual compliance determination.

6 So these helped us to levels of prices that  
7 would respond to the various constraints that we had  
8 in addition to the, to the management directive. So  
9 we, we also looked at some of the, some of the sort of  
10 traditional pricing relationships, where we would try  
11 to keep certain price relationships in balance.

12 But then, in addition to that we were given  
13 guidance on some other, you mentioned classes of mail.  
14 The package services class, for the first time at  
15 least that I can recall the package services class as  
16 a class failed to cover its costs. And so most of the  
17 products in that class got above-average, and I  
18 believe outside of the four- to six-percent range,  
19 they got increases outside of that range. So we had  
20 some guidance there that we should exceed the range in  
21 order to try to move that particular class of mail  
22 closer to covering its cost.

23 And the same is true with the periodicals  
24 class of mail. We were given guidance on that, both  
25 with respect to the overall price, but also as to the

1 amount if dispersion that we thought we should allow  
2 in developing the prices.

3 CHAIRMAN GOLDWAY: Dispersion?

4 THE WITNESS: The range around the average.  
5 Whether it should be close to average or far.

6 CHAIRMAN GOLDWAY: Were you given guidance  
7 that everything should be pretty much around the  
8 average? Or were you told that you could give wide  
9 differences within each class?

10 THE WITNESS: We were asked to keep, we were  
11 asked to keep within the range, and generally close to  
12 the average, with certain, certain exceptions were  
13 allowed.

14 In the case, I mentioned periodicals, we  
15 were asked to keep the prices of most categories under  
16 10 percent, the price increases under 10 percent.

17 CHAIRMAN GOLDWAY: And small parcels? Were  
18 you given guidance on those?

19 THE WITNESS: Yes, we were.

20 CHAIRMAN GOLDWAY: Was that also under 10  
21 percent? Or was it --

22 THE WITNESS: No.

23 CHAIRMAN GOLDWAY: What was the percentage  
24 for that?

25 THE WITNESS: When you say small parcels, I

1 assume you mean standard mail parcels.

2 CHAIRMAN GOLDWAY: Yes.

3 THE WITNESS: Yes. No, we were given  
4 guidance to increase those by larger than 10 percent.  
5 And the, we worked with some of the managers in our  
6 product management area, and went back and forth with  
7 a number of different pricing scenarios, and developed  
8 a -- the approximately 23-percent result was, was  
9 close enough to the guidance that we were given that  
10 it was found acceptable.

11 CHAIRMAN GOLDWAY: I'll ask a question from  
12 the ACWU, and then I'll see about my fellow  
13 commissioners. This is adapted from an ACWU question  
14 1, and also follows, follows up on POIR 3, question 1.

15 In POIR 3, question 1, you were asked about  
16 the Postal Service's belief that the electronic  
17 diversion of first class single-piece mail was  
18 essentially unaffected by price. In the response you  
19 discuss the behavior of individuals who send  
20 remittances.

21 Did your analysis also examine the behavior  
22 of non-household senders of single-piece mail? For  
23 instance, businesses that send single-piece mail? And  
24 if you did, what did you rely on, and how did it  
25 affect your conclusions regarding single-piece mail?

1           THE WITNESS: My understanding is that the,  
2           that our conclusions were not sort of bifurcated into  
3           an analysis, a separate analysis of parcels versus  
4           single piece, but was more of a whole. That the  
5           factors that, that we understand were the driving  
6           forces behind diversion of single-piece mail to  
7           electronic alternatives were not, did not arise from  
8           the old price of single-piece mail, but rather were  
9           heavily influenced by let's say transactions mailers.  
10          And I think some of the information that we have seen  
11          suggests that, that some of these forces would not be,  
12          would not necessarily affect individuals or households  
13          differently than small business mailers, for example.

14                 I think I mentioned in my statement that  
15          there's a general sort of familiarity and a sense of,  
16          there's a great sense of convenience, especially among  
17          some of the younger generations, with the use of  
18          electronic communications, and a preference for the  
19          use of electronic communications over hard-copy mail.

20                 This certainly would manifest itself in  
21          their decisions to send either personal hard-copy mail  
22          letters, or emails or other types of electronic  
23          communication. And if they worked in a small  
24          business, it would be, I didn't think that we'd see  
25          any real difference.

1 I've also seen some research that was  
2 prepared for use of the Postal Service by the Boston  
3 Consulting Group, where they, in fact, indicated that,  
4 if my memory serves me right, that some of the  
5 transactions mailers might be more willing to force  
6 the issue with businesses than with households.

7 So the part that I saw did not distinguish  
8 between larger businesses and smaller businesses, but  
9 it may well be that it would flow on down to the small  
10 businesses, where they may be more assertive in trying  
11 to drive some of this business mail into the  
12 electronic channels.

13 CHAIRMAN GOLDWAY: But your decision on  
14 raising the single-piece first class mail by two cents  
15 and an additional ounce was presuming that first class  
16 single-piece mail is unaffected by price.

17 And what we can see is that about one half  
18 of single-piece mail is sent by households. The other  
19 half, therefore, is sent by a variety of businesses,  
20 some large, some small; and that single-piece mail,  
21 businesses may have a different sensitivity to price.

22 And are you saying that Boston Consulting  
23 Group did a study on businesses, and found out that  
24 their single-piece mail is also not affected by price?

25 THE WITNESS: No, I didn't mean to make that

1       assertion.

2                   What I was saying is that on the issue of,  
3       of the price, the effect of price on volume, there is,  
4       of course, the choice of, the price may have an effect  
5       on how you send, I would say how much mail you send;  
6       but it also may affect whether you send mail at all.  
7       Which is sort of like the extreme end of, you know,  
8       how much you mail.

9                   The Boston Consulting Group information that  
10       I saw suggested that, that the decision, or that many  
11       transaction mailers were attempting to persuade or  
12       otherwise encourage, or perhaps even compel, some of  
13       their customers to use electronic forms of bill  
14       payment and presentment of payment.

15                   And I did not see that there was -- well,  
16       what I saw in some of that information was that some  
17       of these transaction mailers might be more willing to,  
18       in fact, use more persuasive, or to compel the issue  
19       with businesses than with single, with households,  
20       with consumers.

21                   I did not see any research by the Boston  
22       Consulting Group that actually measured the price  
23       sensitivity of, and let's say the traditional  
24       elasticity effect of small businesses versus  
25       households. I believe that our forecasting group does

1 our demand analysis. They measure the elasticity for  
2 single-piece mail, but they don't differentiate  
3 between households and businesses. I don't have a  
4 differential.

5 CHAIRMAN GOLDWAY: For businesses, you  
6 didn't have a different --

7 THE WITNESS: No.

8 CHAIRMAN GOLDWAY: Was it felt that the  
9 availability of Forever stamps would mitigate, to some  
10 extent, the price increase reaction for single-piece-  
11 mail users?

12 THE WITNESS: Well, the Forever stamp  
13 certainly is a, is a convenient way to mitigate some  
14 of the difficulties that, that arise from a price  
15 change. And it may provide sort of a temporary  
16 transition.

17 But I think that the Forever stamp, it  
18 provides a convenient way to make a transition.  
19 Because over time, the Forever stamp goes up in price.  
20 So it's not like the -- unless one stockpiles large  
21 quantities of Forever stamps, in which case one could,  
22 if they never run out, one could offset the effects of  
23 a price change.

24 But what it does is, it's more of a  
25 convenience. Because eventually, when one runs out of

1 Forever stamps, one has to go and buy them at whatever  
2 the current price is.

3 CHAIRMAN GOLDWAY: So you don't think it  
4 affects the elasticity at all.

5 THE WITNESS: I don't know. I haven't  
6 studied that. I haven't seen any data on that.

7 CHAIRMAN GOLDWAY: Anyone else want to jump  
8 in? Vice Chairman Hammond?

9 VICE CHAIRMAN HAMMOND: I think both of  
10 these are in the general category, before we get into  
11 specific classes. But, good morning, Dr. Kiefer.

12 THE WITNESS: Good morning.

13 VICE CHAIRMAN HAMMOND: Thank you for being  
14 here. I listened to Mr. Neri this morning, and he  
15 talked about moving mailers to more efficient behavior  
16 of operations to lower costs. And I think these  
17 mailers are doing so; yet, they're not necessarily  
18 receiving the savings by moving to more automation.

19 Would you say that that is the case? Or  
20 would you dispute that? Or, how would you respond?

21 THE WITNESS: Well, we believe that our  
22 prices do send signals, and that -- I'm not sure the  
23 exact context of, of Mr. Neri's, I'm not sure exactly  
24 what he might have meant. But in general, when we  
25 have discounts for automation, we believe that they do

1 have an effect.

2 VICE CHAIRMAN HAMMOND: So you would say  
3 that they, indeed, end up receiving these savings by  
4 moving to more automation. That's essentially what  
5 you would say, then, by that?

6 THE WITNESS: If a, the discount that we  
7 offer for automation does reflect savings. So if  
8 somebody prepares mail such that it's automation-  
9 compatible, and we can put it on our automated  
10 equipment, they are entitled to whatever discounts are  
11 given to that. And so they can enjoy the savings.

12 VICE CHAIRMAN HAMMOND: Okay, all right.  
13 Okay. The other thing that I was wondering about, and  
14 I asked Mr. Neri the same question. But I was  
15 wondering, have you ever designed on your own, or been  
16 asked by personnel at the Postal Service, to design  
17 anything on any class or subclass of mail that would  
18 end up driving mail out of the system because it's  
19 supposedly unprofitable to the Postal Service, and the  
20 Postal Service would end up losing less money if that  
21 particular type of mail left the system? Have you  
22 ever looked at that, or done anything towards that?

23 THE WITNESS: I have absolutely never been  
24 told to, directed, or suggested, or anyhow been  
25 advised to price, develop a set of prices that would

1 drive unprofitable mail out of the system. I've never  
2 done that. I've never heard of anything like that.

3 VICE CHAIRMAN HAMMOND: So that's like not  
4 even a feasible thought.

5 THE WITNESS: Let me try to give a little  
6 context here. We can look at various categories of  
7 mail. And if we look at the, at our cost level  
8 analysis for 2009, we see that there are certain  
9 categories that are indeed failing to cover their  
10 costs.

11 But we do not focus solely on the sort of  
12 instantaneous, you know, profit or loss of particular  
13 categories of mail. I mean, all of the, the products  
14 that we now offer, we believe are capable of earning  
15 the Postal Service a profit or covering their cost,  
16 given appropriate management, over time.

17 And so our goal is to try to achieve that;  
18 really to try to get these products to cover their  
19 cost. Recognizing that, to the extent that we may  
20 increase prices, that the volume may adjust. I mean,  
21 that's a fact of life in pricing.

22 But we think that we can bring these  
23 products to a position where they will cover their  
24 costs, and bring a profit. It will, this is a long-  
25 term goal.

1 I think, as I said in the statement, it was,  
2 the Postal Service decided that it would not try to  
3 force some of these products to get up to the full  
4 cost coverage in one step. The Postal Service is very  
5 concerned about what impacts the, its pricing  
6 decisions can have on its customers. And particularly  
7 in this era when there is, there are electronic  
8 alternatives available.

9 And I think I mentioned at several points in  
10 my statement that the Postal Service is concerned that  
11 very large increases in a very short amount of time  
12 could push some of these mailers past a tipping point,  
13 where this, this mail may disappear. They may decide  
14 just they're not going to stay in the mail.

15 So we realize it's an eventual process, it's  
16 an evolutionary process. We realize that we don't  
17 have forever to do this. But we realize that there is  
18 a role pricing can play, and there's definitely a role  
19 that efficiencies can play. To close the gap.  
20 Profitability is not just a matter of pricing, it's  
21 not just a matter of cost. It's the inter-  
22 relationship between the two.

23 VICE CHAIRMAN HAMMOND: Okay. Well --

24 CHAIRMAN GOLDWAY: Could you --

25 VICE CHAIRMAN HAMMOND: I was just going to

1 say thank you for your responsive explanation. I  
2 don't have any more questions on general, thank you.

3 CHAIRMAN GOLDWAY: Well, it follows directly  
4 on this discussion. Which is, could you define for us  
5 what the term "rate shock" means in your statement?

6 THE WITNESS: I do use the term "rate shock"  
7 in a number of cases. Mainly in conjunction with  
8 discussing price changes that would, with relation to  
9 certain work-sharing categories. Because this is, in  
10 fact, a term in the, in the law and in the PRC  
11 regulations.

12 I don't think that rate shock is a term that  
13 can be defined absolutely. By saying that this number  
14 is rate shock, it's the same number for all products,  
15 it is the same number in all circumstances.

16 Rate shock refers to an assessment that a  
17 particular price change would cause unacceptable harm  
18 or damage to a particular product, or customers for  
19 that product.

20 In determining what constitutes rate shock,  
21 the Postal Service as a whole kind of looks at a  
22 number of factors. It obviously considers economic  
23 conditions, general economic conditions. It considers  
24 conditions that may be a little bit more particular to  
25 the individual category. It looks at the individual

1 mailers who mail within the category.

2 The industry, and whether the industry is  
3 healthy or is ailing. All of this, this information  
4 is taken into account, and an informed judgment is  
5 made as to whether a particular price increase would  
6 lead to rate shock.

7 And this, given the fact that this is, as I  
8 explained, a bit specific to the set of circumstances,  
9 it could change over time. But it also, a level of  
10 increase that would constitute rate shock for one  
11 product may not necessarily constitute rate shock for  
12 another.

13 CHAIRMAN GOLDWAY: Well, one presumption is  
14 that a range between four a six percent you determined  
15 would not be rate shock.

16 THE WITNESS: In general, yes. That this  
17 was, that this would not cause rate shock to the  
18 category.

19 CHAIRMAN GOLDWAY: Do you have any specific  
20 percentage above which rate shock would be considered  
21 likely?

22 THE WITNESS: We would use really a specific  
23 judgment based on individual sets of circumstances.  
24 So what might be rate shock to one price category of  
25 mail may not, in our judgment, be rate shock to

1 another.

2 No, I don't have a specific sort of broad-  
3 brush number.

4 CHAIRMAN GOLDWAY: Well, this is a bit of a  
5 homework assignment for you. For each discount, where  
6 you do assert in your filing the rate shock exception,  
7 could you please file with the Commission your planned  
8 timeline for phasing out the excess discount?

9 THE WITNESS: We will respond to that, yes.  
10 Thank you.

11 CHAIRMAN GOLDWAY: Anyone else want to jump  
12 in?

13 COMMISSIONER BLAIR: Madame Chair, thank  
14 you. Dr. Kiefer, in your testimony beginning on page  
15 53 you discuss the objectives and factors.

16 In reviewing the factor objectives, did you  
17 give more or greater weight to some objectives over  
18 other objectives and some of the factors, are some  
19 more equal than others?

20 THE WITNESS: Well, in general, this is also  
21 a case-by-case basis. In responding to the  
22 Commission's rules, which require us to show how in  
23 particular our price changes help promote the, or  
24 respond to the factors and objectives, we interpret  
25 this as not meaning that every single price is, needs

1 to, let's say, necessarily promote or respond to, in a  
2 particular way, to every single factor and objective.

3 So to the extent that we look at this as  
4 overall, that our prices do help, let's say, promote  
5 the factors. But we may be, that doesn't necessarily  
6 mean that you could take every single price of the  
7 thousands of prices we offer, and say specifically how  
8 this particular price promotes factor X more than,  
9 more than this other price cell, or promotes factor X  
10 more than factor Y. It's more generalized.

11 COMMISSIONER BLAIR: The reason I'm asking  
12 that is that we had a previous discussion regarding  
13 flats. And I just was wondering how much of a  
14 priority on cost coverage the Postal Service, what  
15 kind of priority or premium on cost coverage does the  
16 Postal Service place?

17 THE WITNESS: A very high priority,  
18 Commissioner Blair. We are, we are very determined to  
19 see that our flats products move toward covering their  
20 costs.

21 At the same time, I think I mentioned this  
22 in some of the earlier discussion, that we're looking  
23 out over time. We're concerned. I mean, some of  
24 these products might need a 15- or 20-percent increase  
25 in order to cover their costs.

1           We determined that that probably would be  
2 counter-productive, to try to reach all the way to  
3 full cost coverage in one step. The fact that we did  
4 not propose prices that went all the way to covering  
5 the costs does not in any way mean that we, we don't  
6 consider that a very high priority.

7           COMMISSIONER BLAIR: I think this is more of  
8 a statement than a question. But where I'm concerned  
9 is that cost coverage is an objective, I'm sorry, a  
10 factor in the Act. But it seems to me that it's  
11 always achieved by increasing rates. And I am just as  
12 concerned that costs be addressed that bring rates,  
13 that can achieve the current, that can achieve lower  
14 rate increases.

15           And so I want to make sure that -- my  
16 concerns are the balance between the two. But I also  
17 noticed on page 58 of your statement, you said that  
18 price change is important to consider in the long  
19 term, rather than simply focusing on this year's  
20 prices in isolation.

21           My view of an exigency is that it's an  
22 emergency, and it addresses a short-term need. You're  
23 saying it addresses a long-term need? And is this a  
24 structural issue that you're invoking? Or as a basis  
25 of the, for a basis of the exigency?

1           THE WITNESS: As I understand your question,  
2 well, let me try to answer that, and then you can tell  
3 me if you think that I've addressed your concern.

4           Well, it's clear from the statements of Mr.  
5 Corbett and Mr. Masse that our needs for revenue are  
6 very much a, sort of a near term; that my  
7 understanding is we may not, if we do not get some  
8 relief -- which can come from several areas; one you  
9 mentioned was reduction in costs, others are increase  
10 in revenues -- the Postal Service could find itself  
11 unable to, to meet its obligations.

12           COMMISSIONER BLAIR: We had a discussion  
13 about this over the last two days, that even with,  
14 should the price, an exigency be found, and the price  
15 increases be granted, it's not sufficient to meet the  
16 cash flow needs in 2011 or 2012.

17           THE WITNESS: That is an area, getting into  
18 that level of detail is really beyond what I --

19           COMMISSIONER BLAIR: I understand that, but  
20 we had this discussion over the two days, and the  
21 postal witnesses acknowledged that. So I'm trying to  
22 put into place -- and you brought it up in your  
23 testimony -- about how this exigency is addressing a  
24 long-term need, or is considering the long term, and  
25 not simply focusing on the year's prices.

1 THE WITNESS: Right.

2 COMMISSIONER BLAIR: And I see a disconnect,  
3 or I don't understand that.

4 THE WITNESS: Okay.

5 COMMISSIONER BLAIR: I thought it's more to  
6 address a short-term need.

7 THE WITNESS: Let me tie, let me try to tie  
8 that statement together, and maybe that will satisfy  
9 you. When I talked about the long-term need -- well,  
10 first of all, the fact that we are requesting an  
11 increase at the level of, on average, of 5.6 percent  
12 is, does try to sort of push revenues up faster than  
13 we think our costs will go. So this will try to cover  
14 part of the need.

15 But the discussion of the long term  
16 generally in my statement was to focus that when we  
17 choose how far we go in our pricing, we always have to  
18 have the long term in mind. Because trying to solve  
19 the problem by let's say increasing the overall prices  
20 by 20 percent, which is probably on the order of  
21 magnitude we may have needed, might have damaged our  
22 customer base. And we really are concerned that this  
23 could do that.

24 In the long term, it would not be wise that  
25 if we felt that we could get a big burst of, of

1 revenues from an extremely high price increase, but  
2 then sort of accelerate it and cause the erosion of  
3 mail volumes such that we would end up destroying the  
4 business.

5 So the long term is, in some sense, a factor  
6 that constrains us from solving the whole exigent need  
7 solely by raising prices. Does that connect that for  
8 you?

9 COMMISSIONER BLAIR: Well, it does, and  
10 again, it sets off concerns with me that I think the  
11 cap right now is about .76.

12 THE WITNESS: Yes. I think we have --

13 COMMISSIONER BLAIR: Or 5.78, I'm sorry. A  
14 little over half a percent.

15 THE WITNESS: Yes, yes.

16 COMMISSIONER BLAIR: So you're proposing  
17 to -- my math is terrible. But you're proposing to  
18 raise prices 10 times that of the cap, basically. So  
19 that fits in the long-term interest of the Postal  
20 Service?

21 THE WITNESS: Well, we take this step  
22 reluctantly.

23 COMMISSIONER BLAIR: I think maybe that's an  
24 unfair question. That's a question that the  
25 Commission has to address.

1 THE WITNESS: Right. But certainly --

2 COMMISSIONER BLAIR: To me, that's 10 times  
3 what the cap would be at a time when, if you've read  
4 the headlines the past few days, the stock market is  
5 again plummeting today; there is a risk that the  
6 recovery is stalling. And where I'm coming from is  
7 saying and we're going to break the cap, and we're  
8 going to do it by 10 times, to address short- or long-  
9 term needs, is something that I'm still trying to get  
10 my head around.

11 THE WITNESS: Right. Well, I think the  
12 situations that you mention certainly are, are factors  
13 that lead us to, that lead us to believe that any  
14 increase in our prices needs to be moderate. And I  
15 realize that, you know, I'm not going to dispute your  
16 math; it may be a fairly high ratio.

17 COMMISSIONER BLAIR: The 5.78 I believe was  
18 based in Postal Service testimony. I want to say it's  
19 about three quarters of a percent, so my math may be  
20 somewhat off. But I think it's still, if it's nine or  
21 seven or five, five times the rate of what is  
22 permitted already under law, and by busting the cap to  
23 do so, is something that I'm still, I'm still troubled  
24 with. And I appreciate your answers on this.

25 THE WITNESS: Could I continue to address

1 this? I realize this is a serious concern for the  
2 Commission.

3 The ratio looks very high. And that is, of  
4 course in part, because the actual level of CPI  
5 inflation is pretty low.

6 Taken as a difference, the number, we're  
7 asking for something that is maybe on the order, maybe  
8 just a little bit under, four to five percent over the  
9 cap.

10 And when we think about this, I think it is  
11 important for the Commission to keep in mind that we,  
12 we are proposing these prices to go into effect in  
13 January of 2011. Our last price change was in May of  
14 2009. I think that's about -- and I will also confess  
15 to not having a calculator-like mind -- but I think  
16 that's about 19 or 20 months.

17 And I think that when we take that, that 5.6  
18 percent, and we sort of annualize it, the actual  
19 increase is something between maybe around three to  
20 three and a half percent.

21 So on an annualized basis, we are asking,  
22 we're asking for more than the rate of inflation. But  
23 we are also trying to keep it as moderate as we could.

24 COMMISSIONER BLAIR: I understand the  
25 difficult position you're in. I just hope that you

1 understand the difficult position you're asking  
2 customers to bear at a time that their costs are  
3 increasing.

4 THE WITNESS: Absolutely. Absolutely.

5 COMMISSIONER BLAIR: And their businesses  
6 are shrinking, and the burden that would be placed on  
7 them by an increase like that. And that's more of a  
8 statement than a question.

9 THE WITNESS: Well, I was just going to say,  
10 speaking of statements, I hope that one message that  
11 came across loud and clear in my statement was our  
12 concern that these price increases might have on our  
13 customers.

14 I mean, I think it came out over and over  
15 again that we are really concerned about our  
16 customers. And at the same time, we're concerned  
17 about paying the bills.

18 COMMISSIONER BLAIR: Thank you.

19 CHAIRMAN GOLDWAY: Commissioner Langley.

20 COMMISSIONER LANGLEY: Thank you. And thank  
21 you, Dr. Kiefer, for being here today. Please be  
22 assured that your concern about over-pricing and, you  
23 know, the interest in your direct testimony, that your  
24 noticing what's happening with your customers comes  
25 across well.

1           In fact, I was intrigued by your discussion  
2           on page 13 of your testimony. You talked about the  
3           tipping point of large first class mailers.

4           And I had read your testimony in preparation  
5           for Mr. Corbett and Mr. Masse, and asked both of them  
6           whether they believed the decline in after-rate volume  
7           estimates adequately reflected the reality of today's  
8           economic environment. And both said that there was a  
9           great deal of reliance on historical information as  
10          far as how customers would react to pricing increases.

11          And I think your statement is a better  
12          reflection, perhaps. And I don't think that you're  
13          intending to contradict them at all.

14          But I'm curious whether or not you believe  
15          that the volume declines estimated are really  
16          reflecting the reality of today's environment.

17          THE WITNESS: When you say the volume, are  
18          you referring to the volume responses to our price  
19          changes contained in Mr. Masse's statement?

20          COMMISSIONER LANGLEY: Yes, I am.

21          THE WITNESS: Okay. Yeah, I think I can,  
22          again, try to put a little context in that.

23          I know that Mr. Masse's analyses used our  
24          elasticities, price elasticities from our forecasts,  
25          our demand models. These are, of course, as all

1 econometric equations are, they're based on historical  
2 data. They remain the best information we have. And  
3 this is, this is what we have to use.

4 I think the discussion on page 13 and around  
5 that section of my testimony was, was designed to  
6 discuss what could happen if we went well out of the,  
7 let's say the -- first of all, if we went well beyond  
8 the sort of, the type of historical experience that we  
9 had.

10 Now, I mentioned a little bit earlier that  
11 there were some who thought that, well, we should  
12 raise prices to cover the costs. And you know, if it  
13 was, it might take 15 to 20 percent or something like  
14 that. You know, I think a 20-percent increase for all  
15 mail is not something that lies within the recent  
16 historical experience of, you know, the Postal  
17 Service.

18 So in that sense, when we're dealing with,  
19 let's say, a potential impact of a hypothetical  
20 increase that, of that size, the elasticities may not  
21 provide as good guidance as they might if we were  
22 dealing with something that is much closer to the  
23 range. And I would say that price increases of five  
24 percent or so I think are within the historical range  
25 that some of these equations were estimated using.

1           My recollection is that, sort of in the old  
2 former Rate Case days, we would wait two or three  
3 years before changing prices. And we would get price  
4 changes, you know, easily, within the four-, five-,  
5 six-percent range.

6           So I would, I think that we want to look at  
7 this in two ways. One is to say that the price  
8 changes we are proposing are not unprecedented. And  
9 the, we wouldn't necessarily feel that we should  
10 discard the elasticity information.

11           On the other hand, when we start going much  
12 higher, if we say that well, why didn't you raise the  
13 prices, you know, 10, 15, 20 percent; well, then we  
14 are concerned that perhaps some of this, I called it  
15 tipping point effect might occur.

16           So I'm not sure that the two are necessarily  
17 totally opposed to each other, you know.

18           COMMISSIONER LANGLEY: So if the economy  
19 were to contract rather than to expand, as is the  
20 expectation of the Postal Service in this particular  
21 analysis, would it be possible at all to even estimate  
22 volume decline?

23           THE WITNESS: Well, I --

24           COMMISSIONER LANGLEY: I think I may be  
25 asking an impossible question.

1 THE WITNESS: Well, it's perhaps as question  
2 I would, I would want to consult with our forecasting  
3 people on. But in general, I mean, there is some  
4 volume -- excuse me, some economic growth factored  
5 into this. Generally, economic growth leads to, to  
6 more mail volume, and more revenue.

7 So I would think that it would not be a  
8 positive development if, if the economy contracted  
9 compared with what we had assumed in Mr. Masse's  
10 exhibits.

11 COMMISSIONER LANGLEY: Thank you. And let  
12 me just ask a final question right now. Obviously,  
13 you, I think you very much appreciate that these price  
14 increases proposed have real meaning to the businesses  
15 that are impacted by them.

16 THE WITNESS: Absolutely.

17 COMMISSIONER LANGLEY: What quantitative  
18 analysis does the Postal Service do to determine what  
19 segments of the industry might be more delicately  
20 situated right now than others?

21 THE WITNESS: Well, I heard this question  
22 asked in a number of contexts. We don't generally  
23 find, it's rather difficult to do numerical analyses  
24 on these. We don't have data, and in many cases,  
25 virtually all cases I know, our judgment about which

1 segments are more delicate than others, it's an  
2 informed judgment. It's based upon considering the,  
3 you know, the individual segments, the economic  
4 conditions, the other, other factors.

5 It does take into account what information  
6 we have from estimated elasticities. But in the end,  
7 it's an informed judgment. It's not something that  
8 we, we found a bunch of data, and put it into a model,  
9 and turned the crank, and it said okay, this segment  
10 is more delicate than that. There is --

11 COMMISSIONER LANGLEY: It's a qualitative  
12 analysis.

13 THE WITNESS: It's a qualitative analysis  
14 based on informed judgment, yes.

15 COMMISSIONER LANGLEY: Do you look at volume  
16 declines?

17 THE WITNESS: Well, yes. I mean --

18 COMMISSIONER LANGLEY: What factors go into  
19 it as you're looking at it?

20 THE WITNESS: Well, as I said before, the  
21 general economic conditions. And we also look at the  
22 individual product information. We have revenue and  
23 volume information on the product. And if products  
24 are losing volume, well, that's a clear sign that  
25 there is, that this is in a precarious position.

1                   And we also look at factors like what some  
2 of the alternatives are. Is this just something  
3 that's going to go down with the economy and bounce  
4 right back with the economy? Or is it something that  
5 is susceptible to electronic diversion, and could  
6 just, you know, the volume's going to go down and  
7 never come back.

8                   COMMISSIONER LANGLEY: Does the Postal  
9 Service go beyond and look at economic forecasts, both  
10 short- and long-term, for a particular industry? See  
11 what outside analysts might be saying?

12                   THE WITNESS: Yes. Well, certainly we look  
13 at economic forecasts. And we also -- yes.  
14 Especially the people in the product management are  
15 continually monitoring the industry media, you know,  
16 the trade press and others. And they see this kind of  
17 information, that forecasters, people say this is  
18 going to grow, or this is not going to grow, or  
19 whatever.

20                   COMMISSIONER LANGLEY: Do you have meetings  
21 among the staff you say who monitor these things?  
22 Product managers and your pricing people, and you go  
23 class by class or product by product? Do you discuss  
24 these things?

25                   THE WITNESS: Well, I would say --

1                   COMMISSIONER LANGLEY: Is there a structured  
2 way to go about this? You're kind of, everything is  
3 very general and amorphous in your descriptions. Is  
4 there a structured way to make these decisions?

5                   THE WITNESS: You mean as to the -- well, as  
6 I said at the beginning, we were given a directive  
7 that constrained the price changes for most products  
8 into the, a narrow range of four to six percent.

9                   There certainly were discussions made,  
10 generally between, since the, since the impetus or the  
11 general guidelines were made by senior management,  
12 much of the discussion with the product management was  
13 between, well, between the product managers and senior  
14 management.

15                   COMMISSIONER LANGLEY: So did they tell you  
16 we want an eight-percent raise for periodicals? You  
17 know, we want a five-percent raise, you know, under  
18 the reg, for standard flats? Did they give you those  
19 specific directions?

20                   THE WITNESS: My understanding is, for  
21 periodicals, eight percent was --

22                   COMMISSIONER LANGLEY: What you were told.

23                   THE WITNESS: -- we were told. How far, how  
24 far would be acceptable as a deviation, I'm talking  
25 now not for individual cells within the range, but for

1       how far the averages could deviate from that and still  
2       be acceptable.

3                   I don't know. We presented eight percent,  
4       and it was accepted.

5                   COMMISSIONER LANGLEY: And the presumption  
6       that standard flats was a delicate industry and needed  
7       some caution in its rate increase was something that  
8       was given to you. You didn't participate in meetings  
9       where your, the people who have knowledge and  
10      expertise and you, the pricing people, met together to  
11      decide on this?

12                  THE WITNESS: Well, let me -- I'm aware that  
13      a case was made to give, that standard mail flats was  
14      a particularly delicate, in a particularly delicate  
15      situation; and that it should receive a lower range of  
16      price increase.

17                  In the end, the considered judgment of  
18      management was that it should stay within the range.  
19      That it should be in the range of very close to five  
20      percent, in the middle of the range.

21                  COMMISSIONER LANGLEY: So upper management  
22      has been giving you pretty clear direction as to what  
23      the price increases should be.

24                  THE WITNESS: Well, we were given a range,  
25      and it was, it was fairly clear. And we were allowed

1 to propose prices that sort of fell within the range,  
2 and in some cases, that the direction was a little bit  
3 more explicit.

4 COMMISSIONER LANGLEY: So with regard to  
5 flats, and your response to POIR-3, question 2, that  
6 you said the Postal Service did not rely on studies or  
7 analysis of the industries that send flat-shaped mail  
8 in various classes, just to determine the size of the  
9 increase that each could tolerate.

10 Instead, you said that you relied on  
11 knowledge gained from meetings with mailers,  
12 conferences, and trade press coverage of the industry.  
13 Were those meetings you were part of?

14 THE WITNESS: No.

15 COMMISSIONER LANGLEY: And how much of that  
16 information, if you don't know, how much of it came  
17 from sources that are not directly affected by those  
18 rates? In other words, did management do any external  
19 surveys, or seek guidance from something other than  
20 talking to the users of flats? Non-industry sources  
21 of information.

22 THE WITNESS: Oh, you mean -- would you  
23 discount, for example, the trade press? Do you mean  
24 to exclude those?

25 COMMISSIONER LANGLEY: Yes. The things not

1 directly related to the --

2 THE WITNESS: Okay. I can't address that  
3 specific question. I mean, I don't know the answer.

4 COMMISSIONER LANGLEY: So the case for how  
5 delicate flats, as a class, were, was made at a higher  
6 level? When you were looking at deciding well, it  
7 should be five percent, did you have some information  
8 about flats that you were using? How did you get that  
9 information?

10 THE WITNESS: I was asked to come up with a  
11 set of prices that were in the, generally in the five-  
12 percent range.

13 The evaluation as to, as to what these, as  
14 to the initial goal, or the five percent, was based  
15 upon a discussion, which I was aware of. But I mean,  
16 I was not in the middle of it.

17 All of the, the individuals who were  
18 involved, have familiarity with the customer areas and  
19 the segments and the industry. How much of it came  
20 from -- well, as I said, some of the information came  
21 from mailers. And they are obviously an interested  
22 party. Some of it comes from news media that report  
23 on these industries.

24 And I don't see a particular reason why they  
25 would not be considered a survey, a disinterested

1 reporter of the facts. I mean, in other words, I  
2 don't think this was just from lobbying groups. This  
3 was, you know, the people who monitor the industry.

4 And there's a real value in getting accurate  
5 information. And so if a particular consulting group  
6 does a study, and says that such-and-such, a  
7 particular type of advertising is going to go up or go  
8 down, then it gets reported. And our people monitor  
9 that, and use it to make their judgments.

10 COMMISSIONER LANGLEY: I see. Okay.

11 THE WITNESS: It wasn't just, I didn't mean  
12 to convey that this was just we were talking to  
13 specific mailer groups only.

14 COMMISSIONER LANGLEY: Well, I certainly  
15 don't deny that you should talk to mailer groups in  
16 this area.

17 THE WITNESS: Oh, no, we get a lot of --

18 COMMISSIONER LANGLEY: Information is very  
19 useful and helpful. I just wanted to get a sense of  
20 the range of information that you were able to  
21 consider.

22 When you were asked about first class mail  
23 and were told the four to six percent, were you told  
24 two cents? Because, you know, you could have come up  
25 with a one-cent increase and other rates within the

1 class. Were you told specifically two cents?

2 THE WITNESS: Well, we started out with a  
3 two-cent increase because that was, that was the  
4 particular change allowing for the convention that we  
5 place the first-class stamp in whole cents.

6 The two-cent increase was the increase that  
7 got us within the range. And although I believe that,  
8 well, I mean, that was what we started with. And I  
9 think that --

10 COMMISSIONER LANGLEY: So you never did  
11 experiment with --

12 THE WITNESS: With the one cent?

13 COMMISSIONER LANGLEY: With the one cent and  
14 the other options that would fall from there?

15 THE WITNESS: No. We didn't --

16 COMMISSIONER LANGLEY: Like 45 cents, you  
17 know. A clear number.

18 THE WITNESS: Certainly no detailed analysis  
19 was done. We started out with the two-cent increase.  
20 I won't say that nobody at any time wondered about a  
21 45-cent stamp. But we started out, because it was, it  
22 fell within the range. And we thought that this was  
23 an appropriate increase.

24 COMMISSIONER LANGLEY: Just for the record,  
25 I'll say that consumers would, I think, pay more for a

1 second ounce and a third ounce if they all fit neatly  
2 into nickels and dimes, and they could remember them  
3 all.

4 THE WITNESS: Duly noted.

5 COMMISSIONER BLAIR: Could I just issue a  
6 clarification for the record?

7 COMMISSIONER LANGLEY: Sure.

8 COMMISSIONER BLAIR: When we were talking  
9 about the CPI caps, I believe in the Postal Service's  
10 testimony you had a half a percent?

11 THE WITNESS: Five-seven-eight I think was  
12 the number that I recollect.

13 COMMISSIONER BLAIR: Right, five tenths, six  
14 tenths. And according to the Commission's web site,  
15 as of the 16th of July, we'll be posting a new one in  
16 the next week or so, we're at .968.

17 THE WITNESS: Okay.

18 COMMISSIONER BLAIR: So just for  
19 clarification purposes, that's still five to six  
20 times --

21 COMMISSIONER LANGLEY: And with the banked  
22 amount, we're pretty much at one percent.

23 THE WITNESS: Okay. Thank you.

24 COMMISSIONER LANGLEY: That's interesting.  
25 A specific question here. With regard to your

1 response to POIR-3, question 4, you identified the  
2 source of retained pre-sort volume of 53 million  
3 pieces is based on management judgment.

4 Again, could you elaborate on your  
5 management judgment? I mean, why was it 53 million  
6 pieces, as opposed to, say, 50 million pieces? This  
7 is for free reply, reply writes free program.

8 THE WITNESS: Okay. I'm sorry, did you say  
9 POIR --

10 COMMISSIONER LANGLEY: POIR-3, question 4.

11 THE WITNESS: -- 3, question 4. The copy I  
12 have here has four -- has several subparts.

13 CHAIRMAN GOLDWAY: I don't know that I have  
14 a page number on it. Question 4, Response A, just  
15 before the Response B.

16 THE WITNESS: Okay.

17 CHAIRMAN GOLDWAY: At the end of A, if they  
18 retain --

19 THE WITNESS: I see it. This is a  
20 definition then.

21 CHAIRMAN GOLDWAY: And in your report, you  
22 have indicated that it will be 53 million pieces. So,  
23 we wanted to get a better sense of how you calculate  
24 these numbers.

25 THE WITNESS: Okay. I can attempt to find

1 that out for you, but I don't know. I didn't do that  
2 particular calculation.

3 CHAIRMAN GOLDWAY: Would you please?

4 THE WITNESS: Yes.

5 CHAIRMAN GOLDWAY: Thank you. Do you have  
6 another question?

7 COMMISSIONER ACTON: Yes. Good afternoon,  
8 Dr. Kiefer.

9 THE WITNESS: Good afternoon.

10 COMMISSIONER ACTON: Thank you for being  
11 here with us. It is a little awkward in how we are  
12 approaching some of these questions, but just so you  
13 know, this is a new format, and hopefully it will stay  
14 novel.

15 But we are working through it by trying to  
16 incorporate in our inquiries some of the community's  
17 important questions, and we are all sort of taking  
18 turns at that opportunity, all right?

19 THE WITNESS: Okay.

20 COMMISSIONER ACTON: But before I do that, I  
21 have a question. How long have you been a pricing  
22 economist at the Postal Service?

23 THE WITNESS: Almost 12 years.

24 CHAIRMAN GOLDWAY: So you were at the  
25 Service doing pricing and setting rates when the

1 reform was enacted in 2006?

2 THE WITNESS: That's correct.

3 COMMISSIONER ACTON: Are you familiar with  
4 the law and statutes as it goes to pricing?

5 THE WITNESS: You are referring to the new  
6 law or the old law?

7 COMMISSIONER ACTON: I am referring to the  
8 Postal Accountability Enhancement Act.

9 THE WITNESS: Somewhat. I mean, I am not an  
10 attorney.

11 COMMISSIONER ACTON: Sure. Neither am I.  
12 When the Act was formulated, I think there is a  
13 provision that calls for the Service to be able to  
14 invoke one last opportunity for an Omnibus Rate Case.  
15 Do you know that?

16 THE WITNESS: Yes, I remember that.

17 COMMISSIONER ACTON: Do you know if there  
18 were discussions at the Service at the time about the  
19 provision in the statute that allowed for that, and  
20 what the thoughts were at the management level?

21 THE WITNESS: Well, ultimately the decision  
22 was made -- and this is my recollection. At the time,  
23 we were awaiting the publication of the Commission's  
24 rules, which came out in Order Number 43, and my  
25 understanding was that we were waiting to see how the

1 rules were, and that was one factor that led to our  
2 decision whether to file the final old style rate case  
3 or not.

4 But once the Commission's rules were filed,  
5 management made its judgment, and decided that it  
6 would not use the old format. I was not part of that  
7 decision.

8 COMMISSIONER ACTON: The reason that I am  
9 inquiring is that I am not privy to the background of  
10 why the Legislators decided that it was important to  
11 include that provision in the new law, but one guess  
12 might be that they were anticipating that the Postal  
13 Service management would look at the requirements of  
14 the law in its totality as far as what sort of costs  
15 and expenses would be called for going forward,  
16 including these new workforce obligation expenses and  
17 what not.

18 And that they might take the opportunity, or  
19 at least give an assessment on whether or not they  
20 would be able to management to adequately cover those  
21 costs without having to dramatically or even  
22 indramatically reset the rate structure.

23 THE WITNESS: As I said, the decision was  
24 made by senior management, and I do not know all of  
25 the factors, or all of the weights, that went into

1 that decision.

2 COMMISSIONER ACTON: I appreciate that, and  
3 I understand that there is some decision making going  
4 on that may not always be in your office.

5 THE WITNESS: Yes, quite a bit.

6 COMMISSIONER ACTON: But my bottom line  
7 point on that is that I am just trying to understand  
8 if the Service reviewed all of these costs, and  
9 anticipated that they didn't need to file the Omnibus  
10 case because they were expecting that they would be  
11 able to work under the new rate cap regime to meet  
12 these obligations.

13 THE WITNESS: Well, one thing that we have  
14 to keep in mind is that if we chose to file a final  
15 rate case under the old scheme, it would have to be as  
16 all the other PRA rate cases would be a break even  
17 case.

18 So there wouldn't be any opportunity for us  
19 to sort of stockpile funds against the possibility  
20 that maybe 3, 4, or 5 years down the road that we  
21 would face difficult circumstances.

22 COMMISSIONER ACTON: No, I wasn't talking  
23 about stockpiling excess funding.

24 THE WITNESS: Okay.

25 COMMISSIONER ACTON: I was talking about the

1 veracity of forecasting, and the hazards involved in  
2 trusting projections that in some cases may not be  
3 very accurate.

4 THE WITNESS: Well --

5 CHAIRMAN GOLDWAY: Or the ability to cover  
6 costs.

7 COMMISSIONER ACTON: And I know that the  
8 Chairman is preparing to adjourn or to break for  
9 lunch, but I have one more of our questions from a  
10 POIR, and also I just want to clarify, that when  
11 Commissioner Langley is talking about her worries  
12 about elasticities, and the Service is bringing a case  
13 which bears upon proving that this is an extraordinary  
14 and exceptional circumstance, if the Commission buys  
15 that, and we end up implementing some of these rates  
16 that you are proposing, how can we not expect that  
17 perhaps in an extraordinary and exceptional  
18 circumstance price elasticity that products may  
19 respond to that in an extraordinary and exceptional  
20 fashion, meaning --

21 THE WITNESS: I understand. All I can say  
22 is that we have a better chance of seeing more typical  
23 behavior with a more moderate increase than we would  
24 if we have one that was sort of unprecedented.

25 COMMISSIONER ACTON: Okay. That's fair.

1 Here is a followup to a Presiding Officer's  
2 Information Request Number 3 was question two.

3 THE WITNESS: Question two. Okay.

4 COMMISSIONER ACTON: And it is for  
5 information --

6 CHAIRMAN GOLDWAY: No, I think we did that  
7 one.

8 COMMISSIONER ACTON: Did we do that one  
9 already?

10 CHAIRMAN GOLDWAY: This is the one from GCA.

11 COMMISSIONER ACTON: Oh, here we are. I'm  
12 sorry. This is adapted from a GCA Question Number  
13 33A. The Postal Service proposes a one cent increase  
14 in the additional ounce rate for single piece flats  
15 and letters, for non-automation presort letters and  
16 flats, and for automation flats.

17 In contrast, no increase is proposed for  
18 additional ounces of single piece parcels, presort  
19 parcels, and automation letters. Can you please  
20 explain the reasoning behind this aspect of your  
21 proposal, including the reason for creating a new  
22 distinction between additional ounce for single piece  
23 letters and parcels?

24 THE WITNESS: In one respect, I think one of  
25 the main factors that led us to moderate the price for

1 -- or for the additional ounce price for first-class  
2 parcels was also part of our proposal for first-class  
3 parcels was a change, such that the first three ounces  
4 would receive a fairly -- well, it would all have the  
5 same price.

6 That meant that one ounce parcels would now  
7 pay the same price as three ounce parcels; and two  
8 ounce parcels, what would now paid a different price,  
9 would now pay the same as three ounce parcels.

10 That led to a significant increase, and in  
11 order to -- we recognize that many of our mailers mail  
12 a range of parcels. So, in other words, it is not  
13 necessarily people only mailing two ounce parcels.

14 Some people mail two ounce parcels, and mail  
15 four ounce parcels. So the moderation of the  
16 additional ounce price for parcels was designed to  
17 sort of work together to maybe mitigate some of the  
18 impact of increasing the zero to one, and one to two,  
19 ounce prices to match that of three ounces.

20 So we would keep prices for parcels that  
21 were a bit above the three ounce range so that they  
22 didn't have such a large increase. So mail over that  
23 sort of that light weight range -- you know, one, to  
24 two, to three ounce parcels, and four ounces, and five  
25 ounces, would have a bit of a mitigation there.

1           COMMISSIONER ACTON: Okay. I think that  
2 wraps -- I'm sorry.

3           CHAIRMAN GOLDWAY: I just wanted to ask more  
4 on that. I forget the number, but the rate increase  
5 for that single ounce parcel --

6           THE WITNESS: For the zero to one ounce  
7 parcel?

8           CHAIRMAN GOLDWAY: The zero to one ounce  
9 is -- well, 50 or 60 -- well, what is the percent? It  
10 is really a significant rate increase.

11          THE WITNESS: Well, yes, it is a significant  
12 rate increase.

13          CHAIRMAN GOLDWAY: Somewhere between a 30  
14 and 50 percent increase in price. That is not rate  
15 shock?

16          THE WITNESS: Well, as I said -- well, let  
17 me explain. We were concerned that the lightest  
18 parcels mailed and that were priced, or that were zero  
19 to one ounce, were not adequately covering their  
20 costs.

21                 And as I said, we looked at the parcel  
22 prices, with the goal of trying to come up with a  
23 pricing that over a reasonable range would be  
24 appropriate. Now, if you only mailed zero to one  
25 ounce parcels, you would be seeing a fairly large

1 increase, although the absolute price would be -- it  
2 is not extremely large. Let me see if I can find it.

3 (Pause.)

4 THE WITNESS: Well, for a retail one ounce  
5 parcel, our proposed price is \$1.71, and we have to  
6 remember that with this comes the ability to mail  
7 something anywhere in the United States for \$1.71.

8 CHAIRMAN GOLDWAY: And what is the cost  
9 coverage when you go up to \$1.71 for three ounces?

10 THE WITNESS: I'm afraid that we don't have  
11 cost -- well, I am sure that we don't have cost  
12 coverages by ounce, but I am not sure what the cost  
13 coverage is for the parcels. The prices that we were  
14 giving were actually for retail parcels, which is the  
15 higher parcel price. I mean, higher than our  
16 commercial parcels.

17 COMMISSIONER ACTON: Dr. Kiefer, I have a  
18 followup question, please, from our Agency analyst.

19 THE WITNESS: Sure.

20 COMMISSIONER ACTON: They would like to know  
21 if you are maybe planning or intending to set letter  
22 and parcel, additional ounce, at the same price at  
23 some time in the future, or if you would keep them  
24 different?

25 THE WITNESS: I am sure that it is something

1 that would be considered. There isn't at this time --  
2 I don't think there is an explicit intent, let's say,  
3 one way or the other. I mean, it is something -- I  
4 mean, the additional ounce price is one that often  
5 varies.

6 It sort of is traditionally a --  
7 traditionally, it is something that has been used to  
8 sort of take up the slack sometimes, and if the first  
9 ounce price goes up quite a bit, sometimes the -- and  
10 as I say, the additional ounce price has been used to  
11 sort of offset some of the impact of the lumpiness  
12 that is caused by the -- you know, by the whole cent  
13 constraint.

14 COMMISSIONER ACTON: Thank you.

15 CHAIRMAN GOLDWAY: Okay. I think we have  
16 had a long morning, and we expect to have a long  
17 afternoon. We have many more questions for you on  
18 periodicals and standard package services, and special  
19 services.

20 So what I propose is that we break for  
21 lunch, and we return at two o'clock sharp. Thank you.  
22 This meeting is adjourned until 2:00 p.m.

23 (Whereupon, at 12:48 p.m., a luncheon recess  
24 was taken.

25 //

- 1 //
- 2 //
- 3 //
- 4 //



1 mailings, and the pieces co-mailed, and bundled co-  
2 mailed, and pallets containing co-mailed flats and/or  
3 bundled?

4 THE WITNESS: I don't know the extent of the  
5 data that is available to address that.

6 CHAIRMAN GOLDWAY: We would really like to  
7 know what kind of data the Postal Service keeps, and  
8 if it does, to obtain it in some form. The point is  
9 that catalog and periodicals mailers believe that they  
10 have become more efficient, and that they followed  
11 directions and in some cases encouraged the Postal  
12 Service to implement procedures to co-mail and develop  
13 pallets, and get out of stacks.

14 And yet they are receiving a higher than  
15 average percentage price increase, and standard plus  
16 gets a price increase that is below the average. And  
17 there seems to be some question of fairness that they  
18 would like to have us explore.

19 THE WITNESS: Okay.

20 CHAIRMAN GOLDWAY: Whatever information you  
21 can provide with regard to data --

22 THE WITNESS: On co-mailing?

23 CHAIRMAN GOLDWAY: Yes, on co-mailing for  
24 periodicals is what we would like. And then can you  
25 answer why did the CRA unit cost of periodicals mail

1 increase by more than double the rate of inflation  
2 between 1996 and 2009, despite the deployment of the  
3 AFSM-100, and the increased amount of work sharing  
4 performed in the periodicals class?

5 THE WITNESS: I'm afraid that is beyond a  
6 pricing scope.

7 CHAIRMAN GOLDWAY: It seemed to be something  
8 that we could ask Mr. Neri either. Do you know who we  
9 might ask?

10 THE WITNESS: The analysis of cost --

11 CHAIRMAN GOLDWAY: CRA cost data, and unit  
12 cost for periodicals went up 54 percent in that 15  
13 year period. The CPI went up 37 percent.

14 THE WITNESS: Right. In pricing, we take  
15 the CRA as an input. That is produced in finance. If  
16 I were to ask that question, they would be the ones  
17 that I would ask.

18 CHAIRMAN GOLDWAY: Is there a particular  
19 person in finance that we should direct this to?

20 MR. RUBIN: I think the finance staff is  
21 aware of this question, and so I can push them to get  
22 some response. It is a pretty complicated question,  
23 but we can provide what we can find out.

24 CHAIRMAN GOLDWAY: Okay. So there are three  
25 questions here on behalf of intervening parties with

1 regard to the basic issue of why costs continue to go  
2 up, and go up more than inflation, when the  
3 periodicals class has implemented itself and with the  
4 AFSM-100, significant automation and efficiency  
5 improvement.

6 And we want any data that we can on the  
7 number of periodicals that can be tracked for having  
8 co-palletization, or other kinds of automation that's  
9 possible, and any explanations in finance as to why  
10 these costs go up so much more than the cost of  
11 inflation.

12 The reported unit cost for delivery for  
13 periodicals flats, and standard flats mail, increased  
14 by 24 percent and 36 percent, respectively, between  
15 2007 and 2009 alone. And we don't seem to have  
16 answers. Now, a question for you, Dr. Kiefer.

17 THE WITNESS: Okay.

18 CHAIRMAN GOLDWAY: When you were asked about  
19 preparing these rates did you think about waiting to  
20 increase the periodicals rate disproportionately as  
21 was recommended to you in advance of the completion of  
22 the periodical study that has been mandated by  
23 Congress?

24 Were you aware of that periodicals study?  
25 What was the thinking in not waiting for that study?

1 THE WITNESS: Well, yes, I was aware that  
2 the periodical study was going on, but we were also  
3 aware that under the current law that the only  
4 opportunity that we have to increase periodicals, or  
5 the overall increase of periodicals prices above the  
6 general rate of inflation would be with an exigent  
7 price change.

8 This particular price change, my  
9 understanding is that this will need to be completed  
10 by the beginning of October, and I am not sure just  
11 when the periodical study will be completed. Once  
12 this exigent price change case is closed, periodicals  
13 is going to be subject to a price cap with whatever  
14 the change in the CPI is.

15 And so this was our opportunity where we  
16 felt that we needed to take to make whatever  
17 adjustment that we thought we could make.

18 CHAIRMAN GOLDWAY: But there isn't any  
19 adjustment for standard and the price cap problem for  
20 standard.

21 THE WITNESS: Well, not exactly. Standard  
22 mail flats --

23 CHAIRMAN GOLDWAY: They are within a class.

24 THE WITNESS: -- is a product within a  
25 class, and so the class as a whole is capped, and so

1 it is possible for us to give above average increases  
2 out into the future -- I should say above CPI, and  
3 changes out into the future for standard mail flats by  
4 just giving more moderate increases to other  
5 categories.

6 So this was an opportunity -- and was sort  
7 of a unique opportunity to be able to make this change  
8 for periodicals. Whereas, we knew that we would have  
9 perhaps have other opportunities for standard mail  
10 flats.

11 I would also point out that standard mail  
12 flats, even with the lower increase, if we look at Mr.  
13 Masse's numbers, it actually ends up moving closer to  
14 full cost coverage than periodicals with a higher  
15 increase.

16 CHAIRMAN GOLDWAY: They start from a  
17 different --

18 THE WITNESS: Oh, definitely. They start  
19 from a different point.

20 CHAIRMAN GOLDWAY: And I would like to point  
21 out for the record that the Commission has been urging  
22 the Postal Service to move forward on this periodical  
23 study for many, many months, and their portions of the  
24 study always seem to be delayed in being produced.

25 So you may not be getting the institutional

1 support that you should to have this available  
2 information before making a decision on prices. We  
3 would have preferred that that study be completed by  
4 now.

5 THE WITNESS: Okay. Thank you.

6 CHAIRMAN GOLDWAY: The next party that has  
7 suggested a question is Time Warner, and I will read  
8 this. Under your pricing proposal, carrier route  
9 flats receive a 9 percent increase, while five digit  
10 automated flats receive a 5.8 percent increase. At  
11 page 40, lines 9 through 16, you explain that this  
12 retains the 9.8 percent rate difference between the  
13 two rates, so as not to encourage more carrier route  
14 presorting that may be unnecessary in an FFS  
15 environment.

16 After the first 100 FFS machines are fully  
17 deployed, what percentage of periodical flats will be  
18 processed on FFS?

19 THE WITNESS: We have checked with our  
20 operations folks, and they told us that their  
21 expectation is that if we look at the total flats,  
22 periodicals and other flats, that approximately one-  
23 quarter to one third of flats would be processed on  
24 the FFS after the first 100 machines were deployed.

25 But that they did not have any way to

1 differentiate between periodicals and other flats, so  
2 that if we had to pick a number, or a range of  
3 numbers, for analyses that we would go with the  
4 average of a quarter to a third.

5 CHAIRMAN GOLDWAY: Why didn't the Postal  
6 Service elect to establish separate rates for carrier  
7 route copies in FFS zones and in non-FFS zones?

8 THE WITNESS: Well, what that was involved  
9 with would be a deaveraging of prices, and when we  
10 decide to deaverage prices, there are usually certain  
11 policy considerations behind it, and one of the  
12 effects of deaveraging prices is an effect that we  
13 call like the push up-push down effect.

14 And if we had established separate zones, we  
15 would have had this push up and push down effect, and  
16 given our directive to keep --

17 CHAIRMAN GOLDWAY: Can you explain what the  
18 push up-push down effect is?

19 THE WITNESS: Oh, surely. If a certain  
20 product -- well, most of our products consist of a  
21 range, or perhaps they are all flats, but they may be  
22 different kids of flats, or from different sources, or  
23 whatever, and different -- or perhaps prepared in  
24 different ways, et cetera.

25 So we are not dealing with a totally

1 homogeneous set of mail. So let's say there is a  
2 different type of operation, for example. For  
3 example, let's pick something like -- well, let's say  
4 that we know that standard mail letters is -- well, I  
5 should maybe not pick that one.

6 But suppose we had -- well, let's take our  
7 parcel post, and right now if you deposit the mail,  
8 and it is going to a particular zone, and it weights a  
9 certain amount, you pay one price.

10 But that doesn't matter whether you are  
11 bringing these pieces, let's say, to a destination  
12 facility or not. We do have separate destination  
13 discounts, but there is a certain amount of mail that  
14 is required, and let's say 50 pieces.

15 If we decided that we wanted to offer  
16 separate prices for people who brought, let's say, 10  
17 pieces to a BMC, or an NBC now, well, perhaps there  
18 are some people who are already doing that. This may  
19 be residual mail from a drop ship mail or whatever.

20 What those people who would take advantage  
21 of this, or are taking advantage of that, would see  
22 their prices fall, and the others, all things being  
23 equal, would see their prices go up, because what you  
24 are doing is you are deaveraging the price.

25 So that is the push up-push down effect. So

1 when you deaverage, some are going to get higher than  
2 they are today, and others are going to get lower, all  
3 other things being equal.

4 If we were to set up and to deaverage the  
5 carrier route price, we would have had a push up  
6 effect that would have gone against the directive that  
7 we had to keep the prices for periodicals categories  
8 within the close range around the 8 percent, and  
9 especially to keep them below a 10 percent increase.  
10 So that was one factor that led us not to do that type  
11 of deaveraging.

12 CHAIRMAN GOLDWAY: Is that because there is  
13 only a quarter of the product that would go to FFS,  
14 and three-quarters that would go to a non-FFS zone?

15 THE WITNESS: And also one consideration  
16 that we would always make is how much of the mail is  
17 this going to affect, and also where -- well, what is  
18 the eventual use, let's say, of FFS versus non-FFS.

19 One of the things that we might take into  
20 consideration, or that we should take into  
21 consideration, is how much of the -- well, the fact  
22 that we are in a transition point now, and whether we  
23 should be establishing deaveraged prices while we are  
24 still sort of in the process of deploying and don't  
25 really know how many pieces are going to end up in the

1 FFS zones versus non-FFS zones.

2 CHAIRMAN GOLDWAY: So how do you encourage  
3 mailers to use the FFS if there isn't some  
4 deaveraging?

5 THE WITNESS: Well, my understanding is that  
6 the FFS will be deployed in certain areas, and the  
7 mail operation for those areas will be a required  
8 preparation. I don't believe that this is going to be  
9 an option. The mail will have to be prepared for FFS  
10 if it can be used on a machine.

11 CHAIRMAN GOLDWAY: And if they don't get a  
12 price rate to do that wouldn't they go to the non-FFS  
13 locations?

14 THE WITNESS: Well, the FFS -- the FFS  
15 machine will -- is for a sort of particular delivery  
16 area. So if mailers want to mail to, let's say,  
17 Northern Virginia, and if Northern Virginia is an FFS  
18 zone, then they have to give us FFS compatible mail.

19 If they want to reach subscribers or  
20 customers in Northern Virginia, this is the kind of  
21 mail prep that they are going to need to do. It is  
22 not like they can give us mail -- well, do you  
23 understand what I am saying?

24 That if it is going to be addressed within  
25 an FFS zone, it is going to have to have FFS

1 compatible preparation.

2 CHAIRMAN GOLDWAY: So the drop shipping --  
3 the mailers will have to pay for the differentiation  
4 in preparation for the FFS zones, and the non-FFS  
5 zones, and they will be burdened with additional costs  
6 to go to the FFS. So it is sort of deaveraging for  
7 them?

8 THE WITNESS: No. We are talking about mail  
9 that is being taken to, let's say, a particular place,  
10 and mailers are already mailing to Northern Virginia,  
11 and let's say that they are drop shopping to that, and  
12 they are giving us the mail.

13 CHAIRMAN GOLDWAY: You are going to require  
14 them if they are drop shipping in Virginia to prepare  
15 the mail to meet FFS standards?

16 THE WITNESS: Well, yeah, but --

17 CHAIRMAN GOLDWAY: But if they are dropping  
18 to -- well, I don't know, somewhere in Ohio or Iowa,  
19 that doesn't have an FFS?

20 THE WITNESS: They will prepare it  
21 differently.

22 CHAIRMAN GOLDWAY: Okay. They will prepare  
23 it differently?

24 THE WITNESS: Yes.

25 CHAIRMAN GOLDWAY: So the mailers get the

1 deaverage across, and they are going to have to pay  
2 more for one than the other, and there isn't any  
3 distinction that you are preparing, the deaveraging?  
4 That is the question.

5 THE WITNESS: Well, I want to make sure that  
6 I understand the question correctly. What we have is  
7 that it is like -- the FFS is like our current DPS  
8 system for letters.

9 CHAIRMAN GOLDWAY: The DPS system?

10 THE WITNESS: Yes, the DPS system for  
11 letters. If you give us mail -- well, the mail in DPS  
12 areas -- well, actually in all areas, and if it is  
13 automation mail, it has to be compatible with our DPS  
14 machines. In order to get the automation prices --

15 CHAIRMAN GOLDWAY: Was the averaging  
16 successful for the DPS?

17 THE WITNESS: I don't -- well --

18 CHAIRMAN GOLDWAY: I mean, there was the  
19 averaging that encouraged DPS, and was it successful?

20 THE WITNESS: A very high percentage of our  
21 letter mail is now automation compatible, and  
22 therefore, DPS'd. I mean, even if it doesn't have the  
23 barcode, it is mail that is machinable that we can  
24 then put our own barcode on and run through the DPS  
25 machines. So there is not a large amount of letter

1 shaped mail that is not machinable left, and on our  
2 prices, they reflect that.

3 CHAIRMAN GOLDWAY: Commissioner Langley had  
4 a question.

5 COMMISSIONER LANGLEY: I am listening to the  
6 discussion and maybe you can help refresh my memory.  
7 Wasn't there a requirement that had something to do  
8 with labels on periodicals that had to do with --  
9 well, the placement of labels on periodicals in order  
10 to be FFS compatible, and this required a great deal  
11 of discussion between periodical mailers and the  
12 Postal Service.

13 And I just don't think there really was a  
14 distinction as to whether or not they would -- you  
15 know, be able to take advantage of FFS.

16 CHAIRMAN GOLDWAY: That they had to re-  
17 engineer the whole front of --

18 COMMISSIONER LANGLEY: Right, they re-  
19 engineered everything.

20 CHAIRMAN GOLDWAY: In order to have a  
21 different spot for their addresses.

22 COMMISSIONER LANGLEY: Yes, and yet they are  
23 not getting the benefit of increased deficiencies. I  
24 mean, what is sort of the status of that? And I think  
25 it goes in with the general discussion.

1 CHAIRMAN GOLDWAY: Yes.

2 COMMISSIONER LANGLEY: We are looking for  
3 efficiencies and --

4 THE WITNESS: Right. An address placement -  
5 - and I don't want to get too far beyond my knowledge,  
6 but I am aware that address placement on flats is an  
7 important component of being able to utilize the FFS.

8 The purpose of the FFS is to hold down flats  
9 processing and delivery costs, and to keep them from  
10 growing. So to the extent that it keeps down those  
11 costs, the mailers do benefit, but they may need to  
12 make some changes. For example --

13 COMMISSIONER LANGLEY: Well, they have to  
14 make changes.

15 THE WITNESS: Yes.

16 COMMISSIONER LANGLEY: I mean, as the  
17 Chairman said --

18 CHAIRMAN GOLDWAY: They have already made  
19 changes, and then they will be required to make more  
20 changes to prepare their mail, in addition to the  
21 address for FFS. But only 25 percent of that mail is  
22 going to be -- have the opportunity to use FFS.

23 THE WITNESS: Yes. Well, this number, the  
24 one-quarter to one-third, refers to the amount of  
25 estimated coverage from the first wave of deployment.

1 I don't think we are claiming that only 25 percent of  
2 the flats mailed will ever be able to get any benefits  
3 from this.

4 I mean, to the extent that it holds down the  
5 costs of our products, all mailers who use those  
6 products will benefit. It doesn't necessarily require  
7 that every change that improves or increases our  
8 efficiency be given with a discount.

9 And in this particular case, we know that  
10 the periodicals and the standard mail flats are  
11 struggling to cover costs. So to the extent that we  
12 have efficiencies gained through FFS, that would mean  
13 that the amount that we would have to increase prices,  
14 and not necessarily where we would end up lowering  
15 prices, but the amount that we would have to increase  
16 prices would be smaller.

17 So as I think I pointed out in some of the  
18 discussion earlier today, that the cost coverage  
19 really is the result of an interaction between costs  
20 and the revenues, or the prices. So to the extent  
21 that we can gain efficiencies through costs, that  
22 means that we have to rely less on price increases to  
23 move these towards full cost coverage.

24 CHAIRMAN GOLDWAY: There is another question  
25 here from Time Warner. It points to the annual

1 compliance determination reports that we issued in  
2 2009, and I will quote from that.

3 "The low pass throughs are problematic for  
4 two reasons. First, they exacerbate the periodicals'  
5 cost to revenue gap, because mailers are not paying  
6 for the full cost of handling bundles and containers."

7 "Second, the combination of low and  
8 differential pass throughs may send conflicting price  
9 signals to mailers, and prevent them from entering  
10 mail in a way that reduces the end-to-end costs.  
11 Current opportunities exist to improve efficiency and  
12 to offer mailers appropriate pricing incentives. The  
13 Postal Service should implement such changes as soon  
14 as practicable."

15 In your statement, you say that in light of  
16 these considerations the Postal Service believes that  
17 an above-average increase of 8 percent, together with  
18 a plan of gradual improvement of cost coverage,  
19 represents a judicious balance between quickly  
20 resolving the periodicals cost coverage problem and  
21 ensuring the best prospects for the long term health  
22 of the periodicals industry.

23 The question is can you clarify what you  
24 mean by a plan of gradual improvement of costs  
25 coverage?

1           THE WITNESS: Well, I think that can be  
2 taken at its face value. The words can be taken at  
3 face value. What we are trying to do is we are trying  
4 to pay attention to the possibilities for enjoying a  
5 cost savings, to the extent that we can get some of  
6 them from some of the initiatives in the flats  
7 initiatives, the flats strategy. We will gain those.

8           We also are going to monitor, for example,  
9 the effects of economic recovery, and to see if this  
10 can sort of help periodicals. We note and I have been  
11 told that there is some improvement in advertising  
12 pages, and this maybe needs some improvement in weight  
13 in some recent data that we have seen.

14           That has the potential for improving the  
15 situation for revenues for periodicals, even aside  
16 from our price increases. We are offering, and we are  
17 asking for a price increase here of eight percent.

18           And we will use pricing to help as one of  
19 the parts to fill in the gap. We realize that this is  
20 not something that can be solved overnight.

21           CHAIRMAN GOLDWAY: You don't have a time  
22 frame?

23           THE WITNESS: We do not.

24           CHAIRMAN GOLDWAY: Gradual improvement means  
25 what?

1           THE WITNESS: Well, it means that we are  
2 going to try to move this along as quickly as we can,  
3 and within the kind of -- in terms of pricing, it  
4 means we will try to move on as quickly as we can  
5 within the restrictions that are on us with respect to  
6 price changes.

7           And we are also going to be looking for  
8 efficiencies, and we note that in the Commission  
9 statement, in the annual compliance determination, the  
10 Commission stated that they believed that there were  
11 some -- they expressed some concern with some of the  
12 pass throughs for some of the container based pricing.

13           CHAIRMAN GOLDWAY: That's right.

14           THE WITNESS: Yes, and that the Postal  
15 Service agrees that there are opportunities there  
16 for --

17           CHAIRMAN GOLDWAY: So does your plan for  
18 gradual improvement include bringing bundle and  
19 container price cost ratios close to a hundred percent  
20 as soon as practicable?

21           THE WITNESS: Well, it was a gradual step of  
22 moving them closer to a hundred percent, and yes, as  
23 soon as practicable, taking into consideration the  
24 fact that we will be looking at what some of these  
25 particular changes may have, and whether they -- you

1 see, we make changes in certain price elements.

2 We have to be aware of the impacts, and  
3 sometimes the impacts can be spread broadly, and  
4 sometimes the impacts are more focused, and they  
5 affect certain segments of an industry more than  
6 others, and that is a consideration that we would want  
7 to take.

8 So we are going to be trying to move as  
9 quickly as we can without sort of overturning the  
10 apple cart.

11 CHAIRMAN GOLDWAY: If we did get cost  
12 coverages that were close to -- or pass throughs that  
13 were close to 100 percent, how much would that improve  
14 the price cost ratios for periodicals?

15 THE WITNESS: Well, I have been told that --  
16 well, are you talking about work share, and all of the  
17 discounts, the ones that exceeded avoided costs?

18 CHAIRMAN GOLDWAY: Yes.

19 THE WITNESS: Okay.

20 CHAIRMAN GOLDWAY: I believe there are nine  
21 of them.

22 THE WITNESS: Yes. We are talking about the  
23 same things, and not necessarily about the cost pass  
24 throughs, for like bundles or something. I have been  
25 informed that bringing these close to a hundred

1 percent would have a positive effect, but a rather  
2 small one.

3 CHAIRMAN GOLDWAY: How much?

4 THE WITNESS: I have seen figures that are  
5 in a single digit millions of dollars, as compared  
6 with overall periodicals revenue of about \$2 billion.  
7 So it is small. It is positive, but small.

8 CHAIRMAN GOLDWAY: And how far would price  
9 cost ratios of bundles and sacks help?

10 THE WITNESS: I don't have a quantification  
11 of that. I do note that we are moving some of those  
12 in the direction. One of the -- well, I'm sorry, but  
13 you said bundles and sacks, and that doesn't focus on  
14 the pallets.

15 One of the effects, or one of the outliers  
16 in our periodicals price changes was that we did  
17 actually give a fairly significant increase for origin  
18 pallets, and so that has a way of moving that.

19 We are also going to be moving other  
20 containers and periodicals in the direction of trying  
21 to increase the recognition of costs in the price. We  
22 have a ways to go. We have made some --

23 CHAIRMAN GOLDWAY: Okay. Throw in pallets,  
24 too. What would be --

25 THE WITNESS: I don't have a figure on that.

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CHAIRMAN GOLDWAY: Can you get it for us?

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THE WITNESS: I will pass that along to some of the folks. I don't know how easy or how difficult that will be to provide an estimate, but I will pass that along.

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CHAIRMAN GOLDWAY: Please try and get that information for us and report back. And while you are at it, do you have a guess as to how many years you are talking about when we are talking about a gradual process of getting --

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THE WITNESS: Well --

CHAIRMAN GOLDWAY: I know that you have been very vague here. Do we have a reference? Two years, four years, or 10 years until we get out to the end of the envisioning of the future? What do you think?

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THE WITNESS: One of the things that I took away from Commissioner Acton's discussion with me right before the break was how difficult it is to predict what might happen in the future. It would be -- I don't actually have a number of years. I can't --

23

24

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CHAIRMAN GOLDWAY: One of the things that Commissioner Acton was pointing out is that we have a regulatory responsibility to assure that the pass

1 throughs are no greater than 100 percent.

2 THE WITNESS: Absolutely. I understand.

3 CHAIRMAN GOLDWAY: That the Postal Service's  
4 pricing is efficient and fair, and I don't know how  
5 long we are going to be able to wait.

6 THE WITNESS: Understood, but I would hope  
7 that the Commission would look and see that we are  
8 making progress, and give us credit for making  
9 progress. I mean, if you look at Mr. Masse's  
10 attachments, you see that we actually have made  
11 significant progress.

12 And if we look at a full years  
13 implementation for periodicals, I think we are up to  
14 around 87 percent cost coverage, which we are  
15 hopeful -- I think we all hope for a variety of  
16 reasons that the economy will improve.

17 But how long it is going to take, it is  
18 difficult to say. There are many conditions that  
19 factor in our ability to raise prices, and the ability  
20 of various customers of ours to absorb price  
21 increases.

22 And how much they will be able to improve  
23 just through the general improvement in economic  
24 conditions. There are so many things out there. What  
25 I would hope that the Commission would do is take a

1 look and see if we are making progress.

2 And perhaps as the economic picture becomes  
3 clearer, we may be able to come up with more  
4 definitive numbers, but I think somebody earlier  
5 mentioned -- I thought someone had mentioned double  
6 dip recession, and we don't know what is going to  
7 happen.

8 CHAIRMAN GOLDWAY: Within the price  
9 structure that you have presented which presort levels  
10 of periodicals and standard flats are given incentive  
11 to migrate to FFS so that they would eventually  
12 benefit from this new efficiency?

13 THE WITNESS: There aren't any price  
14 incentives to migrate to FFS. FFS is going to be --  
15 once FFS is deployed in an area, it is my  
16 understanding that that is going to be the -- well, in  
17 order to get the automation prices, that is going to  
18 be the preparation that is going to be required.

19 So it is not like -- this is not like a  
20 choice between presorting to three digits or five  
21 digits. It is preparation that if you want to get our  
22 automation prices in a particular area, you are going  
23 to have to use this particular preparation.

24 Not that these preparations are especially  
25 erroneous. In fact, it may be that they will be less

1 difficult. I mean, when I am talking about the actual  
2 preparation, in terms of how the mail is presented,  
3 and not whether they will -- well, things like address  
4 placement.

5 COMMISSIONER LANGLEY: Are you talking about  
6 the costs to the mailer as not being erroneous? Like  
7 the re-engineering label plate?

8 THE WITNESS: No, I was talking about that  
9 once that process is done, I was talking about --  
10 well, you see, I understand that the Postal Service  
11 is publishing some new rules that allow mailers to  
12 enter mail prepared for FFS, where they don't have to  
13 make the small bundles anymore.

14 They can give us larger bundles that are set  
15 up for the FFS schemes now. So that would in fact  
16 ease the preparation burden on that for actually  
17 preparing mail, and this is a separate issue from  
18 address placement. I mean, that is something that is  
19 needed, because otherwise FFS is not going to work.

20 CHAIRMAN GOLDWAY: Okay. I am going to  
21 yield to Commissioner Acton for questions.

22 COMMISSIONER ACTON: Thank you, Madam  
23 Chairman. There is a handful of questions that I have  
24 on improvements.

25 THE WITNESS: Sure. Are we talking about

1 operational efficiencies?

2 COMMISSIONER ACTON: No, we are willing to  
3 discuss any aspect of this improvement that you are  
4 willing to talk about, but let me just cite for you  
5 the portion of the ACD that I am referring to.

6 THE WITNESS: Okay. Yes, please.

7 COMMISSIONER ACTON: We make a note that  
8 opportunities exist to improve efficiency and to offer  
9 mailers appropriate pricing incentives, and we  
10 encourage the Postal Service to implement such  
11 strategies -- I'm sorry, such changes as soon as  
12 practicable.

13 THE WITNESS: Yes. Okay. In that  
14 particular quote, it is about pricing, using pricing  
15 as an incentive to get more appropriate mailer  
16 behavior. Well, we expect that each time we change  
17 the prices, we expect to try to move in the  
18 appropriate direction.

19 We think that there are opportunities, such  
20 as trying to reflect more of the container costs at  
21 the various container levels in the prices, and we  
22 expect that these will be reflected in our subsequent  
23 price changes.

24 COMMISSIONER ACTON: So you can see that  
25 what encourages us a lot when we had these

1 interactions with you, and for instance, with your  
2 predecessor here this morning, Mr. Neri, is that when  
3 we have some definitive sort of information about time  
4 frames -- and, for instance, at the closing of Mr.  
5 Neri's discussion, he indicated that come August that  
6 there will be a critical path assessment for some  
7 important productivity measures which we are looking  
8 forward to having.

9 THE WITNESS: Well, as I said, we expect to  
10 take steps -- well, under the PAEA, we now engage in  
11 fairly regular price changes, and in those price  
12 changes, we expect to be moving these prices in a way  
13 that should encourage efficiencies.

14 So this is -- well, I don't think that the  
15 Postal Service can commit to, let's say, going to a  
16 hundred percent cost coverage the next time we change  
17 prices.

18 COMMISSIONER ACTON: Don't misunderstand me.  
19 I don't believe that we are talking you to make that  
20 type of commitment. What we would like you to commit  
21 to do is to develop a time frame, a tentative time  
22 frame for us to look at some aspects, so that we can  
23 better understand how quickly you may be planning as  
24 an organization to address these recurring problems.

25 Let me just ask. Have you developed any

1 benchmarks that you may be using to measure your  
2 success in implementing these types of change?

3 THE WITNESS: Are we talking specifically  
4 about --

5 CHAIRMAN GOLDWAY: Pricing incentives.

6 THE WITNESS: Well, pricing incentives, for  
7 example, such as the ones that were requested in the  
8 ACD. I am not aware of those, but I would have to  
9 check with --

10 COMMISSIONER ACTON: Well, I think what we  
11 are focusing on are efficiency in pricing benchmarks.  
12 Some sort of meaningful milestones which we can look  
13 to, to understand what sort of detailed progress we  
14 are making.

15 CHAIRMAN GOLDWAY: I think for your own  
16 management, it seems to me that you should be saying,  
17 okay, we are going to try and address 25 percent of  
18 this problem every year for the next four years, or 30  
19 percent of the problem for the next three years.

20 THE WITNESS: Understood.

21 CHAIRMAN GOLDWAY: Or some sort of  
22 quantifiable, relatively reasonable, accomplishable  
23 goal.

24 THE WITNESS: Well, I think that last word  
25 is a key element, and perhaps one of the things that

1 makes it difficult to  
2 -- let's say address some of the periodicals problems  
3 through pricing is that periodicals as a class is  
4 price capped, and that restricts the amount of price  
5 changes that we can make on an annual basis.

6 And we don't know the change, and to say  
7 that we can -- for example, let's look at Mr. Masse's  
8 estimate that if we had a full year of the new prices  
9 for periodicals that we think that we would end up  
10 covering under the assumptions -- you know, the  
11 economic assumptions, and we would cover about 87 or  
12 so percent of our costs.

13 To say that we would be able to eliminate  
14 that over the next three years, we are talking 12-1/2  
15 percent or 13 percent, and would require a significant  
16 change. If it were to all fall on pricing, it is not  
17 clear that we would have the capability, and it would  
18 be achievable to increase periodicals prices as 3 or 4  
19 percent a year if inflation turns out to be 1 or 2  
20 percent a year.

21 CHAIRMAN GOLDWAY: Couldn't you commit to a  
22 combination of pricing and efficiency gains, because  
23 apparently Mr. Neri doesn't have any benchmarks either  
24 in terms of efficiency gains for the --

25 THE WITNESS: Well, I understand your

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1 frustration with that, and the postal service really  
2 is concerned about this, and if we were to give -- you  
3 know, let's say two percent a year, because that  
4 happens to be the inflation rate for the next 3 or 4  
5 years, we still wouldn't get there. We would need to  
6 get more from efficiency improvements.

7 We are going to try to do our best, and I  
8 realize that that is a challenge for us to do, and for  
9 you to rely on, but we have to try to use sort of both  
10 blades of the scissors. I mean, they have to work  
11 together.

12 COMMISSIONER ACTON: We are not trying to  
13 discourage you.

14 THE WITNESS: No, I understand that.

15 COMMISSIONER ACTON: I think we have made  
16 our point. We are just trying to understand what your  
17 proposal may be for how you are going to approach this  
18 going forward.

19 THE WITNESS: We will try to capture all  
20 efficiencies, operational efficiencies that we can,  
21 that through the analysis process that if we invest in  
22 some of these efficiency measures that we are  
23 discussing, that Mr. Neri discussed, we ought to make  
24 sure that they actually gain something close to what  
25 we are expecting to make the payoff worth the

1 investment.

2 We don't want to find ourselves even further  
3 in the hole than we were. So all of those have to be  
4 put through their analysis, and they will give us some  
5 of the -- sort of one-half of the equation, and the  
6 other half, we will have to see what we can do with  
7 pricing.

8 But at this time, I don't have projections  
9 for cost savings, and I don't have or I don't know  
10 that we can commit to a specific timetable. We will  
11 try to increase prices in a way that utilizes our  
12 legal capacity to do so as long as we don't feel that  
13 we are doing it in a way that is going to cause damage  
14 to our customer base.

15 COMMISSIONER BLAIR: Dr. Kiefer, I am  
16 sensing from you from what you have been saying today  
17 that there is a general frustration -- and I don't  
18 know if you are reflecting the Postal Service's  
19 frustration with the price cap mechanism.

20 THE WITNESS: Well, I think that -- well, I  
21 am not sure that I can -- I don't know how far I  
22 should go in speaking for the Postal Service on this,  
23 but I should point out that the price cap mechanism  
24 applied at the class level enables us to handle  
25 situations.

1           For example, like standard mail flats, where  
2           it is a portion of a class that is not covering its  
3           costs, and we have opportunities to move along, but  
4           stay within the cap, but the current system poses some  
5           significant challenges to the Postal Service.

6           And I think we all feel that frustration  
7           that the only -- well, the only mechanism that I know  
8           of to break through the cap is the exigent price  
9           change, and it doesn't handle the situation where a  
10          whole class is not covering its costs.

11          I mean, it is applied at the class level,  
12          and so we can only increase the price of periodicals  
13          outside of an exigent price change at the regular CPI  
14          rate.

15          COMMISSIONER BLAIR: So would it be fair to  
16          say that if Congress had not passed the PAEA in 2006  
17          that periodicals rates would be significantly higher  
18          today than they would have been otherwise?

19          THE WITNESS: Well, that may be more than I  
20          could say, but there is a requirement that if Congress  
21          had not passed the PAEA, and we were under the former  
22          regime, the PRA regime, that had a requirement that  
23          some classes of mail would cover their costs, and they  
24          would have increases as large as was required to cover  
25          the costs.

1           Now, here has been several price changes and  
2 other situations going on between that. I am not sure  
3 how everything would have played out, but we would  
4 have been required to propose prices that cover the  
5 costs. I mean, that is just part of the way the law  
6 went. So I think that certainly is possible, that  
7 prices would have been higher.

8           COMMISSIONER BLAIR: And I think that is  
9 probably one of the reasons that Congress passed the  
10 PAEA and the price cap mechanism must have kept rates  
11 down, and it caused the Postal Service to make  
12 efficiencies, and cut costs.

13           THE WITNESS: That is clear, but I wanted to  
14 couch my answer, or make clear that my answer was  
15 referring mainly in the periodicals area, because we  
16 would have been required to cover those costs.

17           If we had not had the PAEA passed, the old  
18 subclasses, which were larger aggregations, would  
19 still have been in existence, and we perhaps would not  
20 have been dealing with the issue of standard mail  
21 flats in the same way that we are dealing with it  
22 today.

23           COMMISSIONER BLAIR: You have been quite  
24 generous in your in your answers, and I know that it  
25 is getting late, but I just hear a yearning for the

1 previous system, and I just wanted to see if you could  
2 clarify that.

3 THE WITNESS: No, I am certainly not  
4 expressing the view of the Postal Service in saying  
5 that we would rather go back. I mean, I have no -- it  
6 is not my call, and even as a professional pricer, it  
7 is a much more complex issue.

8 But there is no system that is perfect, and  
9 I think we are still fairly young in the life of the  
10 PAEA system, and I think we have found out fairly  
11 early on some of the difficulties, and that is what I  
12 wanted to illustrate, and not to damn the whole  
13 system.

14 But we recognize that we have  
15 not found a good way to deal with the situation where  
16 we know we need to adjust prices for a class, and we  
17 are limited by a price cap.

18 CHAIRMAN GOLDWAY: It is a dilemma.

19 THE WITNESS: Absolutely.

20 CHAIRMAN GOLDWAY: And that efficiency gains  
21 are meant to address.

22 THE WITNESS: Yes.

23 CHAIRMAN GOLDWAY: With regard to the PAEA,  
24 the PAEA does give the Postal Service great  
25 flexibility with regard to pricing for competitive

1 products, and in your testimony on page 11, you say  
2 that for purposes of developing prices for this  
3 request, we have used planning assumptions concerning  
4 the prices for certain competitive products that will  
5 take effect in January of 2011.

6           Could you discuss the basic feature of these  
7 assumptions and explain how they were applied to  
8 periodicals, or to other market dominant products?

9           THE WITNESS: I am not sure that this was --  
10 that this really applied to periodicals, but I can  
11 give you an example in -- for example, in --

12           CHAIRMAN GOLDWAY: We weren't sure. What  
13 does it apply to?

14           THE WITNESS: Well, okay, here is a very  
15 precise example. In standard mail certain residual  
16 pieces -- and because there is no single piece price  
17 for standard mail, but certain residual pieces must  
18 pay either first-class prices, or if they weigh more  
19 than the upper limit for first-class, they pay  
20 priority mail prices.

21           Priority mail, of course, is a competitive  
22 product. So in order to estimate what the overall  
23 effect of our price change was, we needed to look at  
24 what the price change would be for priority mail to  
25 estimate what would be the effect on this rather small

1 segment of standard mail.

2 I believe that for the purposes of that  
3 estimate, we put it at a number like -- I think we put  
4 in five percent, which is sort of the mid-range of our  
5 market dominant. I mean, that is not to say that  
6 priority mail on average is going to go up by five  
7 percent, but we use that as a planning assumption.

8 That is the purpose of this portion of my  
9 statement. It did not refer to periodicals. I am not  
10 aware that the two are that connected to periodicals.

11 CHAIRMAN GOLDWAY: Any other questions?

12 COMMISSIONER ACTON: Did you want to  
13 complete the sheet?

14 CHAIRMAN GOLDWAY: I think we can move on to  
15 standard.

16 THE WITNESS: All right.

17 CHAIRMAN GOLDWAY: And try and get through  
18 some of these before we take a break.

19 THE WITNESS: Surely.

20 CHAIRMAN GOLDWAY: With standard mail, I  
21 will begin with some of the questions referred to by  
22 our participants. The Greeting Card Association  
23 points to your statement where you use the phrase  
24 "full coverage".

25 They have questions about its meaning as to

1 "we". On page 7, lines 14 to 15 of your statement,  
2 what is meant by the phrase "gradually moving to full  
3 coverage"?

4 THE WITNESS: In general, when I use the  
5 term "full coverage", it meant that we would cover our  
6 attributable costs.

7 CHAIRMAN GOLDWAY: Does full coverage mean -  
8 - do you mean the system-wide average cost coverage,  
9 or just a hundred percent of attributable costs?

10 THE WITNESS: When I applied that -- I'm  
11 sorry, when I used the term, I believe I was talking  
12 about individual products, or classes of mail, and  
13 that meant that they would fully cover at least a  
14 hundred percent of their attributable costs.

15 CHAIRMAN GOLDWAY: Now, the Greeting Cards  
16 Association asked for a timeline as to gradually move  
17 to full coverage, but I am afraid to ask the question.

18 THE WITNESS: Yes.

19 CHAIRMAN GOLDWAY: I think we have covered  
20 the issue of whether we are going to have any fully  
21 accountable, quantifiable timeline from the Postal  
22 Service, at least from your answers in the negative.

23 The next question is from Valpak, and their  
24 question is the price increase for standard flats is  
25 below the 5.6 percent average. It is 5.1 percent.

1 Why do you believe that incurring continued  
2 substantial losses is reasonable and equitable for the  
3 Postal Service, particularly when other mailers are  
4 required to pay higher coverages to offset these  
5 losses?

6 THE WITNESS: Well, under the -- if we were  
7 required to reach a breakeven or a particular level of  
8 revenue, I would say that the other mailers might be  
9 required to sort of make up the difference, but at  
10 this point we're overall we're losing money. So I'm  
11 not sure I agree with that part of the statement. But  
12 I want to address the question that sort of it's  
13 behind that.

14 I want to point out first of all that  
15 standard mail flats, which is a major one of our  
16 products that is being used, you know, large part by  
17 the catalog industry, is being given a significant  
18 increase, you know, 5.1 percent. This is not higher  
19 than the average but it was, the Postal Service is  
20 concerned that this is, the catalog industry is in a  
21 delicate position. It has had to withstand the  
22 effects of the economic recession, retail sales are  
23 down, that's one of those driving factors that affect  
24 the catalog business.

25 We're concerned that raising the prices very

1 rapidly or in large steps on, for this particular  
2 product, might cause significant harm to the hard copy  
3 mail catalog industry. There is an electronic  
4 alternative to this. We believe though that there is  
5 great value in catalog mail, and we also believe that  
6 as a whole, taken as a whole, that catalog mail, this  
7 catalog industry, is a profitable industry for us.

8 We definitely want to move standard mail  
9 flats toward full cost coverage, but we do not want to  
10 take steps that might cause catalog mailers to trim  
11 their mailing lists or get out of the hard copy mail  
12 system altogether. There are other mail products that  
13 these catalog mailers use which contribute, make  
14 positive contributions. And we think that on the  
15 whole we're making money on this industry and we don't  
16 want to take steps that's going to drive it away.

17 CHAIRMAN GOLDWAY: Do you have any  
18 statistical information, any data, to show the  
19 relationship between catalogers and the other parts of  
20 the mail stream that they use that would in any way  
21 indicate that the, that industry provides at least a  
22 breakeven for you, if not a profit as you suggest?

23 THE WITNESS: The Commission asked POIR  
24 number 3 question 7, asked about this, and I checked  
25 with our product management folks and they provided

1 some information which is actually submitted in public  
2 form in response to this, and we actually I think sent  
3 a nonpublic version, that shows the usage of the top  
4 600 catalog mailers in the various products. Before  
5 this hearing began we were approached and asked about  
6 one of the labels on the --

7 CHAIRMAN GOLDWAY: Right.

8 THE WITNESS: Commissioner, do you have  
9 this?

10 CHAIRMAN GOLDWAY: Yes, and --

11 THE WITNESS: You have it available?

12 CHAIRMAN GOLDWAY: There was a confusion  
13 about --

14 THE WITNESS: Yeah, there was a confusion, I  
15 apologize for that confusion. We have been pretty  
16 busy lately and sometimes things slip through the  
17 cracks. We have contacted those who are familiar with  
18 this analysis and I can confirm that the data, like  
19 the revenue and volume data in this table, are for  
20 Fiscal Year 2009. So that the label, the first line  
21 label where it says, it says Q2 FY 2010, that is  
22 erroneous. That is, these data here are for 2009,  
23 Fiscal Year 2009.

24 If you look at the top line there, these  
25 estimates suggest that we are more than covering our

1 costs from these catalogers. So the Postal Service  
2 does believe that this is a, although it's a  
3 vulnerable segment of our business, the customers are  
4 vulnerable, and we want to move gradually toward full  
5 cost coverage, we note that they're users of a broad  
6 range of products. Standard mail flats is not  
7 covering its costs, we think it should.

8 We think we have the opportunity to as the  
9 economy improves and the catalog industry is more able  
10 to withstand more increases in this particular product  
11 that we can move toward adjustments. And we also hope  
12 that some of the flat strategy initiatives will give  
13 us that sort of that other branch of the equation, you  
14 know, so that we can get some efficiencies on one hand  
15 and on the other make appropriate price adjustments.

16 But we think this is a profitable segment of  
17 our business and we're reluctant to try to push it all  
18 the way, push this particular product all the way to  
19 100 percent because we know it, we're aware of the  
20 fact that it could be seriously damaged, that catalog  
21 mailers will trim their lists or maybe even just give  
22 up on paper catalogs.

23 CHAIRMAN GOLDWAY: My staff tells me they're  
24 going to be asking more questions about this --

25 THE WITNESS: Okay.

1           CHAIRMAN GOLDWAY: Document that you've  
2 submitted now that they have a better understanding of  
3 what the headings are.

4           THE WITNESS: Surely.

5           CHAIRMAN GOLDWAY: But one of the questions  
6 that they had was sort of related to this was that,  
7 you've stated that it's believed the Postal Service  
8 has only a small percentage of the total of  
9 fulfillment shipments from catalogs, catalogers?

10          THE WITNESS: Yes.

11          CHAIRMAN GOLDWAY: Aren't you concerned that  
12 you're providing this special consideration to  
13 catalogers and not getting any commitment in return  
14 from them?

15          THE WITNESS: Well, I think there are  
16 opportunities for sort of contractual arrangements, I  
17 mean like NSAs or other types of arrangements where we  
18 can sort of have a, we can make arrangements for if we  
19 give you sort of a contract pricing that you would  
20 agree to use our shipping products. At this point I'm  
21 not aware of any, I'm pretty sure there wasn't any  
22 kind of quid pro quo in doing this. I note that the  
23 Catalog Mailers Association has joined with other  
24 parties in opposing this particular -- we're trying to  
25 do what we think is best for the catalog industry, and

1 so --

2 CHAIRMAN GOLDWAY: I believe it was  
3 Commissioner Langley who pointed out that that kind of  
4 an NSA would be a very good opportunity and we've been  
5 disappointed that we haven't seen that kind of NSA  
6 from the Postal Service. So you can take back our --

7 THE WITNESS: We'll take your concerns.

8 CHAIRMAN GOLDWAY: Our comments that we're  
9 interested in that. And then one other question  
10 before I offer my Commissioners other opportunities.  
11 You know, the periodical mailers tell us the same  
12 thing, that if you add up the first class mail that  
13 they, and the standard mail that they include in the  
14 system for billing and for advertising and for  
15 communications and for special packages that are part  
16 of a subscription, that their products also would more  
17 or less cover costs. Have you done any research with  
18 regard to the periodicals mailers?

19 THE WITNESS: I'm not sure that, I  
20 personally haven't done it, I'm not sure whether  
21 something like this has been done. I believe in  
22 response to one of these questions we did send along  
23 some information that indicated, I believe it was some  
24 usage by periodicals of other portions of mail.  
25 Commissioner, before lunch Commissioner Hammond, I

1 believe it was, asked the question whether we ever  
2 were trying to develop let's say prices or other  
3 programs to get rid of customers. The answer is  
4 absolutely not.

5 We value our customers in the catalog  
6 industry, we value our customers in the periodicals  
7 industry. And as I said in response to that, we look  
8 to the long term, and we think that all of these  
9 products, that the periodicals products and others can  
10 be profitable to us. We are at the same time we are  
11 constrained, you know, by some of the goals and  
12 factors of the PAEA to try to ensure that periodicals  
13 cover their costs.

14 So we're always in a balancing situation.  
15 We hear from the Commission and we've heard it, we've  
16 seen it in the ACDs, I'm hearing it today, there's  
17 very great concern about our products that are not  
18 covering our costs. We also are thinking that we want  
19 to retain these. I mean I'm not sure whether if  
20 somebody told me to come up with a plan to get rid of  
21 unprofitable mail or to get rid of a lot of mail that  
22 was not, whether just jacking up the prices wouldn't  
23 be the best answer. We're not trying to get rid of  
24 mail, we think mail can be profitable, we want to make  
25 it cover its costs, but we're not going to try to lose

1 it by making it prohibitively expensive or making the  
2 cost increases too hard to swallow.

3 CHAIRMAN GOLDWAY: Commissioner Acton?

4 COMMISSIONER ACTON: Dr. Kiefer, in your  
5 response to the presiding officer's information  
6 request number 3 question 8 --

7 THE WITNESS: Question 8.

8 COMMISSIONER ACTON: You indicated "The  
9 Postal Service has not yet been able to produce home  
10 price elasticity estimates for standard mail flats"?

11 THE WITNESS: That's correct.

12 COMMISSIONER ACTON: And we'd like to know  
13 if the Service has endeavored to produce these  
14 estimates, and if so what types of challenges have you  
15 encountered and why have you been unable to produce  
16 those home price elasticity numbers?

17 THE WITNESS: This is not my area of  
18 expertise, but I can report to you that our  
19 forecasting people have made attempts to do that. One  
20 of the challenges that they face is that the kind of  
21 information that they need, they don't have, in their  
22 view they don't have sufficiently long time series to  
23 be able to do that.

24 Standard mail flats is a relatively,  
25 although we have had standard mail flats and standard

1 mail for quite some time, the kind of data that they  
2 feel they need has only been available for a  
3 relatively shorter period of time. I think it, I have  
4 asked about this and I believe response I get is that  
5 it will be a little while, maybe several more years,  
6 before they feel that they will have enough data to be  
7 able to produce demand equations with sufficient  
8 significant values, statistically significant values,  
9 to be able to use.

10 COMMISSIONER ACTON: Okay. I think we can  
11 move to package services, right?

12 CHAIRMAN GOLDWAY: Well, I just, I don't  
13 want to get into a long discussion about this because  
14 we did a long discussion about this issue with regard  
15 to periodicals.

16 THE WITNESS: Yes.

17 CHAIRMAN GOLDWAY: But I do want to point  
18 out, and staff has, that in our ACD the Commission has  
19 asked the Postal Service to devise a plan to improve  
20 the cost coverage of standard mail flats products and  
21 to narrow the differences between standard mail  
22 letters and standard mail flats. And you have  
23 indicated that unlike periodicals standard mail flats  
24 and letters are within a general class and there is an  
25 opportunity over time to make adjustments to respond

1 to the concerns that we've articulated in the annual  
2 compliance determination.

3 THE WITNESS: Right, right.

4 CHAIRMAN GOLDWAY: So my question is, is  
5 there a time line for the Postal Service to achieve  
6 the goals that the Postal Regulatory Commission has  
7 directed you to achieve?

8 THE WITNESS: Okay. Again I don't have a  
9 time line, although certainly I think it would be  
10 clear that given the urgency of moving standard mail  
11 flats to full cost coverage we would be giving, it  
12 would be likely that provided that we felt confident  
13 that the types of price changes that we were giving  
14 would not be damaging that we would be ready to give  
15 above average increases to that. Now given that  
16 standard mail, letters and flats are pretty much  
17 exhaust standard mail, the only way you can give a  
18 above average increase to standard mail flats would be  
19 giving a below average increase to the letters.

20 I would point out, and I don't want to make  
21 too big of a deal about this, but if you turn to page  
22 28 of my statement and you see that the various  
23 categories, that standard mail flats in this  
24 particular case is actually given a slightly higher  
25 percentage increase than standard mail letters. It's

1 a minimal amount, but it's, we take seriously the  
2 concerns expressed by the Commission.

3 CHAIRMAN GOLDWAY: What I would like from  
4 you is, if it's at all possible, is some specific  
5 answer with regard to standard mail flats and letters  
6 that addresses the concerns raised in the annual  
7 compliance determination and gives us some idea of a  
8 time line that includes both cost efficiencies and  
9 prices. We didn't get very much information from Mr.  
10 Neri and we're not getting very much information from  
11 you, and this concern of ours goes well beyond the  
12 exigency case to the heart of the regulatory process.  
13 But I'm taking this opportunity to ask you to provide  
14 a document for us that gives us some indication that  
15 you're looking at the nexus of cost savings and  
16 pricing and that you have a commitment that's  
17 measurable to addressing those concerns in the next  
18 few years, two or three years.

19 COMMISSIONER ACTON: It could be something  
20 to keep in mind, Dr. Kiefer, when you're preparing  
21 your annual compliance report, since you are being --  
22 you talked earlier about what the Service should  
23 deserve credit for and what you certainly deserve  
24 credit for, and we had this discussion in board rooms  
25 when we were looking over this proposal, and that is

1 that regardless of your particular approach in this  
2 particular request, you are understanding our concerns  
3 that we outlined in the annual compliance  
4 determination --

5 CHAIRMAN GOLDWAY: Yes, that's true.

6 COMMISSIONER ACTON: And you're making some  
7 movement in most instances to try to resolve it. I'm  
8 not saying that the movement you're making is what we  
9 would endorse. What we're looking for is a little  
10 more information of the type that the Chairman's  
11 describing because that would give us a little more,  
12 in fact quite a lot more, enlightenment about whether  
13 or not what you're proposing is something that we can  
14 approve.

15 THE WITNESS: I hear you, and we will send  
16 you something.

17 CHAIRMAN GOLDWAY: Okay, with that I think  
18 we've completed standard mail. And our next topic  
19 would be package services. But I think we'll take a  
20 break for 15 minutes and come back. I think package  
21 services and special services should take less time,  
22 and hopefully we'll be out of here by 4:30, that's my  
23 goal.

24 THE WITNESS: I hope so.

25 CHAIRMAN GOLDWAY: Okay, see you in 15

1 minutes.

2 (Whereupon, a brief recess was taken.)

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1                   CHAIRMAN GOLDWAY: We're reconvening.  
2                   Unless any of my colleagues tell me differently I  
3                   think there's only one question regarding package  
4                   services, is that right? And it involves the  
5                   relationship between low weight parcel post and  
6                   priority mail. The Postal Service proposes to allow  
7                   prices for low weight parcel post to vary by zone for  
8                   the first time, leading to parcel post rates that are  
9                   higher than retail priority mail counterparts.

10                  THE WITNESS: Yes.

11                  CHAIRMAN GOLDWAY: On page 64 of your  
12                  testimony you state that the constraint that parcel  
13                  post rates must be lower than unzoned priority mail  
14                  rates is "no longer relevant". Does the Postal  
15                  Service intend to keep low weight priority mail rates  
16                  below corresponding parcel post rates? And is this an  
17                  appropriate price signal to send to mailers?

18                  THE WITNESS: The situation is really boils  
19                  down to one of timing. As I mentioned, and I believe  
20                  you referred to this earlier, that we, when we were  
21                  developing prices, we have not yet finalized the  
22                  prices for our competitive products, and that includes  
23                  priority mail. So the prices that we are proposing  
24                  for single piece parcel post, in a few price cells, in  
25                  the 1 and 2-pound area, they do exceed the current

1 prices for retail priority mail. As I indicated, I  
2 believe it was on page 11 of my statement, we will be  
3 adjusting competitive prices, and my understanding is  
4 that when the priority mail prices are adjusted these  
5 cells, the priority mail prices in these cells will  
6 not be below the single piece parcel post prices.

7 CHAIRMAN GOLDWAY: So you do think that in  
8 principle having the parcel post prices lower than  
9 priority mail prices is the appropriate structure?

10 THE WITNESS: Well, I am, in general I  
11 personally think that it's good to have -- well I  
12 think they shouldn't be above. I mean I don't know  
13 whether the people who price the competitive products  
14 -- I realize that we're talking about the one zone  
15 that is still -- I shouldn't say zone. I don't know  
16 whether, well I would not be the one to rule out their  
17 pricing them in certain cells at the same price. So  
18 I'm just saying they will, I understand they will not  
19 price priority mail below parcel post. So I can't,  
20 the prices have not been finalized, my --

21 CHAIRMAN GOLDWAY: Since the service for  
22 parcel post is less than the service for priority  
23 mail, it seems to me that that is not a logical  
24 pricing strategy to offer to customers.

25 THE WITNESS: Well, I will convey that --

1           CHAIRMAN GOLDWAY: But you're assuring me  
2           that at least in the short run for this particular  
3           proposal you're making that you believe priority mail  
4           prices will not be lower than parcel post. You're not  
5           assuring me that they'll be higher?

6           THE WITNESS: Okay, what I'm --

7           CHAIRMAN GOLDWAY: And I mean one assumes  
8           that the competitive prices will come out at the same  
9           time that they came out last year, which is January.

10          THE WITNESS: Yes, we intend to file --

11          CHAIRMAN GOLDWAY: So if the Commission  
12          gives you the approval to raise these prices --

13          THE WITNESS: Yes.

14          CHAIRMAN GOLDWAY: You have the discretion  
15          to raise prices for priority mail anyway.

16          THE WITNESS: Yes, yes.

17          CHAIRMAN GOLDWAY: One assumes that those  
18          prices will be higher than these prices?

19          THE WITNESS: All I, I have been informed  
20          that the people who price the competitive products  
21          will not price priority mail below that. I will  
22          convey your concerns to them about that, that you  
23          believe they should be higher.

24          CHAIRMAN GOLDWAY: You could also tell them  
25          that, you know, the PAEA really anticipated that there

1 was going to be a lot more profit generated from those  
2 competitive products than we've seen so far, and I'm  
3 not sure keeping prices below or at parcel post prices  
4 is a good way to generate profit.

5 THE WITNESS: I will pass your concerns  
6 along.

7 CHAIRMAN GOLDWAY: Commissioner Hammond,  
8 Vice Chairman Hammond had a question about first class  
9 mail, and I'm afraid since we were hungry and breaking  
10 for lunch I didn't give him a chance to ask that  
11 question.

12 THE WITNESS: Okay.

13 CHAIRMAN GOLDWAY: So I'm giving him that  
14 opportunity now.

15 VICE CHAIRMAN HAMMOND: Thank you, Madam  
16 Chairman. I know, Dr. Kiefer, we beat standard class  
17 to death and beat periodicals flats to death, but we  
18 haven't had the opportunity on first class presort  
19 flats necessarily.

20 THE WITNESS: Okay.

21 VICE CHAIRMAN HAMMOND: So that's what I  
22 wanted to get into because I had a special concern  
23 about that. So in response to a couple of the  
24 presiding officer information questions you told us  
25 that relative price increases for flats in first class

1 standard and periodicals are basically based on  
2 knowledge of the industries that use those products,  
3 and I was wondering could you tell us what industries  
4 are the major users of first class presort flats?

5 THE WITNESS: I have some ideas, but I think  
6 I can give you a more precise list, I know that, well  
7 I could --

8 VICE CHAIRMAN HAMMOND: Would you, if I were  
9 to say --

10 THE WITNESS: Yes.

11 VICE CHAIRMAN HAMMOND: That financial  
12 statements, insurance, shareholder reports, proxies,  
13 et cetera, things like that, would you agree that  
14 those could be the major users of presort first class  
15 flats?

16 THE WITNESS: I know that they are  
17 significant users. Their proportion of use is not  
18 something that I can say with confidence without  
19 checking.

20 VICE CHAIRMAN HAMMOND: But if we were  
21 speaking at least in generality, they are users --

22 THE WITNESS: Okay, I can accept that.

23 VICE CHAIRMAN HAMMOND: I won't hold you to  
24 specific volume amounts necessarily.

25 THE WITNESS: Okay.

1                   VICE CHAIRMAN HAMMOND: Okay, if we can  
2                   assume that, okay. And basically from those that I  
3                   mentioned and those that you know of are some of those  
4                   mailers using first class instead of standard because  
5                   they're legally obligated to do so?

6                   THE WITNESS: To the extent that they are  
7                   statements and communications that contain individual  
8                   correspondence or communications, yes they would be  
9                   required to do so.

10                  VICE CHAIRMAN HAMMOND: Okay, so they're  
11                  basically what I have thought of for years as like  
12                  captive mailers and really don't have much choice.  
13                  They are told that they will provide that information  
14                  to the person and it's either going to be by first  
15                  class mail or as we get to electronic diversion it's  
16                  going to be one or the other, but first class mail,  
17                  which it goes into presort first class flats, would be  
18                  a good portion of that, wouldn't you say?

19                  THE WITNESS: Yes.

20                  VICE CHAIRMAN HAMMOND: Yes, okay. So how  
21                  would you characterize the current state of those  
22                  industries that use those first class flats?

23                  THE WITNESS: Well, certainly the banking  
24                  industry is at least certain segments of the banking  
25                  industry has had some difficult times, and some of the

1 other ones, the financial industry has certainly had  
2 some difficult times.

3 VICE CHAIRMAN HAMMOND: Okay, so and but I  
4 do take it from your pricing proposal, because let's  
5 see, roughly standard flats are getting about 5  
6 percent, periodicals are getting about 8 percent, and  
7 these first class presort flats are going to get about  
8 a 12 percent increase, right?

9 THE WITNESS: They will get a, I believe  
10 it's, yeah, 11 plus percent.

11 VICE CHAIRMAN HAMMOND: Okay, and they are  
12 already well beyond their cost coverage for Postal  
13 Service, are they not? If I were to say that they are  
14 currently covered at least probably 130 percent if not  
15 more, cost coverage currently, you probably would not  
16 dispute that?

17 THE WITNESS: I don't have that number here.  
18 I can't dispute it, I don't have the number.

19 VICE CHAIRMAN HAMMOND: Do you think they're  
20 currently not covering their costs?

21 THE WITNESS: I don't have -- no, I don't  
22 believe that they're not covering their costs, but I  
23 don't have -- well, let me see. Okay, I look at Mr.  
24 Masse's paper, I think first class flats have a  
25 healthy cost coverage.

1           VICE CHAIRMAN HAMMOND: Okay, so those first  
2 class presort flats are already more than covering  
3 their costs, and they are for the most part people who  
4 must be in the mail unless they receive specific  
5 permission from people to be sent that information  
6 electronically rather than being in the mail, and  
7 they're going to receive at least, about a 12 percent  
8 increase in this exigency case. And I take it from  
9 the proposal that you think these industries that's in  
10 these first class flats are in a better position to  
11 withstand a large price increase than others, was that  
12 your reasoning?

13           THE WITNESS: Well, in this particular case  
14 I believe that, I've discussed this in my statement,  
15 that much of this increase is coming about because of  
16 the, the Postal Service is trying to respond to  
17 directives, the problem is that some of the, much of  
18 this mail is presort as you say, it's workshared,  
19 heavily workshared, and these pieces, the Commission's  
20 rules and the PAEA require us to set the presort  
21 discounts at no more than avoided costs or otherwise  
22 provide a justification, one of the four allowable  
23 justifications.

24           As I explained in the statement there was an  
25 error discovered in the flats cost model in 2008 that

1 lead us to realize that the avoided costs were much  
2 lower than we had thought previously, and so that  
3 therefore the discounts were too high, that the  
4 passthroughs were substantially over 100 percent. And  
5 so the Postal Service has been taking steps, and I  
6 believe the Commission has been sort of working with  
7 us on this and the fact that we didn't try to reduce  
8 the passthroughs down to 100 percent all in one big  
9 step but we're taking significant steps along the way,  
10 and we were giving them various categories of above  
11 average increases in order to reduce the passthroughs.

12 Now even with the fairly high increases that  
13 we are proposing for standard mail presort flats in  
14 this particular price adjustment, we are still going  
15 to be above 100 percent cost coverage. We don't think  
16 that we can go, we didn't think we could go any  
17 farther, and I believe that we used the rate shock  
18 justification for sort of as a reason to limit these  
19 to 100 percent. But we felt --

20 VICE CHAIRMAN HAMMOND: So you're saying,  
21 you just said "rate shock". Does that mean you would  
22 have really liked to have raised them higher than the  
23 12 percent that you're proposing now?

24 THE WITNESS: No, no, as I said we were  
25 responding to the Commission's directives to reduce

1 excess passthroughs to 100 percent but we were using  
2 rate shock as the justification for not going higher.  
3 I mean again this is a balancing situation between  
4 trying to work to adjust the passthroughs to where the  
5 Commission would like to have them and concern over  
6 the amount of increase that and its impact would have.  
7 So at this particular time we felt that we should not  
8 be asking these mailers to go above, I think it was 11  
9 to 12 percent.

10 CHAIRMAN GOLDWAY: And by the 12 percent  
11 increase what is the passthrough percentage that  
12 remains?

13 THE WITNESS: At the top of the presort  
14 ladder, the automation ADC flats passthrough relative  
15 to the automation mixed ADC flats after this price  
16 changes will be 220 percent, which is still --

17 CHAIRMAN GOLDWAY: 400?

18 THE WITNESS: I'm sorry --

19 CHAIRMAN GOLDWAY: 200.

20 THE WITNESS: 220 percent. So, which is  
21 significantly above the 100 percent direction we're  
22 heading in.

23 VICE CHAIRMAN HAMMOND: So it is the fault  
24 of the Postal Regulatory Commission and the postal  
25 reform legislation that you proposed a 12 percent

1 price increase here?

2 THE WITNESS: Well --

3 VICE CHAIRMAN HAMMOND: I'm sorry, that's  
4 what I thought I heard you say. Is that correct?

5 THE WITNESS: I was not saying it was  
6 anybody's fault, I was saying we were trying to  
7 respond to the requirements in the law and in the  
8 Commission's rules to adjust these down to 100  
9 percent, and we gave an above average increase up to  
10 the point where we felt that the rate shock  
11 justification would apply.

12 VICE CHAIRMAN HAMMOND: Well, I am not sure  
13 I agree, but --

14 THE WITNESS: I understand.

15 VICE CHAIRMAN HAMMOND: But I won't go much  
16 --

17 CHAIRMAN GOLDWAY: Can I ask? I don't  
18 recall whether the extra ounce rate affects this  
19 product at all. Did you say -- not giving an increase  
20 on the extra ounce rate to this product or are you?  
21 Does that make a difference in what the averages will  
22 be?

23 THE WITNESS: I'll have to look that up.  
24 Let's see.

25 CHAIRMAN GOLDWAY: Am I right in that? I

1 think the increase is large but when you take into  
2 account that they're not getting the increase in the  
3 extra ounce it winds up being less, or am I wrong?  
4 I'm wrong about that?

5 THE WITNESS: For presorted flats the  
6 additional ounce rate does increase from 17 cents to  
7 18 cents.

8 CHAIRMAN GOLDWAY: Oh it does.

9 THE WITNESS: But that particular increase,  
10 what 18 over 17 is, I don't know I'm going to say it's  
11 maybe 5 or 6 percent, so it's, you know, it's a penny  
12 but it's about 5 or 6 percent, so it would have the  
13 effect of for heavier pieces it would have the effect  
14 of drawing down the --

15 CHAIRMAN GOLDWAY: I think that's what our  
16 staff said that the average weight of those --

17 THE WITNESS: Yeah, they tend to be higher.

18 CHAIRMAN GOLDWAY: Annual reports and  
19 various documents that we get in the mail, financial  
20 documents, is on the heavier side.

21 VICE CHAIRMAN HAMMOND: Well, I mean I don't  
22 know, I'm --

23 CHAIRMAN GOLDWAY: So that the average  
24 increase is not quite as high, but it's still higher  
25 than the rest of the class.

1           VICE CHAIRMAN HAMMOND: Yes, we're still  
2 coming up with the 12 percent increase and I'm told  
3 that we achieve a 220 percent passthrough with a 5  
4 percent increase. That sound make any sense?

5           CHAIRMAN GOLDWAY: No, I don't --

6           THE WITNESS: No, no, the 220 percent was  
7 the passthrough between the benchmark for ADC  
8 automation flats, which is the, it's the first level  
9 of presort, and its benchmark which is the mixed ADC  
10 flats, it's 220 percent after the 12 percent. In  
11 other words had the increase been lower the  
12 passthrough would have been higher than 220 percent,  
13 and conversely had the increase in the price been  
14 higher the passthrough would have been lower.

15           VICE CHAIRMAN HAMMOND: Well, do you see any  
16 potential for the Postal Service to assist in its own  
17 demise by driving mail to electronic delivery by such  
18 price increases? I mean that just, you know, those  
19 people have to mail or they have to get permission  
20 from someone, millions of people, to deliver  
21 electronically. Now, you know, we've all been getting  
22 for years now the request that we do the simple  
23 electronic delivery and a bunch of us have not done  
24 so, but wouldn't, couldn't this be the increase which  
25 gets those companies, those institutions, those

1 businesses, to think, well this is going to be worth  
2 it for us to actually spend money now to get people to  
3 go to electronic delivery which will save us in the  
4 long run because we can leave the U.S. Postal Service?

5 THE WITNESS: I understand your concerns,  
6 and I think that we have in general made the argument  
7 in respect to other categories of mail that, the exact  
8 same argument you made. I take it from your statement  
9 that you think we've gone too far on this one.

10 VICE CHAIRMAN HAMMOND: Yes, I'm sorry, I  
11 do.

12 THE WITNESS: I understand.

13 VICE CHAIRMAN HAMMOND: So I will not pursue  
14 this any further. Thank you very much.

15 CHAIRMAN GOLDWAY: I'm glad you brought that  
16 up, Commissioner Hammond, we'll certainly discuss it  
17 among ourselves as well, thank you. So we have one  
18 more category which is special services. And I had  
19 better get out, I got so involved in the first class I  
20 forgot about this. So this is a question about  
21 confirm service.

22 THE WITNESS: Okay.

23 CHAIRMAN GOLDWAY: Which had a negative  
24 contribution in Fiscal Year 2009. On page 52 you  
25 stated that a primary cost driver for confirm is data

1 storage that has largely been driven by the scans  
2 provided to platinum service tier customers. Further  
3 you stated that you believe that the increases given  
4 to each of the four tiers will be sufficient to  
5 achieve full cost coverage for confirm. How did you  
6 determine the price increase for each tier?

7 THE WITNESS: I believe that the, let me see  
8 if I have. When we change the prices of the various  
9 tiers in confirm the subscription prices for the  
10 bronze, silver, and gold categories, that is the  
11 smaller user type categories, we attempted to put  
12 those within the general increase range of 4 to 6  
13 percent, and the fees for confirm range from 4 percent  
14 for bronze and silver, 4 percent increases for bronze  
15 and silver, and 6 percent for gold.

16 Then because, as stated or as mentioned in  
17 the statement, we believe that the costs have been  
18 driven largely by the extra data storage needed to  
19 handle the demands of the platinum customers, we  
20 determined what would be the amount of increase needed  
21 to reach a full cost coverage for the product, and  
22 that was the increase that was given to the, assigned  
23 to the platinum customers.

24 CHAIRMAN GOLDWAY: So the 25.6 percent  
25 increase is what you determined was necessary to cover

1 the cost?

2 THE WITNESS: Well, the data, that may be --  
3 yes, if that's the, the data I have here is by tier,  
4 but if the 25.6 is the increase for all of confirm,  
5 yes, that would be --

6 CHAIRMAN GOLDWAY: No, no, that's just for  
7 platinum.

8 THE WITNESS: Oh, platinum? I have a  
9 different number here. It actually says 28 percent.

10 CHAIRMAN GOLDWAY: You have 28? We have, my  
11 chart says 25.6 percent.

12 THE WITNESS: Oh, okay, well.

13 CHAIRMAN GOLDWAY: But how did you get that  
14 number? You know, did you look at the cost of data  
15 storage?

16 THE WITNESS: Well, it was, we looked at the  
17 cost of the product, of confirm. I mean didn't break  
18 out specifically.

19 CHAIRMAN GOLDWAY: So you just looked at the  
20 gap between the overall cost of the service and what  
21 was lost in 2009?

22 THE WITNESS: Right, right.

23 CHAIRMAN GOLDWAY: Gave the others a sort of  
24 general increase and put the biggest amount on  
25 platinum assuming that they're the ones who use the

1 most of it and --

2 THE WITNESS: They're the ones who, it was  
3 our belief, yes, that they were the ones who are  
4 driving the cost and resulting in the fact that we  
5 were failing to cover our costs, and so --

6 CHAIRMAN GOLDWAY: So and in 2009 in the ACD  
7 you explained that the big cost increase was because  
8 you had to purchase a whole lot of new data storage  
9 processing equipment to handle confirm, and that's why  
10 the prices went up?

11 THE WITNESS: Yeah, well the platinum users  
12 have unlimited scans, and so these are largely  
13 resellers, they're ones who buy this service and then  
14 sell it to others. And, you know, the more they, if  
15 it is underpriced they will sell, they will put ever  
16 increasing demands on us and we have to go out and buy  
17 additional storage. So it was our belief that these  
18 customers were primarily responsible for the gap and  
19 so we gave the others a price changes that fell within  
20 the prescribed range and asked the platinum  
21 subscribers to cover the difference.

22 CHAIRMAN GOLDWAY: So my staff is concerned  
23 that you don't yet know what your budget is for 2011,  
24 and these prices would go into effect in 2011, and  
25 that there might be significant additional

1 expenditures for new data storage. If you're just  
2 pricing up to what was expended in 2009 do you have  
3 any indication that these new prices are in fact going  
4 to cover the costs of 2011?

5 THE WITNESS: I understand your concerns.  
6 I'm looking at Mr. Masse's tables and I don't believe  
7 that they have, I don't see confirm broken out.  
8 Clearly if these -- I understand the concern but all I  
9 can say at this time is that as we, if we increase the  
10 price to the resellers some of that may be passed  
11 along to some of their customers, which may have the  
12 effect of dampening the sort of the growth in the  
13 demand that the resellers place on us to buy new  
14 storage, if you know what I'm saying. So in other  
15 words they will have to increase the price and that  
16 may sort of help to bring the demand down a little bit  
17 so that the resellers are not going to be asking us  
18 for more --

19 CHAIRMAN GOLDWAY: But we hate to see more  
20 loss making products. So could you perhaps provide an  
21 answer to my question about your planned expenditures  
22 for IT and data collection with regard to confirm  
23 service in 2011?

24 THE WITNESS: Okay, yes, I'll pass this  
25 along so we can get that for you to the extent that --

1 MR. RUBIN: We'll be happy to. We tried to  
2 respond to this in providing information in request  
3 number 3 question 15, and we weren't, I guess, yeah,  
4 it says Postal Service has not fully determined plans  
5 for Fiscal Year 2011.

6 CHAIRMAN GOLDWAY: Yes, so --

7 MR. RUBIN: So do we --

8 CHAIRMAN GOLDWAY: You may not have fully  
9 determined them, but I'm sure you have as we do some  
10 general indications whether that's going to be a  
11 potential area for spending.

12 THE WITNESS: Okay.

13 CHAIRMAN GOLDWAY: And we would like to know  
14 what you know.

15 THE WITNESS: Well, we will make sure that  
16 we provide the best information we have on that.

17 CHAIRMAN GOLDWAY: Okay.

18 MR. RUBIN: Okay.

19 CHAIRMAN GOLDWAY: Thank you. That  
20 concludes my list of questions. Commissioner Langley?

21 COMMISSIONER LANGLEY: I have just a  
22 question.

23 THE WITNESS: Sure.

24 COMMISSIONER LANGLEY: You've been very  
25 straightforward, forthright, answering when you can.

1 If the exigent rate increase isn't approved has Postal  
2 management asked you to prepare for any contingency?

3 THE WITNESS: No.

4 COMMISSIONER LANGLEY: Thank you.

5 CHAIRMAN GOLDWAY: In other words you  
6 haven't looked at the legal rate cap to see what you  
7 could do with that?

8 THE WITNESS: We have not prepared any  
9 prices that are, that would fit into the price cap as  
10 of I don't know what date. We are not a large staff,  
11 and that is certainly a, would be a challenge to try  
12 to pursue two sort of rate designs at the same time.  
13 We haven't been asked to do that, no.

14 COMMISSIONER ACTON: Have you been asked to  
15 perhaps estimate the approximate revenue that may be  
16 available to the Service under the 1 percent cap?

17 COMMISSIONER LANGLEY: As well as the banked  
18 amount.

19 THE WITNESS: Well, I should point out that  
20 our pricing function, in the past we used to estimate  
21 the revenue that, we don't do that anymore. I'm not  
22 aware of whether our forecasting people or our budget  
23 people were asked that question. We don't do revenue  
24 projections anymore.

25 COMMISSIONER ACTON: Thank you.

1 CHAIRMAN GOLDWAY: Any other questions?

2 (No response.)

3 CHAIRMAN GOLDWAY: Well, Dr. Kiefer, you  
4 have done yeoman's duty today. We all appreciate your  
5 answers and your patience with us, and as I said  
6 yesterday I think we all have the best interests of  
7 the Postal Service at heart.

8 THE WITNESS: Absolutely.

9 CHAIRMAN GOLDWAY: But the questions in  
10 front of us and in difficult times are not easy to  
11 answer. And I hope that the concerns and questions  
12 raised by the Commissioners here today will be brought  
13 back to top level management in addition to the people  
14 that you work with directly so that we can all come up  
15 with better answers in the future. I would like to be  
16 able to clarify just when we will get the answers to  
17 questions that we've asked for in the last three days  
18 from the Postal Service. Mr. Rubin, can you help me  
19 with that?

20 MR. RUBIN: Our plan is to get them within a  
21 week of each day's hearing.

22 CHAIRMAN GOLDWAY: Is that going to be  
23 satisfactory, Mr. Sharfman, given how difficult it is  
24 for us to answer questions?

25 MR. RUBIN: Well, also I expect to have

1 POIRs to work on.

2 CHAIRMAN GOLDWAY: We're going to be  
3 submitting additional POIRs, that's true.

4 MR. RUBIN: So, yeah.

5 THE WITNESS: We are a lean staff.

6 CHAIRMAN GOLDWAY: All right, we will agree  
7 then that within a week, seven days including  
8 Saturdays and Sundays, we will receive answers to the  
9 questions that we asked from the bench for each day  
10 that we asked them.

11 MR. RUBIN: Yes.

12 CHAIRMAN GOLDWAY: Thank you.

13 VICE CHAIRMAN HAMMOND: Madam Chairman?

14 CHAIRMAN GOLDWAY: Commissioner Hammond?

15 VICE CHAIRMAN HAMMOND: While you're on  
16 that, I noted you made comment this morning of this  
17 suggestion of request information by the Alliance of  
18 Nonprofit Mailers and Magazine Publishers which you  
19 said we're going to honor, and I'm certainly glad that  
20 you're seeing that this is done. They put a request  
21 that that information be provided by Friday, August  
22 13th.

23 CHAIRMAN GOLDWAY: Is that possible? Yes.

24 VICE CHAIRMAN HAMMOND: So because that is  
25 possible, we're not talking about what you were doing

1 today being a whole week away from before they would  
2 provide that or, because I know we all care about this  
3 was a very excellent suggestion for request for  
4 information.

5 CHAIRMAN GOLDWAY: Yes.

6 MR. RUBIN: Well, I had in mind that we had  
7 that deadline for tomorrow.

8 CHAIRMAN GOLDWAY: Okay, that deadline is  
9 for tomorrow, but the questions that we asked from the  
10 bench are a week from when we asked them.

11 MR. RUBIN: Yes.

12 CHAIRMAN GOLDWAY: Okay, and we will submit  
13 POIRs and if we need them to be answered sooner than  
14 that we'll have to indicate that to you, we'll see  
15 what the schedule is. After all we have a very  
16 limited time to make a decision. With that, I will  
17 adjourn these hearings, conclude them, and again thank  
18 you, Dr. Kiefer, thanks to the Postal Service  
19 attorneys for their participation and for the  
20 audience. And we'll get back to work behind closed  
21 doors to try and sort our these issues. Thank you  
22 very much.

23 (Whereupon, at 4:20 p.m., the hearing in the  
24 above-entitled matter was adjourned and concluded.)

25 //

REPORTER'S CERTIFICATE

DOCKET NO.: R2010-4

CASE TITLE: Rate Adjustment Due to Extraordinary or  
Exceptional Circumstances

HEARING DATE: August 12, 2010

LOCATION: Washington, D.C.

I hereby certify that the proceedings and evidence are contained fully and accurately on the tapes and notes reported by me at the hearing in the above case before the (Enter Agency Name Here).

Date: August 12, 2010



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