

**DOCKET SECTION**

**MOAA-RT-1**

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

**POSTAL RATE AND FEE CHANGES, 1997**

**Docket No. R97-1**

**REBUTTAL TESTIMONY  
OF  
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Vice President  
L. E. Peabody & Associates, Inc.**

**On Behalf Of  
MAIL ORDER ASSOCIATION OF AMERICA**

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Due Date: March 9, 1998

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## LIST OF EXHIBITS

<u>ITEM</u> <u>(1)</u>	<u>TITLE</u> <u>(2)</u>
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Exhibit__MOAA-RT-1A	Summary of Witness Haldi's Constructed Rates for Letters
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## REBUTTAL TESTIMONY

ROGER C. PRESCOTT

## I. PURPOSE OF TESTIMONY

I have been requested by Mail Order Association of America ("MOAA") to review the direct testimony and recommendations proposed in Witness John Haldi's testimony submitted

1 on behalf of Val-Pak Direct Marketing Systems, Inc., Val-Pak Dealers' Association, Inc. and  
2 Carol Wright Promotions, Inc. (collectively referred to herein as "VP-CW"). Specifically, I  
3 have been asked to evaluate the appropriateness of the adjustments proposed by Witness Haldi  
4 to the USPS' rate schedule for the ECR subclass. Witness Haldi's proposed rates are  
5 summarized in Table 6 to his testimony (Tr. 27/15087).

6 The results of my analyses are summarized under the following topics:

- 7 II. Summary and Conclusions
- 8 III. Comparison of USPS' and Witness Haldi's Proposed Rates
- 9 IV. Identification of "Bottom-Up" Costs
- 10 V. Witness Haldi's Rate Procedures
- 11 VI. Sortation Discounts Proposed By USPS and Witness Haldi

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- 1 costs, faulty criteria for allocating costs, and arbitrary procedures for calculating rates.
- 2 Each of these conclusions is discussed in detail in the remainder of my testimony.

1           **III. COMPARISON OF USPS' AND WITNESS HALDI'S PROPOSED RATES**

2           The USPS proposed rate structure for the ECR subclass of Standard (A) mail incorporates  
3           sortation discounts for automation (letters only), high-density and saturation mail. Destination  
4           entry discounts are also offered for mail entered at the BMC, SCF or DDU. The USPS'  
5           proposed rates were developed and presented by Witness Moeller (USPS-T-36, page 31).

6           Val-Pak's<sup>1/</sup> mail consists exclusively of letter-shaped mail "entered at the Standard (A) Mail  
7           ECR Saturation Rate" (Tr. 27/15044). For this mail, "98 percent is entered at the destination  
8           Sectional SCF" and "2 percent is entered at BMCs..." (Tr. 27/15046). Witness Haldi does not  
9           specifically identify the type of mail prepared by Carol Wright<sup>2/</sup> but states that its "mail consists  
10          of both letter mail and nonletter mail primarily sent at the Standard (A) Mail ECR High-Density  
11          rate" (Tr. 27/15043). He also states that the Carol Wright mail reflects a "highly targeted  
12          geographic and demographic distribution..." (Tr. 27/15048).

13          Witness Haldi develops his rate proposal in Appendix A and Appendix C of his testimony.<sup>3/</sup>  
14          His rate proposal is summarized in Table 6 of his testimony (Tr. 27/15087).

15          A comparison of the USPS' proposed rates for ECR mail with Witness Haldi's proposal is  
16          shown in Table 1 below. The USPS' proposed rates are shown in Column (2) of Table 1.  
17          Witness Haldi's proposed rates are shown in Column (3) of Table 1. The difference between

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<sup>1/</sup> Val-Pak refers to Val-Pak Direct Marketing Systems, Inc. and Val-Pak Dealers' Association, Inc.

<sup>2/</sup> Carol Wright refers to Carol Wright Promotions, Inc.

<sup>3/</sup> Appendix B to Witness Haldi's testimony develops the margin for ECR mail under the USPS' proposed rates. Appendix D of his testimony discusses the relationship of weight and cost. Neither of these appendices directly affect his proposed rates.

the USPS' proposal and Witness Haldi's proposal is shown in Column (4) of Table 1. Those items where the two proposals differ are noted in bold print.

Table 1				
<b><u>Comparison of USPS' and Witness Haldi's Rate Proposals</u></b>				
<u>Item</u>	<u>R97-1 Proposed Rates (cents)</u>			
	<u>USPS<sup>1/</sup></u>	<u>Haldi<sup>2/</sup></u>	<u>Difference<sup>3/</sup></u>	
(1)	(2)	(3)	(4)	
<b><u>LETTERS</u></b>				
1. Base Rate - Per Piece	16.4¢	16.7¢	0.3¢	
2. Discount For Sortation - Per Piece				
a. Automation	0.7	0.7	0.0	
b. High-Density	2.1	2.5	0.4	
c. Saturation	3.0	3.8	0.8	
3. Discount For Destination Entry - Per Piece <sup>4/</sup>				
a. BMC	1.5	1.5	0.0	
b. SFC	1.8	1.8	0.0	
c. DDU	2.3	2.3	0.0	
<b><u>NONLETTERS</u></b>				
4. Base Rate - Per Piece (Piece Rated)	16.4¢	16.7¢	0.3¢	
5. Base Rate - Pound Rated				
a. Per Piece	5.5	5.8	0.3	
b. Per Pound	53.0	53.0	0.0	
6. Discount For Sortation - Per Piece				
a. High-Density	1.1	1.7	0.6	
b. Saturation	2.3	2.9	0.6	
7. Discount For Destination Entry - Per Pound				
a. BMC	7.2	7.2	0.0	
b. SCF	8.8	8.8	0.0	
c. DDU	11.0	11.0	0.0	
<sup>1/</sup> Witness Moller, page 31.				
<sup>2/</sup> Witness Haldi, Table 6 (Tr. 25/15087).				
<sup>3/</sup> Column (3) minus Column (2).				
<sup>4/</sup> The per piece discount is also applicable to nonletters mailed at the per piece rates.				



1       Witness Haldi suggests that the USPS' proposal should be modified by measuring the  
2       sortation discounts for high-density and saturation mail in the ECR subclass. Specifically, for  
3       high-density letters, Witness Haldi proposes a discount of 2.5 cents per piece which is 0.4 cents  
4       per piece greater than the USPS' proposal of 2.1 cents per piece (Table 1, Line 2b). For  
5       saturation letters, Witness Haldi proposes a discount of 3.8 cents per piece which is 0.8 cents  
6       per piece greater than the USPS' proposal of 3.0 cents per piece (Table 1, Line 2c). Finally,  
7       Witness Haldi proposes that the per piece discount for nonletters equal 1.7 cents per piece for  
8       high-density mail and 2.9 cents per piece for saturation mail, which is 0.6 cents per piece  
9       greater than the USPS' proposal of 1.1 cents per piece and 2.3 cents per piece, respectively  
10      (Table 1, Line 6).

11       According to Witness Haldi, his proposed rates "have been designed to provide the same  
12       revenues and contribution to institutional costs as the rates proposed by [USPS'] Witness  
13       Moeller..." (Tr. 27/15086). Stated differently, Witness Haldi's proposal is, overall, revenue  
14       neutral with the USPS' proposal.

15       In order to accomplish this neutrality, Witness Haldi increased the USPS' proposed base rate  
16       from 16.4 cents per piece to 16.7 cents per piece for both letter and nonletter mail (Table 1,  
17       Line 1 and Line 4). For pound-rated nonletters, the per piece component of the USPS proposed  
18       rate is increased by 0.3 cents per piece from 5.5 cents per piece to 5.8 cents per piece (Table 1,  
19       Line 5a)<sup>4/</sup>

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<sup>4/</sup> The per piece increase conforms to the USPS' proposal which results in mail weighing 3.3 ounces paying the same amount on a per piece basis or on a per piece/per pound basis.

1       As part of Witness Haldi's rate design, he has not modified the USPS' proposed discounts  
2       for destination entry (Table 1, line 3 and line 7) or the automation discount for letters (Table 1,  
3       line 2a). Finally, Witness Haldi's rate proposal accepts the USPS' proposed pound rate for  
4       pound-rated nonletters. In this proceeding, the USPS has proposed a rate of \$0.53 per pound  
5       for pound-rated nonletters. Witness Haldi states that he examined the proposal submitted by  
6       USPS' Witness Moeller and considered the "recommended pound rate to be conservative,"  
7       (TR 27/15172).

1                                    **IV. IDENTIFICATION OF "BOTTOM-UP" COSTS**

2            Witness Haldi differentiates between rates developed using costs derived from a "top down"  
3            approach and a "bottom-up" approach. "Top down" costs are computed, according to Witness  
4            Haldi, when the USPS "determines a base cost for a rate subclass, and then computes costs  
5            avoided, or costs saved, and deducts the avoided costs from the base cost to arrive at the  
6            estimated net cost for individual rate categories or rate cells"<sup>5/</sup>.

7            Witness Haldi refers to "bottom-up" costs as costs determined when the USPS "computes  
8            the amount of volume-variable costs incurred, and adds costs incurred for different functions and  
9            activities, such as sorting and transportation, to arrive at the estimated costs for individual rate  
10           categories or rate cells."<sup>6/</sup> Based on Witness Haldi's claim that data is now available for ECR  
11           rates to be calculated using a "bottom-up" approach, Witness Haldi states that his testimony has  
12           the following three purposes:

13                    "(1) to develop bottom-up costs for Standard (A) ECR mail; (2) to use those  
14                    bottom-up costs to examine the Postal Service's proposed rate design; and (3) to  
15                    propose alternative rates for Standard (A) ECR Mail that are designed within the  
16                    context and economic logic of bottom-up costs." (Tr. 27/15042)

17            Witness Haldi asserts that the USPS' "reliance on a top down rate design methodology  
18            rather than a bottom up" methodology has resulted in contribution levels for saturation mail that  
19            are high and disproportionate as compared to other ECR mail (Tr. 27/15067). As discussed in  
20            the following sections of my testimony, Witness Haldi has not followed his theory of calculating

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<sup>5/</sup> Tr. 27/15049. (emphasis and footnote omitted)

<sup>6/</sup> Tr. 27/15049. (emphasis omitted)

1 rates from a "bottom-up" approach. In order for Witness Haldi's proposal to be consistent with  
2 a "bottom-up" approach for calculating rates, the rates for each rate cell would have to be based  
3 on "bottom-up" costs.<sup>7/</sup> Aside from the fact that he has not accurately calculated the volume-  
4 variable costs for each rate cell, Witness Haldi's rate design for ECR mail deviates from the  
5 "bottom-up" approach in several significant aspects:

- 6 1. For letter rates, only the rates proposed for destination entry at the BMC are based on  
7 Witness Haldi's underlying "bottom-up" costs. The other rate cells (no destination  
8 entry, SCF and DDU) are derived utilizing the USPS' proposed rate discounts which  
9 reflect costs avoided. Therefore, of the 16 rate cells for letters, only 4 reflect Witness  
10 Haldi's calculation of "bottom-up" costs;
- 11 2. If Witness Haldi followed his "bottom-up" approach for each of the 16 letter rate cells,  
12 Part C of Table C-2 in his testimony (Initial Target Rates) shows that the letter rates  
13 would vary significantly from his proposed rates. For example, his Initial Target Rate  
14 for basic letter mail without any destination entry would equal 15.8 cents per piece  
15 which is 0.6 cents per piece less than the USPS' proposed rate of 16.4 cents per piece.  
16 Conversely, Witness Haldi's Initial Target Rate for saturation mail entered at the DDU  
17 equals 11.5 cents per piece which exceeds the USPS' proposed rate of 11.1 cents per  
18 piece by 0.4 cents per piece.
- 19 3. For the 12 nonletter rate cells in Witness Haldi's proposal, none are based on "bottom-  
20 up" costs. The base rate for nonletters is set at the letter rate for basic, no destination  
21 entry. The destination entry discounts in Witness Haldi's proposal equal the USPS'  
22 proposed discounts (i.e., a deduction reflecting costs avoided). The sortation discount  
23 proposed by Witness Haldi reflects a 60 percent passthrough of his calculation of the  
24 costs avoided; and,
- 25 4. Witness Haldi does not adjust either the pound rate for nonletters proposed by the USPS  
26 of \$0.53 per pound or the pound rate for dropshipped mail, although his calculation of  
27 "bottom-up" costs assume an arbitrary amount for costs associated with weight.

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<sup>7/</sup> For purposes of the testimony, the rate cells for ECR mail reflect the shape of mail (letter and nonletter), dropshipping entry point (no destination entry, BMC, SCF and DDU) and level of sortation (basic, letter automation, high-density and saturation). This matrix equals 16 rate cells for letters and 12 rate cells for nonletters.

- 1 In summary, the failure of Witness Haldi to apply the logic of "bottom-up" costs in his rate
- 2 proposal invalidates his results.

1                                   **V. WITNESS HALDI'S RATE PROCEDURES**

2           The rates proposed by Witness Haldi for ECR mail are developed in Appendix A and  
3   Appendix C to his testimony.<sup>8/</sup> The goal of these appendices is to restate the USPS' base rates  
4   and sortation discounts, following Witness Haldi's theory of the "bottom-up" approach, so that  
5   the total revenues for letters and nonletters remain the same as developed by the USPS' Witness  
6   Moeller. My summary of Witness Haldi's procedure and a general critique of his methodology  
7   are discussed under the following topics:

8           A. Witness Haldi's Procedures

9           B. General Critique

10          **A. WITNESS HALDI'S PROCEDURES**

11         Exhibit (MOAA-RT-1A) summarizes Witness Haldi's procedures that he uses to develop  
12   his proposed rates for letters. Because the procedures followed by Witness Haldi for nonletters  
13   are based on the inputs derived from his analysis of letters and arbitrary assumptions regarding  
14   the cost per piece related to weight, I have not developed an exhibit summarizing his procedures  
15   for nonletters. The steps followed by Witness Haldi are summarized below.

16           Step 1.   The aggregate revenues for letters and nonletters are developed from the USPS'  
17                       volumes, rates and discounts.

18           Step 2.   The aggregate costs were developed for letters and nonletters based on Test Year  
19                       After Rates ("TYAR") volumes and Test Year unit costs. The total costs for

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<sup>8/</sup> Appendix B to Witness Haldi's testimony summarizes the margins and mark-up ratios for the USPS' proposed rates and does not impact his rate design.

1 ECR mail matches the USPS' Cost and Revenue Analysis ("CRA") volume  
2 variable costs utilized by Witness Moeller.

3 Step 3. Based on the USPS' unit costs per pound for destination entry and the TYAR  
4 pounds developed from USPS data<sup>9/</sup>, the aggregate costs for dropshipping are  
5 developed for each rate cell (sortation category and destination entry). These  
6 costs are converted to unit costs based on Witness Haldi's calculation of the  
7 average weight per piece.

8 Letter Rates

9 Step 4. The unit costs for each rate cell are developed utilizing the USPS' mail  
10 processing and delivery costs and the transportation/other costs are developed in  
11 Step 3 above.

12 Step 5. The aggregate costs for each rate cell are computed by multiplying the TYAR  
13 volumes by the unit costs in Step 4 above. Because the calculated aggregate  
14 costs of \$463.2 million do not match Witness Haldi's calculation of the aggregate  
15 cost for letters of \$491.0 million (Step 4 above), he calculates a cost "true-up"  
16 of 0.32 cents per piece.

17 Step 6. The revised volume variable costs are computed as the base unit costs (Step 4)  
18 plus the cost "true-up" of 0.32 cents per piece (Step 5). The USPS' contingency  
19 factor of 1 percent is utilized to calculate the final costs for each rate cell.

20 Step 7. Rates are calculated for each rate cell based on a combination of rates reflecting  
21 a fixed margin of 8.20 cents per piece (90 percent weighting) and rates reflecting  
22 a fixed mark-up percentage of 2.4405 (10 percent weighting).

23 Step 8. Witness Haldi's constructed rates for mail at the BMC destination entry are  
24 summarized in the following tabulation.

	<u>Sortation</u>	<u>Cents Per Piece</u>
25		
26	a. Basic	15.5
27	b. Automation	14.8
28	c. High-Density	13.0
29	d. Saturation	11.8

30 The constructed rates for the other rate cells are not used. This fact was  
31 confirmed by Witness Haldi in response to interrogatories (Tr. 27/15183).

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<sup>9/</sup> The pounds for letters and piece rated nonletters are based on 1996 statistics. The pounds for pound-rated nonletters are based on Witness Moeller's aggregate data.

- 1 Step 9. The rates for no destination entry, SCF and DDU were based on Witness  
2 Moeller's destination entry discounts, thus creating an Initial Target Rate for  
3 each rate cell. The difference between the no destination entry rate and BMC  
4 rate equals plus 1.5 cents per piece. The difference between the rates for BMC  
5 and SCF equals a reduction of 0.3 cents per piece. The difference between the  
6 rates for BMC and DDU equals a reduction of 1.8 cents per piece.
- 7 Step 10. The Initial Target Rates (Step 9) were multiplied by the TYAR volume for each  
8 rate cell to determine estimated revenues. Because the Initial Target Rates  
9 produce, in aggregate, more letter revenues than the USPS' proposal (Step 1),  
10 a revenue "true-up" of 0.33 cents per piece was developed.
- 11 Step 11. The Initial Target Rates for each rate cell (Step 9) are reduced by the revenue  
12 "true-up" (Step 10) and equal the final rate for each rate cell as summarized in  
13 Table 2 below.

14 **Table 2**  
15 **Summary of Haldi Rate Proposal - Letters**  
16 **(Cents Per Piece)**

	No Destination Entry	BMC	SCF	DDU
<u>Sortation</u> (1)	<u>Entry</u> (2)	<u>(3)</u>	<u>(4)</u>	<u>(5)</u>
17 a. Basic	16.7¢	15.2¢	14.9¢	14.4¢
18 b. Automation	16.0	14.5	14.2	13.7
19 c. High-Density	14.2	12.7	12.4	11.9
20 d. Saturation <sup>1/</sup>	12.9	11.4	11.1	10.6

21  
22  
23  
24 <sup>1/</sup>Because of rounding, the revenue "true-up" for saturation mail equals 0.4 cents per piece.

25 **Nonletter Rates**

- 26 Step 12. For nonletters, Witness Haldi's rate design utilizes the same basic rate as letters  
27 of 16.7 cents per piece (Table 2, Column(2), line a).
- 28 Step 13. The discount for sortation (high-density and nonletter saturation) is based on  
29 Witness Haldi's assumption of a passthrough of 60 percent of the cost savings  
30 that he develops for piece rated nonletters with no destination entry  
31 (Tr. 27/15184). The sortation cost savings developed by Witness Haldi are  
32 based on the unit costs for mail processing and delivery costs included in Step 2



1                   above along with an adjustment of 2.33 cents per piece determined from the  
2                   average weight for piece rated nonletters.

3           Step 14.   The per pound rate (53.0 cents per pound) and the per pound discount for  
4                   destination entry are based on the USPS' proposal submitted by Witness Moeller.

5           Step 15.   Witness Haldi's proposed per piece rate for pound rated pieces (5.8 cents per  
6                   piece) is based on his proposed basic rate (Step 12) and the per pound rate  
7                   (Step 14).<sup>10/</sup>

8    **B. GENERAL CRITIQUE**

9           Rates based on Witness Haldi's theory of "bottom-up" costs begin with volume variable  
10       costs and add the costs for specific functions and activities. The procedures summarized above  
11       do not reflect the "bottom-up" approach in the following seven (7) ways:

- 12           1. Witness Haldi derives his rates based on numerous assumptions which are unsupported.  
13           His separation of costs between letters and nonletters as well as his determination of  
14           weight related costs are based on faulty or unsupported logic. In addition, his analysis  
15           contains numerous input or mathematical errors. My specific critique of each of the  
16           tables in his Appendix A and Appendix C is contained in my Exhibit\_MOAA-RT-1B.
- 17           2. In Step 5 above, Witness Haldi adds a cost "true-up" per piece amount which is not  
18           reflective of any activities or function, but rather a correction factor for each rate cell;
- 19           3. In developing Initial Target Rates in Step 7, Witness Haldi bases 90 percent of the rate  
20           on a fixed margin which does not reflect any adjustment for a specific function or  
21           activity.
- 22           4. The adjustment to recognize destination entry (Steps 8 and 14) is not based on the cost  
23           activities and functions developed by Witness Haldi, but rather the analysis of  
24           dropshipping savings calculated by Witness Moeller. Witness Moeller's destination  
25           entry cost savings do not identify the difference in costs between letters and nonletters;

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<sup>10/</sup> The per piece rate for pound rated pieces is calculated at the breakpoint of 3.3 ounces, i.e., 16.7 cents per piece less (53.0 cents per pound ÷ 16 ounces/pound x 3.3 ounces) equals 5.8 cents per piece.

- 1        5. The final rates for letters utilize a reduction to rates of 0.3 cents per piece (Step 10  
2        above) which does not reflect any specific function or activity, but rather is a correction  
3        factor for the overrecovery of revenues under Witness Haldi's Initial Target Rates;
- 4        6. The basic rate for nonletters is not reflective of activities or cost functions but instead  
5        equals the basic rate for letters; and,
- 6        7. The discount for nonletter sortation is based on piece rated nonletter mail reflecting an  
7        arbitrary weight adjustment of 2.33 cents per piece and an arbitrary passthrough  
8        percentage (Step 13).

**VI. SORTATION DISCOUNTS PROPOSED  
BY USPS AND WITNESS HALDI**

As shown above, the difference between the USPS' proposed rates for ECR mail and Witness Haldi's proposal reflects the different sortation discounts. The difference in base rates (see Table 1 above, Lines 1, 4 and 5a) results from Witness Haldi's sortation discounts and the constraint that the aggregate revenues in his analysis must equal the USPS' proposed revenues. For both the USPS and Witness Haldi, the sortation discounts shown in Table 1 above (Lines 2 and 6) are based on the cost differentials developed in their respective analyses. Table 3 below summarizes the cost analyses and the differentials in sortation as developed by the USPS' Witness Moeller and Witness Haldi.

**Table 3  
Comparison of Cost  
Differences for Sortation**

<u>Item</u> (1)	<u>Cost Per Piece (cents)</u>		<u>Difference From Basic (Cents Per Piece)</u>	
	<u>USPS<sup>1/</sup></u> (2)	<u>Haldi<sup>2/</sup></u> (3)	<u>USPS</u> (4)	<u>Haldi</u> (5)
1. Cost Per Piece - Letters				
a. Basic	6.4363¢	7.1281¢	xxx	xxx
b. High-Density	4.2367	4.9463	2.2¢	2.2¢
c. Saturation	3.3297	3.8391	3.1	3.3
2. Cost Per Piece - Nonletters				
a. Basic	8.6042¢	8.9900¢	xxx	xxx
b. High-Density	5.8426	6.1588	2.8¢	2.8¢
c. Saturation	4.1816	4.2113	4.4	4.8

<sup>1/</sup> Moeller, workpaper 1, page 18 — reflects mail processing and delivery costs.

<sup>2/</sup> Haldi Table A-13 (with contingency), BMC column for letters and Table A-18 (with contingency), no destination entry column as discussed at TR 27/15184.

1       The cost differential between basic and high-density mail is the same in both the USPS' and  
2       Witness Haldi's analyses, equalling 2.2 cents per piece for letters (Table 3, line 1b) and 2.8  
3       cents per piece for nonletters (Table 3, line 2b). However, in Witness Haldi's analysis, the cost  
4       difference between basic mail and saturation mail is greater than in the USPS' analysis. For  
5       letters, Witness Haldi's cost savings equals 3.3 cents per piece versus the USPS' value of 3.1  
6       cents per piece (Table 3, line 1c). For nonletters, Witness Haldi's analysis shows a cost  
7       difference of 4.8 cents per piece versus the USPS difference of 4.4 cents per piece (Table 3,  
8       line 2c).

9       In the USPS' analysis, the sortation discount considers only mail processing and delivery  
10      costs. In addition to mail processing and delivery costs, Witness Haldi has incorrectly included  
11      transportation and other costs ("shipping costs") in his differential for sortation. Because he  
12      applied the costs on a pound basis and the fact that saturation mail in Witness Haldi's analysis  
13      weighs less than basic mail, he develops a larger cost difference due to sortation than calculated  
14      by the USPS. Table 4 below summarizes Witness Haldi's calculation of the average weight and  
15      the shipping costs for letter and nonletter mail.

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<p>Table 4</p> <p>Comparison of Average Weight and</p> <p>Shipping Costs In Witness Haldi's Analysis</p>		
Item	Average Weight Per Piece - lbs <sup>1/</sup>	Per Piece Shipping Costs <sup>2/</sup>
(1)	(2)	(3)
1. Letters		
a. Basic	0.0815	0.39c
b. Saturation	<u>0.0566</u>	<u>0.27</u>
c. Difference	0.0249	0.12c
d. Percent (L1c ÷ L1a)	31%	31%
2. Nonletters		
a. Basic	0.1039	1.43c
b. Saturation	<u>0.0843</u>	<u>1.16</u>
c. Difference	0.0196	.27c
d. Percent (L2c ÷ L2a)	19%	19%
<sup>1/</sup> Haldi, Table A-5 (Tr. 27/15105) - BMC for letters and no destination entry for nonletters.		
<sup>2/</sup> Haldi Table A-10, (Tr. 27/15110) — BMC for letters and no destination entry for nonletters.		

19 As shown in Table 4 above, the difference in shipping costs in Witness Haldi's analysis is  
20 exactly the same as the difference in the average weight per piece (31 percent for letters and 19  
21 percent for nonletters).<sup>11/</sup> As with the USPS' proposal, the difference in costs related to shipping  
22 costs should only be recognized in the destination entry discounts, not the sortation discount.

23 Finally, in addition to his inappropriate costs, Witness Haldi's rate design reflects  
24 modification of the USPS' passthrough of the cost savings related to sortation. Table 5  
25 compares the cost savings and discounts proposed by the USPS and Witness Haldi.

<sup>11/</sup> The difference between the cost savings in Table 4 and Column (5) of Table 3 is attributed to rounding and the application of the contingency factor is 1 percent.

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Table 5  
Summary of Cost Savings and  
Proposed Discounts -- Sortation

Item (1)	Amount (Cents Per Piece)		Percent <sup>3/</sup> (4)
	Cost Savings <sup>1/</sup> (2)	Proposed Discount <sup>2/</sup> (3)	
1. Letters -- High-Density			
a. USPS	2.2¢	2.1¢	95%
b. Haldi	2.2	2.5	114
2. Letters -- Saturation			
a. USPS	3.1	3.0	97
b. Haldi	3.3	3.8	115
3. Nonletters -- High-Density			
a. USPS	2.8	1.1	39
b. Haldi	2.8	1.7	60
4. Nonletters -- Saturation			
a. USPS	4.4	2.3	52
b. Haldi	4.8	2.9	60

<sup>1/</sup> Table 3 above.  
<sup>2/</sup> Table 1 above.  
<sup>3/</sup> Column (3) ÷ Column (2).

22 For letters, Witness Haldi has proposed sortation discounts which are 114% to 115% of his  
23 calculation of the cost savings while the USPS proposed discounts are 95% to 97% of the cost  
24 savings. The passthrough percentage for Witness Haldi's proposed sortation discount for letters  
25 (Table 5, lines 1b and 2b) exceed 100 percent because of his methodology which develops 10  
26 percent of the rate based on a fixed mark-up ratio of 2.4405. Stated differently, Witness Haldi's

1 discounts reflect a 90 percent weighting of a cost savings per piece and a 10 percent weighting  
2 of the cost difference multiplied by 2.4405.<sup>12/</sup>

3 For nonletters, Witness Haldi's discounts are 60 percent of the cost savings while the USPS  
4 has proposed discounts equal to 39 percent of the cost savings for High-Density mail and 52  
5 percent of the cost savings for saturation. Aside from the fact that the passthrough percentage  
6 is arbitrary, Witness Haldi's procedures for nonletters bears no relationship to the procedures  
7 he has followed in developing the sortation discounts for letters.

8 In summary, Witness Haldi has offered no support for his adjustment to sortation discounts  
9 proposed by the USPS and should be rejected.

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<sup>12/</sup> High density letters equal: [2.2 cents per piece x .90] plus [2.2 cents per piece x 2.4405 x .10]. Saturation letters equal: [3.3 cents per piece x .90] plus [3.3 cents per piece x 2.4405 x .10].

**STATEMENT OF QUALIFICATIONS**

My name is Roger C. Prescott, I am a Vice President and economist with the economic consulting firm of L. E. Peabody & Associates, Inc. The firm's offices are located at 1501 Duke Street, Suite 200, Alexandria, Virginia 22314.

I am a graduate of the University of Maine from which I obtained a Bachelor's degree in Economics. Since June 1978 I have been employed by L. E. Peabody & Associates, Inc.

I have previously participated in various Postal Rate Commission ("PRC") proceedings. In Docket No. R90-1, Postal Rate And Fee Changes, 1990, I developed and presented evidence to the PRC which critiqued and restated the direct testimony of the United States Postal Service ("USPS") as it related to the development of the proposed rate structure on behalf of third class business mailers. I also submitted Rebuttal evidence in PRC Docket No. MC95-1, Mail Classification Schedule, 1995 Classification Reform I, regarding recommendations of intervenors in response to the USPS' proposed reclassification of Third Class Bulk Rate Regular ("TCBRR") rate structure.

The firm of L. E. Peabody & Associates, Inc., specializes in solving economic, marketing and transportation problems. As an economic consultant, I have participated in the direction and organization of economic studies and prepared reports for railroads, shippers, for shipper associations and for state governments and other public bodies dealing with transportation and related economic problems. Examples of studies which I have participated in organizing and directing include traffic, operational and cost analyses in connection with the transcontinental movement of major commodity groups. I have also been involved with analyzing multiple car



movements, unit train operations, divisions of through rail rates and switching operations throughout the United States. The nature of these studies enabled me to become familiar with the operating and accounting procedures utilized by railroads in the normal course of business.

In the course of my work, I have become familiar with the various formulas employed by the Interstate Commerce Commission ("ICC") (now the Surface Transportation Board ("STB")) in the development of variable costs for common carriers with particular emphasis on the basis and use of Rail Form A and its successor, the Uniform Railroad Costing System ("URCS"). In addition, I have participated in the development and analysis of costs for various short-line railroads.

Over the course of the past sixteen years, I have participated in the development of cost of service analyses for the movement of coal over the major eastern, southern and western coal-hauling railroads. I have conducted on-site studies of switching, detention and line-haul activities relating to the handling of coal. I developed the carrier's variable cost of handling various commodities, including coal, in numerous proceedings before the ICC/STB. I have presented testimony related to the development of variable costs in ICC Docket No. 39002, Utility Fuels, Inc. v. Burlington Northern et al., ICC Docket No. 39386, The Kansas Power and Light Company v. Burlington Northern Railroad Company, et al. ("KPL"), ICC Docket No. 38783, Omaha Public Power District v. Burlington Northern Railroad Company ("OPPD"), ICC Docket No. 38025S, The Dayton Power and Light Company v. Louisville and Nashville Railroad Company ("DPL"), and ICC Docket No. 41191, West Texas Utilities Company v. Burlington Northern Railroad Company ("WTU").

As part of the variable cost evidence I have developed and presented to the ICC/STB, I have calculated line specific maintenance of way costs based on the Speed Factored Gross Ton ("SFGT") formula. In DPL and WTU, my testimony presented the evidence which calculated maintenance of way costs based on the SFGT formula.

In October 1993, I presented the history and use of the SFGT formula at a conference attended by shippers, railroads, association members and Commission staff. The conference, titled "Maintaining Railway Track-Determining Cost and Allocating Resources," examined the methodologies used to determine maintenance of way costs over freight and passenger rail lines.

I have developed and presented evidence to the ICC/STB related to maximum rates, and "Long-Cannon" factors in OPPD and KPL. I have also submitted evidence on numerous occasions in Ex Parte No. 290 (Sub-No. 2), Railroad Cost Recovery Procedures related to the proper determination of the Rail Cost Adjustment Factor.

In the two recent Western rail mergers, Finance Docket No. 32549, Burlington Northern, et al. -- Control and Merger -- Santa Fe Pacific Corporation, et al. and Finance Docket No. 32760, Union Pacific Corporation, et al. -- Control and Merger -- Southern Pacific Rail Corporation et al., I reviewed the railroads' applications including their supporting traffic, cost and operating data and provided detailed evidence supporting requests for conditions designed to maintain the competitive rail environment that existed before the proposed mergers.

## **Summary Of Witness Haldi's Constructed Rates For Letters** (Cents Per Piece)

### **II. Development of Proposed Rates By Rate Cell**

<u>Sortation</u> (1)	<u>Initial Target Rates</u>				<u>Revenue True-Up</u> (6)	<u>Final Rates</u>			
	<u>No Dest. Entry</u> (2)	<u>BMC</u> (3)	<u>SCF</u> (4)	<u>DDU</u> (5)		<u>No Dest. Entry</u> (7)	<u>BMC</u> (8)	<u>SCF</u> (9)	<u>DDU</u> (10)
1. Adjustment For Destination Entry 1/	1.5	xxx	-0.3	-0.8	xxx	xxx	xxx	xxx	xxx
2. Basic	17.0340	15.5340	15.2340	14.7340	-0.334	16.7	15.2	14.9	14.4
3. Automation	16.3351	14.8351	14.5351	14.0351	-0.334	16.0	14.5	14.2	13.7
4. High Density	14.5379	13.0379	12.7379	12.2379	-0.334	14.2	12.7	12.4	11.9
5. Saturation	13.2712	11.7712	11.4712	10.9712	-0.334	12.9	11.4	11.1	10.6

1/ USPS proposal, Moeller, USPS-T-36, page 31.

Sources:

Column (2): Column (3) + Column (2), Line 1.  
Column (3): Exhibit\_MOAA-RT-1A, Page 1 of 2, Column (11).  
Column (4): Column (3) + Column (4), Line 1.  
Column (5): Column (3) + Column (5), Line 1.  
Column (6): Haldi, Table C-3.  
Column (7): Column (2) - Column (6).  
Column (8): Column (3) - Column (6).  
Column (9): Column (4) - Column (6).  
Column (10): Column (5) - Column (6).

## **Summary Of Witness Haldi's Constructed Rates For Letters**

(Cents Per Piece)

### **I. Development of Proposed Rates By Sortation Level -- BMC**

<u>Sortation</u> (1)	<u>Volume Variable Costs</u>				<u>Cost True-Up</u> (6)	<u>Total Costs</u>		<u>Constructed Rates</u>		
	<u>Mail Processing</u> (2)	<u>Delivery</u> (3)	<u>Shipping</u> (4)	<u>Total</u> (5)		<u>Without Contingency</u> (7)	<u>With Contingency</u> (8)	<u>Fixed Margin</u> (9)	<u>Mark-up Percentage</u> (10)	<u>Weighted</u> (11)
1. Basic	1.9840	4.3670	0.3872	6.7382	0.3193	7.0575	7.1281	15.3271	17.3961	15.5340
2. Automation	2.3891	3.3570	0.3872	6.1333	0.3193	6.4526	6.5172	14.7162	15.9053	14.8351
3. High Density	0.3611	3.7590	0.4579	4.5780	0.3193	4.8973	4.9463	13.1453	12.0714	13.0379
4. Saturation	0.3611	2.8520	0.2687	3.4818	0.3193	3.8011	3.8391	12.0381	9.3694	11.7712

**Sources:**

Column (2) and Column (3): Haldi, Table A-1.

Column (4): Haldi, Table A-10.

Column (5): Column (2) + Column (3) + Column (4).

Column (6): Haldi, Table A-12.

Column (7): Column (5) + Column (6).

Column (8): Column (7) \* 1.01.

Column (9): Column (8) + 8.199 cents per piece (Haldi, Table C-2).

Column (10): Column (8) \* 2.4405 (Haldi, Table C-2).

Column (11): Column (9) \* 90% + Column (10) \* 10% (Haldi, Table C-2).



**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

1     **A. TABLE A-1**

2           This table develops the average unit costs for letters and nonletters by level of sortation.  
3     First, Witness Haldi's underlying Test Year unit costs for the separation of volume variable costs  
4     rely on overall average volume for letters and flats combined for the transportation component  
5     (0.1877 cents per piece) and the other component (0.4519 cents per piece). These two  
6     components reflect approximately 10 percent of the overall unit costs. Stated differently, 10  
7     percent of Witness Haldi's costs cannot be separated between letters and nonletters.

8           Second, Witness Haldi's value for the "other" component (Table A-1, Column (4)) is not  
9     supported. When asked in interrogatories to provide the support for this value, Witness Haldi  
10    stated that he was "unable to locate the work..." and would "supplement this response after we  
11    locate it" (Tr. 27/15219). To date no support has been provided for his calculation of the  
12    "other" component for his Test Year unit costs. The lack of support for one of the underlying  
13    unit costs in his analysis renders his results meaningless. Without support for this value neither  
14    the PRC nor I can evaluate the appropriateness of his separation of costs into rate cells.

15    **B. TABLE A-2**

16           This table multiplies the unit costs from Table A-1 by the USPS' volumes to develop  
17    aggregate costs for letters and nonletters by level of sortation. Because of the errors in Table  
18    A-1, the separation of the costs between letters and nonletters cannot be validated.

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

**C. TABLE A-3 THROUGH TABLE A-5**

These tables develop the average weight per piece based on the 1996 Billing Determinants.

I agree with these calculations.

**D. TABLE A-6**

Table A-6 develops the TYAR pieces for each of Witness Haldi's rate cells. Witness Haldi's separation of total pieces for ECR pound rated mail by destination entry profile in Table A-6 is based on the USPS' separation of the pounds by destination entry profile<sup>2/</sup>. Stated differently, Witness Haldi has assumed that all pound rated nonletter mail weighs the same regardless of where the mail is entered in the mailstream. Witness Haldi's analysis reflects that all basic pound rated piece mail weighs 0.32 pounds per piece, high-density mail weighs 0.34 pounds per piece, and saturation mail weighs 0.30 pounds per piece.<sup>3/</sup> Under his analysis, the weight shown above was applied to the level of sortation regardless of the destination entry location in order to determine the number of pieces.

Furthermore, comparison of the implicit average weights used by Witness Haldi in Table A-6 with the average weight using actual 1996 Billing Determinants (Table A-5) indicates large disparities. For example, high-density mail entered at the BMC had a 1996 average weight of 0.21 pounds per piece which reflects a 29 percent reduction from Witness Haldi's value of

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<sup>2/</sup> The USPS' separation is shown in Witness Moeller's workpaper 1, page 20.

<sup>3/</sup> Total pounds in Table A-7 divided by total pieces in Table A-6.

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

1     0.34 pounds per piece. His assumption regarding pounds is false based on the same 1996 Billing  
2     Determinant data that he used elsewhere in his analysis. In summary, Witness Haldi's  
3     distribution of pounds for nonletter-pound rated mail distorts the true weight applicable to each  
4     of his rate cells, thus, the number of pieces for each rate cell derived from this average weight  
5     is also incorrect

6     **E. TABLE A-7**

7     Table A-7 develops the aggregate pounds for each rate cell. For letter mail and piece rated  
8     nonletter mail, Witness Haldi based the pounds on total pounds and pieces from the USPS' 1996  
9     Billing Determinants. However, in developing the pounds for automation letters, Witness Haldi  
10    "assumed that these [automation] letters have the same average weight as Basic Presort  
11    Letters..." (Tr. 27/15182) This assumption is false as shown in Witness Haldi's own data.  
12    Table A-5 of Witness Haldi's testimony shows that automation letters average 0.0509 pounds  
13    per piece while Basic Presort Letters have an average weight of 0.0464 pounds per piece, a  
14    difference of 10 percent. His analysis does not adjust for this difference in average weight.

15    **F. TABLE A-8**

16    In Table A-8, Witness Haldi summarizes the USPS' unit costs for shipping by point of  
17    entry. The nontransportation costs for SCF shown by Witness Haldi equals 0.72 cents per



**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

1      pound and is not correct. The actual value from the USPS' Library Reference LR-H-111 equals  
2      0.73 cents per pound.

3      **G. TABLE A-9**

4              This table develops the aggregate shipping costs by level of sortation and destination entry.  
5      Because of the errors in the average weight for automation letters and pound rated pieces (Table  
6      A-6) and the error in Witness Haldi's unit costs for destination entry at the SCF (Table A-8),  
7      these aggregate costs are not correct.

8      **H. TABLE A-10**

9              In Table A-10, Witness Haldi develops the unit costs for shipping for each rate cell. The  
10      difference in shipping costs related to sortation are entirely due to the average weights utilized  
11      by Witness Haldi. Because of the errors noted above, these unit costs are not correct. In  
12      addition, Witness Haldi's analysis assumes that shipping costs for piece rated mail (i.e., below  
13      3.3 ounces) vary in direct proportion to weight. This assumption has not been shown to be valid  
14      and, in fact, is refuted by the data shown in Witness Haldi's Appendix D.<sup>4/</sup>

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<sup>4/</sup> Witness Haldi's Appendix D, which is based on Library Reference LR-H-182, shows that a carrier route letter mail weighing 1 ounce costs more than letters weighing from 2 to 4 ounces.

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

1     **I. TABLE A-11**

2             Table A-11 summarizes Witness Haldi's total unit costs for letters by rate cell. Because of  
3     the errors in the underlying unit costs and weights, the unit costs in this table are not correct.

4     **J. TABLE A-12**

5             In order for the aggregate letter costs in Table A-2 to match his costs by rate cell, Witness  
6     Haldi's Table A-12 develops a cost "true-up" for letters of 0.32 cents per piece. However,  
7     Witness Haldi's procedures mask the wide variation in the cost "true-up" for each level of  
8     sortation. Assuming that the distribution of costs between letters and flats in Table A-2 and the  
9     unit costs in Table A-11 were correct (and in fact, are not correct), the variation within Witness  
10    Haldi's composite cost "true-up" is shown in Table 1 below:

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

Table 1				
Summary of Witness Haldi's Development of Costs By Level of Sortation — Letters				
Sortation (1)	Aggregate costs (000)		Difference	
	from Table A-2 (2)	from Table A-12 (3)	Total (000) <sup>1/</sup> (4)	Cents Per Piece <sup>2/</sup> (5)
1. Basic	\$221,866	\$212,832	\$9,034	0.23c
2. Automation	131,524	126,789	4,735	0.28
3. High-Density	18,705	17,323	1,382	0.35
4. Saturation	<u>118,910</u>	<u>106,240</u>	<u>12,671</u>	<u>0.41</u>
5. Total	\$491,006	\$463,184	\$27,822	0.32c
<sup>1/</sup> Column (2) minus Column (3).				
<sup>2/</sup> Column (4) ÷ letter volume by sortation level in Table A-6.				

Overall, the costs developed by Witness Haldi in Table A-12 are understated by \$27.8 million (Table 1, Line 5 above). Witness Haldi corrects for this understatement by converting the aggregate total difference to a per piece amount which equals 0.32 cents per piece. This per piece amount is applied as the unit cost for each letter rate cell.

However, Witness Haldi's procedures mask the fact that his methodology overstates the cost "true up" for Basic mail (0.23 cents per piece) and for Automation mail (0.28 cents per piece) while understating the cost "true-up" for High-Density mail (0.35 cents per piece) and Saturation mail (0.41 cents per piece). If the "true-up" factor were calculated for each sortation level,

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

Witness Haldi's "bottom-up" costs for basic and automation letters would be less than he has calculated. Conversely, if the cost "true-up" were calculated by sortation level, Witness Haldi's "bottom-up" costs for high-density and saturation letters would be greater than he has calculated.

**K. TABLE A-13**

Utilizing the unit costs developed in Table A-11 and the 0.32 cent per piece cost "true-up" developed in Table A-12, Table A-13 of Witness Haldi's analysis develops the adjusted TYAR unit costs. These costs are then increased by the USPS' contingency factor of 1 percent. Because of errors in the underlying data in Table A-11 and the misapplication of the cost "true-up" in Table A-12, Witness Haldi's TYAR unit costs are incorrect.

**L. TABLE A-14**

Table A-14 begins Witness Haldi's analysis of the cost for each nonletter rate cell assuming that 2.33 cents per piece is weight related. Witness Haldi feels that the USPS has "failed to present any reliable evidence concerning which costs should be treated as pound-related and which costs should be treated as piece-related...." (Tr. 27/15055). Therefore, Witness Haldi assumes that 2.33 cents per piece should be considered weight related for all nonletters. He admits that the treatment of "2.33 cents per piece as weight-related cost is arbitrary..." (TR 27/15057). Witness Haldi's analysis of the costs associated with weight as utilized in Table A-14 (or subsequent Tables) have no bearing on his ultimate rate design for pound-rate

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

1 mail. Witness Haldi has accepted the per pound rate of Witness Moeller of \$0.53 per pound as  
2 "conservative" (TR 27/15172)

3 **M. TABLE A-15**

4 In Table A-15, Witness Haldi attempts to separate his assumed weight related costs of 2.33  
5 cents per piece between piece rated mail and pound rated mail. Aside from the fact that his  
6 underlying assumption regarding costs is not supported (see the discussion of Table A-14 above),  
7 Witness Haldi's table contains a mathematical error. Witness Haldi uses a divisor for total  
8 pounds of 3,909 million pounds (Table A-15, Line 2). The correct value for nonletter mail  
9 pounds following Witness Haldi's procedures, equals 3,893 million pounds as shown in Table  
10 A-7 of his statement. This causes the results in this table to be in error.

11 **N. TABLE A-16**

12 Table A-16 summarizes Witness Haldi's unit costs for nonletters. This analysis does not  
13 summarize "bottom-up" costs for two reasons. First, he assumes that the per piece portion of  
14 the costs for pound rated mail does not vary by destination entry (i.e., the costs for saturation  
15 nonletters with no dropshipping equals the costs for saturation letters dropshipped at the DDU).  
16 Second, for the pound portion of pound-rated mail, Witness Haldi assumes that costs do not vary  
17 with sortation or destination entry, (e.g., the pound portion of pound rated mail for basic

**APPENDIX B:**  
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sortation without dropshipping is the same as the pound portion for saturation mail dropshipped at the DDU).

**O. TABLE A-17**

As with letter mail, Witness Haldi develops a "true-up" cost per piece to bring his constructed costs derived from Table A-16 in line with the costs for nonletters as developed in his Table A-2. Table A-17 reflects his development of a cost "true-up". Witness Haldi's procedures mask the difference in his costs by level of sortation as shown in Table 2 below.

Table 2 Summary of Witness Haldi's Development of Costs By Level of Sortation — Nonletters				
Sortation (1)	Aggregate Costs (000)		Difference	
	From Table A-2 (2)	From Table A-17 <sup>1/</sup> (3)	Amount (000) <sup>2/</sup> (4)	Cents Per Pound <sup>3/</sup> (5)
1. Basic	\$945,821	\$985,418	\$(39,597)	(-)1.75
3. High-Density	70,075	67,168	2,907	1.29
4. Saturation	<u>359,870</u>	<u>302,136</u>	<u>57,734</u>	<u>4.11</u>
5. Total	\$1,375,766	\$1,354,722	\$21,044	0.54
<sup>1/</sup> Sum of costs for piece rated nonletters, piece portion of pound rated nonletters and the pound portion of nonletters.				
<sup>2/</sup> Column (2) minus Column (3).				
<sup>3/</sup> Column (4) divided by number of pounds in Table A-7.				

Overall, the costs developed by Witness Haldi in his two tables are close, differing by only \$21 million or 0.54 cents per pound (Table 2, Line 5). However, a comparison of his initial

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

1 costs (Table A-2) with his constructed costs (based on the arbitrary assumption of 2.33 cents per  
2 piece related to weight) shows that his analysis underrecovers the costs for Basic nonletter mail  
3 by 1.75 cents per pound (Table 2, Line 1) and overrecovers the costs for high-density nonletter  
4 mail by 1.29 cents per pound. In addition, the cost "true-up" for nonletter saturation mail is  
5 extremely large, i.e., 4.11 cents per pound.

6 Witness Haldi's per pound "true-up" as calculated in Table A-17 is flawed because of the  
7 dramatic under and overrecovery of costs by level of sortation. Specifically, following Witness  
8 Haldi's procedures, the cost "true-up" for Basic nonletters should be a negative adjustment. In  
9 addition, the true-up for saturation mail should be approximately 8 times the value calculated  
10 by Witness Haldi. If cost "true-ups" separated by sortation are used, Witness Haldi's unit costs  
11 for basic nonletter mail would be less than he has calculated while the unit costs for high density  
12 and saturation mail would be higher than Witness Haldi calculated.

13 **P. TABLES A-18 AND A-19**

14 Tables A-18 and A-19 develop Witness Haldi's revised unit costs and restated aggregate  
15 costs for nonletters. The flaws discussed above invalidate the unit costs and aggregate costs  
16 shown these tables.

**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

1     **Q. TABLES A-20 THROUGH A-25**

2             Tables A-20 through Table A-25 in Witness Haldi's testimony repeat the mathematical  
3     exercise he performed for nonletter mail utilizing 0.5825 cents per piece as weight related  
4     instead of the 2.33 cents per piece. First, Witness Haldi's rate proposal never relies on these  
5     tables. Second, like his prior analysis using 2.33 cents per piece, the value of 0.5825 cents per  
6     piece is arbitrary and not supported by workpapers. Therefore, the analysis in these tables have  
7     not been and should not be considered in designing rates for ECR mail.

8     **R. TABLE C-1**

9             Table C-1 summarizes Witness Haldi's calculation of the unit costs for letters by rate cell.  
10     For the reasons outlined above under my discussion of Witness Haldi's Table A-1 through Table  
11     A-13, his unit costs are incorrect and should be rejected.

12     **S. TABLE C-2**

13             Table C-2 develops Witness Haldi's Initial Target Rates for letters based on his unit costs  
14     (Table C-1) with 90 percent of the rates based on a constant margin of 8.199 cents per piece and  
15     10 percent based on a constant mark-up ratio of 2.4405. Three problems exist with these Initial  
16     Target Rates. First, as discussed in the previous sections, Witness Haldi only relies on the  
17     results for BMC mail in his rate proposal. Second, the 90%/10% allocation is arbitrary and not  
18     supported. If the distribution is changed, then the Initial Target Rates change.



**APPENDIX B:**  
**ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

Finally, Witness Haldi's constant margin and mark-up percentages are wrong because he failed to make changes after his errata was filed. Table 3 below summarizes Witness Haldi's development of the constant margin and mark-up ratio for letters with the correct values.

Table 3 Comparison of Witness Haldi's Constant Margin and MarkUp Ratio For Letters — As Stated and Revised			
Item (1)	Source (2)	As Used in Haldi's Table C-2 (3)	Corrected (4)
<b><u>Constant Margin</u></b>			
1. Revenue Requirement	Haldi, C-12	\$1,210,277 <sup>1/</sup>	\$1,194,629 <sup>2/</sup>
2. Volume Variable Costs	Haldi, A-2	495,916	495,916
3. Margin	L1 - L2	\$714,361	\$698,713
4. Pieces (000)	Haldi, A-6	8,712,800	8,712,800
5. Margin Per Piece	L3 ÷ L4	8.199¢	8.019¢
<b><u>Mark-Up Ratio</u></b>			
6. Amount	L1 ÷ L2	2.4405	2.4089
<sup>1/</sup> As shown in his original testimony.			
<sup>2/</sup> As revised in errata and submitted in testimony.			

Witness Haldi's rate proposal for letters relies on constructed rates utilizing a constant margin of 8.199 per piece and mark-up ratio of 2.4405. The correct values are a constant margin of 8.019 cents per piece and a mark-up ratio of 2.4089. Witness Haldi's failure to utilize these corrected values invalidate his results.

**APPENDIX B:  
ERRORS AND ASSUMPTIONS IN WITNESS HALDI'S PROCEDURES**

**T. TABLE C-3**

Table C-3 adjusts Witness Haldi's letter rates so that his proposal is revenue neutral with the USPS' proposal. The adjustment errors are discussed in previous sections to my testimony.

**U. TABLES C-4 THROUGH C-11**

Tables C-4 through C-11 summarize the various statistics for nonletter mail and develop the aggregate revenue based on Witness Haldi's proposed rates for nonletters. Because of the errors discussed earlier in this section, his calculations are in error.

**V. TABLE C-12**

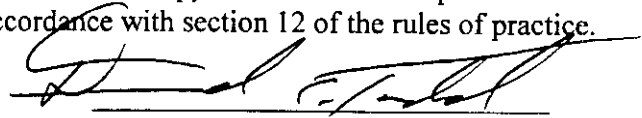
Table C-12 summarizes the USPS' revenues separately for letters and nonletters. I agree with Witness Haldi's calculations.

**V. SUMMARY OF CRITIQUE OF  
WITNESS HALDI'S APPENDIX A  
AND APPENDIX C**

As shown in this exhibit to my testimony, Witness Haldi's development of ECR rates is based on numerous faulty (or unsupported) assumptions and mathematical errors which invalidate his results. Because of the interrelationship of these errors, it is impossible to restate his results based on a theory of "bottom-up" costs for setting rates.

### CERTIFICATE OF SERVICE

I hereby certify that I have caused to be served a copy of MOAA-RT-1 upon all participants of record in this proceeding in accordance with section 12 of the rules of practice.

A handwritten signature in black ink, appearing to read "David C. Todd", is written over a horizontal line.

David C. Todd

March 9, 1998