

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

MODIFICATION OF ANALYTIC PRINCIPLES IN  
PERIODIC REPORTING (PROPOSALS THREE  
THROUGH EIGHT)

Docket No. RM2010-12

RESPONSES OF THE UNITED STATES POSTAL SERVICE TO  
QUESTIONS 1-9 OF CHAIRMAN'S INFORMATION REQUEST NO. 1  
(October 25, 2010)

The Postal Service hereby files its responses to questions 1-9 of Chairman's Information Request No. 1, issued on October 14, 2010. Each question is stated verbatim, and followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.  
Chief Counsel, Pricing & Product Support

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Eric P. Koetting

475 L'Enfant Plaza West, S.W.  
Washington, D.C. 20260-1137  
(202) 268-2992, FAX: -5402  
October 25, 2010

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

1. Proposal Four would change the way In-Office Cost System (IOCS) distributes retail window service acceptance costs when mail bears non-retail indicia and includes Extra Services such as Certified or Return Receipt. The material supporting Proposal Four includes a table which shows the cost impact of the proposal on the market dominant products, but does not show its cost impact on the associated Extra Services. Please provide the impact of the proposal on the costs for the following Extra Services:

- a. Certified;
- b. Insured;
- c. Return Receipt;
- d. Delivery Confirmation;
- e. Signature Confirmation;
- f. COD; and
- g. Registered.

**RESPONSE:**

The following table summarizes the impact of Proposal Four

<b>Extra Service</b>	<b>FY09 Cost Impact (Proposed – Current) \$(000)</b>	<b>FY09 Attributable Cost \$(000)</b>	<b>Percent Change Attributable Costs</b>
Certified	(\$7,565)	\$659,480	-1.1%
Insured	(\$1,586)	\$116,869	-1.4%
Return Receipt	(\$127)	\$61,562	-0.2%
Delivery Confirmation	(\$7,122)	\$261,113	-2.7%
Signature Confirmation	(\$117)	\$50,598	-0.2%
COD	\$0	\$6,596	0.0%
Registered	\$0	\$50,586	0.0%

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

2. [Proposal Four] The background section of the proposal states “[c]urrently in IOCS, when a mailpiece is accepted at a retail window and includes an Extra Service, that acceptance cost is assigned to the Extra Service to the host mailpiece....”

a. Please explain the rationale for assigning the entire acceptance cost to the Extra Service rather than allocating the cost between the host piece and the Extra Service.

b. Restricted Delivery is not identified as one of the Extra Services included in this proposal. Please explain why Restricted Delivery is not included among the identified Extra Services.

**RESPONSE:**

a) Currently, if the Extra Service is considered to be the primary cost driver of an operation, the entire tally cost is attributed to the service; otherwise, it is attributed to the host piece. This is because the Extra Service is the primary source of the combined transaction time. When there are multiple Extra Services, the one considered the primary driver for that operation receives all of the cost. Because the Extra Service is purchased in conjunction with the host piece (and not simply in the same transaction), it is extremely difficult to measure the portion of time associated with each. Moreover, IOCS relies upon a “moment in time” approach and is not equipped to split the window acceptance cost between the host piece and one or more Extra Services. At this time, the Postal Service does not have a reliable basis to make the more refined measurements required to split cost between the host piece and the Extra Service.

b) Restricted Delivery can only be purchased in association with another Extra Service such as Registered, Insurance, COD or Certified. Currently these associated Extra Services always take precedence, so no IOCS tally cost is attributed to Restricted Delivery.

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

3. [Proposal Four] Please describe any changes to the IOCS questionnaire necessary to implement Proposal Four. If no changes are anticipated, describe fully the methodology that would be used to ensure that costs are assigned to the host mailpiece rather than the Extra Service.

**RESPONSE:**

No changes are required to the IOCS survey instrument. The methodology would be implemented by changes to the mainframe processing program ALB080 that assigns the tally cost to an Extra Service when appropriate conditions are met.

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

4. [Proposal Four] What changes, if any, would have to be made to the "B" workpaper for Segment 3, specifically worksheet 3.2.1, to effectuate the change in costing described in Proposal Four?

**RESPONSE:**

No changes are needed to the "B" workpaper for Segment 3. Costs will be assigned to appropriate activity codes during IOCS data processing, and no further changes are needed in any downstream processing steps.

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

5. Proposal Five would change the distribution key used to assign collection costs on rural routes to products. The proposal is intended to better align the distribution of collection costs with the manner in which rural carriers are compensated by assigning to letters/flats the relevant collection costs of prepaid parcels that weigh less than 2 pounds.

- a. Please identify where the revenue from these prepaid parcels that weigh less than 2 pounds is recorded.
- b. Please confirm that under this proposal collection costs related to parcels that weigh less than 2 pounds will be attributed to letters/flats.
- c. If so, please confirm that there will be a misalignment between the attribution of revenue and costs for parcels.

**RESPONSE:**

a. The revenue for these prepaid parcels goes to the rate category in which they are mailed. The revenue for a prepaid First-Class Parcel, for example, is assigned to the product First-Class Parcels.

b. Not confirmed. This proposal does not shift costs between products, rather it assigns collection costs to products in accordance with the manner in which rural carriers are compensated for collected parcels. Under this proposal, a prepaid First-Class Parcel will move from the Parcels Accepted cost pool to the Letters/Flats Collected cost pool, but the collection costs will still be assigned to the product First-Class Parcels.

c. Not applicable. Please refer to response to part b.

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

6. [Proposal Six] Please refer to the Excel file, ICRA09\_ib-bycgrp\_v.xls, and worksheet tab CS 6 Attrib Cost, which shows CS 6 – City Carriers Office Activity costs for Canada, Industrialized Countries (ICs) and Developing Countries (DCs) for the five categories of inbound mail: Surface AO, Air LC, Surface Parcels, Air Parcels, and Express. Also, please refer to Library Reference USPS-RM2010-12/NP1, the Excel file, Reports (Booked).xls, and worksheet tab Pivot1b, which allocates CS 6 – City Carriers Office Activity costs for Canada, ICs and DCs by inbound mail category between “Delivery (\$000)” and “Other Domestic (\$000).” For each of the subparts below, show all calculations in electronic form, and provide citations to all sources used.

- a. Please show how CS 6 – City Carriers Office Activity costs are allocated between “Delivery” and “Other Domestic.”
- b. Please show how “Delivery” costs are allocated among Canada, Industrialized Countries (ICs), and Developing Countries (DCs).
- c. Please show how “Other Domestic” costs are allocated among Canada, ICs, and DCs.
- d. Please show how the costs developed in response to subpart b., above, are allocated to the inbound mail categories.
- e. Please show how the costs developed in response to subpart c., above, are allocated to the inbound mail categories.

**RESPONSE:**

a. The purpose of this proposal is to directly provide the information calculated in the PRC analysis provided in the workbook PRC-ACR2009-NP-LR3\_IOCS Analysis.xls. CS 6 costs are not allocated between “Delivery” and “Other Domestic” per the usual definitions. Delivery is comprised of CS 6, 7, 8 10 and 12; and Other Domestic are 1, 11, 13, 15, 16, 18, and 20. Thus, there is no allocation of CS 6 to Other Domestic.

PRC-ACR2009-NP-LR3\_IOCS Analysis.xls in essence replaces the ICRA Foreign Origin cost data by product for CS 2, 3 and 6 with data reallocated to include splits by country classification: Canada, ICs less Canada and DCs. Thus, the totals for the Foreign Origin costs do not change in any of these segments by product; however, costs by country classification do change.

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

Pivot1b is a table that merely summarizes calculations made elsewhere in the ICRA and as such does not contain calculations other than summations. There is a staging area on this sheet to the right of the pivot table which provides data in a format consistent with the "Summary Table 1" from the PRC-ACR2009-NP-LR3\_IOCS Analysis.xls.

As an overview, total Foreign Origin Costs in the allocations by country classification match. Total Foreign Origin costs by each segment are shown in the ICRA, while Pivot1b shows costs by the general cost categories: Mail Processing, Delivery, Other Domestic and Domestic Transportation. Note that the Pivot1b amounts match the grand total in cell n65 on the Summary sheet of PRC-ACR2009-NP-LR3\_IOCS Analysis.xls at the bottom of Supporting Summary Table 2. An overall comparison shows that both the total Foreign Origin costs by Total Cost Segments and the total Foreign Origin costs in cell n65 match closely the results from Pivot1b, which merely summarizes calculations by 232 individual countries as reflected on the ICRA Database sheet.

b. Delivery costs are allocated by country classification based on unitized costs developed on the CRA Staging sheet of Reports (Booked). The cost calculations follow previous ICRA, except that additional rows were added to various tables in order to reflect not just product distinctions, but also country classification. Rows 81 through 97 of this sheet now contain information for CS 2, 3 and 6 which are now allocated by country classification. The addition of these rows expanded the table of unit costs at cells ao56 through az107. Only mail processing and delivery costs vary by country classification. Piece volumes are populated into as91:97 and unitized costs are developed in at81:aw97. These country category specific unitized costs are then transferred to the summary table at g5:k35, named as the range ForOr\_Unit\_Costs, which is the source of lookup values for the ICRA Database. For a delivery cost example, see the calculation for "alc" - air letterpost - for Albania at cell u1426 of the ICRA Database. The data on the ICRA Database are organized into a table format that can serve as a pivot table source. This

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

information is the source data for Pivot1b which aggregates country-specific results to country classifications.

c. Other domestic costs are allocated based on unitized costs summarized in the same table as delivery costs, starting at row 1659 of the ICRA Database. There is no "mechanical" difference in the calculations made on the ICRA Database sheet, except that other domestic costs do not vary by country classification.

d. The example in subpart b. referenced the inbound mail category "alc" for air letterpost. The other inbound mail categories are calculated in columns v through ai of the ICRA Database sheet.

e. The calculation of other domestic costs for inbound mail categories parallels the description in subpart d.

While doing the background for these responses, the Postal Service discovered the reasons for the small differences between PRC-ACR2009-NP-LR3\_IOCS Analysis.xls and what was calculated in the Reports (Booked) file. First, there were two issues in the data on the CRA Cost Segments of Inputs.xls:

- 1) The direct tallies are brought in at rows 99-133, but in cells H118 and H132 for component 3.3, there are no tallies for Air Parcel Post for ICs and DCs, although Air LC/AO tallies should have been assigned to Parcels, and
- 2) For component 2.5, total tallies for components 2.1 through 2.4 are used as the distribution key, but the costs of those components should have been used instead.

Second, in the staging area on Pivot 1b, the composites for Air and Surface LC/AO combined and Air and Surface Parcels combined were reversed between ICs and DCs.

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

Making these corrections results in differences only at the fifth decimal place for unit costs by country classification. By separate notice, a revised version of USPS-RM2010-12/NP1, correcting these errors and containing a revised Reports (Booked) file with pink-highlighted cells in rows 81-97, columns e and f, is filed today under seal.

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

7. [Proposal Seven] Please refer to Docket No. ACR2009, USPS-FY09-11 (Flats Cost Model) worksheet "STD\_Reg\_flts.xls" tab "CRA Flats." Several cost pools that are categorized as Piece Sorting, Unexpected, or Allied Support in the Flats Cost Model appear as fixed in worksheet "Prop.7.STD PARCEL-NFM MP MODEL.xls" tab "Cost Pool Data." Consequently, these cost pools do not receive proportional or piggyback (*i.e.*, fixed and proportional) treatment. For each cost pool that is not categorized as fixed in the Standard Mail Flats Cost Model, but would receive fixed treatment in Proposal Seven, please provide a rationale for the different treatment.

**RESPONSE:**

In Docket No. R2006-1, the Postal Service filed the First-Class Mail presort cards / letters and Standard Mail presort letters mail processing cost models in USPS-LR-L-48. The First-Class Mail presort flats, Periodicals flats, and Standard Mail presort flats mail processing cost models were filed in USPS-LR-L-43. The Parcel Post, Bound Printed Matter, and Media Mail / Library Mail mail processing cost models were filed in USPS-LR-L-46.

In the library references that supported the Opinion and Recommended Decision in that docket, the Commission instituted a new cost pool classification methodology for the letters and flats mail processing cost models filed in PRC-LR-12 (First-Class Mail), PRC-LR-14 (Periodicals), and PRC-LR-15 (Standard Mail). This methodology was proposed by intervening parties; it was not proposed or supported by the Postal Service. The Commission did not extend this new methodology to the parcel mail processing cost models contained in PRC-LR-16.

The Docket No. R2006-1 parcel cost pool classification methodology has been relied upon in the parcel mail processing cost models that were filed in the FY 2007, FY 2008,

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

and FY 2009 annual compliance reports (ACR). Given that the Proposal Seven mail processing cost model is a parcel cost model, the Docket No. R2006-1 (FY 2007, FY 2008 and FY 2009 ACR) parcel cost pool classifications were used, with the exception that the "SPBS OTH" and "SPBSPRIO" cost pools were reclassified as proportional, as described in Proposal Seven.

As implied in this question, the Standard Mail flats mail processing cost model was not the starting point that was used to develop the Standard Mail parcel / NFM mail processing cost model. Instead, the parcel cost models were used as the basis for developing the cost model in Proposal Seven, as the product in question consists of parcels, not flats. Given that the Proposal Seven cost model relies on the "Commission-approved" parcel cost pool classification methodology with the two modifications described above, the analysis discussed in this question has never been performed.

It is unknown why the Commission did not choose to apply its revised cost pool classification methodology to the parcel mail processing cost models in Docket No. R2006-1. It should be pointed out, however, that the parcel mail processing cost models differ from the letters and flats mail processing cost models (with the exception of the current version of the Periodicals mail processing cost model) in that the parcel mail processing cost models also explicitly estimate costs related to container movements and platform activities. Consequently, the cost pools that depict platform activities at processing and distribution centers, network distribution centers, and delivery units in the parcel mail processing cost models are all classified as proportional.

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

8. Proposal Eight would distribute empty equipment transportation costs using a new distribution key based on aggregate pound-miles. The Postal Service provided a table identifying the cost impact of this proposal. Please provide the pound-miles distribution key used to estimate the impact on product costs and its derivation.

**RESPONSE:**

The table below provides the requested information. The proposed (column 1) distribution key is derived using PQ4FY09 data sampled from Transportation Cost System (TRACS). The methodology used is identical to the one documented in USPS-FY09-36 except that the final distribution factors are based on pound-miles rather than their respective cost driver (e.g. pounds, cube, or cubic-foot miles). The final distribution factors incorporate data from all modes sampled by TRACS which includes the following contract types: Commercial Air, UPS, FedEx Day, FedEx Night, Intra-SCF, Inter-SCF, Intra-BMC, and Inter-BMC. The current distribution key (column 2) is derived using the established methodology. Column 3 computes the cost impact of the proposal by product.

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

<b>Product</b>	<b>Proposed PQ4FY09 Lb- Mile Distribution Key (1)</b>	<b>Current FY09 Distribution Key (2)</b>	<b>Cost Impact \$(000) (3)=((1)- (2))*95,909<sup>1</sup></b>
<b>First Class</b>			
Single-Piece Letters	7.287%	6.468%	\$785
Single-Piece Cards	0.086%	0.126%	\$(38)
Presort Letters	12.940%	10.398%	\$2,438
Presort Cards	0.268%	0.294%	\$(25)
Flats	7.946%	5.570%	\$2,279
Parcels	1.729%	3.387%	\$(1,590)
Outbound First Class Mail International	0.160%	1.058%	\$(861)
Inbound International Single-Piece Letter Post	0.387%	2.039%	\$(1,584)
<b>Standard Mail:</b>			
High Density and Saturation Letters	0.080%	0.071%	\$9
High Density and Saturation Flats and Parcels	0.962%	0.301%	\$634
Carrier Route	2.828%	1.190%	\$1,571
Letters	7.636%	3.567%	\$3,903
Flats	11.830%	4.008%	\$7,502
Not Flat-Machinables and Parcels	1.122%	1.421%	\$(287)
<b>Periodicals:</b>			
In County	0.000%	0.000%	\$0
Outside County	11.407%	4.757%	\$6,378
<b>Package Services:</b>			
Single-Piece Parcel Post	5.250%	5.966%	\$(687)
Inbound Surface Parcel Post (at UPU Rates)	0.109%	1.833%	\$(1,653)
Bound Printed Matter Flats	0.831%	0.325%	\$485
Bound Printed Matter Parcels	2.005%	0.940%	\$1,021
Media and Library Mail	7.175%	2.637%	\$4,352
<b>Free Mail – blind, handicapped &amp; servicemen</b>	0.182%	0.166%	\$15
<b>USPS Mail</b>	0.645%	0.884%	\$(229)
<b>Total Competitive Domestic</b>	16.201%	36.125%	\$(19,109)
<b>Total Competitive International</b>	0.931%	6.467%	\$(5,310)

<sup>1</sup>The total relevant empty equipment costs in FY09 are \$95.9 M. Source: USPS-FY09-32, workbook CS14, Tab '14.4, Cells V51+Z51

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

9. [Proposal Eight] The *Summary Description of USPS Development of Costs by Segments and Components, FY 2009*, filed with the Commission on July 1, 2010, indicates that the intra-Alaska and intra-Hawaii volume variable costs are distributed on the basis of pound-miles developed by special studies. Please compare and contrast the development of the intra-Alaska and intra-Hawaii pound-miles distribution key with that proposed for the distribution of empty equipment transportation costs.

**RESPONSE:**

The pound-miles distribution key that is proposed for empty equipment costs is derived by summing the pound miles (PM) by mode for product *i* across all sampled Transportation Costs System (TRACS) modes *j* and dividing by total TRACS pound miles for all products. The exact formula for the proposed distribution key (DK) for product *i* is the following:

$$DK_i = \frac{\sum_{j=1}^8 PM_{ij}}{\sum_{j=1}^8 PM_j}$$

The TRACS modes *j* include four air modes, Commercial Air, United Parcel Service, FedEx Day, and FedEx Night and four highway modes, Intra-SCF, Inter-SCF, Intra-BMC, and Inter-BMC. The estimation methodology for air (control totals known) and highway modes (control totals not known) are different and are explained in detail in USPS-FY09-36 pages 4-17 (highway) and pages 18-29 (air). The methodology used for this proposal is identical to the one documented in USPS-FY09-36 except that the final distribution factors are based on pound-miles rather than their respective cost driver (e.g. pounds, cube, or cubic foot miles). The estimation methodology used to derive the distribution keys for the

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

intra-Alaska and intra-Hawaii special studies submitted as part of Docket No MC97-2 (typographical error in Summary Description) is the same as is currently used for TRACS air modes – a separate ratio estimator with known control totals.

## **CERTIFICATE OF SERVICE**

I hereby certify that I have this date served the foregoing document in accordance with Section 12 of the Rules of Practice and Procedure.

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Eric P. Koetting

475 L'Enfant Plaza West, S.W.  
Washington, D.C. 20260-1137  
(202) 268-2992, FAX: -5402  
October 25, 2010