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Consideration of Technical Methods To Be Applied in Workshare Discount Design	: : :	Docket RM2010-13

INITIAL COMMENTS OF GREETING CARD ASSOCIATION

The Greeting Card Association (GCA) submits these Comments pursuant to Order No. 537 (September 14, 2010). They are directed, in accordance with the Commission's invitation, to the choice of a new benchmark for the calculation of worksharing rates in First Class. GCA believes, however, that this proceeding and its predecessor (Docket RM2009-3) have revealed the need for substantial rethinking of the way in which these worksharing rates are developed.[1] In addition to suggesting a new benchmark, therefore, we offer a number of comments on other aspects of ratemaking for First Class.

Accordingly, Part I summarizes GCA's overall position; Part II summarizes descriptively all the issues we discuss, arranged under several headings. Part III discusses standards by which a benchmark should be chosen. In Part IV we analyze and make recommendations concerning the benchmark question proper. Part V discusses new ratemaking issues entailed by the Commission's expansion of the definition of "worksharing" in Docket No. RM2009-3 – in particular, the importance of inquiring whether, and how far, these new worksharing activities require discount treatment. In Part VI we address other ratemaking problems, relating to the cost pools and the cost modeling techniques involved in

[1] Consequently, some parts of these Comments are, as a practical matter, addressed to the Postal Service as well as to the Commission.

constructing First-Class Mail rates. Part VII discusses other issues concerning costs avoided, and Part VIII briefly summarizes our main conclusions.

I. SUMMARY OF GCA POSITION IN LIGHT OF COMMISSION GOALS IN THIS CASE

A weighted "average" cost of traditional metered, and IBI letters would provide the best benchmark and in fact IBI constitutes most of the MODS cost pool data labeled "metered" in the 2010ACR data submitted by the Postal Service. Although the history of IBI mail is not very long, clearly it seems to be the major non-stamp indicia for single piece letters for the foreseeable future that holds out the possibility for conversion to workshared mail.

While the Postal Service's response on January 18, 2011 to the Chairman's Information Request No. 1 leads to a similar conclusion by default because of data limitations in the measurement of IBI, metered, and BMM, we argue that even if separate cost data were available in response to the Chairman's request, the same choice of a benchmark going forward would be made.

The Commission's broadening of the definition of worksharing in RM2009-3 does not necessarily comport with its ECPR standard for setting discounts, and much of that broadening consists of the Postal Service quality standards for the work performed by the mailer, not the nature of the work itself.[2]

[2] The Commission took care to specify that address hygiene and density would be considered part of worksharing *insofar as they are required by Postal Service eligibility rules.* See Order No. 536, pp. 43 et seq. This fact carries with it the necessity to recognize that "non-traditional" worksharing activities not required by eligibility rules (and thus not incorporated in the definition of worksharing) are not automatically entitled to a price incentive; this question must be decided on the specific facts. The distinction between Postal Service-mandated activity and such activity in general is therefore important in setting Presort rates, and will be discussed below (Part V; see especially fn. 17 and subparts B. and C.).

As the Commission notes on page 19 of Order No. 536, setting costs avoided requires "two reference points," the single piece benchmark and the initial presort tier to be compared with it. Direct costing of mail processing for a 5 Digit automation letter is preferable in our view to the use of mixed AADC residual mail for measuring costs avoided relative to the benchmark. "Tinkering" with the CRA-based proportional adjustment factor by de-averaging it or by arguing that almost all cost pools are pretty much all worksharing-related proportional does not solve the fundamental problem with the cost models, namely that (as of the 2010 ACR) they do not explain 40 percent of actual CRA mail processing costs. In particular creating two such problematic proportional adjustment figures out of one problematic one is not a material improvement in the cost models.

II. A SUMMARY OF ALL THE ISSUES

While the primary purpose of this proceeding is to accomplish what Order No. 536 in RM2009-3 did not, namely choosing a benchmark from which to calculate avoided costs for First Class workshared mail, there are several other issues related to defining and measuring costs avoided for which the Commission has asked for comments.

The benchmark issue relates to the Commission's finding in Order No. 536 that First Class single piece mail that is metered or bears information based indicia (IBI) is a conversion candidate to worksharing. Together, for FY2010 in the RPW data, metered and IBI letters constitute about 36 percent of all single piece letters. In GCA's view, the choice of a benchmark depends critically on what the Commission has defined as conversion mail.

A. Benchmark Issues

1. Benchmark options: (a) BMM; (b) metered mail; (c) white mail; (d) IBI mail; (e) a weighted average of BMM and IBI mail; (f) qualified PC postage mail; (g) average total single piece letters; (h) some other subset of single piece mail.

2. Specific cost characteristics that the selected benchmark should have.

3. De-averaging rates for FCM by indicia.

4. Using two benchmarks with BMM being the lower bound and average single piece the upper bound.

B. Broadening the definition of costs avoided

In Order No. 536, the Commission added address hygiene and density, insofar as required by Postal Service eligibility rules, to the established definition of worksharing. It also indicated that in the present docket collection costs would be considered as a category of costs avoided.[3] Collection costs, at first glance, would appear to be a problematic candidate for a category of avoided costs once the Bulk Metered Mail (BMM) benchmark – which presupposes entry of trayed mail at a Postal Service facility – is being discarded. The proposition that collection costs might still qualify as costs avoided seems to rest on the assertion that mail targeted by presort bureaus is, or at least includes, mail which the Postal Service would otherwise collect. Whether this is true (and if so, how far it is true) is an important factual issue of the kind we discuss in Part III of these Comments.

By adding required address hygiene and density to the definition of the relevant worksharing activities, the Commission has implicitly raised other issues,

[3] See particularly Order No. 536, p. 63, and fn. 46.

particularly as regards (i) the changed rule of Efficient Component Pricing in First-Class Mail ratemaking, and (ii) the proper rate treatment, if any, of address hygiene and density beyond those required by Postal Service regulations. We discuss these issues in Part V.

C. Cost Model and MODS Cost Pool Issues

1. Revisions to Postal Service models of cost avoidance by rate category; choice of worksharing reference point to be compared with the benchmark.

2. Pendulum swings in the way some cost pools in the MODS data base are classified: worksharing related proportional; worksharing related fixed; non-worksharing related.

3. More general re-evaluation and modification of cost pools back to the R2005-1 methodology.

4. Use of two rather than a single proportional CRA based adjustment factor for cost models.

D. Other Issues with Costs Avoided

1. The way delivery costs and “other costs” are estimated in calculating costs avoided.

2. Establishing a discount for single piece mail (PC postage) that is CASS-certified and bears an IMb.

III. STANDARDS FOR CHOOSING A BENCHMARK

Order No. 536 contains a number of general indications as to how (by what standard) the Commission expects to go about selecting a benchmark for First-Class Letters. Before we discuss the characteristics such a benchmark should have and consider various candidates for that role, some observations on these general indications are in order.

Indications from Order No. 536. Two concepts appear to weigh heavily in the inquiry as Order No. 536 describes it: incentive, and commonality of demand characteristics. At page 21, for example, the Commission states that

> A factual inquiry is required to identify an appropriate base group. The purpose of the inquiry is to determine what mail shares the cost and demand characteristics of the workshared group, and therefore, is likely to convert if a large enough discount is offered.

This approach is amplified at page 49:

> For ECP logic to apply, however, the categories of mail whose rates should be set with reference to each other must be in the same market so that the price of postage is the most important factor in the mailer's decision to use one category or the other. If non-price considerations dominate the mailer's decision to choose one category of mail over the other, even a discount that is equal to the difference in cost will not incentivize efficient behavior by mailers. If categories of mail are in different markets, their rates need to reflect those different market conditions if they are to be economically efficient.

The Commission cites some academic studies which indicate at least some single piece mail is in the same market as Presort, in light of the respective own price elasticities for the two groups of mail.[4] In particular, the Commission concludes that these studies, along with other work, cannot establish that year to

[4] Order No. 536, p. 13, including footnote 6.

year Presort price elasticities are higher than those for single piece. This may be true in some years, but the opposite is true in others.

The Commission goes on to explain that the existence in Single-Piece of a large quantity of "white mail," and its similarity to Presort in economic purpose and functionality, shows that Presort and "a substantial minority of Single-Piece First-Class Mail" are in a worksharing relationship. Thus there is "market overlap between single-piece and presort First-Class Mail."[5]

This market overlap forms a substantial part of the basis for the Commission's finding that an important grouping of Single-Piece mail stands in a worksharing relationship with Presort. Order No. 536 appears to conclude that if this grouping can be delineated – that is, if we can mark off all the Single-Piece mail that "shares the cost and demand characteristics" of Presort – it follows that we have *eo ipso* identified all the mail that is "likely to convert."[6]

The practical possibility of conversion must be considered. While it may be relatively straightforward to model the structure of the "overlapping market" on the basis of entire categories of mail, actual conversion to Presort necessarily involves individual mailers and mailings. Thus in addition to (average) costs and "economic purpose and functionality" the practical possibility of conversion also must be considered. One prominent factor is the availability of (third-party) consolidation for mailings that share the physical and cost characteristics and the economic purpose of Presort but are too small to qualify. How far such consolidation is available, for what size mailings, and at what cost per piece are all factors that would influence the extent to which a benchmark and a discount structure based on relatively broad considerations of economic purpose and on

[5] Order No. 536, p. 54.

[6] "All" in this context does not, of course, mean "every piece." Presumably even within the benchmark group there will be some mailers, or mailings, for which a discount constructed on the usual cost-avoided model will prove inadequate to motivate conversion.

per-piece cost estimates would actually bring about conversion of the targeted pieces.

Impracticability of considering incentive alone. This seems clear especially if we consider the consequences of focusing exclusively on the presence of an incentive to shift.[7] Order No. 536 seems to envision a spectrum of fairly readily definable subgroups of Single-Piece mail, with potentially differing responses to a given change in the worksharing discount(s). Reduced to its thinnest possible meaning, "incentive" in this context would signify nothing but an economic reason to shift from a higher- to a lower-priced category of service. On that basis, however, it could be argued that *any* subgroup in Single-Piece[8] would have such an incentive. As a standard for choosing a benchmark, therefore, simple presence of an economic incentive, ignoring other considerations, is not helpful. For if (i) the response of any given subgroup depends on the size of the discount, and (ii) the size of the discount (dictated by the characteristics of the benchmark) depends on which subgroups would be likely to convert (and thus be available as possible benchmarks[9]), the price-setter's task would become insolubly circular. Accordingly, some additional considerations must be incorporated, along with economic incentive, in the process of choosing a benchmark.

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[7] One observation in Order No. 536 could be construed as doing this. At p. 8 the Commission says,

> If they serve the same market, the selection of an appropriate benchmark depends on what types of mail within the base group would have incentive to shift to the workshared group in response to changes in their relative prices.

We read the Order in its entirety as not taking such a restricted view.

[8] This is the case even if we restrict “Single-Piece” to that segment which shares a market with Presort.

[9] Perhaps more exactly, which subgroup would be the "marginal" one, i.e., the subgroup with the smallest benefit to itself from shifting at a given level of discount. The discussion at p. 14 of Order No. 536 seems to suggest that the Commission's target is such a marginal subgroup. Selection of an "inframarginal" subgroup (i.e., one whose benefit from shifting to Presort would be greater than that of some other subgroup not chosen as the benchmark) would result in an incentive larger than necessary to elicit worksharing behavior by the latter subgroup, and thus, to that extent, inefficient.

Choosing a benchmark to achieve efficient and lawful results. The notion of "having an incentive," should thus be taken in the real-world sense of "having a practical reason, based on relative prices, to shift to Presort, with due regard paid to the availability and cost of any changes or additional (third-party) services needed to effect the shift." What these changes or additional services are, at any one time, is a factual inquiry. We believe that selection of a benchmark depends on its outcome.

Subtypes of Single-Piece for which there is no realistic possibility of adaptation to the requirements of Presort should not be considered to "have an incentive" to shift, and so should not be thought of as potential benchmarks.

Given this limitation of the field of possible benchmarks, selection of the subgroup which has the best case for being considered the marginal one[10] would have a better chance of producing the efficiency which the Commission seeks. The Commission would avoid the error of choosing a subgroup which exhibits high intrinsic costs relative to Presort, but also has no practical possibility of conversion.

A benchmark corresponding to such an unrealistically-chosen subgroup would entail a large discount, but one which few if any mailers in the subgroup could use. Other mailers, including all those for whom a smaller discount would suffice to motivate conversion, would receive a windfall; the resulting revenue loss would have to be made up by other mailers. Moreover, the discounts set using the benchmark are meant to equal avoided cost. If they are set at a level at which the assumed cost avoidance is purely theoretical – that is, if they

[10] The marginal pieces of Single-Piece conversion mail today appear to be the general office mail that the Postal Service refers to as "white mail". The practical difficulty in, or opportunity for, converting such mail depends on its collection costs for Presort bureaus. One stop in a tall urban center office building, which can collect 1,000 pieces of white mail at once from 50 businesses, is a more likely candidate for conversion than making 50 stops at 50 different locations to assemble the same 1,000 pieces.

assume conversion of mail which will never actually convert – they will exceed avoided cost.

This would raise substantial questions of their lawfulness under 39 U.S.C. § 3622(e)(2), which provides only limited exceptions[11] to the rule that workshare discounts may not exceed cost avoided.

IV. BENCHMARK ISSUES

1. Choice of Benchmarks

Bulk metered mail (BMM) is the current benchmark, and is now viewed by many or most observers as being obsolete. This is mail that is properly faced with a meter strip and placed in Postal Service trays at volumes that qualify it for worksharing discounts. As distinguished from white mail, BMM is a mailstream that over the decades of automated processing has most likely already been converted to automation presort mail by Presort Bureaus. For this reason alone it is no longer a good benchmark. There are other reasons, notably the questionable practice of using delivery costs of non-automation presort mail as a proxy for the delivery costs of BMM, which are not measured directly.

In the pre-PAEA Postal Service MODS data base of mail processing cost pools, the worksheets showed only one cost pool, (1CANCMPP), that was different between single piece metered mail and BMM. This amounted to only three tenths of a cent in Docket R2000-1. (See Docket R2000-1, USPS LR-I-81.) In the 2010 ACR data submitted by the Postal Service it appears that the costs of BMM and metered mail generally, or single piece metered, are the same. (See Docket RM2010-13, Response of the United States Postal Service to Chairman's Information Request No. 1, p. 3.) This change in MODS costing appears to pave

[11] None of which is plainly applicable here.

the way for a new benchmark that will in fact be a few tenths of a cent higher than BMM was by simply sweeping the cost difference between the two under the rug.

"White mail" is defined by the Postal Service as general office mail that has uniform envelope size, bears machine generated addresses with a meter strip, and has been targeted by Presort Bureaus for conversion. Density also appears to be a factor delineating "white mail" from metered mail generally. Practically speaking it is hard to distinguish between such white mail and metered mail generally. Hypothetically, white mail could be considered that subset of all metered mail, including IBI-metered mail, that is the easiest to convert and that is at the top of consolidators' ongoing plans for conversion. In Postal Service cost data, the mail processing costs of white mail appear identical to metered mail; and what is labeled in the MODS costs as metered costs are mostly costs of IBI mail, not metered mail per se. (See Docket RM2010-13, Response of the United States Postal Service to Chairman's Information Request No. 1., p. 6.)

PC postage is another benchmark possibility noted by the PRC, yet the Chairman's Information Request No. 1 in RM2010-13 does not ask for its cost. PC postage is left in an ambiguous position as a benchmark if it is also a candidate for a discount.[12] While not all discounts are due to worksharing, the one proposed for PC postage by Stamps.Com among other parties, and discussed by the Commission in Order No. 536, clearly is. (See Order No. 536, p. 10.) In fact the Commission explicitly notes the dilemma without viewing it as such, and concludes: "Under that circumstance, rates for automation presort letters would not be directly tied to the undiscounted Single-Piece First- Class Mail rate." (Order No. 536, p. 64.) On the one hand, such a circumstance comes dangerously close, in GCA's view, to introducing "delinking" through the back door, a concept the Commission firmly rejected in this order, albeit with respect

[12] Such a discount has been proposed by Stamps.com; see Order No. 536, pp. 9, 64.

to all differences in attributed costs between single piece and workshared, not just mail processing cost differences. On the other hand, a PC Postage benchmark could negate or more than offset raising benchmark costs by three tenths of a cent by basing it on metered mail generally rather than BMM.

An average of all single piece letters is not a viable benchmark because most of this mail is not a good candidate for conversion, as shown in Table One below. In a related vein, the Postal Service has pointed out that only in Cost Segment 6 in-office delivery costs of the CRA is there a "measured difference between the costs of the average single-piece letter and the cost of the "Metered" letter." Notably, that cost is lower for average single piece (3.3 cents) than it is for metered (3.6 cents). (RM2010-13, Response to ChIR No. 1, p. 9.) One could make an argument that this counter-intuitive result would allow for a 0.3 cent downward adjustment in the cost of metered mail as a new benchmark, a result which would change the benchmark without raising its cost.

Table One
Single-Piece Letters by Indicia
FY 2010

Indicia Type	Pieces	Percent of Total
Permit Imprint	1,903,848,826	7.01%
Metered	766,166,913	2.82%
Stamped	15,334,388,340	56.48%
PVI	101,709,507	0.37%
IBI	9,000,498,767	33.15%
Other	41,305,940	0.15%
Total	**27,147,918,293**	

Source: RPW Report - First Class and Standard Mail by Indicia FY 2010

In summary, quite apart from the data limitations noted by the Postal Service in response to ChIR No. 1 there appear to be far fewer benchmarks that are discrete and separable than the list of possibilities noted by the Commission in Order No. 537 establishing this docket. BMM and metered mail are now claimed to have identical cost pools. Metered mail and white mail are virtually indistinguishable from a cost standpoint, but the latter may be the "easiest" metered mail to convert. Logically, PC Postage per se cannot both be a Single-Piece benchmark and a rate category with a worksharing related discount. The average of all single piece mail cannot be a benchmark because it includes a substantial volume of mail, 56 percent of all Single-Piece, that is not conversion mail, at least with current consolidators' goals and capabilities.

Because metered mail volumes have declined substantially over recent years while IBI-metered postage has grown, IBI appears to be the best single benchmark for the foreseeable future, and its costs are identical in Postal Service data to that for metered letter mail. In GCA's view, whether adopted as a benchmark or not, MODS cost data should be labeled "IBI" in place of the word "metered" starting with the 2011ACR.

2. Specific cost characteristics that a single piece benchmark and prebarcoded reference point should have

The two reference points for measuring costs avoided should be stable parts of the First Class mailstream for the foreseeable future. As a benchmark, the large volume of IBI mail and its continued growth as a percentage of all Single-Piece make it a good candidate. By contrast, the continued reduction in metered mail volume make it a less suitable benchmark. Consequently, looking to the future, it is also questionable whether metered white mail would make a good benchmark, or even part of a weighted average benchmark assuming there

were separate costs for the two indicia. What about the workshared reference point?

MAADC letters constitute a very small percentage of all automation letters. Presort bureaus view MAADC and AADC as “residual mail,” that is, mail that cannot be presorted to a 3 Digit or 5 Digit level. Mailers have a strong financial incentive to minimize the amount of such residual mail in their daily sort schemes, and have progressively succeeded in doing so. As a result, it is questionable whether MAADC (or AADC) mail has sufficient volume and stability to be the reference point for measuring costs avoided for the future.

In addition, before the increasing use of DPS percentages to help estimate in-office delivery costs, the delivery costs associated with MAADC were based on a very small fraction of non-automation presort mail, namely machinable non-automation presort. Machinable non-auto presort has also been a delivery cost proxy used for BMM, and in R2006-1 was only 52 percent of the in-office delivery costs for single piece mail. (See R2006-1, USPS T-22.) By the time barcoded and sorted metered and single piece mail reach a carrier in the office, the in-office delivery costs cannot possibly exhibit a variance between BMM and single piece that is this wide. Either the calculation for single piece was too high, or the proxy for BMM was too low.

The overwhelming percentage of Automation Presort Letters is either 5 Digit prebarcoded or 3 Digit prebarcoded mail. Conversion mail is clearly not converted to mixed AADC or AADC mail, but to 3 Digit or 5 Digit mail, other than the small amount of residuals which that evening's sort scheme result in. Almost all costs that mailers and consolidators actually avoid for the Postal Service are associated with presorting automation letters to three or five digits.

Second, the single piece benchmark and worksharing reference point chosen by the Commission in this docket for measuring costs avoided should

have enough of a history to validate that the ongoing measurement of costs makes sense in light of past cost patterns. In terms of a single piece benchmark, metered mail achieves this cost characteristic better than any other single piece benchmark that can constitute potential conversion mail. As a practical matter most of the mail being costed as metered is in fact IBI-metered mail. For this reason, there seems little loss of continuity in moving from a BMM benchmark to an IBI benchmark.

In terms of a worksharing reference point used to calculate costs avoided from the new benchmark, the 5 Digit presort letter certainly has a sufficient cost history to validate ongoing measurements in the future, with one caveat. The estimated cost of processing a 5 Digit mailpiece through the Postal Service network has been based on cost models and not direct cost measurement since MC95-1. The success of these cost models in accounting for all CRA direct mail processing costs of Presort rate categories since they were first introduced in MC95-1 has been dubious at best. Whether a direct measurement of 5 Digit presort letter mail processing costs would validate or invalidate the measurements of the cost models historically is an open question, but any material difference could be gradually factored into annual compliance review data rather than changed all at once.

A *third* cost characteristic that a benchmark and an automation presort reference point used for calculating costs avoided should have is a minimal use of cost proxies and associated anomalies such as insufficient or impure IOCS sample sizes and bizarre cost avoided calculations. The problematic history of using fractional breakdowns of non-automation presort delivery costs in connection with costs avoided estimates illustrates the cost characteristics that

neither a benchmark nor a worksharing reference point used for calculating costs avoided should ever have.[13]

A *fourth* and final cost characteristic that the benchmark and the base tier automation rate absolutely must have in light of the problematic history of Postal Service cost models is a reliance on directly measured costs to help improve the accuracy of cost models. PAEA's mandated annual review of presort discounts in light of costs avoided should have before now led to a thorough review and substantial overhauling of the cost models.

Five Digit may be the best worksharing reference point to use for measuring costs avoided from the single piece benchmark. The full-service intelligent mail barcode IMb will enable the Postal Service to identify exactly what mail going through its network is entered as 5 Digit (or 3 Digit) mail. Such direct costing would be preferable to the use of cost modeling for 5 Digit (and/or 3 Digit) mail. Other automation rates could be estimated from a 5 Digit reference point as

[13] In the R2000-1 rate case, the Postal Service estimated that costs avoided for non-automation presort letters was negative. (See USPS-T-21, Tables 1 and 2, USPS-LR-K-48 and LR-K-110.) In R2005-1, a Postal Service witness indicated that the negative anomaly in R2000-1 may have been due to certain automation mail being mixed in with the IOCS tallies for non-automation presort. Other problems existed with the estimation of delivery costs for non-auto presort. These were used to estimate in office delivery costs for metered mail, but the variance between the 4.044 cents and the 7.78 cents for single piece was not plausible. The source of this anomaly may have been the much larger sample sizes in the IOCS used for single piece than those for the machinable non auto presort delivery cost proxy used for metered mail and the BMM benchmark.

These problems were "solved" in R2005-1 and R2006-1 by abandoning direct cost measurement of non-auto presort letters in favor of using a modeled cost approach. (See R2006-1, USPS-T22, p. 6, line 2.) However, this approach solved one set of problems while creating arguably worse ones in measuring costs of mail processing and in-office delivery for non auto presort letters. A 32.3% drop in non-auto presort unit delivery costs in TY 2008 due to an unexplained 21.9% drop in "direct casing" costs led to yet another data anomaly. Using non-auto presort delivery costs as a proxy for metered letters and BMM created a negative cost avoidance for unit delivery costs for MAADC mail. Non-automation machinable delivery costs for MAADC and AADC letters were lower than their prebarcoded counterparts, 4.040 cents for the former and 4.182 cents for the latter. (See R2006-1, Transcript 3368 (response of Postal Service witness Kelley to MMA/USPS-T30-17.d).

easily as from an MAADC reference point by adding back rather than subtracting cost elements due to lower levels of presortation.

2. De-averaging rates for FCM by indicia and other criteria

One notion of de-averaging has stressed the high cost of selling single piece stamps at brick and mortar retail post offices. A "universal" workshare discount would be available for small volumes of single piece mail so long as the postage evidencing did not take the form of stamps purchased at Postal Service windows.[14] Such a discount would encourage the purchase of stamps at retailers ranging from grocery stores to Wal-Marts. The discount would only be offered at such alternative sites to post offices, and all stamps sold at these sites would receive the discount.

If this is what is meant by "de-averaging," then GCA could support it. Such a discount would increase efficiency within the Postal Service by shifting the purchase of stamps away from expensive Postal Service brick and mortar sites, which ideally would allow for the closing or consolidation of thousands of post offices. GCA does feel that the value of other services at post offices warrants keeping a sufficient number open so that those services could continue, and that raising revenue at Postal Service retail facilities from non-postal sources such as retail banking is a non-mutually exclusive alternative to making them profitable by cutting window costs.

"De-averaging" has other meanings in proposals that GCA could not accept and that we think are, arguably, unlawful as well as bad public policy. For example, in its initial comments in RM2009-3 Pitney Bowes, Inc. has suggested

[14] See, for example, Docket No. R2006-1, Direct Testimony of Lawrence G. Buc on Behalf of Pitney Bowes, Inc., REVISED, November 6, 2006.

splitting First Class single piece into various and sundry “homogeneous” categories priced at the cost of each category.[15] They contemplate a green rate, a security rate, a clean mail rate, a higher value for small business rate, etc. Section 3622 (c)(6) of PAEA makes “simplicity” of rate structure and "simple, identifiable" relationships between rates a factor to be considered, and we would argue this is especially true with postage that citizen mailers typically purchase and use.

De-averaging the First Class single piece rate by indicia is yet a third distinct notion. Unfortunately, as the Postal Service has stated in its response to ChIR No. 1, its current data bases do not permit a breakdown of costs between metered, IBI-metered, or white mail. Its argument is that in any event, the costs for these three indicia are very likely the same, and all are measured by costs for metered letters. The only actual de-averaging the Postal Service could submit to the Commission was between metered costs and all single piece letters on average.

3. Using Two Benchmarks

This notion was put forward by Pitney Bowes, Inc. in RM2009-3. (Initial Comments of Pitney Bowes, Inc., pp. 8-10.) It held that no single benchmark could be used to adequately measure costs avoided. It proposed that two benchmarks be created, and the one adopted in any period for costs avoided be between a BMM minimum and an average total single piece cost maximum. GCA opposes this proposal for a benchmark for the following reasons.

As many mailers and the Postal Service have pointed out, most single piece mail today is not a good candidate for conversion yet those pieces,

[15] RM2009-3, Initial Comments of Pitney Bowes, Inc., pp. 5-6.

including stamped mail constituting 56 percent of all single piece indicia by volume, would be included in calculating PB's maximum benchmark. Clearly, by definition a benchmark can only include the costs of conversion mail. Furthermore, the benchmark range proposal seems a bit transparent in creating a benchmark that would by design be higher than BMM, the current benchmark. When any mid-range estimate between the minimum and maximum benchmark was adopted, as it would almost always be by framing the issue in this way, costs avoided would appear higher than they did using a BMM benchmark.

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V. FUTURE RATEMAKING PROBLEMS ASSOCIATED WITH BROADENING THE DEFINITION OF WHAT MAILER ACTIVITIES CONSTITUTE "WORKSHARING"

While the Commission aims, in the present Docket, to establish a new benchmark for First-Class Letter mail, its adoption in Docket RM2009-3 of a broadened definition of worksharing raises important additional questions which will have to be answered in the course of constructing discounts under the new rule. Although in past proceedings GCA has opposed broadening the definition[16], we are concerned here only to show that under the new definition the Postal Service and the Commission will face novel ratemaking issues that in the past have not often had to be addressed.

More specifically: the Commission has significantly expanded "worksharing" beyond the area in which the Efficient Component Pricing Rule (ECPR) can both imply that discounts are appropriate in the circumstances and dictate their proper level. Consequently, the mere inclusion of a mailer activity

[16] See Docket No. R1006-1, Initial Post-Hearing Brief of the Greeting Card Association, pp. 10-18. Broadening the definition also raises problems concerning the Postal Service's ability to refine eligibility requirements and economize on facilities for entering mail into the system; see, e.g., Docket ACR2010, Comments of the National Postal Policy Council on Annual Compliance Review, pp. 6-10, and Reply Comments of the Greeting Card Association.

under the "worksharing" rubric no longer implies the need for a price incentive. Each such instance must be evaluated on its own footing. In each case, the Postal Service and the Commission need to ask whether, and how far, a mailer activity newly included as "worksharing" should be the subject of a discount at all. It would be easy, but incorrect, to assume that all such activities newly included should receive a discount simply because they are now designated as "worksharing."[17] It is this misleading assumption which we analyze below.

A. Effects of reliance on the Efficient Component Pricing Rule

How ECPR has been used and what it assumes. At least since Docket MC95-1, the Commission has relied on the Efficient Component Pricing Rule (ECPR). While it has not been applied mechanically, it has been generally used and forms part of the basis of the Commission's repeated rejection of delinking in First-Class Letters.[18] One effect of reliance on ECPR, however, has been to

[17] That notion might be suggested by a superficial reading of the Commission's statement in Order No. 536 that

> . . . If the Postal Service requires that mail with one of the four specified workshare traits [i.e., mailer-supplied sorting, barcoding, handling, or transportation] also have an associated worksharing performed before it is submitted, and the presence of the associated worksharing substantially increases the amount of Postal Service costs that the specified trait avoids, the associated trait should be viewed as integral, and thereby ancillary to the named trait for purposes of section 3622(e).

Docket No. RM2009-3, Order No. 536, p. 43. But the key to rational application of this idea is, as the Commission observed, the presence of a Postal Service *requirement* that the associated step be taken. Such a requirement takes the question out, or part way out, of the sphere of incentive pricing; it amounts, instead, to a partial definition of the strict worksharing trait which the Commission may adopt through its § 3622(e) rulemaking power. (Indeed, it seems that if the associated trait is really to be "integral" to the strict worksharing trait, the Commission – which has the statutory authority to define the latter – *must* concur in the addition of the associated trait to the definition.) In the case of potentially cost-reducing ancillary activities which are not also eligibility requirements, it is thus still an open question whether a price incentive is appropriate and, if so, how it should be constructed.

[18] PRC Op. R2006-1, ¶¶ 5064-5090; Docket No. ACR2009, Annual Compliance Determination, pp. 69 et seq.; see also Docket No. RM2009-3, Order No. 536, pp. 51-54.

obscure the question whether any given mailer activity[19] requires a price incentive.

This comes about because ECPR assumes that the mailer activity to which the discount attaches displaces a corresponding activity performed by the Postal Service.[20] The correct price for the non-monopoly subservice, under ECPR, is its average incremental cost (AIC) as performed by the carrier. If the mailer's AIC to perform the subservice is lower than the Postal Service's, a discount set equal to the Service's AIC provides a positive margin for the customer, leading it to take over provision of the subservice. If it is higher, the margin would be negative and the customer will leave the work to be performed by the Postal Service. ECPR, in other words, seeks to bring it about that the Postal Service is indifferent as to whether it or the customer provides the subservice, so that it is always provided by the lower-cost candidate.

All of this rests on the (presumed) fact that a discrete activity[21] which would be performed by the Postal Service is, under appropriate conditions, allocated by the price mechanism to the mailer instead. For ECPR to work at all, the activity must be one which, absent worksharing arrangements, the Postal Service would perform.[22] If it is not one the Service would perform, the Service would expend no resources on it and it would have no AIC. Without such an AIC, there is nothing with which to compare the mailer's cost to perform the activity, and so no basis for setting a discount.

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[19] "Mailer activity" includes activities performed by an intermediary such as a presort bureau.

[20] Or, in more technically precise language: that a non-monopoly subservice such as sorting or barcoding is being performed by the customer rather than the carrier (which is assumed to have a monopoly over at least one other subservice – in this case, delivery). The thought is sometimes expressed by saying that the subservice to which ECPR applies is one in which the Postal Service and the mailer compete.

[21] Strictly, we should perhaps speak of "achieving results" rather than "performing activities," since the techniques by which, e.g., the mailer applies barcodes are different from those the Postal Service would use. GCA believes that the difference in technique should not matter.

[22] This issue arose in Docket No. R2006-1; see discussion in Initial Post-Hearing Brief of the Greeting Card Association, pp. 14-18.

In short, *in the ECPR view of the world,* the price-setter can achieve efficient results by (i) recognizing all and only those types of worksharing which displace performance by the carrier of a corresponding costly activity, and (ii) awarding all and only those types of worksharing a discount equal to the carrier's AIC.[23] The price incentive is a necessary effect of the allocation of tasks between the Service and the mailer, and its magnitude follows from the recognition that efficient work allocation is maximized by setting the discount equal to the Service's AIC. But – also in the strict ECPR view – there can be no price incentive for the mailer to perform an activity which does not *eo ipso* relieve the Postal Service of the need to perform a corresponding activity. And this is true even if it can be shown that the activity in question really does – in some other way – lower the overall cost of the mail in question.

Broadly defined worksharing creates situations in which ECPR cannot work. Now that the Commission has adopted a broader definition of worksharing, not limited to activities which displace a corresponding activity on the Postal Service's part, the question whether a particular mailer activity should receive discount treatment will have to be addressed on its own.[24] It is no longer answered, more or less automatically, by ECPR. The Commission, as noted in fn. 17 above, has expressed one important, and necessary, limitation on this broadening: that the activities newly labeled as worksharing must be required by the Postal Service on the ground that they enable or preserve the value of the traditional worksharing features.

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[23] One might say that ECPR functions, essentially, by allocating *work* rather than by allocating *savings.*

[24] We should note that in what follows we simplify the discussion by speaking of a discount "for" certain features not included in the traditional definition of worksharing. This does not necessarily imply a separate or explicit discount for such features; it also covers the situation in which a workshared category's discount price is constructed so as to include a component corresponding to the additional feature. The problems facing the Postal Service and the Commission are the same in either case.

B. Cost-reducing mailer activity with no Postal Service counterpart

One immediately apparent question is how to treat mailer activity which does not displace a corresponding Postal Service activity, but is capable of displacing some *different* Postal Service activity having an identifiable cost. A concrete example is the frequent claim that application of address hygiene techniques to bulk mailings should be recognized with a discount because it reduces the incidence of undeliverable-as-addressed (UAA) pieces.[25] In First Class, such pieces are entitled to (costly) forwarding or return service. To the extent that address cleansing reduces the percentage of such pieces, the Service obtains an overall saving. A specific level of address quality is required by Postal Service eligibility rules[26] and so has been attached to the definition of pre-barcoding. The question is whether address cleansing beyond that so required should be recognized in pricing.

ECPR cannot be used to ground a discount in this situation. First, the cost saved by the mailer activity is not one which the Postal Service would incur but for the mailer's undertaking it. The Postal Service does not maintain mailers' lists or apply the addresses to their mailpieces. There is, therefore, no Postal Service AIC to serve as one term of the ECPR comparison. Second, the theory of ECPR seems to assume that the activity being allocated between carrier and customer on the basis of comparative AIC will be performed on every piece.[27] But even a minimally-maintained list will presumably contain mostly correct addresses. Consequently, only a fraction of any mailing would require forwarding or return. A hypothetical per-piece discount equal to the average cost of forwarding (or return) would clearly be excessive. It might be thought that a discount pegged at

[25] Accepted by the Commission insofar as it is a Postal Service requirement. Docket No. RM2009-3, Order No. 536, pp. 8, 13, 48-49.

[26] See DMM 233, §§ 3.5, 3.6

[27] This is perhaps especially clear if we think of the price of a workshared piece as an access price, charged for using the Postal Service's (monopoly) delivery function. Clearly, each piece must pay that access price.

the average unit cost of forwarding (or return) actually observed for the workshared category, which would recognize that not every piece requires one of those extra services, would solve the problem. This arrangement, however, would have the odd property that insofar as the discount elicited more address-cleansing by mailers, it would tend to shrink. More address-cleansing would lead to fewer UAA pieces, which would in turn reduce the category-wide average cost of forwarding or return. This makes obvious the difference between this situation and an ordinary ECPR-based discount, where an increase in the prevalence of the worksharing activity produces a greater overall saving and, at least in principle, does not reduce the per-piece saving.

Thus assuming that because address hygiene is now designated as "worksharing" it should have a discount, and that such a discount is to be calculated by using ECPR, will produce unsatisfactory results. The problem is not one of allocating to the lower-cost candidate an operation which must be performed on every mailpiece, but of providing a cost-effective incentive for mailers to do additional work with the object of reducing the percentage of pieces needing forwarding and return.

We have referred above to the distinction between (i) the degree of address management necessary to insure that the "quality of the work"[28] is adequate to secure the cost-reduction benefit of mailer pre-barcoding (and thus embodied in Postal Service eligibility rules) and (ii) such further degrees as might have some cost-reducing effect but are not required for this purpose. Pricing recognition of (ii) remains an open question. "Address hygiene," in other words, is not an unanalyzable notion which automatically carries with it entitlement to a price incentive regardless of whether the degree or nature of the activity is just that necessary to preserve the value of pre-barcoding. Whether a discount is appropriate for address cleansing beyond the eligibility-requirement level cannot

[28] Order No. 536, p. 45; quoting Postal Service Response to Notice of Inquiry No. 1, p. 10.

be determined by applying ECPR but only by comparing its specific costs and benefits.[29]

C. Cost-reducing activities undertaken for reasons other than cost reduction

Address hygiene exemplifies one sort of pricing problem that will arise under the broad definition of worksharing, but there are others. Some cost-reducing mailer activities will be undertaken, wholly or in part, for reasons other than minimizing postal costs. Density, now recognized by the Commission as an ancillary worksharing feature to the extent it is required by the Postal Service[30], is an example.

A mailing may be of a larger size, and thus potentially[31] of a greater density, because of (i) a desire to maximize discounts by converting as many pieces as possible to a finer presort level, (ii) back-office savings generated for the mailer by consolidating several smaller mailings into one large one, (iii) business necessities, such as the need to send bills simultaneously to all customers on a particular billing cycle or to advertise a time-limited offer to all customers, or (iv) some combination of (i) – (iii). None of these motivations seems to entail a separate incentive for density. Greater conversion of 3 Digit

[29] Assuming for argument's sake that the investigation shows that a discount would be worthwhile, the evident way to construct it is to ascertain the actual (or confidently predictable) savings from some given intensity of address-cleansing activity, compare it with the unit cost of that activity, and set the discount so that both the mailer and the Service derive some benefit. The discount, in other words, should be large enough to elicit the desired address maintenance effort but not so large as to consume all the savings that effort produces.

This, in turn, suggests necessary questions regarding the information needed to carry out such investigations, and how it is to be obtained. Since ECPR will not generate an efficient discount in cases like this, advocates of discount treatment will have to be ready to show (i) that the discount is needed at all to elicit the mailer activity in question, and if so (ii) the magnitude of the savings the Postal Service can expect from it, and (iii) finally – particularly if the suggested "split-the-savings" approach is adopted – the cost to mailers to perform the activity.

[30] Order No. 536, pp. 44-45.

[31] That is, assuming the same number of ZIP codes – or at least a less than proportionate increase in ZIP codes – in the larger mailing.

pieces to 5 Digit, for example, certainly saves postal costs, but the Postal Service already compensates this choice through the spread between the 3 Digit and 5 Digit rates, or at least should be doing so.[32]. Back-office savings constitute an "internal incentive" to the mailer, and business necessities such as maintaining a billing cycle are just that: necessities.

It seems clear that insofar as internal savings or business necessities dictate fewer and larger mailings, there is no need for a price incentive. The Postal Service is not obliged to pay mailers to conduct their own businesses economically. As with address hygiene, we are dealing not with an unanalyzable unit called "density" but with (i) a degree of density which sustains the value of presortation, and (ii) higher degrees of density which may perhaps save Postal Service costs but in any event are not necessarily undertaken with that purpose. With respect to the definition of "presortation" pursuant to § 3622(e), the Commission has agreed to incorporate (i), but this does not imply any need to incorporate (ii) as well. In this case, as with address cleansing above the eligibility-requirement level, it is an open question whether any discount treatment at all is appropriate. If, as the Commission has indicated, a worksharing discount is an incentive to perform cost-reducing activity, and if the mailer already has compelling reasons to perform that activity, a discount simply, and unnecessarily, reallocates dollars from the Postal Service to the mailer.

D. A theoretical basis for "non-ECPR" incentives

As regards mailer activity not required by Postal Service eligibility rules, and thus not incorporated in the definition of a strict worksharing activity by Order No. 536, there are thus two main questions:

[32] A larger, and therefore denser, mailing increases the *total* saving to the Postal Service. Since the increased density carries with it a larger average saving per piece by reason of the larger proportion of letters sorted to, e.g., five rather than three digits, the logical way to reflect the greater saving is by correctly fixing the spread between presort tiers.

- Is there any reason to attach a price incentive to the activity, even if it can be shown to reduce postal costs? and

- If an incentive is found to be appropriate, how should it be constructed?

Some discussion of the second question is appropriate at this point.

We showed earlier that cost-reducing mailer activity which does not displace a corresponding Postal Service activity cannot be priced (assuming arguendo that some discount is appropriate) by using ECPR. The problem is not one of allocating an unavoidable task to the lower-cost candidate but of providing an incentive for both parties which will elicit performance of a useful activity. A discount equal to the demonstrated savings to the Postal Service from performance of the activity is not an incentive for it since it gains no benefit from the mailer activity. Correspondingly, a discount equal to the cost to the mailer to perform the activity is not an incentive to perform it.[33] The obvious answer is a "split-the-savings" approach which is profitable both to the mailer (the discount is greater than its cost to perform the extra work) and to the Postal Service (part of the cost saving is retained as net revenue).

VI. COST MODELS AND COST POOL ISSUES

A. The Modeled Cost Approach Remains Highly Flawed and Subject to Arbitrary Changes

[33] This assumes that the mailer has no other incentive to engage in the activity. Of course, it may have one: additional work to maintain up-to-date addresses could make an advertising campaign more effective because more pieces would reach the intended recipient on time. Such a side benefit might sometimes justify performing the work even if it were not fully compensated through a postage discount. See Postal Service Response to Notice of Inquiry No. 1, pp. 10-11.

In MC95-1, the Commission enunciated a new principle for calculating avoided costs, the ECPR, and its new benchmark for measuring them became BMM. A "Basic Automation" rate was created that replaced the basic presort rate. Costs avoided became attributed mainly to prebarcoding rather than presorting.

The modeled cost approach has been fraught with serious problems since its inception.[34] The Postal Service justified its creation on the grounds that with automation, the value of presorting goes down. Incremental discounts were added to the discount for Basic Automation if the prebarcoded letter was also presorted to 3 digits or 5 digits. The role played by the Basic Automation rate in calculating the basic tier of avoided costs is today played by the mixed AADC rate.

The highly criticized 1.39 proportional adjustment to the cost model estimates calculated by a Postal Service witness in MC95-1came to be viewed as the degree of error in the cost models. The higher the proportional adjustment percentage, the less accurate and credible was the model. In R97-1, the cost models also underestimated actual CRA-based mail processing costs and an

[34] Most recently, a problem with sample size in the IOCS for MODS data has been noted in ACR2010, in the Public Representative's Comments in Response to Order No. 636, February 2, 2011, pp. 22-25.

In the R97-1 rate case, the Postal Service put forward a new "modeled costs" methodology created in MC95-1 for calculating costs avoided in the automated environment: (1) mail processing costs were now estimated by "cost pools" in the MODS data base; and (2) those costs were broken down by rate category through "cost models" which "ran" a hypothetical 10,000 pieces entering the network for each level of Presort and produced an "output" of mail flows which purported to show how those mail pieces moved through the modeled network. The procedure was intended to show for each level of Presort what mail processing steps each of the 10,000 pieces went through, and which ones were excluded. From the modeled output mail processing costs by Presort tier were estimated. When added together the modeled costs were found in R97-1 (and initially in MC95-1) to be less than actual CRA direct mail processing costs.

As a result, a CRA proportional adjustment factor had to be applied to the modeled rate category costs so that when they were summed they equaled actual CRA direct mail processing costs. In-office delivery costs judged to be costs avoided by mailers were calculated by a different method and added to mail processing costs adjusted to arrive at a total costs avoided measure which was then used to estimate discounts from BMM. Often, delivery costs for specific rate categories were proxies based on some other mailstream.

adjustment factor of 1.16 was applied to the model cost estimates to reconcile them with actual CRA costs. This was viewed as an improvement over MC95-1.[35]

In other rate cases, the cost models have over-estimated actual CRA mail processing costs and a negative CRA proportional adjustment factor has been added. For example, in R2000-1, Postal Service witness Miller "overdetermined" CRA costs with his cost models. To reconcile his cost models with actual CRA data, he had to use an adjustment factor of 0.891 for proportional cost pools and 0.665 as a fixed cost pools adjustment. (See Docket R2000-1, ABA & NAPM T-1, pp. 26-28).

In the 2010 ACR, fifteen years after mail processing costs in an automated environment were first modeled, the CRA proportional adjustment factor is an extraordinary 1.667, far worse than the 1.39 that led to substantial criticism of the cost models when introduced in MC95-1.[36] This number means that by worksharing rate category on average, Postal Service modeled costs only measure 60 percent of actual FY2010 CRA direct mail processing costs, when aggregated. For worksharing rates and associated discounts to be at all credible and judged lawful under PAEA, a radical overhauling of the cost models is absolutely necessary and, candidly, five years overdue.

The growing lack of explanatory power of the cost models in explaining CRA costs by presort rate category in recent years cannot be excused or rationalized as an "improvement" starting with 2007 ACR data due to treating most all cost pools applicable to letters as being worksharing-related proportional. This latest swing of the pendulum in MODS classifications is nothing new. Indeed it is simply the opposite end of the pendulum's range of motion in wholesale tinkering done to cost pool classifications between R97-1

[35] To some degree in recent years this issue of the lack of sufficient explanatory power of the cost models has been swept under the rug by simply stating that these are "non-modeled costs".
[36] Other recent proportional adjustment factors have also left the modeled cost approach with little if any remaining credibility. For 2007, the CRA proportional adjustment factor was 1.617, in 2008 1.586, and in the 2009 ACR, it was 1.597.

and R2000-1. Many of the cost pools labeled as proportional in R97-1 became labeled as fixed or non-worksharing related in R2000-1. The latter swing of the pendulum was initiated by the Postal Service, the latest one by the Commission and the parent company of a large presort bureau. The difference is that the CRA proportional adjustment factor was only 1.19 in R97-1 whereas today it has deteriorated to 1.667.

B. Removing the Highest-Volume Rate Category from Cost Models and Directly Costing It Through Use of IMb Data Would Greatly Improve the Modeled Cost Approach

One way in which the modeled cost approach could be substantially improved, and made immune to the pendulum swings in cost pool classifications is to directly measure the mail processing costs associated with 5 Digit presort mail, much as was done with carrier route presort, in its day the rate category that avoided the most costs for the Postal Service. The costs for other Presort rate categories could then be modeled, and costs avoided calculated. This approach stands the best chance of greatly reducing any proportional adjustment factor, and greatly improving the cost models because it would remove from the modeling the largest volume rate category and remove its costs from the CRA in the calculation of a proportional adjustment factor. Directly measuring the mail processing costs of 3 Digit Presort might produce an even more accurate set of modeled costs because it would remove even more costs from the CRA that needed to be reconciled with modeled costs. Despite being lower in volume than 5 Digit, the unit mail processing cost for 3 Digit is above that for 5 Digit and it forms a larger percentage of CRA direct mail processing costs than any other rate category.

Direct costing of mail processing and in-office delivery of prebarcoded 5 Digit (and/or 3 Digit) presort mail would become the worksharing reference point used with a benchmark to estimate costs avoided as noted earlier. Under this approach, mail that has less worksharing than 5 Digit presort would be modeled

and costed as differences from the costs of 5 Digit presort, in essence "adding back" costs to 5 Digit in the process of setting rates for the less-workshared mail.

In order to directly cost 5 Digit (or 3 Digit) prebarcoded letters, there would need to be an identifying mark on each piece when it entered the Postal Service mail processing network. The operations which a 5 Digit letter and/or a 3 Digit letter go through, and which they avoid, could be directly measured, for example, if such letters were identified as 5 Digit or 3 Digit in an Intelligent Mail Barcode. As IMb technology becomes more fully utilized, GCA believes the planning for such a change to the cost models can be done now and implemented when the percentage use of IMb reaches some critical threshold that would enable statistically sound samples of the direct network mail processing costs for a 5 Digit (and/or) a 3 Digit letter to be made.

C. Problems with the current workshared reference point for measuring costs avoided and a proposed solution

The mixed AADC mailpiece has had a highly problematic history for use as the workshared reference point to estimate costs avoided from worksharing. It is a peculiar evolution: the transformation of a basic presort rate into a basic automation rate, made by the Postal Service and the Commission in Docket MC95-1, arguably by using little else than a magic wand. Notably, as a reference point, the discount afforded MAADC has typically exceeded the costs it avoids compared to the BMM benchmark. One question this has always raised is whether the costs avoided by prebarcoding are in fact as large as claimed coming out of MC95-1.

The in-office delivery costs for MAADC as well as BMM have been based on a proxy created from breakdowns of non-automation presort mail. When further subdivided into numerous subsets as non-auto presort has been, the in-office delivery cost estimates can easily suffer from lack of an adequate sample. Whether because of this or some other factor, as a highly flawed workshared

reference point, MAADC mail has actually exhibited negative delivery costs avoided relative to the BMM benchmark.

Mixed AADC is “residual mail” from Presort Bureaus estimated to be less than 6 percent of all such mail and declining. Its cost has no direct bearing on the costs of the large mailers and presort bureau mail streams – 3 Digit and 5 Digit prebarcoded letters, nor on actual costs avoided for the Postal Service from worksharing at one of these two presort tiers.

When the benchmark issue is settled in this case, single piece conversion mail will not be (and seldom has been) presorted to a mixed AADC or AADC level, but to a 3 Digit or 5 Digit level, except for small residuals coughed out from that process. Therefore, the discount measured from that benchmark should be based on the costs avoided from that benchmark by 5 Digit (and/or 3 Digit) letters, not MAADC letters.

Even a 0.2 – 0.3 cent increase in the new benchmark compared to BMM will still leave a passthrough of worksharing discounts of well over 100 percent of costs that MAADC letters avoid. As a result, the costs avoided for every presort tier will be less than the total discount from the benchmark each tier receives, as they are now. That situation may be viewed as lawful or unlawful under PAEA’s guidelines that discounts not exceed costs avoided, since other criteria also affect the discounts. At the very least, however, the workshared reference point compared to the benchmark should be 5 Digit (and/or 3 Digit) letters, not MAADC residual mail. Furthermore, it should be 5 Digit (and or 3 Digit) letters directly costed through use of IMb identifiers, not modeled cost estimates.

D. Changes to the way some cost pools in the MODS data base are classified: worksharing related proportional; worksharing related fixed; non-worksharing related.

In R97-1, Postal Service witness Hatfield classified 37 cost pools as worksharing related proportional, that is those mail processing activities that are related to the level of worksharing. Nine cost pools were classified as worksharing related fixed, that is those mail processing activities affected by worksharing but not varying by the level of worksharing. No cost pools were classified as non-worksharing related in R97-1. In R2000-1 Postal Service witness Miller made substantial changes to these classifications, with far fewer cost pools being proportional (11), and many more being non-worksharing related (35). Clearly, the two classifications could not both be correct. Since R2000-1 and through R2006-1, cost pool classifications have gravitated toward a middle ground between the Hatfield R97-1 and Miller R2000-1 classifications.

In R2006-1, a Pitney Bowes (PB) witness made an argument that most all cost pools should be classified as proportional, that is varying directly with the level of presort. Since R2006-1, the Postal Regulatory Commission clearly has moved substantially toward the classification of most cost pools as worksharing related proportional, though many of these are now bifurcated, with most of the individual cost pool being classified as worksharing related proportional and the remainder being classified as worksharing related fixed.

One might say that the modeled cost classifications have now come full circle between R97-1 and currently, with both methods maintaining most cost pools are worksharing related proportional. Whether coming full circle is progress, however, in better estimating worksharing rate category direct mail processing costs is quite a different question to ponder.

Table Two - A compares all the recent classification changes to cost pools as between worksharing related proportional, fixed or non-worksharing related. For all presort letters in R2006-1, worksharing related proportional cost pools accounted for 3.234 cents of MODS cost pools while worksharing related fixed cost pools accounted for 1.766 cents. In the first annual compliance

determination, ACR2007, one sees the pronounced shift in MODS costs away from fixed to proportional. In total about one cent in MODS costs was shifted from the fixed column to the proportional column. The new classification scheme remains in place, as can be seen from the data for ACR2010 in Table Two – A. As noted earlier, the only equally bold shift in cost pool classifications in the history of modeled costs was that of Postal Service witness Miller in R2000-1, who moved a number of costs from worksharing related proportional to non-worksharing related.

APWU has also participated in these cost pool classification debates. It prefers a methodology like that used in R2005-1, the last of the middle ground classifications that fell between the R97-1 and R2000-1. It has also stressed the need for greater accuracy in the PAEA environment. The cost pool classifications preferred by APWU are shown in Table Two – B. These are readily distinguished from the classifications in Table Two - A adopted by the Commission from ACR2007 to the present. In R2005-1, 59 percent of the cost pools were labeled as proportional whereas from R2006-1 forward, this percentage has grown from 65 percent to 87 percent.

Finally, Table Three compares the classifications of cost pools used in the ACR2010 with those used in R97-1, also using the Commission's 100 percent volume variable assumption. As can be seen, both classifications are based on the viewpoint that almost all cost pools are worksharing related proportional. In R97-1, 92 percent of the cost pools were classified as proportional and in ACR2010 as the pendulum swings back in that direction again, 87 percent of the cost pools are classified as proportional.

Table Two-A
FIRST-CLASS MAIL PRESORT LETTERS
CRA MAIL PROCESSING COSTS
ACR2010, ACR2007, and R2006-1

Cost Pools		ACR2010 Worksharing-Related Proportional (Cents)	ACR2010 Fixed (Cents)	ACR2010 Non-WS Related (Cents)	ACR2007 Worksharing-Related Proportional (Cents)	ACR2007 Fixed (Cents)	ACR2007 Non-WS Related (Cents)	R2006-1 Proportional (Cents)	R2006-1 Fixed (Cents)
MODS 11	BCS/	0.000			0.000			0.000	
MODS 11	BCS/DBCS	2.520			1.626			1.498	
MODS 11	OCR/	0.004			0.098			0.161	
MODS 12	FSM 100	0.023	0.003	0.000	0.015	0.003	0.000		0.010
MODS 12	FSM/	0.000	0.000	0.000	0.000	0.000	0.000		0.000
MODS 12	FSM/1000	0.000	0.000	0.000	0.005	0.001	0.000		0.008
MODS 13	MECPARC	0.000	0.000	0.000	0.001	0.000	0.000		0.000
MODS 13	SPBS OTH	0.007	0.001	0.000	0.008	0.001	0.000		0.007
MODS 13	SPBSPRIO	0.004	0.001	0.000	0.000	0.000	0.000		0.000
MODS 13	1SACKS_M	0.009	0.001	0.000	0.006	0.001	0.000		0.011
MODS 13	1TRAYSRT	0.221	0.032	0.001	0.103	0.020	0.001		0.163
MODS 14	MANF	0.008	0.001	0.000	0.005	0.001	0.000		0.005
MODS 14	MANL	0.251			0.284			0.285	
MODS 14	MANP	0.005	0.001	0.000	0.003	0.001	0.000		0.005
MODS 14	PRIORITY	0.009	0.001	0.000	0.005	0.001	0.000		0.002
MODS 15	LD15	0.143			0.185			0.077	
MODS 17	1CANCEL		0.115			0.073			0.066
MODS 17	1DISPATCH	0.083	0.012	0.000	0.071	0.014	0.000		0.087
MODS 17	1FLATPRP	0.005	0.001	0.000	0.010	0.002	0.000		0.022
MODS 17	1MTRPREP		0.009			0.009			0.011
MODS 17	1OPBULK		0.036			0.043		0.037	
MODS 17	1OPPREF		0.187			0.217		0.180	
MODS 17	1OPTRANS	0.032	0.005	0.000	0.027	0.005	0.000		0.032
MODS 17	1PLATFRM	0.426	0.061	0.001	0.388	0.074	0.002		0.433
MODS 17	1POUCHNG		0.009			0.012		0.017	
MODS 17	1PRESORT	0.029	0.004	0.000	0.046	0.009	0.000		0.021
MODS 17	1SACKS_H	0.010	0.001	0.000	0.014	0.003	0.000		0.019
MODS 17	1SCAN	0.038	0.005	0.000	0.033	0.006	0.000		0.034
MODS 18	BUSREPLY			0.002			0.005		0.004
MODS 18	EXPRESS	0.001	0.000	0.000	0.003	0.000	0.000		0.001
MODS 18	MAILGRAM			0.000			0.000		0.001
MODS 18	REGISTRY			0.001			0.001		0.001
MODS 18	REWRAP	0.002	0.000	0.000	0.004	0.001	0.000		0.003
MODS 18	1EEQMT	0.037	0.005	0.000	0.012	0.002	0.000		0.014
MODS 18	1MISC	0.035	0.005	0.000	0.050	0.010	0.000		0.058
MODS 18	1SUPPORT	0.025	0.004	0.000	0.022	0.004	0.000		0.019
MODS 19	INTL ISC	0.004	0.001	0.000	0.006	0.001	0.000		0.006
MODS 19	PMPC	0.000	0.000	0.000	0.000	0.000	0.000		0.000
MODS 41	LD41	0.008			0.031			0.027	
MODS 42	LD42	0.005			0.000			0.001	
MODS 43	LD43	0.172			0.196			0.182	
MODS 44	LD44	0.071			0.069			0.072	
MODS 48	LD48 EXP	0.000	0.000	0.000	0.000	0.000	0.000		0.005
MODS 48	LD48 OTH		0.046			0.041			0.036
MODS 48	LD48_ADM		0.023			0.022			0.030
MODS 48	LD48_SSV			0.007			0.006		0.009
MODS 49	LD49		0.059			0.142			0.207
MODS 79	LD79		0.053			0.056			0.114
MODS 99	1SUPP_F1	0.000	0.000	0.000	0.000	0.000	0.000		0.000
MODS Subtotal		**4.188**	**0.682**	**0.014**	**3.323**	**0.774**	**0.017**	**2.536**	**1.445**
BMCS	MANP	0.000	0.000	0.000	0.000	0.000	0.000		
BMCS	NMO	0.000	0.000	0.000	0.000	0.000	0.000		0.000
BMCS	OTHR	0.003	0.000	0.000	0.002	0.000	0.000		0.000
BMCS	PLA	0.007	0.001	0.000	0.004	0.001	0.000		0.001
BMCS	PSM	0.000	0.000	0.000	0.004	0.001	0.000		0.000
BMCS	SPB	0.000	0.000	0.000	0.000	0.000	0.000		0.000
BMCS	SSM	0.000	0.000	0.000	0.000	0.000	0.000		0.000
BMCS	TRAYSORT	0.004	0.001	0.000	0.002	0.000	0.000		
BMC Subtotal		**0.015**	**0.002**	**0.000**	**0.010**	**0.002**	**0.000**	**0.000**	**0.001**
NON MODS	ALLIED	0.118	0.017	0.000	0.107	0.020	0.001		0.138
NON MODS	AUTO/MEC	0.104			0.248			0.233	
NON MODS	EXPRESS	0.000	0.000	0.000	0.001	0.000	0.000		0.000
NON MODS	MANF	0.004	0.001	0.000	0.006	0.001	0.000		0.000
NON MODS	MANL	0.470			0.468			0.465	
NON MODS	MANP	0.005	0.001	0.000	0.001	0.000	0.000		0.002
NON MODS	MISC	0.098	0.014	0.000	0.116	0.022	0.001		0.177
NON MODS	REGISTRY			0.001			0.005		0.003
Non MODS Subtotal		**0.799**	**0.032**	**0.002**	**0.947**	**0.044**	**0.006**	**0.698**	**0.320**
Total		**5.001**	**0.716**	**0.016**	**4.280**	**0.821**	**0.023**	**3.234**	**1.766**
Percentage		**87.2%**	**12.5%**	**0.3%**	**83.49%**	**16.01%**	**0.45%**	**64.7%**	**35.3%**

Sources: ACR2010, USPS-FY10-26; ACR2007, USPS-FY07-26; & R2006-1, USPS LR-L-99.

Table Two-B
FIRST CLASS MAIL AUTOMATION LETTERS
CRA MAIL PROCESSING COSTS
R2005-1

Cost Pools		Total (Cents)	Proportional (Cents)	Fixed (Cents) Worksharing related	Fixed (Cents) Non Worksharing related
MODS 11	BCS/	0.112	0.112		
MODS 11	BCS/DBCS	1.159	1.159		
MODS 11	OCR/	0.099	0.099		
MODS 12	FSM 100	0.003			0.003
MODS 12	FSM/	0.000			0.000
MODS 12	FSM/1000	0.005			0.005
MODS 13	MECPARC	0.000			0.000
MODS 13	SPBS OTH	0.002			0.002
MODS 13	SPBSPRIO	0.001			0.001
MODS 13	1SACKS_M	0.012			0.012
MODS 13	1TRAYSRT	0.137			0.137
MODS 14	MANF	0.002			0.002
MODS 14	MANL	0.215	0.215		
MODS 14	MANP	0.006			0.006
MODS 14	PRIORITY	0.009			0.009
MODS 15	LD15	0.065	0.065		
MODS 17	1CANCEL	0.050		0.050	
MODS 17	1DISPATCH	0.069			0.069
MODS 17	1FLATPRP	0.015			0.015
MODS 17	1MTRPREP	0.007		0.007	
MODS 17	1OPBULK	0.029		0.029	
MODS 17	1OPPREF	0.145		0.145	
MODS 17	1OPTRANS	0.030			0.030
MODS 17	1PLATFRM	0.308		0.308	
MODS 17	1POUCHNG	0.018		0.018	
MODS 17	1PRESORT	0.004		0.004	
MODS 17	1SACKS_H	0.020			0.020
MODS 17	1SCAN	0.032			0.032
MODS 18	BUSREPLY	0.002			0.002
MODS 18	EXPRESS	0.001			0.001
MODS 18	MAILGRAM	0.001			0.001
MODS 18	REGISTRY	0.001			0.001
MODS 18	REWRAP	0.001			0.001
MODS 18	1EEQMT	0.009			0.009
MODS 18	1MISC	0.035		0.035	
MODS 18	ISUPPORT	0.014		0.014	
MODS 19	INTL	0.001			0.001
MODS 19	PMPC	0.002			0.002
MODS 41	LD41	0.030	0.030		
MODS 42	LD42	0.000	0.000		
MODS 43	LD43	0.107	0.107		
MODS 44	LD44	0.060	0.060		
MODS 48	LD48 EXP	0.000			0.000
MODS 48	LD48 OTH	0.021			0.021
MODS 48	LD_ADM	0.022			0.022
MODS 48	LD48_SSV	0.008			0.008
MODS 49	LD49	0.156		0.156	
MODS 79	LD79	0.045		0.045	
MODS 99	1SUPP_F1	0.000		0.000	
Mods Subtotal		**3.073**	**1.848**	**0.812**	**0.413**
BMCS	NMO	0.000			0.000
BMCS	OTHR	0.001			0.001
BMCS	PLA	0.000			0.000
BMCS	PSM	0.000			0.000
BMCS	SPB	0.000			0.000
BMCS	SSM	0.000			0.000
BMC Subtotal		**0.001**	**0.000**	**0.000**	**0.001**
NON MODS	ALLIED	0.243		0.2431	
NON MODS	AUTO/MEC	0.184	0.184		
NON MODS	EXPRESS	0.000			0.000
NON MODS	MANF	0.005			0.005
NON MODS	MANL	0.241	0.241		
NON MODS	MANP	0.003			0.003
NON MODS	MISC	0.085			0.085
NON MODS	REGISTRY	0.002			0.002
Non Mods Subtotal		**0.763**	**0.424**	**0.243**	**0.095**
Total		**3.836**	**2.272**	**1.055**	**0.509**
Percentage			**59.2%**	**27.5%**	**13.3%**

Source: R2005-1 USPS- LR-K-99

Table Three

FIRST-CLASS MAIL PRESORT LETTERS
CRA MAIL PROCESSING COSTS

ACR2010

Cost Pools		Worksharing Related Proportional (Cents)	Fixed (Cents)	Non-WS Related (Cents)
MODS 11	BCS/			
MODS 11	BCS/DBCS	X		
MODS 11	OCR/	X		
MODS 12	FSM 100	X	X	X
MODS 12	FSM/			
MODS 12	FSM/1000	X	X	X
MODS 13	MECPARC	X	X	X
MODS 13	SPBS OTH	X	X	X
MODS 13	SPBSPRIO	X	X	X
MODS 13	1SACKS_M	X	X	X
MODS 13	1TRAYSRT	X	X	X
MODS 14	MANF	X	X	X
MODS 14	MANL	X		
MODS 14	MANP	X	X	X
MODS 14	PRIORITY	X	X	X
MODS 15	LD15	X		
MODS 17	1CANCEL		X	
MODS 17	1DISPATCH	X	X	X
MODS 17	1FLATPRP	X	X	X
MODS 17	1MTRPREP		X	
MODS 17	1OPBULK		X	
MODS 17	1OPPREF		X	
MODS 17	1OPTRANS	X	X	X
MODS 17	1PLATFRM	X	X	X
MODS 17	1POUCHNG		X	
MODS 17	1PRESORT	X	X	X
MODS 17	1SACKS_H	X	X	X
MODS 17	1SCAN	X	X	X
MODS 18	BUSREPLY			X
MODS 18	EXPRESS	X	X	X
MODS 18	MAILGRAM			
MODS 18	REGISTRY			X
MODS 18	REWRAP	X	X	X
MODS 18	1EEQMT	X	X	X
MODS 18	1MISC	X	X	X
MODS 18	1SUPPORT	X	X	X
MODS 19	INTL ISC	X	X	X
MODS 19	PMPC			
MODS 41	LD41	X		
MODS 42	LD42	X		
MODS 43	LD43	X		
MODS 44	LD44	X		
MODS 48	LD48 EXP	X	X	X
MODS 48	LD48 OTH		X	
MODS 48	LD48_ADM		X	
MODS 48	LD48_SSV			X
MODS 49	LD49		X	
MODS 79	LD79		X	
MODS 99	1SUPP_F1			
BMCS	MANP	X	X	X
BMCS	NMO			
BMCS	OTHR	X	X	X
BMCS	PLA	X	X	X
BMCS	PSM	X	X	X
BMCS	SPB			
BMCS	SSM	X	X	X
BMCS	TRAYSORT	X	X	X
NON MODS	ALLIED	X	X	X
NON MODS	AUTO/MEC	X		
NON MODS	EXPRESS	X	X	X
NON MODS	MANF	X	X	X
NON MODS	MANL	X		
NON MODS	MANP	X	X	X
NON MODS	MISC	X	X	X
NON MODS	REGISTRY			X
Total		**5.001**	**0.716**	**0.016**
Percentage		**87.2%**	**12.5%**	**0.3%**

First-Class Mail Processing CRA Unit Cost Calculations
as Adjusted for PRC Order Number 1203
CRA Letter Mail Processing Unit Costs by Cost Pool

R97-1

Location	Cost Pool	Proportional Costs (Cents)	Fixed Costs (Cents)
mods	bcs/	X	
mods	ocr/	X	
mods	fsm/	X	
mods	lsm/	X	
mods	mecparc	X	
mods	spbs Oth	X	
mods	spbsPrio	X	
mods	manf	X	
mods	manl	X	
mods	manp	X	
mods	priority	X	
mods	LD15	X	
mods	1OPbulk	X	
mods	1OPpref	X	
mods	1Platfrm		X
mods	1POUCHNG	X	
mods	1SackS_m		X
mods	1SackS_h		X
mods	1SCAN	X	
mods	BusReply	X	
mods	express	X	
mods	MAILGRAM	X	
mods	Registry	X	
mods	REWRAP	X	
mods	1Bulk pr	X	
mods	1CancMPP	X	
mods	1EEQMT	X	
mods	1MISC	X	
mods	1SUPPORT	X	
mods	INTL	X	
mods	LD41	X	
mods	LD42	X	
mods	LD43	X	
mods	LD44	X	
mods	LD48 Exp	X	
mods	LD48 Oth	X	
mods	LD48_SSv	X	
mods	LD49	X	
mods	LD79	X	
BMCs	nmo		X
BMCs	Othr		X
BMCs	Pla		X
BMCs	psm		X
BMCs	spb		X
BMCs	ssm		X
Non Mods		X	X
		4.841	**0.450**
		91.5%	**8.5%**

'Source: R97-1, USPS-LR-H-324 and ACR2010, USPS-FY10-26

E. Using Two CRA Proportional Adjustment Factors

If Postal Service cost models for different presort levels of automation letters were good estimators, there would be no need for any CRA proportional adjustment factor, let alone two or more. The modeled costs by rate category would just equal actual CRA mail processing costs. However, since they were first introduced in R97-1, the cost models have not only not achieved their potential, they seem clearly to have devolved into allocating fewer and fewer CRA direct mail processing costs by rate category. As noted earlier, in the 2010ACR data submitted by the Postal Service, the single proportional adjustment factor is 1.667, indicating that the cost models in general only "explain" 60 percent of actual CRA mail processing costs.

A fundamental flaw in the modeled cost approach, especially when the proportional adjustment factor differs significantly from one as it has consistently in the past few years is that it presumes the distribution of non-modeled costs can be allocated based on the distribution of relative modeled costs.

The proposed two-part CRA proportional adjustment technique[37] takes one adjustment factor whose level lends little credibility to the cost models and creates two adjustment factors from it that do nothing to improve the explanatory power of the cost models in explaining CRA direct mail processing costs. The two-part procedure takes advantage of the fact that 5 Digit presort letters avoid all non-Incoming Secondary (NIS) sorts in the mail flow models, but do incur Incoming Secondary (IS) sorts, which sort 5 Digit letters to carrier route DPS. IOCS tallies for each of the nine MODS and non-MODS letter sorting costs are divided into IS and NIS components, and from this, two proportional adjustment

[37] See RM2009-3, Initial Comments of Pitney Bowes, Inc., pp.11-14, Appendix I, and Appendices II and III, which group IOCS tallies for the nine letter sorting MODS and Non-MODS cost pools as to whether they fall under modeled mail flow schemata Incoming Secondary sorts (which sort mail entered into the network as 5 Digit presort by carrier route and delivery point sequencing), or Non-Incoming Secondary sorts (which sort other than 5 Digit prebarcoded letters).

factors are calculated, a lower one which applies only to 5 Digit letters, and a higher one which applies on average to all other automation rate categories.

The proposed two-part CRA proportional adjustment creates a bias if the proportional adjustment factor for mail other than 5 Digit is higher for other rate categories such as 3 Digit than a separate CRA adjustment factor for that mailstream would produce.

Such a “de-averaging” of the proportional adjustment factor could probably also be done for 3-Digit presort, which would exhibit a lower proportional adjustment factor than that remaining for the rate categories other than 3 and 5 Digit. Carried to its logical conclusion, instead of a single proportional adjustment factor well in excess of that which would lend credibility to the modeled cost approach applied across the board to each presort rate category, there would be a hierarchy of proportional adjustment factors that allocates so-called “non-modeled” CRA costs such that the highest percentage allocation is assigned to the highest modeled cost rate category and the lowest allocation is assigned to the lowest modeled cost rate category. Such an allocation of non-modeled costs does not fundamentally improve the explanatory power of CRA costs in the cost models, it simply reallocates the nonmodeled costs among the rate categories compared to a single proportional adjustment factor. For example, using FY2010 data, the single average proportional adjustment factor of 1.667 would simply be de-averaged into two, three or more numbers. Such a de-averaging would not change the fact that the cost models in their totality still only explain 60 percent of actual CRA costs.

VII. OTHER AVOIDED COST ISSUES

A. Changes to the way delivery costs and “other costs” are estimated in calculating costs avoided.

A recent issue has arisen as to whether in-office delivery costs remain a material part of the costs that worksharing avoids. In R2006-1 the witness for at least one intervenor, Pitney Bowes, Inc. maintained that no worksharing related in-office delivery costs were included in estimates of costs avoided. To some degree this issue arises as DPS percentages rise, and as the Postal Service begins to substitute DPS percentages for older methods of estimating in-office delivery costs. The Postal Service believes that in-office delivery costs vary inversely with the DPS percentage, approaching zero as the DPS approaches 100 percent. An issue related to DPS has been raised by a witness for MMA as to whether actual DPS percentages by worksharing tier are being used or whether the DPS percentages themselves are modeled, with all the attendant problems associated with the models.

The continuing difficulty of measuring delivery costs for purposes of measuring total costs avoided from worksharing is also exemplified by looking at Postal Service data submitted in the 2009 ACR, and then in the 2010 ACR. The issues relate, of course, to the non-automation presort letter proxies used for this purpose.

In the ACR2009, the worksharing related unit delivery costs for metered letters (BMM) was estimated at 4.647 cents, for MAADC and AADC letters respectively at4.938 cents and 4.646 cents, for 3 Digit automation at 4.633 cents and for 5 Digit automation at 4.412 cents.

Using the above numbers, delivery cost savings were *negative* for MAADC compared to BMM and essentially zero for AADC and 3 Digit automation letters. Only 5 Digit automation letters had a tangible positive cost avoidance in worksharing related delivery costs, and it was only 0.235 cents.

In the ACR2010, MAADC letters still had negative delivery costs avoided, while the finer levels of presort had unit delivery cost savings ranging from 0.14 cents to 4.1 cents for 5 Digit. Much of the change was due to the shift in benchmarks from BMM to metered, a change which increased the benchmark by about 0.2 cents.

The trend in Postal Service costing of worksharing related delivery costs appears clearly to acknowledge positive costs avoided for 5 Digit letters, but effectively no delivery costs avoided for all other automation rate categories.

Negative and zero costs avoided for worksharing delivery costs is not a new phenomenon either. In R2006-1, the Postal Service also maintained that there were no worksharing related unit delivery costs avoided. Although the Commission rejected that position, its own approach "produced tiny delivery cost savings for most categories an[d] NEGATIVE savings in one instance."[38]

A related and longstanding issue has been whether delivery costs for non-automated presort can be used as a proxy for the delivery costs of BMM and MAADC and AADC mail. As noted earlier, the major issue here has been the credibility of such a proxy in the face of numerous and never ending problems with cost and cost avoidance estimates for non-auto presort. Part of the problem is that these proxies are not calculated from all non-auto presort mail, which in and of itself is a very small volume rate category. Rather, the benchmark delivery cost proxies are estimated using one of eight breakdowns of all non-auto presort into even smaller volume classifications as low as one one-hundredth of a percent of all presort volumes where statistically valid cost estimates become questionable due to sample size from a minuscule population.

B. Establishing a discount for single piece mail (PC postage) that is CASS-certified and bears an IMb.

[38] See Docket RM2009-3, Follow-On Comments of the Major Mailers Association (September 11, 2009), p. 21.

The Postal Service and the greeting card industry are already involved in a pilot plant study wherein IMb technology would allow the Postal Service to directly bill the manufacturer of greeting cards for the cost of postage used to send such mail. This would be a convenience both to the Postal Service from a lesser need for “high cost” stamps purchased at a window, and for consumers of greeting cards since each card and IMb envelope would not need a stamp to be mailed.

The proposal put forth most recently by Stamps.Com in RM2009-3[39] for a discount for “pc postage” has merit and as with the pilot plant study using IMb technology for mailing greeting cards, holds out the possibility for attenuating the decline of single piece first class mail through the convenience of the Internet and use of other high-technology means of stimulating first class single piece mail volume.

VIII. SUMMARY

To summarize, GCA believes that:

1. A weighted average benchmark comprising IBI and traditional metered mail would be the best choice;

2. The choice of a benchmark must be governed by the practical likelihood of conversion, as well as by commonality of cost and demand characteristics and the effect of an incentive;

3. The Commission's broadening of the definition of worksharing means that each instance of these "non-traditional" worksharing activities must be examined

[39] See RM2009-3, “Initial Comments of Stamps.Com”, May 26, 2009.

separately to see if discount treatment is warranted; application of ECPR to them cannot give correct results; and

4. Persistent problems with the modeled cost approach suggest that direct costing of 5 Digit Automation letters – now the dominant category – would be superior to current practice for the development of a worksharing reference point to use in conjunction with the benchmark.

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Respectfully submitted,

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