

Before the  
POSTAL REGULATORY COMMISSION  
WASHINGTON, DC 20268-0001

Consideration of Technical Methods to :  
Be Applied in Workshare Discount Design : Docket No. RM2010-13

AMENDED REPLY COMMENTS OF THE GREETING CARD ASSOCIATION

The Greeting Card Association (GCA) files these Reply Comments pursuant to the Commission's Order No. 537 (September 14, 2010). In this introductory section we outline the topics covered in the document as a whole.

Section I (Introduction) points out that the benchmark to be chosen in this Docket will affect all Presort rates – not just a rate intended to attract Single-Piece mail at the margin of conversion – and discusses the importance of this fact for both the efficiency of First-Class Mail rates and the justness and reasonableness of the First-Class rate schedule. The Commission must balance these two equally important mandates of the statute (39 U.S.C. § 3622(b)(1), (8)) in arriving at its conclusion.

Section II analyzes the argument that the alleged heterogeneity of conversion-ready Single-Piece letters requires a higher benchmark – specifically, one inflated by inclusion of collection costs, which are not part of the Bulk Metered Mail (BMM) benchmark. We point out that mail sought for consolidation and conversion to Presort is no more heterogeneous today than a decade ago. Next, in subsection B, we show that including collection costs would produce a benchmark higher than any plausible estimate of the cost of "heterogeneous" conversion mail. This discussion shows that collection costs would not be an appropriate component of the new benchmark. Subsection C, narrowing the focus, de-

monstrates that the collection cost the Postal Service reports for metered Single-Piece letters – the mail deemed conversion-ready by advocates of including collection cost – is in any case substantially higher than the probable collection cost of the subset of those letters claimed to be conversion candidates requiring collection.

Section III discusses separately the information furnished to National Association of Presort Mailers (NAPM) by several of its member firms, and filed by NAPM in this case. It reinforces the conclusion, stated above, that conversion mail has not changed in many years and that, accordingly, the benchmark need not now be inflated to accommodate it.

Section IV analyzes, and points out flaws in, the Postal Service's novel estimate of delivery costs for metered letters, which adds nearly a cent to the cost which would be reflected in the benchmark.

Section V first discusses the Postal Service's explanation of its approach to the modeling of cost pools. GCA agrees with much of what the Service says, but not with its assertion that there is no connection between the size of the CRA adjustment factor used to bring the modeled results in line with recorded costs and the accuracy of the modeling process. Next, we add further considerations, with particular reference to the effects on inter-tier spreads of (i) the Postal Service's classification of some cost pools from proportional to fixed and (ii) Pitney Bowes' (PB) proposal for a two-part CRA adjustment factor.

## I. INTRODUCTION

At the outset, some observations are in order with respect to the context in which the benchmark the Commission seeks to establish will operate. The Commission faces the challenging task of choosing a benchmark which will re-

spond to the theoretical demands of pricing efficiency as regards Presort Letters, while at the same time conforming to all the requirements of 39 U.S.C. § 3622. Much of the discussion in the initial comments in this Docket (including GCA's) has focused on Single-Piece letter mail at the margin of conversion. The same could be said of Order No. 536.<sup>1</sup> In these Reply Comments, we raise at least equally important questions regarding the overall effect of the new benchmark on the whole structure of First-Class letter rates.

The benchmark, because it consists of a single subset of Single-Piece Letters whose makeup is similar to Presort, for the purpose of setting Presort rates, necessarily governs the construction of rates paid not just by the “marginal” letters extensively discussed so far, but also the rates paid by all other Presort mailers – i.e., those for whom discounts constructed on the Bulk Metered Mail benchmark have proved adequate (or excessive) – and, given the ratemaking system established by the 2006 legislation, Single-Piece rates as well.

Perhaps most important is the inescapable fact that the benchmark the Commission chooses will be employed in a price-cap system. The Postal Service is subject to statutory limits both on the total additional revenue it can collect from First-Class Letters and, since the cap is applied class-by-class, on its ability to impose disparate revenue increases on different classes.<sup>2</sup> Because of its current and foreseeable financial challenges, the Service can be expected to use all the rate increase authority that § 3622(d)(1)(A) gives it. This means, in practice, that any unnecessary sacrifice of revenue resulting from increasing discounts across all the Presort categories will have to be paid for by increases imposed on Sin-

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<sup>1</sup> See, e.g., Docket No. RM2009-3, Order No. 536, pp. 13, 14, and 19, fn. 11.

<sup>2</sup> By contrast, the techniques of marginal analysis focused on so far tend to assume that the firm is free to set prices for all its products, independently of one another, at what appear to it to be efficient levels. For example, if the analysis points to the possibility of increasing prices for some products by more than the rate of inflation, the firm is presumed to be able to do so. The Postal Service, being subject to a class-by-class price cap pegged to the change in the CPI-U, does not have this freedom.

gle-Piece.<sup>3</sup> This, in turn, means that the choice of a benchmark in this Docket implicates not only the “increased efficiency” mandate of § 3622(b)(1) but also the requirement of § 3622(b)(8) that the Commission “establish and maintain a just and reasonable schedule for rates and classifications.” It should be recalled, in this connection, that Presort is already a substantially larger category, in volume terms, than Single-Piece<sup>4</sup>, and that only a fraction of today's Single-Piece is claimed by the proponents of a higher benchmark to be available for conversion to Presort. To award unnecessarily large discounts to existing Presort mail, as a byproduct of providing for conversion of that fraction, and to impose the cost of those excess discounts on Single-Piece would be neither just nor reasonable.

Viewed superficially, it may seem that the objectives of efficiency and a just and reasonable rate schedule are in conflict. The possibility of such conflict between mandatory objectives, and the necessity of resolving it by accommodating both, are recognized in the statute: § 3622(b) requires the Commission to insure that “each of [the nine objectives] shall be applied in conjunction with the others.” Thus, the Commission should make it a guiding principle that the purpose of this Docket is not simply to design a rate which will attract further mail into the Presort category, but to develop a general rule which will control the design of *all* the worksharing rates for First-Class Letters, and will necessarily affect the rates for Single-Piece mail too.

## II. THE JOINT COMMENTERS' BENCHMARK AND COLLECTION COSTS ARGUMENTS

### A. Heterogeneity of Conversion Mail in the Past and Present

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<sup>3</sup> The Commission concluded in Order No. 536 (p. 13), based on outside studies, that Single-Piece and Presort did not differ greatly in sensitivity to price changes. Thus it can be expected that such excessive increases would lead to underconsumption of Single-Piece.

<sup>4</sup> In FY 2010 the Postal Service recorded 43.3 billion Presort Letters and 27.1 billion Single-Piece Letters. Docket No. ACR2010, Public Cost and Revenue Analysis Report.

The Joint Commenters<sup>5</sup> discuss some results of three surveys conducted as part of their initial comments: one by National Association of Presort Mailers (NAPM) for 90 relatively new customers of 36 member consolidators, one by George Mason University (GMU) on the existing mail composition for 225 small to medium sized businesses and their willingness to convert to presort, and one from 18 members of National Postal Policy Council (NPPC) and Major Mailers Association (MMA), large firms whose combined volume of 8 billion presort and automation pieces constitutes about 20 percent of all annual presort and automation letters.

The surveys were intended to provide support for the argument that conversion mail today is heterogeneous, not homogeneous as the BMM benchmark mail was. The salient results are that for the large NPPC/MMA mailers and consolidators, 97.5 percent of the mail entered was automation presort while only 2.5 percent was entered as single piece<sup>6</sup>; for the small to medium firms GMU surveyed that might convert, 90 percent of the postage evidencing was postage meters and PC postage while 10 percent was stamped<sup>7</sup> and for the relatively new customers in the NAPM survey who had converted, 40 percent reported entering 40.6 percent of the mail using only meters, 10 percent reported entering 8.2 percent of the mail using only stamps, and 35.6 percent reported entering 40.6 percent of the mail using stamps and meters. Fourteen and four tenths percent evidently did not respond to the NAPM survey question, for eight percent of the mail.

Because the Joint Commenters do not present the findings of the NAPM survey in a way which allows one to look at the overall percentages of mail in the

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<sup>5</sup> See Joint Comments of the American Bankers Association, the Bank of America Corporation, the Direct Marketing Association, Discover Financial Services, the Major Mailers Association, the National Association of Presort Mailers, and the National Postal Policy Council (hereafter, "Joint Comments" and "Joint Commenters").

<sup>6</sup> Joint Comments, p. 16.

<sup>7</sup> See Joint Comments, p. 15; see also p. 16 for those surveyed most likely to convert.

survey as either metered/PC postage or as single piece, and because the detailed survey results are non-public, one cannot calculate the weighted average mail processing and in-office delivery costs when single piece is factored in along with metered. For both the NPPC/MMA and GMU surveys, however, such a weighted average cost is possible to calculate from the results noted by the Joint Commenters. We accomplish this in Section B below.

One problem with the argument made by the Joint Commenters that heterogeneity is a new element of conversion mail that should lead the Commission to raise benchmark costs is that consolidators have throughout their history had to contend with residual single piece mail that was stamped. There is nothing new here in the percentages reported by the NPPC/MMA and GMU surveys that stamped mail continues to be a residual (2.5 percent to 10 percent) part of an evening's presort activities as it has been in the past.

A second problem with their argument is that single piece metered mail has several of the characteristics that stamped mail does, and to this extent many of the higher costs attributed to stamped mail are also built in to the cost of metered letters. These include the types of envelopes acceptable or optimized for automation mail, the sizes of envelopes, what type faces can be read by an OCR that are also in conformance with Postal Service regulations, the color of envelopes, the absence of facing, a barcode clear zone.

Not only do the Joint Commenters exaggerate the heterogeneity of single piece stamped mail relative to single piece metered mail, they also underestimate the percentage of stamped mail that is clean mail such as credit card payments, business reply envelopes, and the like.

The heterogeneity of First Class Single-Piece mail is mainly an argument concerning mail originating in households, not offices. The overwhelming percentage of this is stamped. The single piece letter volumes for FY2009 by indicia are

listed below in **Table One**, since the latest Household Diary Study (HDS) available is for FY2009. While some stamped mail may originate from offices, a high percentage originates from households. From the Household Diary Study for FY2009, 12.19 billion First Class mail pieces were sent from households to non-households, and 5.48 billion was sent by households to households. Of the 12.19 billion pieces, 2.44 billion was transactions mail sent to phone/utility companies, 1.83 billion was transactions mail sent to credit card companies, 1.22 billion was responses to advertising mail, and 7.31 billion pieces was “all other business mail”.

<b>Table One Single Piece Letters by Indicia FY2009</b>		
<b>Indicia Type</b>	<b>Pieces</b>	<b>Percent of Total</b>
Permit Imprint	1,792,773,604	5.97%
Metered	1,278,167,437	4.26%
Stamped	17,258,158,659	57.50%
PVI	102,539,313	0.34%
IBI	9,540,886,144	31.79%
Other	43,939,529	0.15%
<b>Total</b>	<b>30,016,464,686</b>	
Source: RPW Report - First Class and Standard Mail by Indicia FY2009.		

The First Class mail totals from the Household Diary Study originating in households totals 17.67 billion pieces, very close to the stamped letters total of 17.26 billion from the RPW report listing letter volume by indicia.<sup>8</sup> The household

<sup>8</sup> This does not mean that all household originated mail is sent stamped; some is sent by other indicia and some stamped mail is sent by non-households. The HDS data is for letters and cards, one reason the HDS totals exceed the letter totals by indicia.

to household mail of 5.48 billion pieces is the closest figure one can estimate for Single Piece mail that is clearly heterogeneous, and that constitutes 31 percent of all household originated mail.

However, it is not at all clear that the other 12.19 billion mail pieces originating from households and sent to non-households is heterogeneous. The reason is that almost all such mail is transactions, advertising or “other business” mail, and therefore quite likely originated with non-households and included a return envelope. Whether these are stamped or pre-paid return envelopes with other indicia, they are all compatible in color and size with automated mail processing, clearly addressed in the bar-code clear zone, and with an 11-digit barcode. This is clean mail and clearly homogeneous with respect to the attributes above. All that differentiates such mail from single piece metered mail is the use of a stamp or some prepaid indicia rather than a postage meter.

Thus, a fairly large percentage of the sixty-nine percent of mail going from households to non-households is homogeneous; put differently, it is no more heterogeneous than metered mail. Indeed, it could be argued that single-piece metered letters, proposed by many in their initial comments to be the benchmark, are more heterogeneous than reply envelopes included with transaction and advertising mail. Single piece metered letters are much less likely to have an 11-digit barcode. The addresses are typed, but not necessarily in the barcode clear zone. The envelopes tend to be standard letter size, while reply mail envelopes are shorter in length and optimized for automated mail processing. There is no assurance with single-piece metered letters that envelope colors are compatible with automated processing.

The HDS data do not state whether household originated mail is stamped or has a pre-paid indicia other than a stamp, but we can approximate this breakdown. According to the Joint Commenters, between 2.5 percent and 10 percent of mail received by consolidators is stamped and we assume that consolidators

produce 50 percent of presort mail annually. Assume also that the other 50 percent of presort mail is produced directly by major mailers and that none of that mail is stamped. Single piece stamped letters received by consolidators would range between 555 million pieces and 2,405 million pieces annually using the 2010 ACR, out of a total of 15,334 million stamped letters for FY2010. Thirty-one percent of this is household to household mail and we assume all of that is stamped, while 69 percent of it is household to non-household mail, based on 2009 HDS data, the latest available, which is applied to the 2010 data. The percentage of household originated mail sent to non-households that has indicia other than stamps would then be between 5.2 percent and 22.7 percent, of 10,580 million pieces that is household to non-household mail for FY2010, or between 550 million and 2,402 million pieces.

Applying those percentages to the FY2009 HDS, single piece stamped mail received by consolidators would range between 621 million pieces and 2,706 million pieces, or 2.7 percent to 10.7 percent of all mail received by consolidators. This is fairly consistent with the 2.5 percent to 10 percent range reported by the Joint Commenters. It would also mean that of the total household to non-household mail for FY2009 of 12,190 million, indicia other than stamps were used for between 621 million and 2,706 million pieces.<sup>9</sup>

The Joint Commenters' argument about heterogeneity would work – if at all – only in those cases where stamped office mail is *not* a small residual of the evening's average mail that is or might be processed, and the cost profile of the heterogeneous benchmark is bifurcated between those customers who mainly stamp their mail and those who mainly meter their mail or use PC postage. However, so far as the reported data of the public GMU survey is concerned, by volume a very high percentage of today's conversion mail is metered (including IBI, Permit Imprint and PVI mail) and only a small percentage is stamped.

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<sup>9</sup> See Appendix II for a derivation of these statistics.

B. Collection Costs in a Metered Benchmark Would Greatly Exceed the Benchmark Costs of Heterogeneous Conversion Mail and Move Rate Design Close to Full Attributable Cost Differences or “De-Linking”

The benchmark proposal of the Joint Commenters has nothing to do with their argument about the heterogeneous make-up and costs of today’s conversion mail. They suggest that because measuring such costs would be very difficult empirically, instead all collection costs should be included in the measurement of costs avoided, along with mail processing and delivery costs. This is a total non-sequitur. If three conditions must be met by the benchmark chosen, as the Joint Commenters maintain, then one benchmark cannot be cited as fulfilling one condition, while an entirely different benchmark is put forth to satisfy other(s).

What the Joint Commenters argue is that since it is difficult to measure the extra costs which would have to be added into the benchmark to account for heterogeneity (as compared to BMM), even though that is theoretically correct<sup>10</sup>, then as a substitute for those extra costs, one should add collection costs to mail processing and in-office delivery costs of the benchmark. The clear implication is that the two benchmarks must be roughly equivalent in cost for one to substitute for the other.

While the worksharing related cost data for metered letters is calculated by the Postal Service, the average total cost of single piece includes both metered and stamped mail. However, it is possible to estimate the average unit cost of stamped letters alone, since we also know the weights of metered and stamped letters. This derivation is found in Appendix Table A-1.

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<sup>10</sup> By theoretically correct, what the Joint Commenters evidently mean is an argument advanced in 2006 on behalf of Pitney Bowes. See R2006-1, PB-T-1, Direct Testimony of John C. Panzar, pp. 28-29.

The average worksharing related cost of stamped letter mail (including “other”) without any metered letter costs influencing that total is a good first approximation as to how the heterogeneous make-up of stamped letters compares with the relatively homogeneous cost make-up of metered letters.

A benchmark consisting of homogeneous metered<sup>11</sup> mail from the 2010 ACR has combined worksharing related mail processing and in-office delivery costs of 19.19 cents, as shown in the second row of numbers in **Table Two**. Using the NPPC/MMA survey finding that 2.5 percent of the new benchmark is single piece stamped and 97.5 percent is metered<sup>12</sup>, the cost of a heterogeneous benchmark is 19.21 cents, 0.02 cents higher than the “clean” metered benchmark. Using the GMU survey that 10 percent by indicia was stamped mail and 90 percent was metered or PC postage, the cost of the heterogeneous benchmark is 0.09 cents higher than the “clean” or homogeneous benchmark.<sup>13</sup> If 50 percent of current conversion mail is stamped, the cost of the heterogeneous benchmark is 19.63 cents.

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<sup>11</sup> Metered category includes metered, IBI, and a small amount of PVI mail (See Docket RM2010-13, Response of USPS to ChIR No. 1, Resp.ChIR.No.1.pdf, p. 9).

<sup>12</sup> Joint Comments, p. 16.

<sup>13</sup> See Joint Comments, p. 15; also see p. 16 and p. 18-19 for more of the GMU survey results for those surveyed who would be most likely to convert. While the overall breakdown of mail for this group consisted of 5 percent single piece, only about half the respondents reported using a meter, while the other half use stamps.

**Table Two**  
**Worksharing Related Mail Processing and Delivery Unit Costs**  
**for FCM Heterogeneous Letters**  
**(Based on Joint Commenters & USPS Methodologies)**

Using USPS Proposed Methodology for Delivery Unit Costs (cents)			
	WS Related Mail Processing*	Delivery w/o Collection	Total Unit Cost
Single Piece Stamped Letters	14.71	5.36	20.07
Single Piece Metered/IBI/PVI Letter:	13.41	5.77	19.19

Heterogeneous Letter Mail Unit Costs (cents)			
	Mail Processing	Delivery	Total Unit Cost
2.5% SP & 97.5% Metered	13.44	5.76	19.21
10% SP & 90% Metered	13.54	5.73	19.28
50% SP & 50% Metered	14.06	5.57	19.63

Using Joint Commenters Methodology (Unit Costs in cents)				
	WS Related Mail Processing	Delivery Unit Cost w/o Collection	Collection	Total Unit Cost
Single Piece Stamped Letters	14.71	5.36		20.07
Single Piece Metered/IBI/PVI Letter:	13.41	5.77	3.81	23.00

\*See Appendix I, Table A-1 for the derivation of the SP stamped letters MP unit cost.

Source: RM2010-13, USPS Response to CHIR Request No. 1.

The question is whether these extra costs associated with heterogeneity approximate the costs of collection. From **Table Two** we can make such a comparison.

Metered benchmark:	19.19 cents
Heterogeneous benchmark:	
(NPPC/MMA survey)	19.21 cents with 2.5% stamped
(GMU survey)	19.28 cents with 10% stamped
High heterogeneity boundary	19.63 cents with 50% stamped
Homogeneous benchmark w/ collection:	23.0 cents with 100% metered

As seen from **Table Two**, there is no plausible mix of metered and stamped letters that would come close to 23 cents by adding collection costs to metered letter costs. Even if the heterogeneous stamped letter cost was

weighted at 50 percent of the mail mix with metered, the combined cost would only be 19.63 cents.<sup>14</sup> Neither the three surveys reported by the Joint Commenters nor the five presort bureau statements submitted by NAPM suggest that stamped mail is anything close to 50 percent of today's conversion mail. That residual stamped mail is closer to 2.5 - 10 percent of today's conversion mail.

Nevertheless, the Joint Commenters make the argument that adding collection costs to a metered mail benchmark creates the best approximation to what the costs of heterogeneity in the new benchmark would be if they could be readily measured.

A single proxy can be used to smooth variations due to mail heterogeneity and to avoid the complexity and data limitations inherent in modeling a composite cost proxy. The single proxy that most closely approximates the cost characteristics of an empirically derived base group is "Metered" mail. The new base group should reflect the mail processing (cost segment 3), carriers' in-office (cost segment 6) and collection (cost segments 7 and 10) costs for "Metered" mail.<sup>[15]</sup>

This argument is untenable. Adding collection costs produces a cost so far out of line with any plausible estimate of the costs of heterogeneity that adopting it as a proxy would be completely arbitrary, and would result in rates bearing little relationship to avoided cost.

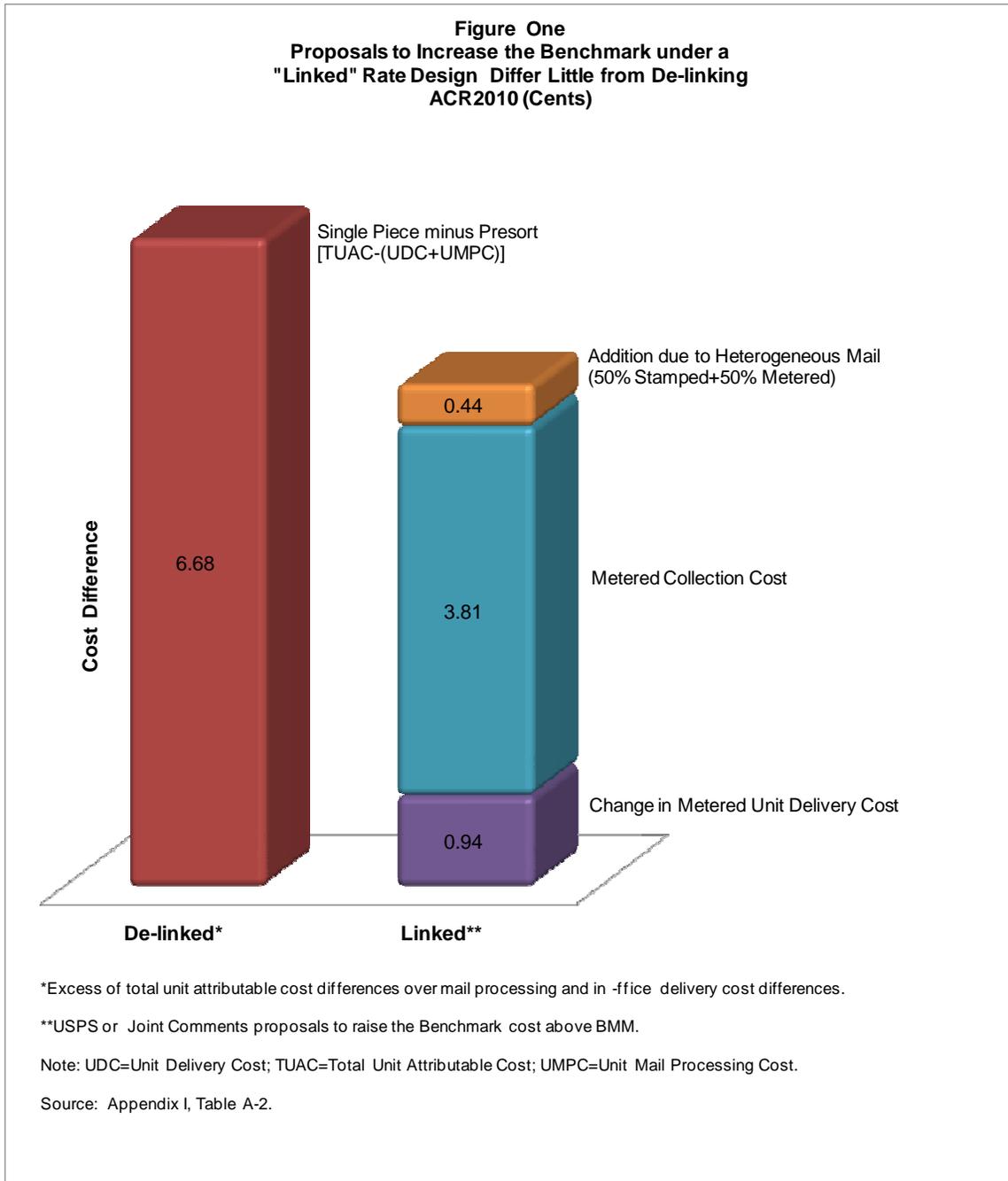
As shown in **Table Two**, the Joint Commenters' proposal for a new benchmark including collection costs would be more than three cents higher than an empirically implausible conversion mail mix of 50 percent stamped and 50 percent metered, 23 cents versus 19.63 cents. Any *plausible* mix of heterogene-

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<sup>14</sup> As noted, a great deal of stamped mail is low cost mail such as credit card and utility bill payments. This letter mail is machine readable and prebarcoded with an 11 digit barcode, and the credit card bill payments in particular have an envelope size that optimizes pieces fed per hour in automation presort operations. When such low cost stamped mail is weighted along with higher cost heterogeneous stamped mail, it is not surprising that the worksharing related unit costs of stamped mail are only about one cent higher than those for metered mail.

<sup>15</sup> Joint Comments, p. 20.

ous stamped and metered letters would be a fraction of a cent above the current metered benchmark. Therefore, the inclusion of collection costs in a metered mail benchmark cannot ever be equivalent to the costs of heterogeneous stamped mail; it will always be substantially larger.



**Figure One** helps us to understand a critical point not raised as yet by anyone in this proceeding. Under de-linking, which the Commission firmly rejected in Order No. 536, presort rates would be based on the total attributable cost difference between single piece letters and presort letters. The additional cost difference de-linking would afford over and above mail processing and in-office delivery cost differences under today's rate design is 6.68 cents, based on 2010ACR data. This is shown in the figure by the bar graph labeled "De-linked." Under de-linking, current presort rates would be reduced by an average of 6.68 cents.

The question is: under the proposals made in this proceeding under a linked rate design, would the outcome be materially different than under de-linking, or are these proposals just a back-door way of generating the same results in the pricing of Presort that would occur under de-linking? The question can be answered by asking how far above the current BMM benchmark the proposals in this proceeding would raise the benchmark. The answer to the question can be found in looking at the second bar graph to the right of the first in **Figure One**.

The height of this bar graph is 5.19 cents, 78 percent of the reduction in presort rates that would occur under de-linking. Under a linked rate design contemplated in this proceeding, the three major proposals made to increase the current BMM benchmark would lead to a 5.19 cent reduction in presort rates.

The largest of the three proposals for raising the benchmark is that of the Joint Commenters. By increasing the benchmark from adding collection costs to it, this proposal alone would reduce presort rates by fifty-seven percent on average in the direction of a de-linked rate design. The Postal Service's proposal for changing the way delivery costs are measured for benchmarking purposes would raise the benchmark by nearly another cent. Increasing the benchmark to reflect the heterogeneity of today's conversion mail as viewed by the Joint Commenters

could raise the benchmark by one-half a cent, and less if smaller proportions of stamped mail are adopted. The choice of 50 percent here is based on the GMU survey, whose results by potential users show half using a meter currently and half using stamps.<sup>16</sup>

### C. Further Considerations Concerning the Joint Commenters' Collection Cost Arguments: How Much Does Collection Really Cost?

The Joint Commenters' proposal to adopt metered mail collection costs as a "proxy" for the collection costs of conversion mail (said to be too heterogeneous to permit precise cost analysis) seems to rest on the argument that since some conversion mail must be collected, that mail has the same collection cost as the average for Single-Piece metered letters as a whole. Since information supplied by the Joint Commenters themselves indicates that conversion mail does not share the collection characteristics of metered mail in general, this argument is evidently unsound as a factual matter. That Single-Piece metered letters exhibit a certain per-piece collection cost does not mean that the subset of these letters regarded as conversion candidates has the same cost.

According to the Joint Commenters' Table 2<sup>17</sup>, 82.16 percent of that share (about half the total) of conversion mail which did require collection was tendered to the Postal Service at the customer's loading dock (44.52 percent); in sacks, tubs, or trays in the building lobby (28.15 percent); or by both methods (9.49 percent). It is a common-sense inference from these figures that, although not entered at a postal facility (and thus requiring collection in the broad sense of the term), most conversion mail was tendered in bulk quantities. Table 2 lists other ways of tendering mail to the Service: handing it to the carrier, leaving it in the

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<sup>16</sup> The Joint Commenters' discussion of GMU survey results have three distinct percentages for stamped indicia. On page 15, the survey results show that for existing presort customers almost 10 percent was stamped. On page 16, for those who might consider using presort services, stamped mail was currently 5 percent. On pages 18-19, about 50 percent of the mailers who would consider using presort services reported using a meter, while the rest used stamps.

<sup>17</sup> Joint Comments, p. 12.

customer's mailbox, using a building's mail chute, or depositing it in a blue collection box. No line of the table reporting volumes tendered by one or a combination of these methods accounted for more than 2.92 percent of collected conversion mail.

Suppose, however, that it were argued in response that the 3.811-cent collection cost reported for metered Single-Piece letters might indeed be an accurate reflection of the collection cost of the 82 percent of conversion mail tendered on loading docks or in trays, sacks, or tubs. This contention would require us to assume either (i) that collecting mail tendered in bulk quantities costs approximately the same, per piece, as collecting mail dropped in blue boxes or left for the carrier a few pieces at a time, or (ii) that the profile of collection methods reflected in Table 2 also applies to metered letters as a whole. The first assumption, if not inherently incredible, would at least require some explicit justification (which Joint Commenters do not provide).<sup>18</sup> The second requires the further assumption that the category of metered Single-Piece letters as a whole is dominated by bulk-quantity mailings in the same way as the conversion mail analyzed in Table 2. That this is most unlikely can be seen by comparing average collection costs for stamped and metered Single-Piece letters. The Postal Service's response to Chairman's Information Request No. 1 shows stamped and metered collection costs of 3.844 cents and 3.811 cents, respectively – a difference of only 0.87 percent. Stamped mail is sent largely by households<sup>19</sup> and smaller businesses and for that reason is deposited singly or in smaller quantities. That the unit collection costs are practically the same for both types of indicia implies that metered Single-Piece letters likewise frequently enter the postal system in small quantities. If, on the other hand, the bulk-quantity mailings reflected in the Joint Commenters' Table 2 dominated the category as a whole in the same way they

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<sup>18</sup> Could it be shown, for example, that collecting a tray of 400 metered letters from a building lobby would cost the Postal Service 100 times as much as collecting four similar letters left for the carrier in a reception area "Out" box?

<sup>19</sup> According to the Household Diary Study for FY 2009, Tables 3.1, 4.1, households sent about 16 billion pieces of First-Class letter mail in that year – approximately 53 percent of total CRA Single-Piece letter volume.

dominate conversion mail, one would expect the unit collection cost for metered letters to be substantially lower. That it is not implies that the conversion mail analyzed in Table 2 has a much lower unit collection cost than the average for metered letters. Adding that average collection cost into a benchmark intended to represent conversion mail would therefore overstate the cost avoided by actually converting that mail to Presort.

This matters for several reasons. First, § 3622(e)(2) requires that discounts not exceed cost avoided, unless one of the exceptions applies (which does not appear to be the case here). A discount incorporating an inflated avoidance figure for one cost element will violate this standard unless, by happenstance, there is an offsetting underestimate elsewhere in the construction of the rate.

Second, inflation of discounts in pursuit of “marginal” conversion to worksharing becomes problematic once we consider (as the statute requires) the price structure of First-Class Letters as a whole. In this connection, an important distinction, mentioned previously (Section I, above), must be emphasized again.

The object of this Docket is not to create a new worksharing discount category for metered Single-Piece letters which, arguably, might still convert to Presort. It is to find a benchmark for the construction of the Presort tariff *as a whole*. The necessity of considering the effects of any benchmark on the entirety of First-Class Letters is ignored by the Joint Commenters, who treat the question simply as one of enabling conversion of some part of the remaining Single-Piece Letter mailstream. This is a basic deficiency in the Joint Commenters' approach.

It bears repeating that the benchmark which will emerge from this proceeding will become part of an established ratemaking system in which (i) a Postal Service which for the foreseeable future will need to use all the rate authority available to it under the price cap, is (ii) correspondingly limited in the rev-

enue increases it can obtain under the cap, and is (iii) similarly prevented by the class-by-class structure of the cap from shifting revenue burdens between classes to alleviate the bad side effects of an inflated benchmark in First Class. The additional dollars such a benchmark would redirect from the Postal Service to bulk mailers must be recovered elsewhere in First Class – in other words, from Single-Piece. Since, as the Commission observed in Order No. 536<sup>20</sup>, Single-Piece is actively responsive to price changes, consumption of Single-Piece Letter mail will necessarily be discouraged.

In volumetric terms, this is far from an insignificant problem. The Joint Commenters exclude stamped letters from the segment of Single-Piece which they consider conversion-ready. In FY 2010, 15.3 billion of the 27.1 billion Single-Piece letters, or 56.5 percent, were stamped.<sup>21</sup> Only the remaining 11.8 billion are potential new targets for the rates based on the new benchmark. It bears emphasizing that it is the proponents of a higher benchmark who exclude from the spectrum of potential conversion mail some 56 percent of Single-Piece Letter volume. It is therefore not an answer to the “just and reasonable schedule” question this situation raises, under § 3622(b)(8), that the proposed benchmark might be “more efficient” for First-Class considered as a whole (i.e., without regard to the Single-Piece/Presort division). That argument, if valid, would not abolish the product distinction between mail that is *or could become* Presort and mail that will remain in Single-Piece. As long as that distinction remains, the § 3622(b)(8) question will be present, and it will be the Commission’s responsibility, as it has been in past cases under both the present statute and the 1970 Act, to reach an appropriate balance between the competing demands of theoretical efficiency and a just and reasonable rate schedule. That balance cannot be achieved by incorporating in the benchmark a collection component which overstates the

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<sup>20</sup> Order No. 536, p. 13, and particularly fn. 6. The Commission stated that there was “no assurance” that Presort is more price elastic than Single-Piece now, or in the future.

<sup>21</sup> Docket ACR2010, U.S. Postal Service, First-Class Mail Revenue, Pieces and Weight by Weight Increment, Shape, and Indicia, FY 2010.

costs which would actually be avoided and thereby causes a revenue deficiency which must be recovered from Single-Piece mailers.

#### E. Summary

The Joint Commenters' proposal to include metered mail collection costs in the new benchmark should be rejected, because –

- The notion that mail at the margin of conversion is today materially different from what it was a decade ago is refuted by history;
- Adding in metered mail collection costs as a “proxy” for the cost effects of (alleged) heterogeneity of conversion mail produces a benchmark cost greatly in excess of any plausible estimate; and
- The Joint Commenters themselves demonstrate that conversion mail does not share the collection characteristics of metered letters as a whole, but are fairly certainly much cheaper to collect – so that using average metered letter collection cost would improperly inflate the benchmark and the resulting discounts.

### III. COMMENTS FROM FIVE NAPM MEMBERS CONFIRM THAT THE NATURE AND MIX OF TODAY'S CONVERSION MAIL IS THE SAME AS THE PAST

#### A. BMM, Single-Piece Metered, and the Frequency of Stamped Mail: Evidence from Five NAPM Members

All five submissions by NAPM members use the exact same wording to make two points: (1) conversion mail today has “the characteristics of metered

*collection mail*”; (2) “the discounts offered . . . should reflect the *full cost differences* between workshared First-Class mail and metered collection mail.”<sup>22</sup>

There is a great lack of clarity in the Joint Commenters’ initial comments and the statements of five member consolidators submitted by NAPM as to whether the added costs for a customer to qualify for worksharing discounts are assumed by the customer or the consolidator. For example, if the customer in the course of entering a contract with a presort bureau takes responsibility for, and does, the work for things such as address hygiene and mail piece design<sup>23</sup>, then it does not increase the costs of the consolidator. It is hard to see how consolidators like NAPM members could argue for extra discounts based on costs that they themselves do not incur. Moreover, the existing level of discounts and the portion the customer receives are obviously sufficient for the customer to enter a contract with a presort bureau.

Florida Mail and Print Solutions Inc. is “a relatively small presort bureau”. It “automates around 45,000 pieces of First Class metered mail” per day.<sup>24</sup> Of particular importance, Florida Mail points out that all its customers have to meet certain “guidelines” and “follow certain standards.” The bureau notes: “The only reason they pay attention to it [standards] now is because they receive a discount. If there was no discount there would be no reason to enforce the guidelines we have put in place.”<sup>25</sup>

What this discussion makes clear is that the pre-conversion mail of established no less than new customers looks different, sometimes markedly different,

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<sup>22</sup> Comments of On-Line Data, p. 3 (emphasis added). See also the Comments of Florida Mail at p. 3, para. 1; Presort Services Inc. at p. 3, para. 1; TC Delivers, Inc. at p. 3, para. 1; and United Mailing Services, Inc. at p. 3. United does not use the term “metered collection mail” though it is clear from the discussion that metered mail is what they convert.

<sup>23</sup> See Joint Comments, p. 19.

<sup>24</sup> Comments of Florida Mail, pp. 1-2.

<sup>25</sup> Comments of Florida Mail, p. 3.

than the mail they send a presort bureau because of guidelines and standards they have to follow. Clearly, these guidelines and standards help qualify the mail for a discount, but they are not part of the worksharing done by a presort bureau. As the quotations from Florida Mail make clear, these costs are borne by the customer as part of the contract to receive a discount, not by the presort bureau. Florida Mail indicates that at a minimum all its customers submit their mail in 1 or 2 foot trays and that it is organized and properly faced. The mail must be sealed properly but is not to be stuck together, the barcode clear zone must be adhered to, and all other factors that would prevent the mailpiece from running through an OCR must be eliminated. The only time a presort bureau incurs costs associated with any of the above factors is when a client fails to follow them, and that is a very small percentage of the mail the bureau receives. These pieces are either fixed at the bureau or sent back to the customer. The portions of the worksharing discount that go to the consolidator and the customer must each be sufficient to induce the work done by the customer and the worksharing done by the consolidator once they enter a presorting contract.

On-Line Data makes points nearly identical to Florida Mail. “I can see no basis for assuming that most mailers would consistently put mail in trays if they didn’t have to in order to get a discount.”<sup>26</sup> On-Line makes the same point about envelope sizes, typefaces that can be read by OCRs, and that are required by USPS regulations, color of the envelope, barcode clear zone, sealed properly and not sticking together, proper facing.

On-Line also notes that about “1 percent of the mail On-Line Data presents to the USPS consists of residual, full paid mailpieces that we tried, but could not qualify for a discount, but still had to tray up to present to the USPS.”<sup>27</sup> This figure is in line with the surveys the Joint Commenters have made.

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<sup>26</sup> Comments of On-Line Data on Consideration of Technical Methods to Be Applied in Workshare Discount Design, p. 4.

<sup>27</sup> *Id.*, p. 6.

Finally, On-Line Data makes an important observation that negates the Joint Commenters' assertion that the conversion mail mix today is different from the BMM of bygone years. **"The point is if there ever was any BMM it converted to worked shared mail a long, long time ago"**<sup>28</sup> Since that time and up through the present, conversion mail has mainly been metered with a residual of single piece. Consolidators have always worked with clients to eliminate stamped mail from what they send as well as having them follow other standards and guidelines that the consolidator sets before it will accept a client's mail for pre-barcoding and presortation.

As this quote from On-Line Data makes clear there is no more extra work today associated with clients' mail than there has been in the distant past, and consolidators have processed this mail at discount levels in effect at the time for many, many years. If the discounts of the past had not been sufficient to cover the costs (including a normal profit) of residual mail that is stamped, that is stuck together, that is not properly faced, or otherwise problematic for an OCR, consolidators would not have processed such mail and/or customers would not have hired the consolidator. Claiming such work is a new cost that must be compensated with an increase in discounts is simply a bogus argument.

Presort Services, Inc. also emphasizes the work that its customers, not itself, must do in order to receive a discount. "There is no reason to assume that most mailers would put mail in postal trays if they didn't have to in order to get a discount. And even if mail is presented in trays, there is no basis for assuming that all the mail in these trays would be properly faced, Move Update compliant, sealed, but not stuck together, have machine readable addresses, or be in enve-

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<sup>28</sup> Ibid. (emphasis added).

lopes that provide the needed contrast or have a barcode clear zone.”<sup>29</sup> And, again: “It takes us many, many hours of working with our customers at the beginning, and constant monitoring and reminding to get our customers to submit mail to us that we can process for workshare discounts.”<sup>30</sup> The point, however, is that this has *always* been true, it is not a new set of costs that consolidators have to contend with. And while not made explicit in the structure of discounts and measurement of costs avoided, these costs have always been covered by discounts. If they had not been, the consolidator would not be in business. Not today nor in the past.

T. C. Delivers Inc. notes, regarding its customers: “But they do what we need them to do because they want the discount. They don’t do it just to make us happy.”<sup>31</sup> And again, as part of a discussion of what customers do before they can enter mail at a consolidator: “Nor, absent a discount, would mailers have any reason to be concerned if some of their envelopes are stuck together or are unsealed when presented to the USPS or their presort bureau.”<sup>32</sup>

T. C. Delivers, Inc. makes statements in its submission to the Commission via NAPM that are identical to those of other NAPM members’ submissions. For example, “It takes us many, many hours of work with our customers at the beginning and constant monitoring and reminding to get our customers to submit mail to us that we can qualify for workshare discounts.” This quote is identical to that made by Presort Services, Inc. above. A second example is that T. C. Delivers, Inc. makes an identical comment (in bold below) to that made by On-Line Data above at p. 6 of their comments. T. C. Delivers states “What you need to under-

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<sup>29</sup> Comments of Presort Services, Inc., on Consideration of Technical Methods to Be Applied in Workshare Discount Design, p. 4.

<sup>30</sup> *Id.*, p. 6.

<sup>31</sup> Comments of TC Delivers, Inc., on Consideration of Technical Methods to Be Applied in Workshare Discount Design, p. 8.

<sup>32</sup> *Id.*, p. 5.

stand is: **if there ever was any BMM it converted to workshared mail a long, long time ago.**<sup>33</sup>

The use of identical phraseology in these comments indicates a coordinated effort, and the invocation of “full cost difference” and “metered collection” mail likewise point to specific objectives. Certainly repeated references to “collection” mail seem congruent with the Joint Commenters’ advocacy of including collection costs in the benchmark. “Full cost difference” suggests a *sotto voce* argument in favor of delinking Presort and Single-Piece, a course which the Commission has already more than once rejected.

Finally, United Mailing Services, Inc., a firm in business since the early 1980s states: **“I simply do not know what this mail [BMM] is, and have never found a customer that understands it either. . . . THIS MAIL SIMPLY DOES NOT EXIST.”**<sup>34</sup> If BMM mail has not existed in the 20 years United has been in business, then clearly what it has been processing all these years is metered letters, and it has received a workshare discount for these that includes all the costs that consolidators are claiming are “new costs” as conversion mail allegedly evolved from BMM to single piece metered.

In light of the NAPM member statements, the Joint Commenters have failed to consider two important points in arriving at their conclusion. First, BMM has not existed (if it ever did) for a very long time, and not just in recent years. Second, what has constituted the conversion mail in the past does not materially differ from today’s conversion mail, in that a small residual of that mail was and remains stamped.

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<sup>33</sup> Id., p. 8 (emphasis added).

<sup>34</sup> Comments of United Mailing Services, Inc., on Consideration of Technical Methods to Be Applied in Workshare Discount Design, p. 3 (emphasis added).

The Joint Commenters conclude that “empirical analyses of the survey data conclusively establish that BMM is no longer a valid base group for First-Class Mail letters.”<sup>35</sup> However, over a decade ago, at least two groups representing large mailers questioned whether BMM existed then, MMA and ABA&NAPM.<sup>36</sup>

After two rate cases in which this benchmark has been used to measure costs avoided following a suggestion made in the Commission’s O&RD in R90-1, it is still not clear that bulk metered mail is an actual, real world mail stream against which to measure savings from worksharing. It comes closer to resembling the Postal Service’s abandoned hypothetical construct of an identical-piece-but-for-presorting, than a real world benchmark like all non-prebarcoded, non-presorted single piece mail.<sup>37</sup>

Furthermore, if the mix of conversion mail was not fundamentally different over a decade ago than recently, then the Joint Commenters case for a higher benchmark falls apart, since that higher cost benchmark depends critically on assumed changes in the nature and mix of conversion mail between yesterday and today with stamped mail constituting a much larger percentage of the mix. The surveys conducted by the Joint Commenters do not support their assertion that the mix of mail today includes substantially more stamped mail than the past. The only material change at the margin of conversion between yesterday and today revealed in the survey results is in the size of the potential customer. Today’s potential customer is smaller than those in the past.

#### B. A Comment on “Real World” Versus Hypothetical Benchmarks

While the Commission has stated in its Order No. 536 (p. 2) that BMM is no longer suitable as the benchmark, it did include BMM in its list of possible

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<sup>35</sup> Joint Comments, p. 17.

<sup>36</sup> Docket R2001-1, MMA Brief, pp. 8-9; Docket R2000-1, ABA&NAPM-T-1, pp. 19-21. Similar statements were made as far back as Docket R97-1.

<sup>37</sup> Docket R2000-1, ABA&NAPM-T-1, p. 18, lines 16-22.

benchmarks to adopt.<sup>38</sup> As a benchmark, while BMM has probably always been more of a hypothetical construct than an actual mailstream, the prior benchmark used by the Postal Service was also hypothetical.

In Docket R97-1, ABA/EEI/NAPM stated

For many years there has been a significant split between the Postal Service and the Commission insofar as what “benchmark” to use for the purpose of calculating worksharing discounts for First-Class letter mail. The Postal Service has based its calculations on a cost avoidance methodology using a purely hypothetical mailstream: a letter identical in all respects to a First Class presorted or automation compatible letter except that it moves through the mail processing and delivery systems as a non-workshared letter.<sup>39]</sup>

While the Joint Commenters base their entire opposition to BMM on the grounds that their surveys show it does not currently exist, the hypothetical nature of any benchmark alone is clearly not sufficient as an argument to abandon it or never create another hypothetical benchmark. BMM was supported by the Commission, and replaced the Postal Service’s support for and use of an identical piece benchmark, but it bears recalling that both benchmarks were hypothetical in nature.

In some circumstances, hypothetical benchmarks may have offsetting advantages which outweigh the negative that they are hypothetical constructs, and we believe this was likely the case at the time these two were adopted – both the Postal Service’s identical piece benchmark and subsequently the Commission’s BMM benchmark. In the current circumstance, the Postal Service’s admission that BMM was measured all along using the available mail processing costs of metered mail<sup>40</sup> means that the proposed change from BMM to a metered mail

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<sup>38</sup> Docket RM2010-13, Order No. 537, p. 2.

<sup>39</sup> See Docket R97-1, ABA/EEI/NAPM-T-1, pp. 11-17.

<sup>40</sup> See Docket No. RM2010-13, Response of the United States Postal Service to Chairman’s Information Request No. 1, January 18, 2011, p. 3.

benchmark is really no change at all, in that the hypothetical has always been approximated by an actual mailstream. However, changing the definition of this data metric does not mean changing the “real world” values, only the label, at least for mail processing costs. Hopefully this will end this debate, which has been going on for well over a decade.<sup>41</sup>

#### IV. THE POSTAL SERVICE'S INCREASE IN METERED DELIVERY COSTS SHOULD BE REDUCED TO THE OLDER PROXY, AND WOULD OFFSET 0.760 CENTS IN ERRONEOUS FACING AND TRAYING COSTS FOR BMM RECEIVED AS A WINDFALL IN COSTS AVOIDED FOR BULK MAILERS

GCA agrees with many of the comments in the Postal Service's Initial Comments in Docket RM2010-13. Their new measurement of delivery costs for a Metered letter is not one of them, however. The ever changing and always confusing “state of play” for measuring worksharing delivery costs appears to have evolved from Docket R2006-1 in the following manner.

In R2006-1 both the Postal Service and PB asserted that no delivery costs were considered in the development of worksharing discounts.<sup>42</sup> Since R2006-1

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<sup>41</sup> It is understandable that an analyst focusing narrowly on the construction of an individual, specific rate to elicit conversion of candidate Single-Piece letters to Presort would want to be sure that the cost basis of that rate reflected mail which actually existed. If it did not, there would be a risk that the new rate would fail to produce any new Presort volume, since the mail at which it was aimed was simply not there. As we have pointed out elsewhere in these Reply Comments, however, the Commission's task is to find a benchmark which will underpin Presort rates as a whole (including categories which may change in relative importance or even, like Carrier Route Letters, disappear altogether), and to do so in conformity to both §§ 3622(b)(1) and (b)(8). In that broader context, whether the benchmark is based on hypothetical or “real” mail is less important.

<sup>42</sup> On page 11 of its brief in R2006-1, Pitney Bowes notes that the Postal Service deviated from past practice by failing to include any CRA in-office delivery costs in its calculations of worksharing related costs. The Postal Service agreed with that assessment, but claimed as did the Commission that the delivery cost differences among presort rate categories was based solely on differences in DPS percentages. Postal Service witness Taufique then claimed that because there was no indication that there were differences in DPS percentages across presort rate categories, there was no inclusion of delivery costs in the calculation of costs avoided from worksharing. (See Docket R2006-1, Brief of Pitney Bowes Inc., December 21, 2006, p. 11; USPS witness Taufique, response to POIR No. 5, June 29, 2006, pp. 4-5.)

the Postal Service, following the Commission, claims to have progressively relied on DPS percentages to determine the spreads in the delivery costs. However, the Postal Service through the 2010 ACR has also relied on non-automation MAADC delivery costs as a proxy for the BMM benchmark and for non-automation MMAADC delivery costs. That cost was 4.84 cents for BMM and Metered mail in the 2010 ACR submitted in December 2010 by the Postal Service.

Before the ink had even become dry in that docket, however, the Postal Service changed the method by which it calculates delivery costs for Metered letters, producing a new estimate of 5.775 cents. It justifies this change for Metered using the peculiar rationale that BMM is no longer the benchmark. Metered letters have never entered the network “faced and trayed”. Now it seems it is no longer appropriate to use trayed and faced non-auto MMAADC presort letters as a delivery cost proxy for Metered.<sup>43</sup> The Postal Service has only now decided to directly measure the delivery costs of single piece Metered mail for the first time for the sake of accuracy, yet it could have made this same measurement any time in the past.

The chart below summarizes the changes in worksharing related in-office delivery costs for Metered and BMM letters that have transpired in Postal Service filings between December’s 2010 ACR and January’s response to a Chairman’s Information Request in RM2010-13.

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<sup>43</sup> See Docket RM2010-13, Initial Comments of the United States Postal Service, p. 10.

		Processing Costs for Facing and Traying	
		Not Trayed 0.960	Not Trayed 0.960
In-Office Delivery Costs	Trayed 4.839	BMM RM2010-13	BMM/Metered 2010ACR
	Not Trayed 5.775		Metered RM2010-13

In the 2010 ACR, it was assumed that both BMM and Metered letters are not trayed (and faced) in mail processing, but already trayed before entering the network insofar as in-office delivery costs are concerned. This is shown in the upper right-hand box above.

In RM2010-13, however, Metered is considered not trayed both in mail processing and delivery. The lower right hand box shows this and in fact it accords with current practice, as does the upper left-hand box.

A. Worksharing Related Cost Data in the 2010 ACR

In the 2010 ACR mail processing cost model the Postal Service did not differentiate the costs of facing and traying in its mail processing analysis as between BMM and Metered.<sup>44</sup> In fact it states that the mail processing costs for BMM are identical to those for Metered letters in every respect.

<sup>44</sup> In its response to ChIR No. 1, the Postal Service is very direct in explaining the history of how BMM mail processing costs came to be identical to metered letter costs. Some intervenor witnesses wanted to increase the costs avoided between BMM and MAADC, and the cost pool costs for facing and traying in the process of cancelation were added to BMM costs despite the fact that BMM does not incur such costs. Using 2010 ACR data, this change increased the costs avoided of MAADC by 0.960 cents, nearly a full cent. In its discussion, the Postal Service states that “an astute observer might notice that the cost models for Metered mail are identical to those for BMM which were filed in the FY 2010 ACR.” (RM2010-13), Response of the United States Postal Ser-

What about delivery costs? In the 2010 ACR in the cost summary for Metered Letters, the delivery cost proxy used for BMM is also used for Metered, and is 4.84 cents. (USPS-FY10-10, file USPS-FY 2010\_fcm\_prst\_letters\_mpfinal.xls.) The reason a non-automation presort machinable MAADC delivery cost has been used as a delivery cost proxy for BMM is because neither BMM nor non-auto MMAADC has to be faced or trayed. By using the same delivery cost proxy for Metered, the presumption must also be that both have identical delivery costs and/or that the two have similar front-end mail characteristics, i.e. neither is faced nor trayed when entering the postal network.

We thus have the entirely contradictory result that while both BMM and Metered are assumed to be mail that has not yet been faced and trayed in mail processing, for purposes of in-office delivery costs, both BMM and Metered are assumed to be mail that has already been faced and trayed.

#### B. Worksharing Related Cost Data in RM2010-13

The Postal Service presents a very different result for this benchmark case. It continues to assume that Metered mail has not yet been faced and

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vice to Chairman's Information Request No. 1, January 18, 2011, pp. 3-4. Traditionally, the mail processing costs of BMM and single piece metered were estimated by dropping the MODS 17 1CANCMP cost pool for cancellation and metered mail preparation for BMM but including it for metered. In R2000-1, for example the unit cost of the 1CANCMP cost pool was 0.3 cents for metered, and the value of that cell was 0.0 for BMM. In recent years including the 2010 ACR this cost pool has been split into two cost pools. One is for mail preparation (1MTRPREP) with a unit value of 0.07 cents, and the other is for 1CANCEL, with a unit value of 0.953 cents. The same values for these two cost pools, rather than zero, are used for BMM in the mail processing cost models. Since the cost for facing and traying between BMM and single piece metered is now identical for these two cost pools, then the difference in facing and traying between the two is no longer being represented in the mail processing costs. The latest detailed definition of CRA cost segments and MODS cost pools was submitted by the Postal Service to the Commission in July of 2010. On page 3-7 is the description for "Cancellation and Mail Preparation (1Cancel, 1MtrPreP). These activities include obtaining mail from windows, drop units, and staging areas; manual and mechanized cancellation of mail; traying canceled mail and loose metered mail for distribution operations; rating short paid mail. These activities primarily handle First-Class mail. For a discussion of BMM, single piece metered, and the older 1CANCMP cost pool, see, e. g., Docket R2000-1, ABA&NAPM-T-1, p. 21, lines 1-15.

trayed in mail processing. However, it now states that Metered mail is suddenly not like non-auto presort MMAADC for purposes of delivery costs, when that has been the convention for years. Nothing has changed about Metered letters that would render this delivery cost proxy inappropriate any longer for Metered letters.

The Postal Service states that “The mail pieces for both categories were also properly faced and entered in trays. With the demise of BMM as the benchmark, the requirement that the [delivery costs in the Metered] mail in the base group be faced and trayed no longer exists.”<sup>45</sup> In-office delivery costs is not where any difference between single piece metered and BMM should be found. Facing and traying are mail processing activities at the front end, not in in-office delivery costs after all letter mail has been fully processed.<sup>46</sup>

All that has changed is that BMM is no longer considered a benchmark, and for that reason and that reason alone, it is said, the Metered delivery cost must be changed. While this change may not be contradictory, it is utterly incoherent as a reason for changing Metered delivery costs and making them different from BMM.

Metered letter in-office delivery costs are now measured “directly” for the first time ever, as are all single piece delivery costs. The newly measured Metered in-office delivery cost yields a number that is above its single piece counterpart, a clear warning sign that something is seriously amiss with the new delivery cost measure for Metered letters.<sup>47</sup>

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<sup>45</sup> Ibid.

<sup>46</sup> BMM and single piece metered letters should not have a different in-office delivery cost. At the point a carrier’s in-office work begins, a metered letter that has been processed and a BMM letter that has been processed are identical pieces. Facing and traying are a MODS cost pool during the initial stages of automated mail processing, not an in-office delivery activity of carriers after mail processing is completed.

<sup>47</sup> BMM and single-piece Metered have now for the first time ever become differentiated in delivery costs, but not in mail processing where the differentiation actually exists. A separate unit in-office delivery cost for Metered could always have been estimated under the BMM benchmark but was not because the in-office delivery costs are the same for Metered and BMM, whether meas-

### C. A Proposed Solution to Problems with the New Delivery Cost Estimate for Metered Letters

Despite the above problems, the Postal Service has nevertheless adopted a higher delivery cost for single-piece metered mail, in part because it is not faced and trayed. The 0.935 difference between these two unit delivery costs, one for (trayed) BMM and one for (untrayed) single-piece metered is almost the same as the combined value (0.960) of the 1CANCEL and 1MTRPREP cost pools in mail processing.

The Postal Service may have unwittingly “embedded” the costs of facing and traying in its unit delivery cost for single-piece Metered by choosing a higher unit in-office delivery cost for single piece metered than non-auto machinable MAADC presort, one which “offsets” the earlier error of the Commission having made BMM mail processing costs the same as Metered.

Worksharing mailers have had the benefit of that artificial increase in the BMM benchmark from having facing and traying costs added to BMM mail processing costs. In the new benchmark, Metered mail should receive a similar benefit in keeping delivery costs at 4.84 cents “as if” Metered Mail were already faced and trayed.

## V. COST POOL AND CRA PROPORTIONAL ADJUSTMENT FACTOR ISSUES

### A. Cost Pool Issues

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ured correctly or not. The unit delivery costs of stamped (or non-metered) single piece letters only (9.2032 cents) is now lower than that calculated for metered letters only (9.5861 cents). Consequently, the unit delivery costs for the new benchmark proposed by the Postal Service have not only increased toward single piece and away from BMM (as measured by the Postal Service in the 2010 ACR, LR 19, cell nor non-auto presort MMAADC.) they have increased beyond and above those for single piece stamped by 0.37 cents. This is not plausible, and seriously undermines the credibility of the Postal Service’s new 5.775 cent estimate of metered letter delivery costs.

Unlike the Postal Service's initial comments on the measurement of delivery costs for its metered mail benchmark proposal, with which GCA is in substantial disagreement, we do find many of the Postal Service's comments on "Cost Pool Classifications" to be a useful perspective in setting forth its rationale for its classifications in this docket, and contrasting its approach with that taken by the Commission in R2006-1 and subsequently, which in its essentials were based on comments and analysis submitted by Pitney Bowes and its witness in that docket.

The Postal Service's proposals in this case, compared to the Commission/PB approach (CPB), would: (1) reduce the costs avoided spreads for AADC, 3 digit and 5 digit letters; while (2) increasing the basic costs avoided between the benchmark and mixed AADC letters by lowering the mail processing cost estimate for mixed AADC from 8.738 cents to 8.174 cents.

The key points made by the Postal Service with which GCA agrees are: (1) the Commission's current cost pool classification is somewhat arbitrary in that the shift of many cost pools into the proportional category compared to R2005-1 (as well as R2000-1 and R2001-1) does not appear to be based on any new or different empirical evidence that these heretofore fixed cost pools in fact vary by presort tier, but from a hypothetical argument made by PB's witness; (2) there is no empirical justification for assigning a percentage of "the Unexpected and Allied/Support cost pools to be proportional based on the metric of what the percentage is of clearly classified cost pools that are proportional; (3) it makes no sense to include as proportional those cost pools that are not modeled, when the very purpose of mail processing modeled costs is trying to divine what cost differences there are between presort rate categories; (4) in particular it does not appear that the following cost pools vary by presort tier: MODS 1PLATFRM, non-MODS ALLIED, MODS 1TRAYSRT, and MODS 1PRESORT; (5) there is not sufficient information to divide with any accuracy a single cost pool into proportional

and fixed parts; (6) there is little reason to continue a three part classification structure.

**Table Three** summarizes some of the major structural differences between the current Commission/Pitney Bowes (CPB) classifications and those proposed by the Postal Service in its initial comments in this case. While the CPB approach classifies 50 cost pools as proportional, the Postal Service would classify 25 as proportional. As the Postal Service points out in its initial comments the CPB approach has the effect of expanding “the differences between rate elements (thus expanding the cost avoidances used to determine available discounts).”<sup>48</sup>

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<sup>48</sup> Postal Service Initial Comments, p. 15

FIRST-CLASS MAIL PRESORT LETTERS CRA MAIL PROCESSING COSTS USPS Version				FIRST-CLASS MAIL PRESORT LETTERS CRA MAIL PROCESSING COSTS PB/Commission Version					
Cost Pools	Total (Cents)	Proportional (Cents)	Fixed (Cents)	Worksharing-Related		Non-WS Related (Cents)	Proportional Cost		
				Proportional (Cents)	Fixed (Cents)		Differences	USPS>PB	PB>USPS
MODS 11	BCS/DBCS	2.520	2.520	2.520			0.000000		
MODS 11	OCR/	0.004	0.004	0.004			0.000000		
MODS 12	FSM 100	0.026	0.026	0.023	0.003	0.000	-0.003334	0.003	
MODS 12	FSM/	0.000	0.000	0.000	0.000	0.000	0.000000		
MODS 12	FSM/1000	0.000	0.000	0.000	0.000	0.000	-0.000022	0.000	
MODS 13	MECPARC	0.000	0.000	0.000	0.000	0.000	-0.000036	0.000	
MODS 13	SPBS OTH	0.008	0.008	0.007	0.001	0.000	-0.001048	0.001	
MODS 13	SPBSPRIO	0.005	0.005	0.004	0.001	0.000	-0.000624	0.001	
MODS 13	1SACKS_M	0.011	0.011	0.009	0.001	0.000	-0.001349	0.001	
MODS 13	1TRAYSRT	0.253		0.221	0.032	0.001	0.220535		0.221
MODS 14	MANF	0.009	0.009	0.008	0.001	0.000	-0.001142	0.001	
MODS 14	MANL	0.251	0.251	0.251			0.000000		
MODS 14	MANP	0.005		0.005	0.001	0.000	0.004686		0.005
MODS 14	PRIORITY	0.010		0.009	0.001	0.000	0.008643		0.009
MODS 15	LD15	0.143	0.143	0.143			0.000000		
MODS 17	1CANCEL	0.115		0.115	0.115		0.000000		
MODS 17	1DISPATCH	0.095		0.095	0.083	0.012	0.082654		0.083
MODS 17	1FLATPRP	0.006	0.006	0.005	0.001	0.000	-0.000798	0.001	
MODS 17	1MTRPREP	0.009		0.009			0.000000		
MODS 17	1OPBULK	0.036	0.036	0.036	0.036		-0.035923	0.036	
MODS 17	1OPREF	0.187	0.187	0.187			-0.187230	0.187	
MODS 17	1OPTRANS	0.036		0.036	0.005	0.000	0.031754		0.032
MODS 17	1PLATFRM	0.488		0.488	0.426	0.061	0.425648		0.426
MODS 17	1POUCHNG	0.009	0.009		0.009		-0.008546	0.009	
MODS 17	1PRESORT	0.034		0.029	0.004	0.000	0.029252		0.029
MODS 17	1SACKS_H	0.011	0.011	0.010	0.001	0.000	-0.001441	0.001	
MODS 17	1SCAN	0.044		0.044	0.038	0.005	0.038307		0.038
MODS 18	BUSREPLY	0.002		0.002		0.002	0.000000		
MODS 18	EXPRESS	0.002		0.001	0.000	0.000	0.001309		0.001
MODS 18	MAILGRAM			0.000		0.000	0.000000		
MODS 18	REGISTRY	0.001		0.001		0.001	0.000000		
MODS 18	REWRAPI	0.002		0.002	0.000	0.000	0.002046		0.002
MODS 18	1EQMT	0.043		0.043	0.037	0.005	0.037242		0.037
MODS 18	1MISC	0.040		0.040	0.035	0.005	0.035210		0.035
MODS 18	1SUPPORT	0.029		0.029	0.025	0.004	0.025275		0.025
MODS 19	INTL ISC	0.004	0.004	0.004	0.001	0.000	0.003659		0.004
				0.000	0.000	0.000	0.000000		
MODS 41	LD41	0.008	0.008	0.008			0.000000		
MODS 42	LD42	0.005	0.005	0.005			0.000000		
MODS 43	LD43	0.172	0.172	0.172			0.000000		
MODS 44	LD44	0.071	0.071	0.071			0.000000		
MODS 48	LD48 EXP	0.000	0.000	0.000	0.000	0.000	-0.000001	0.000	
MODS 48	LD48 OTH	0.046		0.046	0.046		0.000000		
MODS 48	LD48_ADM	0.023		0.023	0.023		0.000000		
MODS 48	LD48_SSV	0.007		0.007		0.007	0.000000		
MODS 49	LD49	0.059		0.059		0.059	0.000000		
MODS 79	LD79	0.053		0.053		0.053	0.000000		
				0.000	0.000	0.000	0.000000		
<b>MODS Subtotal</b>		<b>4.883</b>	<b>3.483</b>	<b>1.400</b>	<b>4.188</b>	<b>0.682</b>	<b>0.014</b>		
BMCS	MANP	0.000		0.000	0.000	0.000	0.000000		0.000
BMCS	NMO	0.000		0.000	0.000	0.000	0.000000		
BMCS	OTHR	0.004		0.004	0.003	0.000	0.003430		0.003
BMCS	PLA	0.008		0.008	0.007	0.001	0.007321		0.007
BMCS	PSM	0.000		0.000	0.000	0.000	0.000005		0.000
BMCS	SPB	0.000		0.000	0.000	0.000	0.000000		
BMCS	SSM	0.000		0.000	0.000	0.000	0.000005		0.000
BMCS	TRAYSORT	0.004		0.004	0.004	0.001	0.003866		0.004
<b>BMC Subtotal</b>		<b>0.017</b>	<b>0.000</b>	<b>0.017</b>	<b>0.015</b>	<b>0.002</b>	<b>0.000</b>		
NON MODS	ALLIED	0.135		0.135	0.118	0.017	0.117562		0.118
NON MODS	AUTO/MEC	0.104	0.104	0.104	0.104		0.000000		
NON MODS	EXPRESS	0.000		0.000	0.000	0.000	0.000066		0.000
NON MODS	MANF	0.005	0.005		0.004	0.001	-0.000652	0.001	
NON MODS	MANL	0.470	0.470	0.470			0.000000		
NON MODS	MANP	0.006		0.006	0.005	0.001	0.004904		0.005
NON MODS	MISC	0.113		0.113	0.098	0.014	0.098339		0.098
NON MODS	REGISTRY	0.001		0.001		0.001	0.000000		
<b>Non MODS Subtotal</b>		<b>0.834</b>	<b>0.579</b>	<b>0.255</b>	<b>0.799</b>	<b>0.032</b>	<b>0.002</b>		
<b>Total</b>		<b>5.733</b>	<b>4.062</b>	<b>1.672</b>	<b>5.001</b>	<b>0.716</b>	<b>0.016</b>	<b>0.242</b>	<b>1.182</b>
<b>Number of</b>									
<b>Proportional Cost Pools</b>			<b>25</b>		<b>50</b>				

Sources: USPS version of CRA mail processing costs is obtained from RM2010-13, Initial Comments of the United States Postal Service, RM10.13.Intl.Cmmnts.xls and the Pitney Bowes/Commission version from RM2010-13, Comments of Pitney Bowes Inc., PB-2.xlsx or ACR2010, USPS-FY10-26.

The Postal Service's classification of far fewer cost pools as proportional would have the effect of reducing the costs avoided between rate cells, although it would increase the spread between its proposed metered benchmark and Automation MAADC letters by 0.564 cents, which represents an increase in total costs avoided for the remaining presort tiers.<sup>49</sup>

The proposed shift can be seen by looking at the row labeled "Total" at the bottom of **Table Three**. In the Postal Service's view, this entails moving 0.939 cents from mail processing costs that vary with the level of presortation in the CPB classification to fixed costs that do not vary with the level of presortation. By cost pool, fourteen of the Postal Service's proportional cost pools are higher than their CPB counterparts, and this is because the Postal Service has added back to these cost pools small margins that CPB considers fixed. These changes add 0.242 cents in total to proportional costs in the Postal Service's proposal. However, for twenty one other cost pools, the proportional costs are higher in the CPB framework than the Postal Service's proposal. This reflects the Postal Service changing these twenty one cost pool classifications from proportional to fixed. These changes reduce proportional costs in total by 1.182 cents compared to the CPB approach as can be seen from the bottom row labeled "Total". The Postal Service proposal also eliminates the CPB procedure wherein the procedure applied to "other costs" transforms most of them into the proportional classification.

**B. The Accuracy of Modeled Costs in Allocating All Actual CRA Mail Processing Costs into Costs by Automation Presort Tier**

In its initial comments in this case, however, the Postal Service also argues that the proportional adjustment factor is relatively high (or "bloated") at 1.667 because most cost pools (87.2 percent of the total costs) have been made proportional as a result of the Commission adopting the PB proposal. By limiting

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<sup>49</sup> See Postal Service Initial Comments, TABLE 1, p. 22.

proportional cost pools to those operations that are modeled, the Postal Service reduces the proportional adjustment factor to 1.354.

While GCA does not challenge the Postal Service's conclusion in this case that it has been able to reduce the CRA proportional adjustment factor as a result of making fewer cost pools proportional, we do not agree with its inference from this that lower, or higher, proportional adjustment factors do not have anything to do with the "accuracy" of the modeled costs approach, and that the models are accurate if and only if no cost pools are modeled except those which have been made proportional. Modeled costs in the past have had low CRA adjustment factors with a high number of cost pools being classified as proportional, just the opposite of the relationship being asserted by the Postal Service in this case. In Docket R97-1, Postal Service witness Hatfield classified 37 of 45 total cost pools as proportional and 92 percent of the costs as proportional, yet his CRA proportional adjustment factor was 1.19.

Witness Hatfield's effort was at the time viewed as an improvement over the CRA adjustment factor of 1.39 first calculated for modeled costs in MC95-1. He responded to much criticism that the MC95-1 adjustment factor was too high for the modeled costs approach to be judged as accurate for determining the mail processing costs of various presort tiers, and brought the CRA adjustment factor down to 1.19 from 1.39.

Whatever the relationship between the magnitude of the CRA proportional adjustment factor and the percentage (by number and cost) of cost pools classified as proportional, the more the absolute value of the adjustment factor deviates from one, the lower is the percentage of actual CRA mail processing costs that are explained and directly allocated across presort tiers by the modeled costs. That was and remains the obvious meaning of "accuracy" when it comes to evaluating modeled costs. Redefining and limiting what "accuracy" means to not classifying cost pools as proportional that are not modeled is an inappropriate

exercise in historical revisionism, and not an improvement in evaluating the modeled cost approach.

C. The Latest Techniques Proposed for Increasing the Spread Between 3-Digit and 5-Digit Automation Presort Letters

1. Does the Two Part CRA Adjustment Factor Fully Distribute All Non-Modeled CRA Mail Processing Costs?

Changing cost pool classifications is not the only effort PB has made in recent years to increase the spread it receives for processing mail to five digits rather than three digits. The company itself acknowledges that its proposed “two-part” CRA proportional adjustment factor would increase the 5-digit letter spread even further than declaring that most all cost pools are worksharing-related proportional. It would do this by creating one CRA adjustment factor that is lower for 5 Digit letters processed in IS letter sorting operations and a separate one that is higher for other presort tiers combined processed in non-IS letter sorting operations.

This proposal has not to date been accepted<sup>50</sup> by the Commission, and it should not be. We discuss the analytical details of this proposal later, but the impact on major volume presort mail processing costs from a two part CRA adjustment factor is as follows:

	<u>3-Digit</u>	<u>5-Digit</u>
Mail processing unit costs with a Single adjustment factor of 1.667	5.902	3.585
Mail processing unit costs with a Two-part adjustment factor:		
3-D factor 1.681	6.164	
5-D factor 0.984		<u>3.174</u>
Difference:	+0.262	-0.411

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<sup>50</sup> Or rejected.

Source: RM2010-13, Initial Comments of Pitney Bowes, February 18, 2011, Excel file PB-2.xlsx, worksheet "2Pt CRA – Presort Letters SUM".

The proposed two part CRA adjustment factor increases the spread for 5-Digit presort letters by almost seven-tenths of a cent ( $0.411+0.262$ ). It raises the mail processing cost of a 3-Digit automation letter by a little under three-tenths of a cent, but it cuts the mail processing cost of a 5-Digit automation letter by over four-tenths of a cent.

One outcome of the two part CRA adjustment factor is that the calculation for non-IS operations for a 3-Digit letter is barely above the single CRA adjustment factor, 1.681 versus 1.667; whereas the separate calculation for IS operations is well below both of those; indeed it is below one, at 0.984. The two part CRA adjustment factor reduces the accuracy for non-IS operations by a small amount relative to the single adjustment factor, while the separate factor for IS operations actually over-determines modeled costs by a small amount.

**Table Four**  
**The Pitney Bowes 3-Part CRA Adjustment Factor for Mail Processing Costs**

	Volume	USPS			Pitney Bowes				
		Model Unit Costs	CRA Adjustment	CRA Adjusted	CRA Adjusted Unit Costs			CRA Adjusted	CRA Adjustment
		Unadjusted	Factor	Unit Costs	Non-IS*	IS*	Other*	Unit Costs	Factor**
Presort Letters Categories	[1]	[2]	[3]	[4]=[2]*[3]	[5]	[6]	[7]	[8]=[5]+[6]+[7]	[9]=[8]/[2]
Nonautomation Nonmachinable Mixed ADC	6,129,952	23.926	1.667	39.893	31.412	5.150	11.781	48.344	2.021
Nonautomation Nonmachinable ADC	2,901,075	16.722	1.667	27.882	19.306	5.150	8.234	32.690	1.955
Nonautomation Nonmachinable 3-Digit	3,719,195	13.164	1.667	21.950	13.326	5.150	6.482	24.959	1.896
Nonautomation Nonmachinable 5-Digit	752,723	5.235	1.667	8.729	0.000	5.150	2.578	7.728	1.476
Nonautomation Machinable Mixed AADC	479,831,977	5.436	1.667	9.064	5.411	2.180	2.677	10.268	1.889
Nonautomation Machinable AADC	160,000,561	5.436	1.667	9.064	5.411	2.180	2.677	10.268	1.889
Nonautomation Machinable 3-Digit	419,093,292	4.716	1.667	7.863	4.283	2.132	2.322	8.737	1.853
Nonautomation Machinable 5-Digit	90,768,325	4.716	1.667	7.863	4.283	2.132	2.322	8.737	1.853
Automation Mixed AADC	2,540,785,141	4.802	1.667	8.006	4.285	2.216	2.364	8.865	1.846
Automation AADC	3,255,007,326	3.704	1.667	6.176	2.538	2.158	1.824	6.521	1.760
Automation 3-Digit	15,367,446,876	3.539	1.667	5.902	2.264	2.157	1.743	6.164	1.741
Automation 5-Digit	20,967,384,785	2.150	1.667	3.585	0.000	2.115	1.059	3.174	1.476

	Pitney Bowes Costs Shift	
	Unit Costs Shift (cents)	Total Costs Shift
Presort Letters Categories	[10]=[8]-[4]	[11]=[1]*[10]
Nonautomation Nonmachinable Mixed ADC	8.451	\$518,013
Nonautomation Nonmachinable ADC	4.808	\$139,479
Nonautomation Nonmachinable 3-Digit	3.009	\$111,898
Nonautomation Nonmachinable 5-Digit	-1.001	-\$7,535
Nonautomation Machinable Mixed AADC	1.204	\$5,779,085
Nonautomation Machinable AADC	1.204	\$1,927,043
Nonautomation Machinable 3-Digit	0.874	\$3,663,824
Nonautomation Machinable 5-Digit	0.874	\$793,521
Automation Mixed AADC	0.859	\$21,815,284
Automation AADC	0.344	\$11,206,520
Automation 3-Digit	0.262	\$40,252,849
Automation 5-Digit	-0.411	-\$86,199,978

\* Pitney Bowes applies 3 adjustment factors of 1.681, 0.984, and 0.492 to modeled costs for each rate category, in order to obtain the CRA adjusted unit costs for "Non-IS", "IS", and "Other", respectively. The sum of these for each rate category divided by modeled costs equals the overall or weighted CRA adjustment factor in column [9].

\*\* The Pitney Bowes "CRA Adjustment Factor" (column [9]) for each presort rate category is obtained by dividing its CRA adjusted unit cost (column [8]) by the modeled unit cost (column [2]) for that category.

Source: Columns [1] through [8] are from RM2010-13, Initial Comments of Pitney Bowes, February 18, 2011, Excel file PB-2.xlsx, worksheet, "2Pt CRA - Presort Letters SUM."

Consider the allocation of total non-modeled CRA mail processing costs. For all automation presort volumes other than 5-Digit, the allocation of non-modeled CRA costs is not far above the allocation with a single CRA adjustment factor. The per unit allocation is based on presort letter volumes of 21.163 billion letters. The increase in the allocation of non-modeled CRA costs to 3-Digit letters is 0.262 cents per letter. Since the volume of 5-Digit letters alone is 20.97 billion letters, the reduction of 41 percent in the CRA adjustment factor to 0.984 leads to a reduction of -0.411 cents per letter.

Put differently, with the two part adjustment factor, the allocation of CRA non-modeled costs is reduced by 0.411 cents per letter for 5-Digit Presort on a volume that is only one one-hundredth less than that for 3-Digit, AADC and MAADC combined; whereas the allocation of CRA non-modeled costs is increased by only 0.262 cents per letter for all remaining automation presort tiers. Approximately 0.149 cents per letter in non-modeled CRA mail processing costs remains unallocated.

It would appear that the two part CRA adjustment factor does not fully distribute non-modeled CRA costs like the single CRA adjustment factor does. **Table Four** shows that the “two-part” CRA adjustment shifts \$86,199,978 in non-modeled costs away from 5-digit presort, which is -0.411 per piece. About half of this is offset by the 0.262 unit cost increase for 3-digit presort, or a total of \$40,252,849. This leaves \$45,947,129 of CRA non-modeled costs (apart from fixed costs) undistributed or unallocated.

As it turns out this undistributed \$45.9 million is in fact allocated to “other”, in addition to IS or non-IS categories. PB’s adjusted CRA unit costs include some “other” costs for every presort rate category as can be seen from **Table Four**. “Other” is defined by PB as tallies from the IOCS schemes or MODS codes that could not be identified as either IS or non-IS. PB states “The costs in the Other category for the letter-sorting cost pools were added to the proportional CRA

costs for the non-letter –sorting cost pools.” (RM2009-3, Initial Comments of Pitney Bowes Inc., p. 18.)

Thus, the PB three - part CRA adjustment (but not the two - part adjustment) factor does allocate all non-modeled CRA costs other than fixed just as the traditional single adjustment factor valued at 1.667 in the 2010 ACR does. However, compared to the two-part CRA proportional adjustment factor, the inclusion of other costs changes the proportional CRA adjustment factors due to the influence of “other” costs. Under the Postal Service’s single CRA adjustment factor the ratio of total CRA adjusted unit costs divided by modeled unit costs equals 1.667 for every rate category for presort, as seen in column 3 of **Table Four**. This is not so in the PB approach, however, as can be seen from column 9 of the table.

The influence of the “other” costs classification affects the PB proportional adjustment factors. The three part CRA adjustment factor for 5-digit is now 3.174/2.150 or 1.476, not .984 using a two part adjustment factor, calculated in the same manner as the USPS single CRA proportional adjustment factor. For 3-digit the three-part adjustment factor is 1.742, not 1.681 as emerges from the two-part adjustment factor. For auto AADC it is 1.760 and for auto MAADC it is 1.846. Ultimately, for non-auto nonmachinable Mixed ADC, the three part adjustment factor is 2.020.

It is only the CRA proportional adjustment factors in column 9 of **Table Four** that are comparable to the single part CRA adjustment factor in column 3, since these are the factors that fully distribute all CRA non-modeled costs that are not fixed. What it calls the “two-part” CRA proportional factor on which PB has placed undue emphasis in its approach is more on the order of an intermediate step, more a set of weights than factors which fully allocate CRA non-modeled costs. (We refer hereafter to it as the PB “two factor adjustment”.) For each rate category, columns 5, 6 and 7 are multiplied by 0.984, 1.681, and 0.492

respectively and then summed in column 8. The CRA proportional adjustment factors that then correspond to 1.667 in column 3 are found in column 9, which equals for each rate category CRA adjusted unit costs from column 9 divided by unadjusted modeled unit costs from column 2. These are the only numbers in PB's proposal that can truly be called CRA proportional adjustment factors, and they are the only numbers that correspond to the manner in which 1.667 is calculated in the traditional USPS approach, namely column 4 divided by column 2.

In summary, while PB itself only speaks of a "two-part" CRA adjustment factor (which entails three parts, not two), such an approach does not allocate all CRA non-modeled costs that are not fixed. As can be seen from **Table Four**, only with the consideration of "other" costs besides IS and Non-IS costs does the PB approach replicate the single CRA proportional adjustment factor of the Postal Service, which by definition allocates all non-modeled CRA costs that are not fixed.

The two part adjustment process, as it has been developed and discussed by PB, therefore masks the key facets surrounding the PB approach that are made visible once all CRA costs are allocated, which can only be done in the PB framework with a three-part CRA adjustment factor, not a two-part factor.

In the past each adjacent presort tier has higher modeled unit costs and because of that higher adjusted unit costs with a single proportional adjustment factor. With the PB approach, the higher unit adjusted costs for each adjacent rate category is based on higher modeled costs and a sequentially higher and higher CRA proportional adjustment factor applied to those modeled costs.<sup>51</sup>

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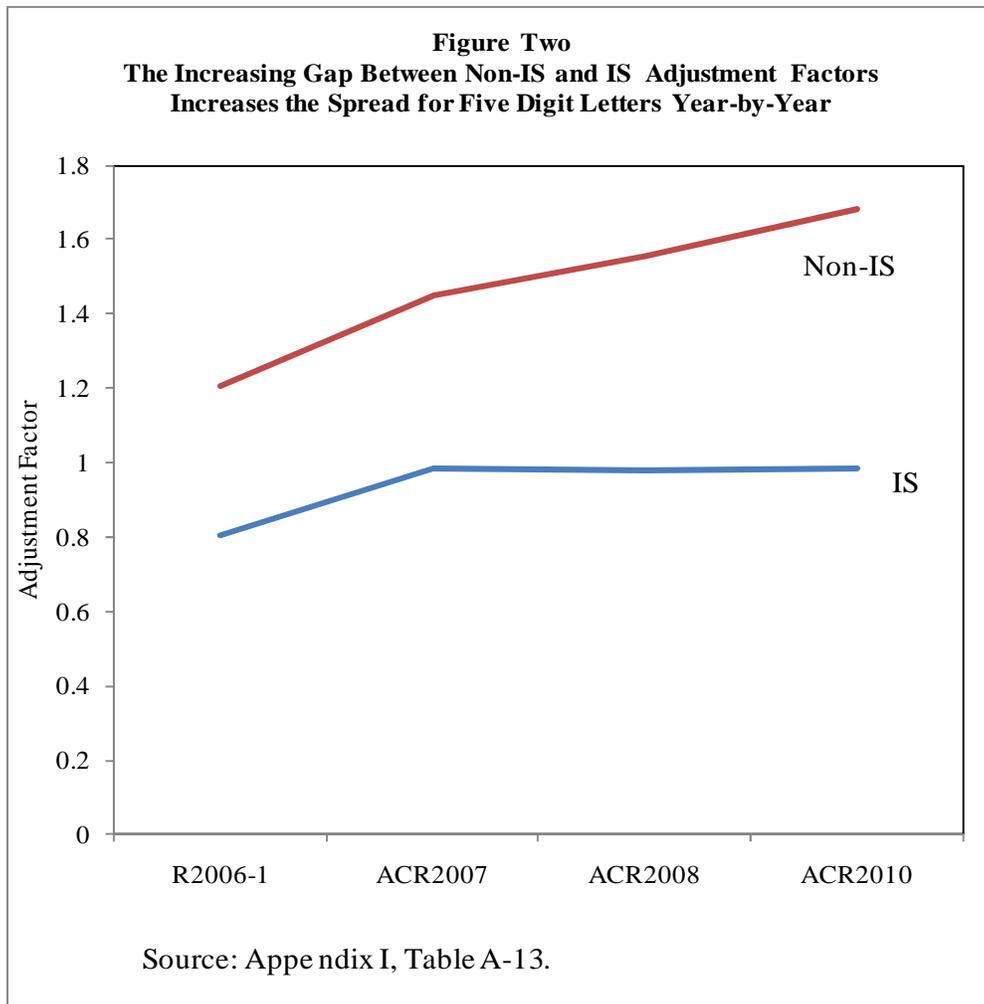
<sup>51</sup> The only exceptions are the 1.853 adjustment factor, which applies to non-auto machinable 3-Digit and 5-Digit, the 1.889 adjustment factor, which applies to non-auto MAADC and non-auto MMAADC, and the repetition of the 5-Digit adjustment factor , 1.476, for the non-auto nonmachinable 5-Digit rate category.

PB achieves an increase in costs avoided for 5 Digit mail as a result of having a higher and higher CRA proportional adjustment factor for most adjacent presort tiers. It may explain away that difference between 5 - Digit and 3-Digit by its two – part adjustment factor argument that 5-digit letters only go through IS mail processing operations, whereas other presort tiers go through non-IS operations as well, even though that is already embodied in modeled cost differences. But, just how does PB explain and justify the mail flows that lead it to re-allocate all non-modeled CRA costs by a three-part CRA proportional adjustment factor which leads to higher and higher proportional adjustment factors, the higher the modeled cost?

2. The Non-IS Adjustment Factor Is Increasing Faster than the IS Adjustment Factor Over the R2006-1 to 2010 ACR Period, so the Spread for 5-Digit Letters Is Increasing Year by Year With the Two Part Adjustment Factor

The technique for creating separate IS and non-IS “adjustment factors” is analytically complex, but it can be explained more succinctly than it has been. It is assumed that the cost models are accurate in replicating the flow of mail pieces through the mail processing network. From the way in which the cost models are designed, it is possible to isolate the mail processing incoming secondary (IS) operations that only 5-Digit letters must go through from the non-incoming secondary (non-IS) operations that other presort tiers go through as well. The IS and non-IS operations become a further input into the SAS modeling the Postal Service uses for IOCS tallies. The model is instructed to separate tallies for each cost pool into IS and non-IS operations. These model outputs are then applied as weights to distribute each cost pool into IS and non-IS portions. The relative weights for each cost pool are then used to distribute costs for that cost pool between IS and non-IS operations. Finally, the standard procedure for calculating a single CRA proportional adjustment factor is used to calculate a separate adjustment factor for IS operation costs and for non-IS operation costs.

Based on PB calculations of what the IS and non-IS CRA adjustment factor would be over the past four years, the non-IS factor is above 1.0 and increasing in each of those years while the IS factor remains steady and below 1.0. This growing gap between the IS and non-IS two-part adjustment factors creates an ever increasing spread in estimated costs avoided for 5 digit letters than for other presort tiers. As shown in **Figure Two**, the factor for non-IS letter sorting costs has risen steadily from 1.205 in R2006-1 to 1.681 in the 2010 ACR. By way of contrast the trend in the adjustment factor for IS letter sorting costs has been fairly steady and just under 1.0.



A final observation in the two part adjustment factor concerns the number of 3-digit operations codes within each cost pool, and the fact that these are in-

creasing more for Non-IS operations than IS operations year by year in general. For example, the number of three-digit-code operations included in the DBCS cost pool for non-Incoming Secondary letter sorting costs (non-IS) has grown significantly from 27 in R2006-1 to 41 in ACR2010. On the other hand, in the Incoming Secondary (IS) letter sorting costs, the number of operations included has only increased from 21 to 25 during the same time period. (See Appendix I, Table A-3). Across all cost pools, operations codes included for non-IS letter sorting costs have increased from 71 to 103 since R2006-1, while operations codes for IS letter sorting costs have only increased from 59 to 68. (See Appendix I, Figure A-1)

This disparity cannot be explained by a difference in the number of letter cost pools between non-IS and IS operations, because there are nine in each. It cannot be ascertained at present why the number of 3-digit operations codes listed is increasing year by year, why it is increasing faster for non-IS operations in the PB modeling, and whether or not it has any implication for the behavior of the non-IS and IS adjustment factors over time, and the increase in the spread for 5-Digit presort automation letters. It can be said that between R2006-1 values and the 2010 ACR, the changes in the number of operation codes do not appear to have consistently altered the weights in the distribution of IOCS tallies between non-IS and IS operations. (See Appendix I, Table A-13).

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Respectfully submitted,

GREETING CARD ASSOCIATION

David F. Stover  
2970 S. Columbus St., No. 1B  
Arlington, VA 22206-1450  
(703) 998-2568  
(703) 998-2987 fax  
E-mail: [postamp@crosslink.net](mailto:postamp@crosslink.net)

## Appendix I

**Table A-1  
Derivation of Mail Processing and Delivery Unit Costs  
for Single-Piece Stamped, Metered and Other Letters**

	<u>Volume</u>	<u>Weights</u>		
Single-Piece Stamped Letters	15,334,388	56.5%		
Single-Piece Metered/IB/PVI	9,868,375	36.4%		
Single-Piece Other Letters	1,945,155	7.2%		
<b>Total</b>	<b>27,147,918</b>			
	<u>Mail Processing</u>	<u>WS Related</u>		
	<u>Unit Costs</u>	<u>Unit Cost</u>		
	<u>(cents)</u>	<u>(cents)</u>		
Single Piece Letters Average	14.38	14.24		
Single-Piece Metered/IB/PVI	13.61	13.41		
Single-Piece Stamped Letters*	14.82	14.71		
	<u>Total Delivery</u>	<u>Collection</u>	<u>Delivery Costs</u>	
	<u>Unit Costs</u>	<u>Unit Costs</u>	<u>w/o Collection</u>	
	<u>(cents)</u>	<u>(cents)</u>	<u>(cents)</u>	
Single Piece Letters Average	9.31	3.83	5.48	
Single-Piece Stamped Letters	9.20	3.84	5.36	
Single-Piece Metered/IB/PVI	9.59	3.81	5.77	
Single-Piece Other Letters	8.73	3.80	4.93	

\* To derive an estimate of "Single-Piece Stamped Letters " mail processing unit cost, it is assumed that "Single-Piece Other Letters" is similar to the "Single-Piece Stamped Letters" and thus the volume weights for the "Single-Piece Stamped Letters" including "Single-Piece Other Letters" is 63.6% and for "Single-Piece Metered Letters" is 36.4%. Given that the mail processing unit cost for metered letters is 13.61 cents with the weight of 36.4% and the unknown mail processing unit cost for stamped letters is X with the weight of 63.6% and the weighted average for single piece letters is 14.38, then X can be calculated to be 14.82 cents and its worksharing related cost to be 14.71.

Source: RM2010-13, Response of USPS to CHIR Request No. 1 (January 18, 2011).

**Table A-2  
Information to Plot Figure One**

	Volume	Total Attributable	MPC (CS3.1)	DC (CS6.7.10)
Single Piece Letters	27,147,918	\$7,376,828	\$2,265,239	\$1,906,112
Presort Letters	43,293,821	\$5,161,839	\$1,432,914	\$1,510,836

Source: FY10 Public CS&C Rpt.xls and FY2010 CRA Report.

	TUAC	UMPC (CS3.1)	JDC (CS6.7.10)	UMPC+UDC	TUAC-(UMPC+UDC)
Single Piece	27.17	8.34	7.02	15.37	11.81
presort	11.92	3.31	3.49	6.80	5.12
Single Piece minus Presort	15.25	5.03	3.53	8.57	6.68

Source: \$ costs divided by the volumes in the above table.

	Unit Cost
Heterogenous( 50%Stamped+50%Metered)	19.63
Pure Metered	19.19
Heterogeneous minus Pure Metered	0.44

Source: See Table Two.

	UDC
Metered (Proposed)	5.77
Metered (Original)	4.84
Change in Metered UDC	0.94

Sources: RM10.13.Intl.Cmmnts.xls and ACR2010, USPS-FY10-19

	Unit Cost
Metered Collection Cost	3.81

Source: RM2010-13, USPS Response to ChR No. 1, excel file ChR.No.1.Delvry.Indicia.Collctn.xls.

	SP-Presort De-linked*	Metered Linked**	Difference
Single Piece minus Presort [TUAC-(UDC+UMPC)]	6.68		
Change in Metered UDC		0.94	
Metered Collection Cost		3.81	
Addition due to Heterogeneous Mail (50%Stamped+50%Metered)		0.44	
Total	6.68	5.19	1.50

Sources: From above tables

**Table A-3**  
**D/BCS Operations by Year for IS and Non-IS**

2006 usps operation codes	2006-1				2006 usps operation codes	2006-1				
	D/BCS NON-IS	ACR200 D/BCS NON-IS	ACR200 D/BCS NON-IS	ACR2010 D/BCS NON-IS		D/BCS IS	ACR200 D/BCS IS	ACR200 D/BCS IS	ACR2010 D/BCS IS	
NO		261	261	261	YES	266		266	266	DBCS-OCR - INCOMING SECONDARY
NO				262	YES		276	276	276	DBCS-OSS - INCOMING SECONDARY
NO			263	263	YES	278				DBCS-OCR - MANAGED MAIL
YES		264	264	264	YES		286	286	286	DBCS ISS - Incoming Secondary
YES		265	265	265	NO		296	296	296	DBCS-ISS/OSS MODE - Incoming Secondary
NO	271	271	271	271	YES			297	297	DBCS-ISS/OSS MODE - Box Section
NO	272				NO		496	496	496	HEADQUARTERS PROJECTS - SUPERVISION
YES	273	273	273	273	YES	866	866	866	866	
YES	274	274	274	274	YES		869	869	869	BCS ON OCR-SECTOR/SEGMENT, 2ND PASS
YES	275				YES	876	876	876	876	
NO	281	281	281	281	YES		877	877	877	MPBCS-BOX SECTION
NO	282	282	282	282	YES	878	878	878	878	
NO	283	283	283	283	YES	879	879	879	879	
YES	284	284	284	284	YES	896	896	896	896	DBCS/DIOSS BCS IC SECONDARY
YES		285	285	285	YES	897	897	897	897	DBCS/DIOSS BCS BOX SECTION
NO		291	291	291	YES	898	898	898	898	DBCS/DIOSS BCS SEC/SEG 1ST PASS
NO				293	YES	899	899	899	899	DBCS/DIOSS BCS SEC/SEG 2ND PASS
NO		295	295	295	YES	909			909	CSBCS - Incoming Secondary
NO		372	372		YES	910	910	910	910	
NO				481	YES	911		911	911	CSBCS - Delivery Point Sequence DPS
NO				483	YES	914	914	914	914	
YES	484		484	484	YES	915	915	915	915	
YES				485	YES	917				
NO		491	491	491	YES	918	918	918	918	DBCS/DIOSS BCS DPS 1ST PASS
NO				494	YES	919	919	919	919	DBCS/DIOSS BCS DPS 2ND PASS
YES				505	YES	926				
YES	854				YES	976	976	976	976	
NO	861				YES	979	979	979	979	
NO		863	863	863						
YES	864	864	864	864						
YES	865	865	865	865						
NO	871	871	871	871						
NO	872	872	872	872						
NO	873	873	873	873						
YES	874	874	874	874						
YES	875	875	875	875						
NO	891	891	891	891						DBCS/DIOSS BCS O/G PRIMARY
NO	892	892	892	892						DBCS/DIOSS BCS O/G SECONDARY
NO	893	893	893	893						DBCS/DIOSS BCS MANAGED MAIL
YES	894	894	894	894						DBCS/DIOSS BCS IC SCF PRIMARY
YES	895	895	895	895						DBCS/DIOSS BCS IC PRIMARY
NO	971	971	971	971						
NO	972									
NO	973		973	973						BCS-OSS-MANAGED MAIL
YES	974	974	974	974						
YES		975	975	975						BCS-OSS-INCOMING PRIMARY
Total Number of Operations										
	27	31	34	41		21	21	24	25	

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf, RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf, and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS\_Code.pdf.

Notes:

- 830C COMPOSITE - MLOCR (831-837)
- 840C COMPOSITE - MLOCR BULKY MOD (841-847)
- 860C COMPOSITE BCS ON OCR (861-869)
- 870C COMPOSITE - MAIL PROCESSING BCS (871-879)
- 890C COMPOSITE DBCS/DIOSS BCS MODE (891-899)
- 908C COMPOSITE CSBCS (908-911)
- 960C COMPOSITE - DIOSS BULKY OCR MODE (961-967)
- 970C COMPOSITE - BAR CODE OUTPUT SUB SYSTEM (971-979)

**Table A-4**  
**OCR Operations by Year for IS and Non-IS**

2006-1 OCR NON-IS	ACR2007 OCR NON-IS	ACR2008 OCR NON-IS	ACR2010 OCR NON-IS		2006-1 OCR IS	ACR2007 OCR IS	ACR2008 OCR IS	ACR2010 OCR IS	
831		831	831	MLOCR - OUTGOING PRIMARY	836	836	836	836	
833	833	833	833				837	837	MLOCR - BOX SECTION
834	834	834	834		846	846	846	846	
835	835	835	835		887				
841	841	841	841			966	966	966	FMBCR-INCOMING SECONDARY
843	843	843	843						
844	844	844	844						
845	845	845	845						
881	881	881	881						
882									
883	883	883	883						
884	884	884	884						
885	885	885	885						
	961	961	961	FMBCR-OUTGOING PRIMARY					
			962	FMBCR-OUTGOING SECONDARY					
	963	963	963	FMBCR-MANAGED MAIL					
	964	964	964	FMBCR-INCOMING SCF					
	965	965	965	FMBCR-INCOMING PRIMARY					
Total Number of Operations	13	15	16	17	3	3	4	4	

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS\_Code.pdf.

**Table A-5**  
**MANL-MOD Operations by Year for IS and Non-IS**

2006-1 MANL-MOD NON-IS	ACR2007 MANL-MOD NON-IS	ACR2008 MANL-MOD NON-IS	ACR2010 MANL-MOD NON-IS	2006-1 MANL-MOD IS	ACR2007 MANL-MOD IS	ACR2008 MANL-MOD IS	ACR2010 MANL-MOD IS
30	30	30	30	160	160	160	160
40	40	40	40	168	168	168	168
43	43	43	43	169	169	169	169
44	44	44	44				
150	150	150	150				
Total Number of Operations	5	5	5	3	3	3	3

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS\_Code.pdf.

**Table A-6**  
**LD41 Operations by Year for IS and Non-IS**

2006-1	ACR2007	ACR2008	ACR2010		2006-1	ACR2007	ACR2008	ACR2010	
LD41	LD41	LD41	LD41		LD41	LD41	LD41	LD41	
NON-IS	NON-IS	NON-IS	NON-IS		IS	IS	IS	IS	
361	361	361	361						
365					826	826	826	826	DBCS-OSS - SECTOR/SEGMENT, 2ND PASS
374					828		828	828	AUTOMATED LETTERS - SECTOR/SEGMENT, 1ST PASS
394					829		829	829	AUTOMATED LETTERS - SECTOR/SEGMENT, 2ND PASS
			804	FSM - INCOMING SCF	905	905	905	905	
		823	823	AUTOMATED LETTERS - MANAGED MAIL	906	906	906	906	
824		824	824	AUTOMATED LETTERS - INCOMING SCF	912	912	912	912	
					913	913	913	913	
					942				
Total Number of Operations	5	1	3	4	8	5	7	8	

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS Code.pdf.

**Table A-7**  
**LD42 Operations by Year for IS and Non-IS**

2006-1	ACR2007	ACR2008	ACR2010		2006-1	ACR2007	ACR2008	ACR2010	
LD42	LD42	LD42	LD42		LD42	LD42	LD42	LD42	
NON-IS	NON-IS	NON-IS	NON-IS		IS	IS	IS	IS	
412					826		826	826	
		414	414	DBCS-ISS/OSS MODE - Incoming SCF			905	905	DELIVERY CS BCS DISTRIBUTION
803							906	906	CARRIER ROUTE SORTATION
							912	912	AUTOMATED LETTERS - DPS, 1ST PASS
							913	913	AUTOMATED LETTERS - DPS, 2ND PASS
Total Number of Operations	2	0	1	1	1	0	5	5	

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS Code.pdf.

**Table A-8**  
**LD43 Operations by Year for IS and Non-IS**

2006-1	ACR2007	ACR2008	ACR2010		2006-1	ACR2007	ACR2008	ACR2010	
LD43	LD43	LD43	LD43		LD43	LD43	LD43	LD43	
NON-IS	NON-IS	NON-IS	NON-IS		IS	IS	IS	IS	
37	37	37	37		161	161	161	161	
	38	38	38				166	166	
	39	39	39					172	
	151	151	151			176	176	176	
		171	171						
Total Number of Operations	1	4	5	5	1	2	3	4	

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS Code.pdf.

**Table A-9**  
**LD44 Operations by Year for IS and Non-IS**

2006-1 LD44 NON-IS	ACR2007 LD44 NON-IS	ACR2008 LD44 NON-IS	ACR2010 LD44 NON-IS	2006-1 LD44 IS	ACR2007 LD44 IS	ACR2008 LD44 IS	ACR2010 LD44 IS
30	37	37	37	769	769	769	769
Total Number of Operations				1	1	1	1

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS\_Code.pdf.

**Table A-10**  
**AUTO-MEC Operations by Year for IS and Non-IS**

2006-1 AUTO-MEC NON-IS	ACR2007 AUTO-MEC NON-IS	ACR2008 AUTO-MEC NON-IS	ACR2010 AUTO-MEC NON-IS	2006-1 AUTO-MEC IS	ACR2007 AUTO-MEC IS	ACR2008 AUTO-MEC IS	ACR2010 AUTO-MEC IS
253	253	253	253	769	826	826	826
361	361	361	361	828	828	828	828
365	364	364	364	829	829	829	829
374				899			
375	375	375	375	905	905	905	905
391	391	391	391	906	906	906	906
392	392	392	392	911	911	911	911
394	394	394	394	912	912	912	912
803	804	804	804	913	913	913	913
821	823	823	823	918	918	918	918
824	824	824	824	925	919	919	919
825	825	825	825	942			
	891	891	891			943	943
		842	842				
		891	891				
			961				
Total Number of Operations				12	11	13	14

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS\_Code.pdf.

**Table A-11**  
**MANL-NONMOD Operations by Year for IS and Non-IS**

2006-1 MANL-NMOD NON-IS	ACR2007 MANL-NMOD NON-IS	ACR2008 MANL-NMOD NON-IS	ACR2010 MANL-NMOD NON-IS	2006-1 MANL-NMOD IS	ACR2007 MANL-NMOD IS	ACR2008 MANL-NMOD IS	ACR2010 MANL-NMOD IS
		37	37	161	161	161	161
39		39	39	166	166	166	166
40	40	40	40	168	168	168	168
	43	43	43			176	176
44	44	44	44	769	769	769	769
50				826			
			52	905	905	905	905
			150	906			
	151	151	151	913			
			170				
		171	171				
		361	361				
			463				
			825				
824							
		912	912				
Total Number of Operations				5	4	9	15

Sources: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS\_Code.pdf.

**Table A-12**  
**FIRST-CLASS MAIL PRESORT LETTERS**  
**CRA MAIL PROCESSING COSTS – with 2-Part CRA Adjustment**  
**Weights from IOCS Tally Analysis**

Cost Pools	FY06	FY07	FY08	FY10	FY06	FY07	FY08	FY10	FY06	FY07	FY08	FY10
	Non-IS	Non-IS	Non-IS	Non-IS	IS	IS	IS	IS	Other	Other	Other	Other
MODS 11 BCS/DBCS	37.87%	36.97%	36.80%	35.10%	61.47%	61.29%	61.31%	62.93%	0.66%	1.75%	1.89%	1.96%
MODS 11 OCR/	86.01%	66.73%	33.30%	81.16%	12.56%	33.27%	65.32%	18.84%	1.43%	0.00%	1.38%	0.00%
MODS 14 MANL	74.64%	80.04%	82.41%	84.67%	25.10%	18.49%	16.81%	13.88%	0.26%	1.47%	0.78%	1.44%
MODS 41 LD41	17.25%	8.24%	10.50%	22.10%	82.75%	91.76%	89.50%	77.90%	0.00%	0.00%	0.00%	0.00%
MODS 42 LD42	100.00%		100.00%	0.00%	0.00%		0.00%	0.00%	0.00%		0.00%	100.00%
MODS 43 LD43	22.64%	22.86%	34.39%	58.28%	57.15%	65.23%	54.89%	35.01%	20.21%	11.91%	10.72%	6.71%
MODS 44 LD44	0.00%	0.00%	0.00%	0.00%	100.00%	100.00%	100.00%	100.00%	0.00%	0.00%	0.00%	0.00%
NON MODS AUTO/MEC	17.34%	16.50%	15.65%	13.38%	82.66%	83.50%	84.35%	86.62%	0.00%	0.00%	0.00%	0.00%
NON MODS MANL	24.82%	27.45%	28.21%	35.46%	73.88%	71.47%	69.18%	62.09%	1.30%	1.07%	2.61%	2.45%

Sources: Pitney Bowes, RM2009-1, 12-10-08-pb\_App\_2-5.zip, RM2009-3, RM2009-3\_PB-2.zip, & RM2010-13 (2/18/2010), PB-2.xlsx.

**Table A-13  
Two-Part Adjustment Factors (IS & Non-IS)  
R2006-1 to ACR2010**

	2-Part Adjustment Factors							
	ACR2010		ACR2008		ACR2007		R2006-1	
	IS	Non-IS	IS	Non-IS	IS	Non-IS	IS	Non-IS
Adjustment Factors	0.984	1.681	0.979	1.557	0.986	1.449	0.804	1.205
Change from Previous Period	0.005	0.124	-0.007	0.108	0.182	0.244		
% Change from Previous Period	0.51%	7.96%	-0.71%	7.45%	22.64%	20.25%		

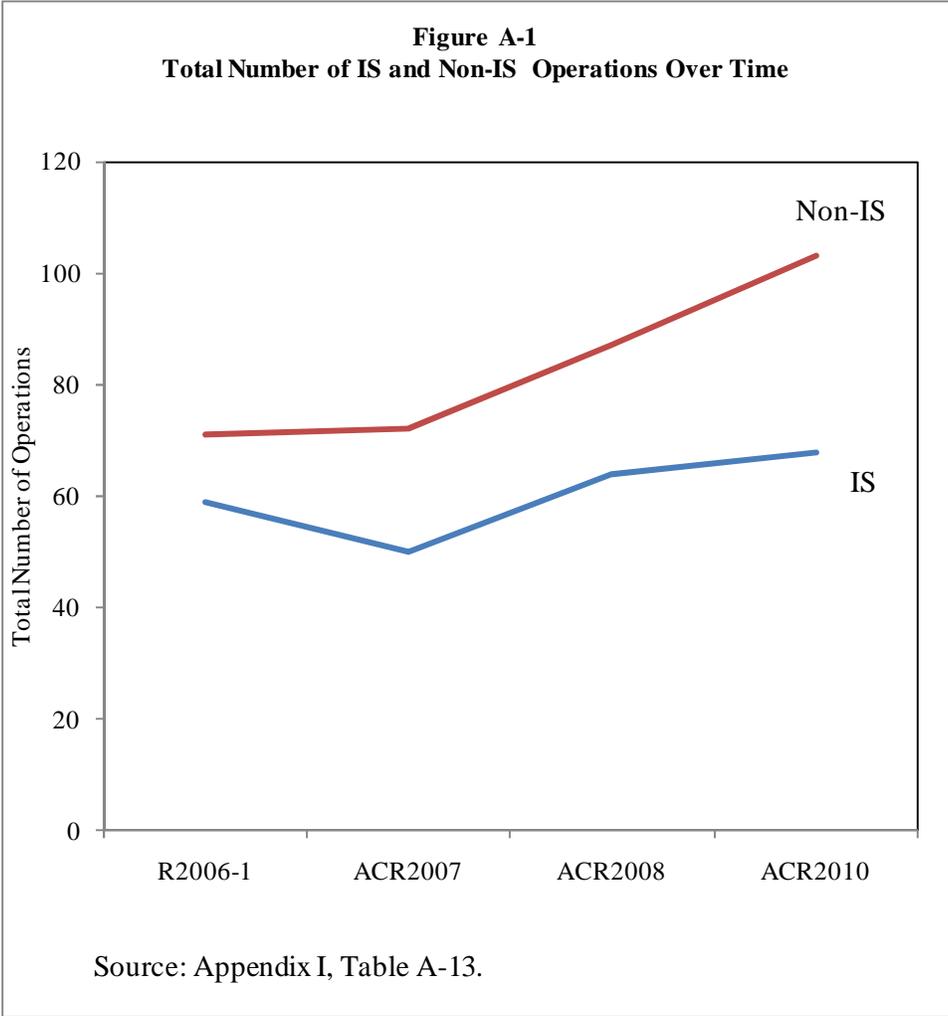
Cost Pools	Number of Operations in each Cost Pool							
	ACR2010		ACR2008		ACR2007		R2006-1	
	IS	Non-IS	IS	Non-IS	IS	Non-IS	IS	Non-IS
D/BCS	25	41	24	34	21	31	21	27
OCR	4	17	4	16	3	15	3	13
MANL-MOD	3	5	3	5	3	5	3	5
LD41	8	4	7	3	5	1	8	5
LD42	5	1	5	1	0	0	1	2
LD43	4	5	3	5	2	4	1	1
LD44	1	1	1	1	1	1	1	1
AUTO/MEC	11	14	11	13	10	11	13	12
MANL-NONMOD	7	15	6	9	5	4	8	5
Total Number of Operations	68	103	64	87	50	72	59	71
Change from Previous Period	4	16	14	15	-9	1		
% Change from Previous Period	6.25%	18.39%	28.00%	20.83%	-15.25%	1.41%		

	Total Number of Operations		Adjustment Factors	
	IS	Non-IS	IS	Non-IS
R2006-1	59	71	0.804	1.205
ACR2007	50	72	0.986	1.449
ACR2008	64	87	0.979	1.557
ACR2010	68	103	0.984	1.681

Sources :

The two-part adjustment factors for R2006-1, ACR2007 & ACR2008 are obtained from RM2009-3, Initial Comments of Pitney Bowes Inc., PB RM2009-3 comments.pdf, Table 2, page 13; and for ACR2010 from RM2010-13, Comments of Pitney Bowes Inc., PB Comments (RM2010-13).pdf, Table 1, page 5.

The number of operations are obtained from Tables A1-A9 in Appendix I of this document which are based on: RM2009-1, Reply Comments of Pitney Bowes Inc., 12-10-08Pb\_App\_2-5.zip, PB-2, PB-2-2006FCM-SAS Code.pdf & PB-4, PB-4-R2007FCM-SAS Code.pdf; RM2009-3, Initial Comments of Pitney Bowes Inc., RM2009-3-PB-2.zip, PB-2-2008FCM-SAS Code.pdf; and RM2010-13, Comments of Pitney Bowes Inc., PB-2-2010FCM-SAS\_Code.pdf.



## Appendix II: Derivations of Numbers Used in Text

### From pages 7-9: Heterogeneity and Stamped Letters in First Class

Total stamped single piece letters in FY 2009: 17.258 billion

Data from 2009 Household Diary Study:

Total households:	117.2 million
From Table A-29:	Household to household pieces/week per household 2009: 0.857
	Household to non-household " " " " : 2.035
	First Class letters and cards
From Table A-28:	Breakdown of Household to Nonhousehold pieces/wk/hh 2009:
	Response to advertising: 0.164
	Transaction to phone/utility company: 0.397
	Transaction to credit card company: 0.286
	All other business mail: 01.159

Household to household pieces 2009:	5.225 billion
Household to non-household pieces 2009:	<u>12.400</u>
Total:	<u>17.625</u>
Household to Nonhousehold pieces 2009:	
	Response to advertising: 0.998
	Transaction to phone/utility company: 2.419
	Transaction to credit card company: 1.742
	All other business mail: <u>7.066</u>
Total:	<u>12.225</u>

Note: The above calculations are based on the number of households (117.2 million) multiplied by the number of weeks (52) then multiplied by the number of pieces per week per household for each category and finally divided by 1000 to convert them to billion pieces (for example, the number of household to household pieces is calculated to be  $117.2 \times 52 \times 0.857 / 1000 = 5.225$  billion).

Assumptions: 1. Half of all presort mail is produced by consolidators  
 2. Between 2.5% and 10% of that is stamped  
 3. No presort mail produced by major mailers uses stamps

2010 ACR data: 15.334 billion stamped letters, 70.4% ( $12.400/17.625 \times 100$ ) of which is household to non-household mail using the 2009 HHD data above.

From assumptions 1-3, between 555 million and 2,405 million stamped letters were received by consolidators in 2010..

For 2009: Using the 2010 percentages applied to FY2009 HHD data, consolidators received between 621 million and 2,706 million stamped letters in FY 2009, which is between 2.7% and 10.7% of all mail received by consolidators.

For 2009 and 2010: The non-household pieces sent by indicia other than stamps should approximate the total number of pieces by indicia that are stamped minus the number of pieces sent by non-households to consolidators that are stamped.