ORIGINAL

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

Mailing Online Service, 1998   )   Docket No. MC98-1

ANSWERS OF THE OFFICE OF THE CONSUMER ADVOCATE
TO INTERROGATORIES OF MAIL ADVERTISING SERVICE ASSOCIATION
WITNESS: JAMES F. CALLOW (MASA/OCA-T100-1-9)
(March 1, 1999)

The Office of the Consumer Advocate hereby submits the answers of James F.

Callow to interrogatories MASA/OCA-T100-1-9, dated February 17, 1999. Each

interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

Emmett Rand Costich

EMMETT RAND COSTICH
Attorney
Office of the Consumer Advocate

MASA/OCA-T100-1. Would your pricing proposal require USPS to incur additional costs for MOL in the following categories listed below? Explain the reasons for each of your answers.

    (a)   Designing software to implement the pricing proposal;

    (b)   Acquiring hardware to implement the pricing proposal;

    (c)   Maintaining hardware for implementation of the pricing proposal;

    (d)   Maintaining and updating software used to implement the pricing proposal;

    (e)   Loss of revenue as a result of lower postage rates than under the USPS proposal in some or all instances.

A.   (a)   Implementation of my proposal would require some code modification by the Postal Service's system developer. Code modification would be concentrated in two principal areas. First, under my proposal, Mailing Online customers would pay rates for which their mailpieces would qualify if entered as hardcopy directly with the Postal Service. This proposal would require the Postal Service to presort mailings at the time they are submitted. At present, the Postal Service creates separate batches for each print site before presortation. Tr. 6/1600 (Garvey). There is no technical barrier to modifying the code to switch the order of presortation. The Postal Service confirms that it would be "technically possible" and "physically feasible" to charge a Mailing Online customer a postage rate for which the customer's mailing would have qualified if submitted in hardcopy. Tr. 7/1669 (Garvey); see also Tr. 6/1412 (Garvey, OCA/USPS-T5-42(b)).

Second, my pricing formula uses experience-based weighted average rates. The derivation of experience-based weighted average rates requires the use of presort-level volume data by job-type/page-count category. The Postal Service states that the

next major release of the Mailing Online software will collect volume data by "batch type" (i.e., job-type/page-count) by presort level. Tr. 8/1771 (Plunkett, OCA/USPS-T5-49). To the extent the volume data is not collected in "look-up" tables, the following code modification would be required: (1) collect each quarter the presort-level volume data by job-type/page-count category in "look-up" tables, see OCA-T-100 at 25-26, lines 19-20, and 1-6, respectively, (2) calculate experience-based weighted average rates for each job-type/page-count category from all quarterly presort-level volume data at the end of each quarter, see OCA-T-100 at 28-29, lines 1-15, and 1-8, respectively, and (3) program the processing center computer to reference the experience-based weighted average rates from the job-type/page-count categories relevant to customer mailings in order to calculate the blended discount rate. See OCA-T-100 at 34, lines 10-17.

(b)   It appears that the Postal Service would not need to incur additional costs to acquire hardware in order to implement my proposal. The Postal Service claims it has over estimated the capacity for (and costs of) Mailing Online. Tr. 3/810 (Stirewalt).

(c)   It appears the Postal Service would not incur any additional hardware maintenance costs. The hardware used to implement my proposal would be the same hardware relied upon by the Postal Service to implement Mailing Online. Since the necessary hardware is already in place (or planned for placement) to operate the Mailing Online service, no special or additional maintenance as a consequence of implementation of my proposal would be required.

(d)   Once the job-type/page-count "look-up" tables are established under my proposal, no code maintenance would be required. However, to the extent new job-types are introduced to the Mailing Online "menu," there would be maintenance with respect to the addition of "look-up" tables. The introduction of new job-types would also require maintenance with respect to the addition of those new features to the pre-mailing service print site "look-up" tables. See OCA-T-100 at 33-34, lines 12-17, and 1-6, respectively. The amount of maintenance required for new job-type "look-up" tables would be comparable to the maintenance required to add new job-types to pre-mailing service fee print site tables.

(e)   There could be a small loss of revenue, or a large gain in revenue. Based upon biweekly reports of the market test filed through February 25, 1999, only two mailings could have reduced revenues by qualifying for deeper discounts than Automation Basic. A rate reduction of 0.9 cents and 2.7 cents would have been available for 956 and 177 pieces, respectively—a revenue reduction of about 14 dollars. More importantly, however, the prospect of deeper discounts for qualifying mailings under my proposal may attract greater volumes. The result would be new net revenue contributions to the Postal Service.

MASA/OCA-T100-2. Have you determined or estimated any of the costs of implementing your pricing proposal in any of the categories listed below? If so, describe what you have done to determine or estimate the costs and the results. If not, explain why you have not done so.

     (a)   Designing software to implement the pricing proposal;

     (b)   Acquiring hardware to implement the pricing proposal;

     (c)   Maintaining hardware for implementation of the pricing proposal;

     (d)   Maintaining and updating software used to implement the pricing proposal;

     (e)   Loss of revenue as a result of lower postage rates than under the USPS proposal in some or all instances.

A.   (a)   No. Implementing my proposal involves three simple tasks: 1) accessing the presorting program that is already part of the Mailing Online system, 2) accessing volume data that is already being collected, and 3) performing simple arithmetic (i.e., the calculation of the blended discount rate via Equation 1). Modification of the code for each of these tasks should take no more than a few minutes. See OCA/USPS-T1-72(a)-(c). Nevertheless, determining whether the code modification would involve additional costs that can be estimated requires knowledge of the method of determining payments to the system developer (i.e., a general fixed-price contract, a job-specific payment, an hourly rate, etc.) for work performed. This information is not known to me.

     (b)   No. I have not estimated any hardware acquisition costs specific to the implementation of my proposal because no additional hardware will be necessary. See my response to MASA/OCA-T100-1(b).

     (c)   No. I have not estimated any hardware maintenance costs specific to the implementation of my proposal because no additional or special maintenance will be required. See my response to MASA/OCA-T100-1(c).

(d)   No. See my response to MASA/OCA-T100-1(d). The incremental cost of maintaining the code would be negligible, if any.

(e)   See my response to MASA/OCA-T100-1(e). Moreover, volume data at the level of detail necessary to estimate any changes in revenue under my proposal are not available. The Postal Service provided no volume estimates by presort level. *See* Tr. 6/1360 (Garvey, OCA/USPS-T1-49(b)(iii)). Nor does the Postal Service's market research "allow informed construction of precise estimates of volumes within subclass/job-type/page-count categories." Tr. 5/1103 (Plunkett, OCA/USPS-T5-35(f)-(i)). *See also* Tr. 2/617 (Plunkett, OCA/USPS-T5-28(b)). This information—presort-level volume data by job-type/page-count category—is necessary to determine any changes in revenue, either positive or negative.

MASA/OCA-T100-3. Confirm that your proposal would require MOL rates to be recalculated to reflect the additional costs incurred in implementing your proposal.

A.   Unable to confirm. I do not understand the phrase "MOL rates to be recalculated" as used in this context. There are Mailing Online pre-mailing service fees. Pre-mailing service fees offered to customers are determined by formula whose elements are contract printing costs, information system costs, and a 25 percent mark-up. If my proposal increases Mailing Online information system costs related to software design and maintenance, the increase would be too small to affect the pre-mailing fee formula.

There are also postage rates. I do not propose to change the single-piece or presort discount rates recommended by the Commission and approved by the Governors pursuant to Docket No. R97-1. Under my proposal, Mailing Online customers would pay postage charges based upon those rates. Mailing Online customers would pay postage charges for which their mailings would qualify under current rates if entered as hardcopy directly with the Postal Service, or postage charges consisting of a blended discount rate calculated by the pricing formula, whichever is lower.

MASA/OCA-T100-4. Referring to page 20 line 15 through page 21 line 2 of your testimony, have you estimated or projected the effect your pricing proposal would have on the postage rates available for Mailing Online, either as a whole or for any particular class or job type? If so, provide your estimates or projections and explain how you arrived at them. If not, why not?

A.   No. See my response to MASA/OCA-T100-3.

MASA/OCA-T100-5. Would your proposal delay the implementation of the MOL experimental service in order to allow development of systems necessary to implement the proposal? If so, how long would the delay last? Explain the basis for your response.

A.   Implementation of my proposal would require modest code modification.

However, it should not take long to complete such work and should not delay the

experimental service. See my response to MASA/OCA-T100-2(a).

MASA/OCA-T100-6. Confirm that the USPS pricing proposal gives a competitive advantage to MOL as compared with competitive service providers by exempting small-volume mailings from the minimum volume requirements for Automation Basic rates.

A.   Confirmed. *See* OCA-T-100, footnote 3, quoting PRC Op. MC98-1 at 35.

MASA/OCA-T100-7. With respect to your pricing proposal:

     (a)   Confirm that the proposal waives the minimum volume requirements for Automation Basic rates during the first quarter of the experimental period;

     (b)   Confirm that beginning in the second quarter the first quarter rates, which are based on a waiver of the minimum volume requirements to Automation Basic rates, will be one of the two factors affecting MOL rates; and

     (c)   State whether your proposal would eliminate the competitive advantage given to MOL in the USPS proposal through the waiver of minimum volume requirements.

     (d)   Explain the basis of your answers, with particular reference to the role played by the assumed single average discount rate in determining rates under your proposal.

A.   (a)   Confirmed. During the first quarter, the minimum volume requirements to

qualify for Automation Basic rates will be waived for mailings with volumes below the

minimum volume requirements. Under the proposed pricing formula, customers

submitting such mailings would pay Automation Basic rates. If a customer submits a

mailing with volumes in excess of the minimum volume requirements, the customer

would pay rates for which the mailpieces would qualify if entered in hardcopy directly

with the Postal Service.

     (b)   Partially confirmed. Refer to Equation 1 on page 29. There are two rate

components—x, representing the experience-based weighted average rate, and y, the

assumed single average discount rate—and a weighting factor, w, affecting the

calculation of the blended discount rate offered to Mailing Online customers. During the

second quarter, the pricing formula (i.e., Equation 1) will use experience-based

weighted average rates (x) derived from the first quarter presort-level volume data of

submitted mailings. The experience-based weighted average rates used in the formula

may or may not be based upon mailings where the minimum volume requirements have been waived. For example, the experience-based weighted average rate for a particular job-type/page-count category may be derived entirely from mailings that exceed the minimum volume requirements. Alternatively, the experience-based weighted average rate for that job-type/page-count category may be derived from mailings where only some of the mailings exceed the minimum volume requirements. It is also possible that the experience-based weighted average rate for the particular job-type/page-count category may be derived solely from mailings that did not meet the minimum volume requirements.

In this latter case, the experience-based weighted average rate used in the pricing formula during the second quarter would be the single piece rate. The result for a customer mailing the particular job-type/page count category is a blended postage rate that is greater than the Automation Basic rate proposed by the Postal Service.

(c) Yes. At the end of the Mailing Online experiment, the weighting factor (w) applied to the experience-based weighted average rate equals 1 (36/36), and the weight applied to the assumed single average discount rate equals 0 (1-(36/36)). See OCA-T-100, footnote 62. Moreover, the experience-based weighted average rate would be derived from presort-level volume data collected during the entire experiment. Should the Mailing Online experiment be extended, customers would continue to pay postage rates for which their mailpieces would qualify if entered as hardcopy directly with the Postal Service, or the historic experience-based weighted average rates

derived at the end of the experiment.

(d)   *See* OCA-T-100 at pages 29-31, lines 9-14, lines 1-14, and lines 1-6,

respectively.

MASA/OCA-T100-8. Referring to page 25 lines 1-3 of your testimony, explain why under your proposal "each customer would be offered the *greater* of its 'stand-alone' rate or a blended discount rate" (emphasis added).

A.   The emphasized word, *greater*, should be changed to "lesser." An appropriate

erratum will be filed. The entire, corrected sentence should read, "During the second

and subsequent periods, each customer is offered the lesser of its 'stand-alone' rate or

a blended discount rate consisting of the assumed single average discount rate and the

experience-based weighted average rate for the submitted job type."

MASA/OCA-T100-9. Under your proposal:

(a)   Would any MOL customer pay a higher postage rate for any mailing than would be available to it if its mailing were delivered to USPS in hard copy, separately from any other mailings? If so, explain in what circumstances an MOL customer would pay a higher rate and why. If not, explain why not.

(b)   Would any MOL customer pay a lower postage rate for any mailing than would be available to it if its mailing were delivered to USPS in hard copy, separately from any other mailings? If so, explain in what circumstances an MOL customer would pay a lower rate and why. If not, explain why not.

A.   (a)   No. Under my proposal, a Mailing Online customer would pay (1) a rate for which his/her mailpieces would qualify if entered as hardcopy directly with the Postal Service or (2) a rate reflecting the greater depths of sort resulting from Postal Service batching and presorting during the experiment, whichever is lower.

(b)   Yes. A customer could pay a lower rate for any Mailing Online mailing under the following circumstances: where, in any quarter, the postage pricing formula (i.e., Equation 1) produces a blended discount rate lower than would be available to that mailing if entered in hardcopy directly with the Postal Service.
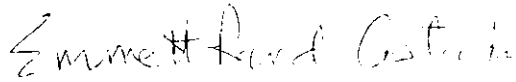
DECLARATION

I, James F. Callow, declare under penalty of perjury that the answers to

interrogatories MASA/OCA-T100-1-9 of the Mail Advertising Service Association are true

and correct, to the best of my knowledge, information and belief.

Executed _March 1 1999_

James F Callow

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the rules of practice.

Emmett Rand Costich

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