

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

POSTAL RATE AND FEE CHANGES, 2006)

Docket No. R2006-1

VALPAK DIRECT MARKETING SYSTEMS, INC. AND
VALPAK DEALERS' ASSOCIATION, INC.
THIRD INTERROGATORIES AND REQUESTS FOR
PRODUCTION OF DOCUMENTS TO UNITED STATES POSTAL SERVICE
WITNESS JAMES M. KIEFER (VP/USPS-T36-6-9)
(June 13, 2006)

Pursuant to sections 25 and 26 of the Postal Rate Commission rules of practice, Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. hereby submit interrogatories and document production requests. If necessary, please redirect any interrogatory and/or request to a more appropriate Postal Service witness.

Respectfully submitted,

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VP/USPS-T36-6.

Please refer to your response to VP/USPS-T36-1(e). Within the context of the minimum-per-piece rate for basic letters in Regular Commercial Standard, you were asked how thinking about your “base piece rate” of \$0.140 was helpful to you in leading to the final minimum per-piece rate of \$0.292.

The first sentence of your response is: “Generally, by establishing piece and pound rates and applying these to both piece-rated pieces and piece-and-pound-rated pieces, consistency at the break point can be easily achieved.”

- a. By “consistency at the break point,” do you mean anything other than that an ordinary graph of per-piece postage vs. per-piece weight (with the former on the vertical axis and the latter on the horizontal axis) does not have a discontinuity at a weight equal to the break point? If you do, please explain with specificity what you mean by achieving consistency at the break point.
- b. If you want to avoid a discontinuity of the kind referenced in part a of this question, please confirm that in “establishing piece and pound rates,” before you “apply” them, you have no choice but to honor the following equation:

$$\text{lb-rate} * 3.3/16 + \text{piece-rate-for-lb-rated-pieces} =$$

$$\text{minimum-per-piece-rate}$$

If you do not confirm, please discuss your reasoning and explain the freedom you see yourself as having in selecting the “piece and pound rates.” (Note: nothing in this question is meant to preclude normal rounding practices.)

- c. You say that by “applying” the various rate elements to the pieces involved, “consistency at the break point can be easily achieved.”
- (i) Please explain how “applying” the “piece and pound rates” helps you achieve consistency.
 - (ii) Please confirm that, in selecting the “piece and pound rates,” unless you purposefully honor the equation presented in part b of this question, consistency cannot and will not be achieved. Please explain fully any non-confirmation.

VP/USPS-T36-7.

Please refer to your response to VP/USPS-T36-1(e). The second and final sentence of your response is: “While letter-shaped pieces having weights greater than the break point do not pay piece and pound rates in the way nonletter-shaped pieces do, the parallel rate element structure used to develop the letter rates is useful in facilitating comparison between the proposed rates for letters and those for nonletter-shaped pieces.”

- a. Would you agree that, over the break point, the only difference between the rates for letters and nonletters is that letters pay a lower piece rate, one that is adjusted downward to reflect the lower costs of letters? If you agree, is this what you meant when you said these letters “do not pay piece and pound rates in the way nonletter-shaped pieces do”? If you disagree or mean something different, please explain how “the way” is different.

- b. By “parallel rate element structure,” do you mean to refer generally to the fact that, when plotted on a graph, the line for letters is parallel to and lower than the line for nonletters? If you mean something else, please explain. (Note: for purposes of this question, a “line” can be horizontal and then begin trending upward, but cannot be a curve and cannot have a discontinuity; also, two lines are parallel if the vertical distance between them is constant.)
- c. (i) Please explain how you found the “parallel rate element structure ... useful in” comparing the rates for letters and nonletters.
- (ii) Does this usefulness refer to anything other than that the vertical difference between the two lines noted in part b is the difference in rates between nonletters and letters of the same weight? If it does, please explain.
- (iii) In your “comparison” of the rates for letters and nonletters, did you give any consideration to the costs of each? If you did, please point with specificity to the costs you examined and to the role they played in establishing the differences. If you did not, please explain why costs would not be a relevant consideration in any “comparison” of the rates for letters and nonletters.
- d. Please consider the subject of VP/USPS-T36-1, that you “have developed a rate design methodology that differs from the ‘formula’ approach in use (with modifications) since Docket No. R90-1.” (USPS-T-36, p. 12, l. 26 to p. 13, l. 1.) Since you confirm in your response to part c of that interrogatory that you

used a “key” formula of some length, and since it seems apparent that you honored a formulaic relationship between the various piece and pound rate elements, to avoid a discontinuity in the rates, is it the case, as far as the rates for letters and flats are concerned, that the only difference between your approach and the earlier formula approach is that you removed from direct recognition in your calculations the cost information relating to differences between letters and flats? If you see any other differences between the approaches, please identify what they are.

VP/USPS-T36-8.

Please refer to your response to VP/USPS-T36-2(e), which presented you with a per-piece postage for mixed ADC machinable letters of 29.2 cents (equal in this case to the applicable proposed minimum-per-piece rate) and a cost for the same letters of 9.784 cents (which would increase to 9.856 cents if the information provided by witness Talmo in USPS-LR-L-135 were incorporated; *see* response of witness Talmo (USPS-T-27) to VP/USPS-T36-2(d), redirected from witness Kiefer, May 30, 2006), yielding a per-piece contribution of 19.42 cents (19.34 cents using the revised cost) and an implied cost coverage of 298.45 percent (296.27 percent using the revised cost), and asked for your confirmation or that you provide revised figures.

In your response to VP/USPS-T36-2(e), you did not confirm or provide any revised figures, except for the update provided by witness Talmo. You provided a three-sentence explanation, as follows, with numbering provided in brackets: “[1] I have seen no study that

provides comparable numbers for the test year and that are consistent with the cost data confirmed in subparts (a) and (b), above. [2] I would also note that there is a potential problem with using an average price estimate for all Standard Mail letters to develop unit costs for a highly de-averaged rate category. [3] I do not know how much the unit costs, exclusive of mail processing and carrier costs, for a non-drop-shipped, minimally presorted letter might vary from the average unit cost, assuming one were available.”

- a. With regard to sentence 1:
 - (i) Please confirm that the cost data in parts a and b of the question are for the test year, as developed by other Postal Service witnesses. If you do not confirm, please describe the vintage of the costs at issue.
 - (ii) Please explain what “numbers” you would need for the test year that are consistent with the test year cost data in parts a and b.
 - (iii) Please explain the nature of the “consistency” that you think is important.
- b. With regard to sentence 2:
 - (i) Please explain where “an average price estimate for all Standard Mail letters” has been used “to develop unit costs for” any category of mail, whether de-averaged or not.
 - (ii) When you refer to “all Standard Mail letters,” do you intend to include ECR and the Nonprofit categories? If not, please clarify the letters to which you are referring.

- (iii) Please clarify the nature of the “potential problem” about which you are concerned, indicating the likely magnitude of the problem and how likely it is to exist.
- c. With regard to sentence 3:
- (i) When you refer to “the unit costs, exclusive of mail processing and carrier costs,” are you referring to the unit cost of 0.7135 cents shown in cell N11 of tab ‘Unit Costs’ of LR-L-135.xls in USPS-LR-L-135? If you are not, please clarify the unit costs to which you are referring.
 - (ii) Is it your suggestion that, if this unit cost were dropship-corrected, the comparison made would be in order and meaningful? If you are not suggesting this, please clarify what you mean.
 - (iii) Please confirm that of the cost of 0.7135 cents, only 0.40 cents is transportation costs. Please explain any failure to confirm.
 - (iv) Please confirm that when dropship adjustments were made for ECR letters (see column I in tab ‘Results’ of workbook LR-L-84.xls in USPS-LR-L-84), the adjustment ranged from 0.138 cents to 0.225 cents. Explain any failure to confirm.
 - (v) Please provide any reason you have for believing that the difficulties to which you refer are significant in magnitude and would change in a meaningful way the picture painted by the per-piece contribution and implied cost coverage figures provided in the question.

VP/USPS-T36-9.

Please refer to the following paragraph in your testimony, USPS-T-36, beginning on line 27 of page 30.

My proposed rate design will also eliminate the Automation Basic rate category for letters. This rate is currently available only for mail sent to sites that do not receive letters from the plant in delivery point sequence. I understand that the Postal Service intends to further centralize the sequencing operations in plants to the greatest extent possible, reducing the dependence on automated or manual sorting in delivery units. (See witness McCrery, USPS-T-42, Section II, Part A, discussion of CSBCS equipment). In this light a two-track pricing scheme for automation letter mail is not warranted. With elimination of this rate I assume, for purposes of revenue estimation, that ECR and NECR Basic Automation letters will migrate to the Regular and Nonprofit Regular subclasses and pay the applicable Automation 5-digit rates. This is the likely rate paid by those letters that are addressed to areas for which the plant delivery point sequences letter mail. [USPS-T-36, p. 30, l. 27 to p. 31, l. 10.]

- a. Would you agree with the general proposition that the primary reason the Commission separated Regular and ECR into separate subclasses in Docket No. MC95-1 was to help recognize differences in demand, elasticity, market characteristics, density, and costs? If not, please explain any extent to which you disagree.
- b. In terms of demand, elasticity, market characteristics, density, costs, and any other factors you believe relevant, please explain any extent to which you find Basic Automation letters in ECR to be any less worthy to be in ECR and to receive any advantages associated with ECR than any other letters or flats in ECR.

- c. Please explain any consistency you see in having (i) fairly developed rates in ECR for Saturation Automation letters, and (ii) fairly developed rates in ECR for High-Density Automation letters, but (iii) no rates at all in ECR for Basic Automation letters. Do you believe any consistency you see is in line with the Postal Service's broad interest in developing and encouraging Automation letter mail?
- d. Did you attempt to develop a suitable rate in ECR for Basic Automation letters and have difficulties? If you did, please state what those difficulties were. If you did not, please explain why not.
- e. As a suitable rate for ECR Basic Automation letters, did you consider an approach such as rating them at 1 cent below the rate for 5-digit Automation letters in Regular, to provide some recognition to the factors listed in part a of this question? If you did, please explain that consideration and why you rejected it.
- f. Please present and discuss any analysis done by you or the Postal Service on the costs of ECR Basic Automation letters and Regular 5-digit Automation letters, and explain any differences in these costs.
- g. Do you agree that eliminating Basic Automation letters from ECR is a classification change rather than a rate change? Please explain any disagreement.