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BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, DC 20268-0001

EXPERIMENTAL PERIODICALS
CO-PALLETIZATION DROPSHIP
DISCOUNTS FOR HIGH EDITORIAL
PUBLICATIONS, 2004

Docket No. MC2004-1

DIRECT TESTIMONY
OF
ALTAF H. TAUFIQUE
ON BEHALF OF
UNITED STATES POSTAL SERVICE

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AUTOBIOGRAPHICAL SKETCH

My name is Altaf H. Taufique. I currently serve as an economist in the office of Pricing at the United States Postal Service.

I have testified before the Postal Rate Commission on eight occasions. In Docket No. MC96-3, I filed rebuttal testimony that addressed the Postal Service's role in the post office box market, and other issues relating to pricing of post office boxes. In Docket No. MC97-5, I rebutted a claim of undue harm to Postal Service competitors due to the proposed packaging service. In Docket No. R97-1, my direct testimony presented the rate proposals for the Periodicals Regular and Within County subclasses, and my rebuttal testimony challenged a proposal to allocate institutional costs based on weighted attributable costs. My testimony in Docket No. MC99-3 addressed the issue of a rate anomaly affecting Nonprofit and Classroom Periodicals mailers. In Docket No. MC2000-1 presented the Postal Service's proposal for an experimental "Ride-Along" classification for Periodicals. I presented the rates for the newly established Outside County and Within County subclasses of Periodicals in Docket No. R2000-1. My testimony, in Docket No. R2001-1, once again presented the rates for the Periodicals Outside County and Within County subclasses. My latest testimony in Docket No. MC2002-3 proposed an experimental per-piece discount for co-palletized and dropshipped mail lacking density to make ADC pallets absent co-palletization.

Prior to joining the Postal Service in July 1996, I was employed by the Gulf States Utilities Company (GSU) in Beaumont, Texas, from 1980 to 1994. At GSU, I served as an economic analyst in the Corporate Planning department and

was subsequently promoted to Economist, Senior Economist and finally to the position of Director, Economic Analysis and Forecasting. My responsibilities at GSU included the preparation of the official energy, load, and short-term revenue forecasts, and the economic forecasts, for the regions served by the Company. I testified before the Public Utility Commission of Texas in Austin and the Federal Energy Regulatory Commission in Washington, D.C, defending GSU's official energy and load forecasts.

I received a Master's Degree in Economics from Central Missouri State University in Warrensburg, Missouri in 1976, and a Bachelor's degree in Economics & International Relations from Karachi University in Karachi, Pakistan. I have also completed thirty-three credit hours of coursework towards a Ph.D. in Economics at Southern Illinois University. I taught economics at Chadron State College in Chadron, Nebraska between 1978 and 1980. During my employment at GSU in Texas, I taught courses in economics at Lamar University in Port Arthur, Texas.

1 **I. Purpose of Testimony**

2
3 My testimony proposes an experimental classification change that will test
4 the extent to which rate incentives will cause Periodicals mailers to co-palletize
5 their mail (especially high-editorial, heavy weight, small circulation publications),
6 and dropship it at either destination Area Distribution Centers (ADCs) or
7 destination Sectional Center Facilities (SCFs).¹ This proposal is a logical
8 extension of the current experimental per-piece discounts for co-palletized and
9 dropshipped pieces (Docket No. MC2002-3). In many instances, high-editorial
10 (editorial content is also referred to as non-advertising content), heavier weight,
11 small publications do not find the current discounts attractive enough to change
12 their behavior. The proposed experiment would provide per-pound discounts for
13 editorial pounds in co-palletized and dropshipped mail, based on the entry points
14 and zones skipped.

15 Similar to the current co-palletization discount, the proposed discounts
16 would offer an incentive for predominantly new worksharing, so rate increases
17 would not be needed to fund the lost revenue from existing activities. In addition,
18 since cost savings estimates are derived from the Docket No. R2001-1 materials,
19 as they were in Docket No. MC2002-3, no new cost studies are needed to
20 support this proposal. I am presenting the only direct testimony, including one
21 exhibit, in this filing. There are no library references or workpapers.

¹ While the Postal Service does not technically have Sectional Center Facilities anymore, this term is still used to refer to service areas for purposes of presorting and destination entry. See DMM § L005.

1 In conjunction with the proposed experimental classification change, I am
2 proposing to extend the current co-palletization experiment so that both
3 experiments expire at the same time. Finally, in a matter unrelated to the
4 experimental co-palletization proposal, I am proposing to add a minor Domestic
5 Mail Classification Schedule (DMCS) clarification to allow sample copies of
6 periodicals to be mailed with parcels using Package Services rates.

7 **II. Background/History**

8 9 **A. Current Co-palletization Experiment**

10
11 The current co-palletization experiment with per-piece discounts (Docket
12 No. MC2002-3) was implemented on April 20, 2003. As might be expected, the
13 program needed to “ramp up.” During Accounting Period (AP) 9 of FY2003, only
14 one printer/consolidator participated, co-palletizing 16 titles and 384,000 pieces.
15 Approximately 382,000 of these pieces qualified for the destination ADC (DADC)
16 co-palletization discount of \$0.007 per-piece. Since that humble start in AP9, the
17 experiment has gathered steam and the number of pieces eligible for the co-
18 palletization discounts for both DADC and destination SCF (DSCF) dropshipment
19 has increased almost every month. The last report filed with the Postal Rate
20 Commission (See www.prc.gov under Docket No. MC2002-3) in November 2003
21 shows over 9 million co-palletized pieces with a corresponding removal of over
22 180,000 sacks from postal operations.

23 We expect additional publications and printers/consolidators to participate
24 in the existing experiment, and at this point in time believe that this experiment

1 will lead to its desired results: better preparation and deeper penetration of
2 Periodicals mail into the postal system.

3 **B. Current Experiment - Not a Panacea**

4 In Docket No. MC2002-3, I testified that mailers make economic decisions
5 to palletize and dropship their mail based on (1) whether the mail volume and
6 density justify preparing pallets of 250 pounds (the minimum required weight),
7 and (2) whether the rate incentives and service benefits available make
8 dropshipping to a destination facility practical. Regarding density, many smaller
9 publications, along with the less dense portion of larger publications, cannot
10 achieve the minimum density required to palletize. I explained that one way to
11 increase mail density is to combine different publications on a pallet. Co-
12 palletization combines bundles of different publications going to the same
13 destination facility on the same pallet. MC2002-3, USPS-T-1, at 3.

14 The rate differential between dropshipped and non-dropshipped mail is of
15 utmost importance as an incentive to dropship the mail to a destination facility. If
16 the postage for destination entry is significantly lower than the postage for non-
17 dropshipped mail, then mailers may find it attractive to provide their own
18 transportation rather than purchasing it from the Postal Service.

19 Regardless of the merits of the flat editorial pound rate as a tool to
20 encourage widespread dissemination of information, both the proponents and
21 opponents of this flat rate would agree that it does not provide any incentive to
22 dropship mail with a high percent of editorial content. In the current rate
23 structure, the editorial pound rate is flat, so, to a large degree, dropshipping rate

1 differentials are a function of advertising content. Dropshipping incentives are
2 limited to per-piece discounts, along with per-pound incentives for the advertising
3 portion of a publication (to the degree that there is advertising content). The
4 higher the advertising content, the greater is the “dropship” to “non-dropship”
5 postage differential.

6 Thus, if we were to compare two small periodicals’ mailings that are
7 identical in all respects except advertising content, we would find that current co-
8 palletization incentives are much lower for the high-editorial publications. A small
9 national publication with a typical pound distribution to zones (based on the
10 profile of 49 small publications prepared in sacks), copy weight of 9 ounces, and
11 75 percent advertising content, pays approximately 50 cents per piece in
12 postage. A publication that is similar in all respects except advertising content
13 (zero percent advertising content) would pay 36 cents in postage. If these
14 publications decided to use the current co-palletization incentive, along with all
15 other available Periodicals incentives, to palletize and dropship their mail to the
16 destination ADC, the high advertising publication would pay 40 cents per piece in
17 postage, a reduction of 10 cents per piece. The high editorial content publication
18 would pay 34 cents, a reduction of only 2 cents. Thus, for “low” to “no”
19 advertising publications, the current co-palletization experiment falls short.

20 Under the proposed discounts for editorial pounds, the same high editorial
21 magazine would pay 31 cents, a 5 cent reduction from the original postage of 36
22 cents per-piece. This would be a reasonable incentive to move towards co-

1 palletization and dropshipment. (See worksheets '75% Ad.' and '0% Ad.' in
2 Exhibit A for the quantitative presentation of this example).

3

4 **C. Rationale for Proposal**

5 As discussed in the earlier example, the current per-piece incentives,
6 though successful with average publications, do not have a sufficient impact on
7 high-editorial publications. As previously described, the current rate structure for
8 Periodicals includes some incentives for mailers to prepare their mail in an
9 efficient fashion and to enter it closer to destination. Current experimental co-
10 palletization incentives work through "sweetening the pot a bit" by offering
11 additional per-piece incentives when mailers go through the extra step of
12 combining their mailings to build pallets and enter the mail deeper into the postal
13 system. Publications with little or no advertising are left out, especially if they
14 have heavier copy weights and lack the density to make single-publication
15 pallets. That is because the important weight ingredient of the "sweetener" is not
16 available for them. The challenge for the Postal Service is to find a middle
17 ground between leaving these publications in sacks, and proposing a more
18 fundamental change in the current rate structure at this time. The classification
19 proposal in this docket is the Postal Service's attempt to strike this balance.

20 The goal of this filing is to provide an incentive, using the editorial pound
21 structure, for eligible publications to co-palletize and dropship their mail. Even
22 when the first request for the experimental discounts for co-palletization and
23 dropshipment was filed in Docket No. MC2002-3, the Postal Service was aware

1 that this would not move all Periodicals mail from sacks to pallets, nor gain
2 greater dropshipping of all publications. This became evident when the Postal
3 Service was approached by a printer and a consolidator prior to the
4 implementation of the current experimental classification. The printer in question
5 had a substantial number of short-run publications with low advertising, heavy
6 copy weight, and national circulation. Most of these publications were prepared in
7 sacks and entered at the origin plant where the mailings are printed. This printer,
8 with the help of a consolidator, wanted to participate in co-palletization and
9 dropshipment as proposed in the current experiment, but was not able to do so
10 due to the high-editorial content of the publications and the subsequent lack of
11 postage savings, as discussed earlier in my testimony.

12 Using data reflecting typical characteristics for high editorial, heavy-weight
13 publications, I considered a couple of rate discount designs. A flat pound
14 incentive applicable to the total weight of the piece would not provide an accurate
15 signal, as it would either overcompensate local publications, or undercompensate
16 publications that needed to go relatively long distances. We concluded that the
17 only rate design solution that appeared to provide a fair, equitable, and adequate
18 incentive would involve discounts that applied to editorial pounds based on the
19 cost savings that the Postal Service would realize as a result of dropshipping and
20 skipping zones; that is, the discounts would reflect the difference between the
21 original zone for the mail if entered at the origin mailer's plant in sacks and the
22 DADC or DSCF entry point resulting from co-palletization and dropshipment.

23

1 **III. Application of Proposed Discounts**

2
3 **A. General Description**

4
5 In addition to meeting all the requirements of the current co-palletization
6 experimental classification, the proposed discounts would apply exclusively to
7 publications with the following characteristics:

- 8 a. Advertising content of 15 percent or less;
9 b. Copy weight of 9 ounces or more; and
10 c. Mailed circulation of 75,000 pieces or less (including all editions,
11 issues and supplemental mailings).

12 These criteria were established to meet the objectives of the experiment
13 that I am proposing. The primary objective is to promote the co-palletization and
14 dropshipping of heavier weight, low-advertising content, small circulation
15 publications. These proposed characteristics are designed to limit the experiment
16 to those publications most in need of an alternative discount structure.

17 The proposed discounts would apply to co-palletized bundles of
18 Periodicals mail that remain intact (the same bundles before and after co-
19 palletization), that move from sacks (absent co-palletization) to pallets presorted
20 to the ADC or SCF, and that are entered at the appropriate destination facility.
21 A publication that would otherwise be prepared in sacks, because it cannot meet
22 the required 250-pound minimum for an ADC pallet at the bindery, would qualify
23 for the proposed discount, if it were co-palletized with other publications on an
24 ADC or SCF pallet, and dropshipped to either the destination ADC or SCF.

1 Residual mail from a qualifying publication that remained after pallets were
2 prepared, would also qualify for the proposed discounts, as long as it was co-
3 palletized and dropshipped (e.g., less than 250 pounds of mail remaining for an
4 ADC, after SCF pallets are prepared for the ZIP Codes in that ADC service area).
5 The consolidator/mailler could preserve originally presorted mail for a single
6 publication on 5-Digit, 3-Digit (optional), SCF, and ADC pallets of 250 or more
7 pounds, but this mail would not qualify for the co-palletization incentives. Mailers
8 could build upon originally presorted SCF and ADC pallets, but only the co-
9 palletized pieces with less than 250 pounds per title or version would qualify for
10 the co-palletization incentives proposed in this experiment, if the pieces were
11 independently presorted for each ADC destination. Multiple versions or titles that
12 are presorted together into bundles through a selective binding operation would
13 qualify, if, as a result of co-palletization, the presorted bundles were to move from
14 sacks to pallets, be dropshipped, and meet the other prerequisites for the
15 discounts.

16 Other dropship and palletization incentives available in the current rate
17 schedule would apply to all pieces based on their eligibility (e.g., all dropship
18 discounts and the \$0.015 dropship pallet discounts for pieces on pallets of 250 or
19 more pounds that are dropshipped to DADCs or DSCFs). The only exceptions
20 would be the experimental Periodicals co-palletization and dropship discounts of
21 \$.01 and \$0.007 per piece. These would not apply to bundles using the proposed
22 per-pound discounts. In other words, mailers could claim either the per-piece or
23 per-editorial-pound experimental discounts, but could not claim both for the same

1 mail pieces. However, mailers might claim the experimental per-piece discount
2 for some bundles and per-pound discounts for some other bundles on the same
3 pallet if they were authorized to participate in the co-palletization experiments.
4 Supplemental mailings (e.g., back issues not part of the mailing of the current
5 issue) meeting the circulation requirement discussed above (i.e., total mailed
6 circulation not exceeding 75,000 copies including supplemental mailings,
7 prepared after, and separate from, the original mailing) would be treated as
8 separate mailings and would have to meet the same requirements for pieces to
9 be eligible for the additional incentives (for co-palletization/dropshipment). That
10 is, for the supplemental mailing, only pieces that could not have been prepared
11 on destination ADC pallets of 250 or more pounds under the original presort
12 before co-palletization would be eligible for the co-palletization incentives.

13 The Postal Service proposes to offer the co-palletization incentive to mail
14 prepared either on ADC or SCF pallets of 250 or more pounds. While mailers will
15 be expected to prepare pallets of at least 250 pounds, the Postal Service
16 recognizes the difficulty in always accurately predicting co-palletized volumes
17 and will allow mailers to claim the new discount for dropshipped pallets weighing
18 less than 250 pounds. It is expected that such pallets will represent an
19 insignificant portion of co-palletized mailings. Less than 250-pound pallets
20 (except overflow pallets) would not be eligible for the existing pallet discounts
21 (e.g., \$0.015 for dropshipped mail on pallets of 250 or more pounds).

22 I do not expect sufficient volumes to create finer levels of co-palletized
23 pallets, and I, therefore, am not proposing to offer additional incentives for this

1 experiment, beyond the DSCF entry level. To limit the scope of the experiment
2 and simplify administration, any mail that is co-palletized on 5-Digit or 3-Digit
3 pallets would not be entitled to the proposed co-palletization incentives.

4 **B. Waiving of “Finest-Level” Requirement**

5 In preparing a co-palletized mailing, mailers/consolidators cannot easily
6 predict co-palletized volumes for each destination. Therefore, during the
7 experiment, co-palletized mail would not be required to be placed on the finest
8 level pallet possible. For example, even if a co-palletized ADC pallet were to
9 contain more than 500 pounds to a particular SCF, an SCF pallet would not be
10 required. Mailers/consolidators would be encouraged to periodically re-evaluate
11 mail volumes for each ADC destination to determine whether additional SCF
12 pallets could be created on a regular basis.

13 **C. Documentation**

14 The consolidator/mailler will provide documentation (e.g., Mail.dat files that
15 can be printed, if necessary) only for the mail that is co-palletized, both before
16 and after co-palletization. To substantiate that mail would have been prepared in
17 sacks, the “before” documentation must be in Mail.dat or similar files that permit
18 easy identification of mailings (e.g., by job ID, segment ID, and container)
19 included in the co-palletization program, separate from mailings that are not
20 included in the program. The “after” documentation must identify publications or
21 segments with 250 or more pounds on a pallet (mail that does not qualify for
22 added co-palletization incentives), and publications or segments with less than
23 250 pounds remaining for an ADC, that do qualify for the new incentives.

1 Documentation would be by title and version, segment, or edition, or by codes
2 representing each title and version, segment, or edition. The consolidator/mailer
3 would develop a new file (e.g., Mail.dat) for the mail after co-palletization showing
4 how the mail was presorted and where it was entered. Data in the “after co-
5 palletization” files would be prepared so that they could be easily reconciled with
6 the “before” Mail.dat files, to validate that proper postage has been paid for all
7 pieces (e.g., the same job IDs and mailing segment IDs appear in “before”
8 Mail.dat files and “after” documentation.

9 The primary goal of this documentation would be to substantiate that,
10 without co-palletization, the mail would have been prepared in sacks (i.e., ADC
11 pallets of 250 or more pounds for any individual title, independently presorted
12 version, or selectively bound pool, could not have been made).

13 In addition to the above, for each title and version for which the per-pound
14 discount is claimed, the mailer would have to provide a detailed listing
15 documenting the distribution of total advertising and editorial pounds to each
16 zone “before” co-palletization, based on origin entry of the mail at the plant where
17 it is printed and presorted into bundles ready for co-palletization and mailing
18 (e.g., a modified version of the “before” postage statement showing the zoned
19 distribution of total copies, total pounds, and advertising pounds, if any, plus an
20 added column showing editorial pounds). This listing would be provided for all
21 publications claiming the discount, including publications with no advertising
22 content. The mailer would also provide a detailed listing that shows the total
23 editorial weight and experimental per-pound discount claimed for each title and

1 version by zone, based on the original zones reported on the zone listing “before”
2 co-palletization. For example, for 210 editorial pounds of mail that would have
3 been entered in Zone 3, if entered in sacks at the origin mailer’s plant, the “after”
4 documentation might show for Zone 3: 120 editorial pounds qualifying for the
5 DADC per-pound discount and 90 pounds qualifying for the DSCF per-pound
6 rate.

7 The Postal Service would retain the right to disallow any documentation
8 showing a change in the office of origin entry, if the physical printing of the title
9 has not moved to a different location.

10 **IV. Development of Discount**

11 **A. General Description**

12
13 Generally, the methodology used in this proposal is very similar to the one
14
15 used in Docket No. MC2002-3, but there are some exceptions. In Docket No.
16 MC2002-3, the Zones 1 & 2 rate was used as a benchmark to derive the
17 transportation and non-transportation cost savings from dropshipping to the
18 destination ADC or SCF. MC2002-3, USPS-T-1, at 11. In the current proposal,
19 all the zone rates are used to calculate the cost differential to the destination
20 ADC and SCF. In Docket No. MC2002-3 the per-pound cost savings were
21 converted to a per-piece basis, using both the average editorial content and
22 average weight of the piece. *Id.* In this proposal the savings are directly applied
23 to editorial pounds based on the zones skipped from the original mailer’s plant
24 when the mail is entered at either the destination ADC or SCF.
25

1 The proposed discounts in Table 1 are applicable just to editorial pounds
2 of the co-palletized mail prepared on an ADC or SCF pallet and entered at the
3 destination ADC and SCF. The discounts vary by the zones skipped as a result
4 of this preparation improvement and dropshipment of mail. For example, if, as a
5 result of co-palletization, 10,000 pounds of editorial material were entered at the
6 destination ADC instead of origin (defined as the postal facility that serves the
7 plant where the mail is printed and presorted into packages before co-
8 palletization), and that origin were six zones away from the destination delivery
9 address, then the value of the discount would be \$0.073 * 10,000, or \$730.

10

TABLE 1

Original Zone	DADC	DSCF
Zones 1 & 2	\$.008	\$.014
Zone 3	\$.013	\$.019
Zone 4	\$.028	\$.034
Zone 5	\$.050	\$.056
Zone 6	\$.073	\$.079
Zone 7	\$.101	\$.107
Zone 8	\$.125	\$.131

11

12 These discounts would be added to all the existing discounts for palletized and
13 dropshipped mail in the current rate chart (but would be instead of the per-piece
14 co-palletization discounts resulting from Docket No. MC2002-3).

1 The discounts were developed using advertising pound rates
2 recommended by the Commission and approved by the Governors in the last
3 rate case. I did not separately analyze potential cost savings, because the
4 differences between the zoned advertising pound rates reflect all pound-related
5 transportation and non-transportation cost savings that accrue to the Postal
6 Service when mail is entered closer to its destination.² This assumption reflects
7 the rate design I proposed in Docket No. R2001-1. MC2002-3, USPS-T-1, at 10.
8 The assumption also applies to the current advertising pound rates agreed upon
9 in the negotiated settlement and recommended by the Commission in Docket No.
10 R2001-1. The settlement pound rates are based on the same methodology as
11 the rates I proposed, with the simple substitution of a uniform rate for editorial
12 pounds.

13 The existing rate structure allows the mailer of advertising pounds to make
14 an economic decision regarding dropshipping based on the existing advertising
15 pound rate differentials. Thus, no additional per-pound incentive for advertising
16 pounds is needed to reflect the related transportation costs. On the other hand,
17 editorial pounds pay a uniform rate regardless of the entry point. This uniform
18 rate does not reflect the savings generated by dropshipping. Therefore, the cost
19 savings for editorial pounds constitute the basis for the development of the
20 proposed incentives.

² Advertising pound rates are calculated by allocating distance-related transportation cost to various zones using pound-miles (the product of advertising pounds and average haul in miles for each zone). Further, the pound-related portion of non-transportation cost savings is fully passed through to estimate the destination entry advertising pound rates.

1 The Postal Service is proposing a two-year experimental classification to
2 allow high-editorial, heavier weight, small circulation publications to receive the
3 proposed discounts on editorial pounds for pieces that are co-palletized and
4 dropshipped, and meet all required conditions. The two year period would allow
5 the Postal Service to gauge the attractiveness of such a change in the discount
6 structure as well as the level of discounts compared to the workshare required.
7 Also, we are requesting that the Commission extend the current co-palletization
8 experiment so that both of these experiments conclude at the same time. It is
9 hoped that any future classification or structural change in the rate schedule
10 would address both experiments together. The proposed classification language
11 would also allow both experiments to continue until a proposal for a permanent
12 discount is resolved, if that proposal is filed before the end of the two year period.

13 **B. Methodology**

14 Using the zoned advertising pound rates, I estimate the cost savings that
15 result from dropshipping editorial pounds from the various zones to both the
16 DADC and DSCF. Thus, a pound of mail entered at the destination SCF,
17 compared to a pound entered in Zone 5, would save the Postal Service 18.6
18 cents (38.9 cents minus 20.3 cents) in transportation and non-transportation
19 costs. Applying a 30 percent passthrough produces a discount of 5.6 cents per
20 editorial pound for pieces that are co-palletized and dropshipped at the
21 destination SCF. Similarly, for the destination ADC the cost savings are 16.6
22 cents (38.9 cents minus 22.3 cents) per pound. Applying, once again, a 30
23 percent passthrough results in the proposed 5.0 cents per editorial pound

1 discount for co-palletized and dropshipped pieces that shift from zone 5 to
2 destination ADC entry. Discounts for all the zones are calculated in a similar
3 fashion for dropshipment to destination ADCs and SCFs. These calculations,
4 including the unrounded numbers actually used, are presented in Exhibit A.

5 **C. Rationale for Conservative Approach**

6 The Postal Service has deliberately chosen a conservative approach in
7 developing these discounts. This approach was motivated by three goals. The
8 first goal is to assure that there is no erosion of the low subclass markup due to
9 this classification change. The second goal is to provide sufficient incentive for
10 high-editorial publications to participate in co-palletization programs. Because of
11 this second goal, I based the discounts on zones skipped. This structure provides
12 a fair and equitable way to provide discounts based on the actual worksharing.
13 The third goal is to ensure that non-participants not only avoid any rate
14 increases, but also receive the benefit of substantial additional cost reductions
15 that may accrue to Periodicals resulting from the proposed discounts.

16 Finally, my conservative (30 percent) passthrough reflects the application
17 of the discount to an editorial pound rate that is already low. The 19.3 cent rate
18 charged for editorial pounds is based on the percent of revenue derived from
19 editorial pounds in the base year of Docket No. R2001-1, and is approximately
20 78 percent of the Zones 1 & 2 advertising pound rate. This rate is not designed to
21 reflect the cost of transporting editorial pounds. Using a 100 percent passthrough
22 of the cost savings would mean providing discount levels that are inappropriately
23 high relative to the base rate.

1 **V. Designation as Experimental**

2
3 **A. Objectives of Experiment**

4
5 The objective of this experiment is twofold. The first objective is to gauge
6 the feasibility of using a discount to change the behavior of publications that are
7 not able to use the current experimental classification for co-palletizing and
8 dropshipping mail. The experiment would allow testing, on a limited basis, of
9 whether we can adequately administer a destination-entry discount based on the
10 number of zones skipped. The second objective is to provide an incentive to
11 reduce the number of sacks and get mail entered at specific destination facilities.

12 **B. Compliance with Section 3001.67**

13
14 **1. Novel in Nature**

15 My testimony in Docket No. MC2002-3 regarding the novelty of the
16 experimental classification applies to my current proposal as well:

17 Providing a worksharing discount, per se, is not novel, but a
18 discount that predominantly applies to new worksharing and does
19 not require a push-up of other rates is unusual in the ratemaking
20 context. This classification targets mail that is otherwise prepared in
21 sacks, that is expensive for mailers to prepare and the Postal
22 Service to handle, and that is almost always origin entered. The
23 proposal is also novel because it focuses on a worksharing
24 discount for less dense publications, and provides an incentive for
25 publishers and printers to cooperate in a fashion that benefits both
26 mailers and the Postal Service.

27
28 MC2002-3, USPS-T-1 at 13-14.

29
30 In addition, the current proposal uses a discount structure that focuses on
31 editorial pounds, and calculates the postage using not only the destination where
32 the mail is entered, but also where the mail would be entered in the absence of
33 this co-palletization and dropshipment.

1 **2. Magnitude of the Proposed Change**
2

3 I believe that the proposed incentives, combined with the existing dropship
4 and palletization incentives, may produce a significant, though limited, reduction
5 in the number of sacks in Periodicals mailings, and lead to a greater portion of
6 Outside County periodicals being entered at either the destination SCF or ADC.

7 Given the advertising, circulation, and copy weight limits, we estimate that
8 approximately 20 million pieces per year would be able to take advantage of
9 these experimental discounts, removing over 400,000 sacks from postal
10 operations (assuming 49 pieces per sack derived from the last report filed with
11 the Postal Rate Commission in November 2003 - See www.prc.gov under Docket
12 No. MC2002-3). Additionally, I believe that some printers, if they are able to co-
13 palletize their high-editorial publications, would choose to eliminate all sacking
14 operations from their plants. Therefore, they would co-palletize all of their
15 publications, including low-editorial publications. Some publications that may not
16 be eligible for the proposed discounts thus would qualify for the existing co-
17 palletization discounts. This would increase the volume for the current
18 experiment.

19 Cost savings are expected to be greater than the estimated revenue
20 leakage, using the conservative passthroughs underlying the discounts.
21 Additional cost savings could accrue due to palletization alone (slightly more than
22 0.5 cents per piece).

23
24

3. Data Collection

The following is a description of the Postal Service's data collection plan for the proposed experiment. The purpose of the data collection is to provide a measure of the experiment's effectiveness, and the data necessary to prepare any request for a related permanent classification change. This plan has been designed to collect data required by the Commission's Rules 64 and 54, and data desired for postal management's evaluation of the proposed discounts.

First, the Postal Service proposes to collect the data that would be reported in the RPW system, that is, the editorial pounds shifting from the various zones to destination ADCs and SCFs.

Second, the Postal Service plans to obtain data from the experiment's participants using a spreadsheet similar to the one being used in the current experiment. Using these data, the Postal Service plans to report the following data:

- number of pieces receiving the ADC discount
- number of pieces receiving the SCF discount
- number of titles receiving one or both of the co-palletization discounts
- number of containers that would have been sacks without consolidation, as well as their weight and the number of addressed pieces
- number of sacks after consolidation, as well as their weight and the number of addressed pieces
- number of pallets qualifying for the ADC discount, as well as their weight and the number of addressed pieces

- 1 - number of pallets qualifying for the SCF discount, as well as
- 2 their weight and the number of addressed pieces
- 3
- 4 - editorial and total pounds shifting to destination ADCs from the
- 5 various zones.
- 6
- 7 - editorial and total pounds shifting to destination SCFs from the
- 8 various zones.
- 9

10 These reports will be filed with the Commission on a schedule matching
11 Postal Service fiscal year quarters. The first report will cover the first two
12 quarters during which the experiment is in effect, although the timing might be
13 adjusted so that the reporting schedule can match the schedule for the existing
14 co-palletization experiment. This first report might be for less or more than two
15 full quarters if the experiment begins in the middle of a quarter. Subsequent
16 reports will cover two full quarters for the duration of the experiment. Reporting
17 data every six months will reduce unnecessary paper flow, while still providing
18 regular and up-to-date information on the progress of the experiment. The Postal
19 Service anticipates that collection of the data and preparation of each report will
20 take between six and eight weeks, following the end of a reporting period.

21

22 **VI. Classification Criteria**

23

24 Section 3623(c) of Title 39 U.S.C. requires the Commission to make its
25 decision on establishing a new classification in accordance with the following
26 factors:

- 27 1. the establishment and maintenance of a fair and equitable
- 28 classification system for all mail;
- 29

- 1 2. the relative value to the people of the kinds of mail matter entered into
2 the postal system and the desirability and justification for special
3 classifications and services of mail;
4
- 5 3. the importance of providing classifications with extremely high degrees
6 of reliability and speed of delivery;
7
- 8 4. the importance of providing classifications which do not require an
9 extremely high degree of reliability and speed of delivery;
10
- 11 5. the desirability of special classifications from the point of view of both
12 the user and of the Postal Service; and
13
- 14 6. such other factors as the Commission may deem appropriate.
15

16
17 I believe that the proposed classification is fair and equitable (criterion 1)
18 in a comprehensive sense, because it improves the preparation of mail for the
19 whole class, and increases dropshipment, thereby reducing costs. Additionally, it
20 does not adversely affect the non-participants. Superficially, an argument could
21 be made that the Postal Service is offering a discount on only some of the mail
22 that is palletized and dropshipped to destination facilities. There is a significant
23 volume of palletized and dropshipped mail that would not qualify for the proposed
24 discount. However, the proposed classification change provides incentives for
25 mailers that physically cannot palletize and, because of high-editorial content, are
26 not able to dropship.

27 My understanding is that preparing mail on pallets, and dropshipping it at
28 a destination facility, is often not a matter of choice, especially if the publication
29 contains little or no advertising. A mailer with limited mail density does not have
30 enough volume for specific destinations, even for an ADC, the broadest
31 destination category for dropshipping Periodicals. Absent co-palletization, these

1 mailers would have no choice but to sack their mail. In fact, my understanding is
2 that preparing mail in sacks is an expensive proposition for the mailer. For the
3 Postal Service, transporting this mail across the country is also costly. Handling
4 of sacks with relatively few pieces requires more work both in transit and at the
5 destination facility, leading to higher costs for Periodicals. By offering this
6 discount exclusively to the publications or portions of publications that do not
7 have the density to make a 250-pound ADC pallet and have zero to little
8 advertising matter, the Postal Service would be making the mail processing for
9 the subclass more efficient, and, thereby, reducing total costs. Thus this
10 classification would benefit all Periodicals mailers.

11 Also, the mailers of publications that do not have the density to make a
12 250-pound ADC pallet will incur additional costs when combining their mail with
13 other similar publications. Besides the additional costs of space, transportation,
14 sortation, and documentation that are mentioned earlier, these publications also
15 might sacrifice some delivery time because the mail is held back for a day or
16 more while being co-palletized. Thus, these mailers may need an additional
17 discount to reach the same level of worksharing as other mailers.

18 In summary, criterion 1 (fairness and equity) would be satisfied, because
19 this proposed classification change would benefit the entire Periodicals Outside
20 County subclass with the prospect of reduced postage costs for participants and
21 improved overall efficiency of the subclass, which benefits nonparticipants. It
22 would provide an incentive to the mailers who currently cannot palletize and
23 dropship on their own due to the nature of their mail. An economic incentive

1 would encourage them to cooperate with other printers and publishers. The
2 benefit received would be less than the postal cost saved, and those who are
3 currently performing these worksharing tasks would not be harmed.

4 Criterion 2 (the relative value to the people of the kinds of mail matter
5 entered into the postal system and the desirability and justification for special
6 classifications and services of mail) would be satisfied in several ways. The
7 discounts would promote the distribution of Periodicals mail with high
8 educational, cultural, scientific, and informational (ECSI) value, given the
9 requirement for 85 percent or more editorial content. Mailers would be
10 compensated for their co-palletization and dropshipment worksharing. Costs from
11 origin-entered sacks could be reduced. Overall, this proposal would help the mail
12 remain affordable for the recipient, and help maintain the widespread
13 dissemination of editorial matter.

14 Criterion 5 (the desirability of special classifications from the point of view
15 of both the user and of the Postal Service) would be satisfied because the Postal
16 Service's costs are reduced, and we expect mailers to gain from the success of
17 this proposed experimental classification.

18 In summary, the proposed experimental classification meets all the
19 applicable criteria.

20

21 **VII. Enclosing Periodicals in Package Services**

22

23 Although not directly related to the co-palletization experiments, I am
24 proposing a minor change to the DMCS regarding what can be enclosed in a

1 piece mailed as Package Services mail. Currently, Section 511(b) of the DMCS
2 states that any mailable matter may be mailed as Package Service mail except:

3 Copies of a publication that is entered as Periodicals class mail,
4 except copies sent by a printer to a publisher, and except copies
5 that would have traveled at the former second-class transient rate.
6 (The transient rate applied to individual copies of second-class mail
7 (currently Periodicals class mail) forwarded and mailed by the
8 public, as well as to certain sample copies mailed by publishers.)
9

10 Even though this section refers to “sample copies”, it has been interpreted
11 as disallowing the enclosure of a sample copy of a publication that is also being
12 mailed as Periodicals class mail. The current language is linked to the former
13 “transient rate” and is too narrow to allow the simple inclusion of a sample copy
14 for promotional purposes, or as a premium for purchasing a product that is being
15 shipped via Package Services. The proposed revision breaks the passage cited
16 above into two subparts, and adds a third subpart that allows:

17 sample copies enclosed or attached with merchandise sent at
18 Parcel Post or Bound Printed Matter rates.
19

20 Although this modification is not a major classification change, it is
21 advisable to note that it is consistent with the relevant factors listed in Section
22 3623(c) of Title 39.³ It is “fair and equitable” (criterion 1) in that it does not
23 adversely affect any existing classifications since existing regulations regarding
24 eligibility (such as the subscriber percentage) for Periodicals rates are not
25 changed. Also, it does not change the relative value of Parcel Post or Bound
26 Printed Matter. Most importantly, the modification is consistent with criterion 5 in

³ See section VI. for a listing of the factors.

1 that it is desirable from the point of view of both the user and the Postal Service.
2 In addition to the general improvement in the clarity of the classification schedule,
3 as a practical matter it provides another avenue for promoting publications. This,
4 of course, helps customers (and printers and advertisers, too) if it results in
5 added subscriptions.

EXHIBIT A

Calculation of Discounts and Revenue/Cost Impacts

CALCULATION OF DISCOUNTS AND COST/REVENUE IMPACTS

Advertising Pound Rates

Zone	Rate
DDU	\$ 0.158
DSCF	\$ 0.203
DADC	\$ 0.223
Zones 1 & 2	\$ 0.248
Zone 3	\$ 0.267
Zone 4	\$ 0.315
Zone 5	\$ 0.389
Zone 6	\$ 0.466
Zone 7	\$ 0.559
Zone 8	\$ 0.638

Zone differential From :

	DADC	DSCF
Zones 1 & 2	\$ 0.025	\$ 0.045
Zone 3	\$ 0.044	\$ 0.064
Zone 4	\$ 0.092	\$ 0.112
Zone 5	\$ 0.166	\$ 0.186
Zone 6	\$ 0.243	\$ 0.263
Zone 7	\$ 0.336	\$ 0.356
Zone 8	\$ 0.415	\$ 0.435

Pass-through	30%
--------------	-----

Discounts applicable to editorial pounds

	DADC	DSCF
Zones 1 & 2	\$ 0.008	\$ 0.014
Zone 3	\$ 0.013	\$ 0.019
Zone 4	\$ 0.028	\$ 0.034
Zone 5	\$ 0.050	\$ 0.056
Zone 6	\$ 0.073	\$ 0.079
Zone 7	\$ 0.101	\$ 0.107
Zone 8	\$ 0.125	\$ 0.131

Total Piece Qualifying	20,000,000	
Pieces Qualifying for ADC entry	18,000,000	90%
Pieces Qualifying for SCF entry	2,000,000	10%
SCF Revenue Leakage		
Pieces	2,000,000	
Weight per Piece	0.594	
Total Weight	1,187,500	
Advertising Content	0.05	
Editorial Content	0.95	
Editorial Weight	1,128,125	

Calculation of Revenue Leakage

	Editorial Pounds	Dist.	Discounts	Revenue Leakage
Zones 1 & 2	215,538	19.1%	\$ 0.014	\$ 3,018
Zone 3	166,437	14.8%	\$ 0.019	\$ 3,162
Zone 4	177,933	15.8%	\$ 0.034	\$ 6,050
Zone 5	214,410	19.0%	\$ 0.056	\$ 12,007
Zone 6	105,407	9.3%	\$ 0.079	\$ 8,327
Zone 7	50,784	4.5%	\$ 0.107	\$ 5,434
Zone 8	197,616	17.5%	\$ 0.131	\$ 25,888
Total	1,128,125			\$ 63,885

Calculation of Cost Savings

	Editorial Pounds	Zone Differential	Cost Savings
Zones 1 & 2	215,538	\$ 0.045	\$ 9,699
Zone 3	166,437	\$ 0.064	\$ 10,652
Zone 4	177,933	\$ 0.112	\$ 19,928
Zone 5	214,410	\$ 0.186	\$ 39,880
Zone 6	105,407	\$ 0.263	\$ 27,722
Zone 7	50,784	\$ 0.356	\$ 18,079
Zone 8	197,616	\$ 0.435	\$ 85,963
Total			\$ 211,924

Total Piece Qualifying	20,000,000	
Pieces Qualifying for ADC entry	18,000,000	90%
Pieces Qualifying for SCF entry	2,000,000	10%
ADC Revenue Leakage		
Pieces	18,000,000	
Weight per Piece	0.594	
Total Weight	10,687,500	
Advertising Content	0.05	
Editorial Content	0.95	
Editorial Weight	10,153,125	

Calculation of Revenue Leakage

	Editorial Pounds	Dist.	Discounts	Revenue Leakage
Zones 1 & 2	1,939,843	19.1%	\$ 0.008	\$ 15,519
Zone 3	1,497,930	14.8%	\$ 0.013	\$ 19,473
Zone 4	1,601,397	15.8%	\$ 0.028	\$ 44,839
Zone 5	1,929,691	19.0%	\$ 0.050	\$ 96,485
Zone 6	948,662	9.3%	\$ 0.073	\$ 69,252
Zone 7	457,058	4.5%	\$ 0.101	\$ 46,163
Zone 8	1,778,544	17.5%	\$ 0.125	\$ 222,318
Total	10,153,125			\$ 514,049

Calculation of Cost Savings

	Editorial Pounds	Zone Differential	Cost Savings
Zones 1 & 2	1,939,843	\$ 0.025	\$ 48,496
Zone 3	1,497,930	\$ 0.044	\$ 65,909
Zone 4	1,601,397	\$ 0.092	\$ 147,329
Zone 5	1,929,691	\$ 0.166	\$ 320,329
Zone 6	948,662	\$ 0.243	\$ 230,525
Zone 7	457,058	\$ 0.336	\$ 153,572
Zone 8	1,778,544	\$ 0.415	\$ 738,096
Total			\$ 1,704,255

Pieces 65,000
 Weight 0.5625
 Advertising 75%
 Editorial 25%
 Total Pounds 36,563

	Distribution	Pieces	Editorial Pounds	Advertising Pounds	Rates	Postage
Zone 1 & 2	19.1%	12,419	1,746	5,239	\$ 0.248	\$ 1,299
Zone 3	14.8%	9,590	1,349	4,046	\$ 0.267	\$ 1,080
Zone 4	15.8%	10,252	1,442	4,325	\$ 0.315	\$ 1,362
Zone 5	19.0%	12,354	1,737	5,212	\$ 0.389	\$ 2,027
Zone 6	9.3%	6,073	854	2,562	\$ 0.466	\$ 1,194
Zone 7	4.5%	2,926	411	1,234	\$ 0.559	\$ 690
Zone 8	17.5%	11,386	1,601	4,804	\$ 0.638	\$ 3,065
		65,000	9,141	27,422		\$ 10,718
Editorial Pounds					\$ 0.193	\$ 1,764
Pound Revenue						\$ 12,482
Piece Revenue @ Basic Automation				65,000	\$ 0.325	\$ 21,125
Nonadvertising					\$ (0.074)	\$ (1,203)
Total Postage						\$ 32,405
Per-Piece Postage						0.50

Current Copalletization Experimental Classification

Advertising Pounds						
DADC				27,422	\$ 0.223	\$ 6,115
Editorial Pounds				9,141	\$ 0.193	\$ 1,764
Pound Revenue						\$ 7,879
Piece Revenue				65,000	\$ 0.325	\$ 21,125
Nonadvertising					\$ (0.074)	\$ (1,203)
DADC Entry Piece Discount				65,000	\$ (0.002)	\$ (130)
Palletized Dropship Discount				65,000	\$ (0.015)	\$ (975)
Per-Piece Experimental Classification Discount				65,000	\$ (0.007)	\$ (455)
Total Postage						\$ 26,242
Piece Postage						\$ 0.40

Pieces 65,000
 Weight 0.5625
 Advertising 0%
 Editorial 100%
 Total Pounds 36,563

	Distribution	Pieces	Editorial Pounds	Advertising Pounds	Rates	Postage
Zone 1 & 2	19.1%	12,419	6,986	-	\$ 0.248	\$ -
Zone 3	14.8%	9,590	5,394	-	\$ 0.267	\$ -
Zone 4	15.8%	10,252	5,767	-	\$ 0.315	\$ -
Zone 5	19.0%	12,354	6,949	-	\$ 0.389	\$ -
Zone 6	9.3%	6,073	3,416	-	\$ 0.466	\$ -
Zone 7	4.5%	2,926	1,646	-	\$ 0.559	\$ -
Zone 8	17.5%	11,386	6,405	-	\$ 0.638	\$ -
		65,000	36,563	-		\$ -
Editorial Pounds					\$ 0.193	\$ 7,057
Pound Revenue						\$ 7,057
Piece Revenue @ Basic Automation				65,000	\$ 0.325	\$ 21,125
Nonadvertising					\$ (0.074)	\$ (4,810)
Total Postage						\$ 23,372
Per-Piece Postage						0.36

Current Copalletization Experimental Classification

Advertising Pounds						
DADC				-	\$ 0.223	\$ -
Editorial Pounds				36,563	\$ 0.193	\$ 7,057
Pound Revenue						\$ 7,057
Piece Revenue				65,000	\$ 0.325	\$ 21,125
Nonadvertising					\$ (0.074)	\$ (4,810)
DADC Entry Piece Discount				65,000	\$ (0.002)	\$ (130)
Palletized Dropship Discount				65,000	\$ (0.015)	\$ (975)
Per-Piece Experimental Classification Discount				65,000	\$ (0.007)	\$ (455)
Total Postage						\$ 21,812
Piece Postage						\$ 0.34

Proposed Copalletization for High Editorial Publications

Advertising Pounds						
DADC				-	\$ 0.223	\$ -
Editorial Pounds						
				36,563	\$ 0.193	\$ 7,057
Pound Revenue						\$ 7,057
Piece Revenue						
				65,000	\$ 0.325	\$ 21,125
Nonadvertising						
					\$ (0.074)	\$ (4,810)
DADC Entry Piece Discount						
				65,000	\$ (0.002)	\$ (130)
Palletized Dropship Discount						
				65,000	\$ (0.015)	\$ (975)
Per-Piece Experimental Classification Discount						
				65,000	\$ -	\$ -
Total Postage						\$ 22,267
Piece Postage						\$ 0.34
Proposed Co-palletization based on Original Zone Distribution						
Zones 1 & 2	\$ 0.008	6,986	(56)			
Zone 3	\$ 0.013	5,394	(70)			
Zone 4	\$ 0.028	5,767	(161)			
Zone 5	\$ 0.050	6,949	(347)			
Zone 6	\$ 0.073	3,416	(249)			
Zone 7	\$ 0.101	1,646	(166)			
Zone 8	\$ 0.125	6,405	(801)			
			(1,851)			
						\$ 20,415
						\$ 0.31

Magazine	Total	Distribution										
39	40	41	42	43	44	45	46	47	48	49		
324	1,255	3,836	1,719	3,832	382	1,017	1,029	306	440	1,239	57,895	19.1%
206	678	1,923	1,279	1,739	352	542	1,083	327	134	618	44,706	14.8%
103	1,381	2,487	1,744	1,981	742	791	758	194	156	995	47,794	15.8%
211	387	1,293	1,862	2,921	608	1,063	1,222	323	325	291	57,592	19.0%
103	172	649	1,142	1,452	409	551	1,007	269	113	98	28,313	9.3%
53	90	245	559	539	239	264	619	339	58	170	13,641	4.5%
525	1,090	1,878	1,236	811	686	909	1,485	1,132	255	884	53,081	17.5%
											303,022	