

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

POSTAL RATE AND FEE CHANGES, 2006

Docket No. R2006-1

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

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AUTOBIOGRAPHICAL SKETCH

My name is Altaf H. Taufique. I serve as an Economist in the office of Pricing, which is a component of Pricing and Classification Department, within the Marketing group at the United States Postal Service headquarters. I testified earlier in this docket, presenting the First-Class Mail rate design proposals of the United States Postal Service (USPS-T-32). I incorporate by reference the autobiographical sketch reflected at page(s) ii to iii of that testimony.

Purpose and Scope of Testimony

The purpose of this testimony is to respond to the alternative Periodicals rate proposals by the Magazine Publishers of America, Inc. and the Alliance of Nonprofit Mailers, and by Time Warner, Inc., and explain why the Postal Service prefers its proposal.

Background

Over the last few years, the rate design philosophy for the Periodicals Outside County subclass has been to move consistently and gradually in the direction of lower-cost preparation, especially by providing incentives for reducing the number of containers, and for destination entry. This gradual approach was brought about by the desire of the Postal Service to temper the rate impact of the changes. In Docket No. R2001-1, the Postal Service proposed a discount for palletized pieces, a discount for editorial pounds dropshipped closer to destination, and new destination Area Distribution Center (DADC) piece and pound rates. The Docket No. R2001-1 settlement resulted in two separate pallet discounts, one general in nature, and one limited to dropshipped pallets. The second discount replaced the proposed dropship incentives for editorial pounds.

After the implementation of the Docket No. R2001-1 rates, the Postal Service worked with the mailing community on experimental rates for publications that were willing to co-palletize their mail pieces with other titles and dropship them at least to the destination ADC. This resulted in the filing of Docket No. MC2002-3 in September of 2002. The Postal Service offered modest

discounts, without pushing up other rates, to change the behavior of mailers that were preparing at least part of their mail in sacks, but were willing to combine their bundles with other mailers to prepare at least an ADC pallet and dropship to the destination ADC or deeper. Today co-palletization is an available option to many mailers because of the success of this co-palletization experiment.¹

The resulting rates have contributed to significant improvements in mail preparation during the last few years. The Postal Service, the Commission, and mailers can be justifiably proud that dropshipment to the destination facilities has increased, along with the number of pieces per container. Table 1 below shows the percentage of dropshipped and palletized Outside County Periodicals mail has increased significantly in the recent several years.

Table 1 Percentage of Dropshipped and Palletized Periodicals Mail

	FY 2003	FY 2004	FY 2005
Total OC Pieces	8,526,522,074	8,375,251,711	8,307,329,578
Total Dropship Pieces	4,306,076,943	5,083,751,740	5,166,251,379
Dropship % of Total	50.50%	60.70%	62.19%
Total Piece on Pallets	4,647,764,731	5,935,720,156	6,024,444,666
Palletized % of Total	54.51%	70.87%	72.52%

Source: FY2003, FY2004, FY2005 Periodicals Billing Determinants

¹ Subsequently, the Postal Service filed another co-palletization experiment in Docket No. MC2004-1, for high-editorial, heavier weight publications. This experiment has not been a success due to changed circumstances, including higher fuel costs, that were beyond the control of the Postal Service as well as the publishers that prepared high-editorial, heavier weight pieces.

Table 2 shows that, as a result of the price signals, Periodicals mail's use of containers also has become more efficient.

Table 2 Periodicals Pieces per Container

	Periodicals Pieces per Container
FY 1996	69.91
FY 2000	95.00
FY 2005	113.49

Note: Copies per Container for FY2000

Source: Periodicals Mail Characteristics Study

For comparison, Standard Mail flats averaged over 400 pieces per container in FY2005. Therefore, further improvements in Periodicals containerization should be possible, with the proper incentives and straightforward price signals.

Current Proposal

The current proposal is a logical continuation of this philosophical approach to provide modest incentives for improvement in preparation, while avoiding large rate impacts for non-participants. Witness Tang's testimony (USPS-T-35) provides the justification for the current proposal and its balanced approach.

During the development of the proposal for Periodicals' rate design, my colleague witness Tang had to consider several options. One option was a complete overhaul of the rate structure, as proposed by our colleagues representing Time Warner, Inc. Another option was to reward mail that is already prepared efficiently, as proposed by our colleagues representing the Magazine Publishers of America, Inc. and the Alliance of Nonprofit Mailers (MPA/ANM),

and supported by U.S. News & World Report, L.P. witness White (USNews-T-1).²

The third option was to continue with the balanced approach that has been pursued by the Postal Service. This approach would continue to improve mail preparation, while being mindful of the impact on a wide variety of mailers who currently may not be in the position of taking advantage of the co-palletization and/or comailing opportunities that are being used by other customers.

This is not to say that the Postal Service is opposed, in principle, to the type of structural changes proposed by Time Warner or the type of de-averaging proposed by MPA/ANM with a 5-digit pallet discount. In principle, the Postal Service generally agrees with cost-based rates, but is concerned with the impact on mailers and implementation issues which are discussed later in this testimony. A 5-digit pallet discount is not a bad idea in the abstract, but that type of discount is premature. The Periodicals' cost coverage is still meager. For all those who are interested in the viability of Periodicals as a subclass, greater weight should be placed on establishing pricing that leads to cost-reducing behavior, rather than simply rewarding existing efficient preparation. While nearly all pricing incentives will reward existing efficient preparation, it is important to construct the incentives such that they are obtainable for a wide range of mailers, especially those that are producing high-cost mailings.

² I recognize that the proponents say that this will encourage new mail to palletize. Nevertheless, the inescapable fact is that 5-digit pallet preparation is already a fairly widespread practice in the community. While it arguably better reflects cost incurrence, it is not the most appropriate tool to encourage more effective containerization either through palletizing or rewarding the more efficient use of sacks.

The Postal Service believes the container rate introduced in the rate proposal sends a consistent and clear signal to the Periodicals community and continues to provide adequate incentives to encourage more mail preparation and worksharing. In witness Tang's response to MPA/USPS-T35-17, she provided the estimate of incentives to 12 publications which are currently co-palletized. It shows the incentives under the proposed rates would be at least comparable, if not bigger, for these current co-palletization participants. Moreover, in her later response to MPA/USPS-T35-28 (c), the updates from the source confirmed that it "may overstate the number of containers for the twelve publications in the "after" scenario, because the container count reflects the containers for the entire co-palletized pool, while the piece count reflects only one publication." While it appears difficult, if not impossible, to isolate container count of a specific publication from the entire mailing in the after-copal scenario, the "after-copal" postage has probably been overstated because of the inflated container count. A reasonable conclusion one can draw is that, the actual after-copal postage would have been lower; hence the incentives offered under the proposed rates would have been even larger.

Impact on Mailers

We applaud the Commission for directing all the parties to evaluate their proposals on the basis of a diverse sample set of mailers — comprising 259 individual titles — that was originally introduced by my colleague witness Tang in Docket No. C2004-1. It was time-consuming and expensive, but the Postal Service was able to gather the data for this evaluation. The results show the

balanced nature of the Postal Service's proposal in terms of its impact on mailers.

Table 3 below shows mean rate increases from among the 259 sampled titles of 13.20 percent for the Postal Service proposal, 15.87 percent for the Time Warner proposal (reflecting the Time Warner revision filed on November 20, 2006), and 13.43 percent for the MPA/ANM proposal. Since the three proposals hit the same revenue target, the different mean rate increases can be attributed to the fact that the sample is not perfectly representative of all Periodicals volume. The key statistic, in my mind, is the standard deviation. Note that the Postal Service proposal has the lowest standard deviation overall (i.e., for "All Mailers"). This reflects the Postal Service's effort to limit the impact of its rate proposal on various mailers to as narrow a range as practicable, while still maintaining adequate incentives for efficient mail preparation. By mailer size, the Postal Service proposal has the lowest standard deviation for large and medium mailers, and the second lowest for small mailers. The result for small mailers is being substantially driven by just one observation among the 259. Note in the range section of the table that there is one small, low-density mailer for whom the Postal Service proposal produces a 43.73 percent rate increase. If just this one mailer is excluded from the sample (as a sensitivity analysis), the Postal Service's standard deviation for small mailers also becomes the lowest among the three proposals.

Table 3 Analysis of 259 Sampled Periodicals Mailings

Analysis of 259 Sampled Periodicals Mailings
Comparative R2006-1 Rate Proposals (Percent Rate Change)

	Range						Mean			Standard Deviation		
	USPS		Time Warner		MPA		USPS	TW	MPA	USPS	TW	MPA
	High	Low	High	Low	High	Low						
Large Mailers	19.30	4.99	24.47	0.15	16.10	1.70	10.54	9.94	9.49	2.30	5.30	2.93
Medium Mailers	18.06	7.38	47.46	3.95	22.20	4.40	11.55	16.27	12.23	2.05	8.92	3.86
Small Mailers	43.73	7.62	58.53	-5.99	22.60	6.40	16.04	18.38	16.48	4.25	12.54	3.52
All Mailers	43.73	4.99	58.53	-5.99	22.60	1.70	13.20	15.87	13.43	3.99	10.51	4.48
Large												
High Density	19.30	4.99	24.47	0.15	16.10	1.70	10.54	9.89	9.48	2.35	5.40	2.99
Low Density	10.75	10.21	11.19	10.97	10.10	9.50	10.48	11.08	9.80	0.38	0.16	0.42
Medium												
High Density	18.06	7.38	47.46	3.95	22.20	4.40	11.23	15.65	11.81	2.01	8.48	3.82
Low Density	16.70	8.69	46.01	8.04	20.40	7.10	11.87	16.90	12.64	2.07	9.38	3.89
Small												
High Density	29.14	7.62	58.53	-5.99	22.60	6.40	15.46	20.69	16.58	3.62	12.94	4.07
Low Density	43.73	11.14	46.31	-5.34	22.50	12.90	16.66	15.94	16.37	4.79	11.75	2.86
All												
High Density	29.14	4.99	58.53	-5.99	22.60	1.70	12.51	15.58	12.75	3.54	10.52	4.72
Low Density	43.73	8.69	46.31	-5.34	22.50	7.10	14.24	16.31	14.45	4.40	10.53	3.89

The following nine charts present scatter diagrams showing the distribution of rate changes around the mean. There is one chart for each combination of proposal and mailer size. In the very first diagram, representing small mailers under the Postal Service proposal, the previously discussed 43.73 percent outlier is evident in the top-right area of the scatter. Generally, the scatter diagrams confirm visually that the Postal Service proposal produces the least variation for large and medium mailers, and slightly more variation for small mailers than the MPA/ANM proposal.

Figure 1: Percent Price Changes for USPS Small Publications

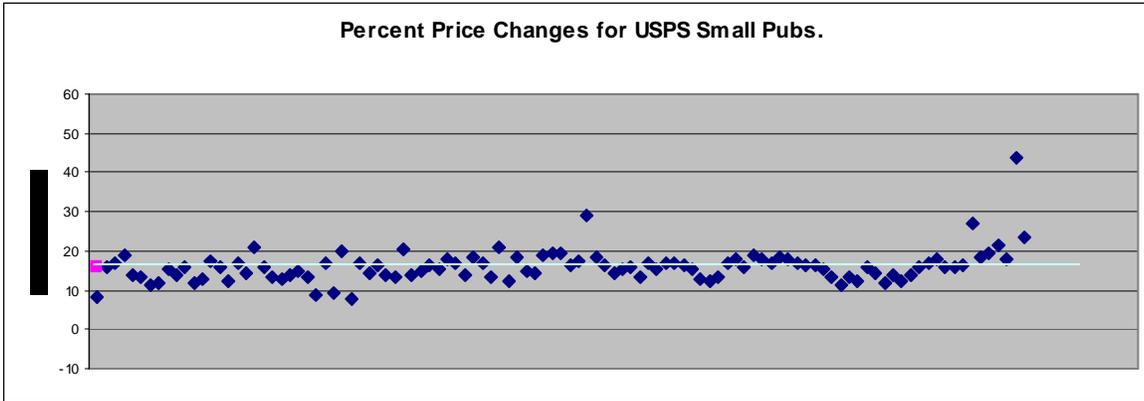


Figure 2: Percent Price Changes for Time Warner Small Publications

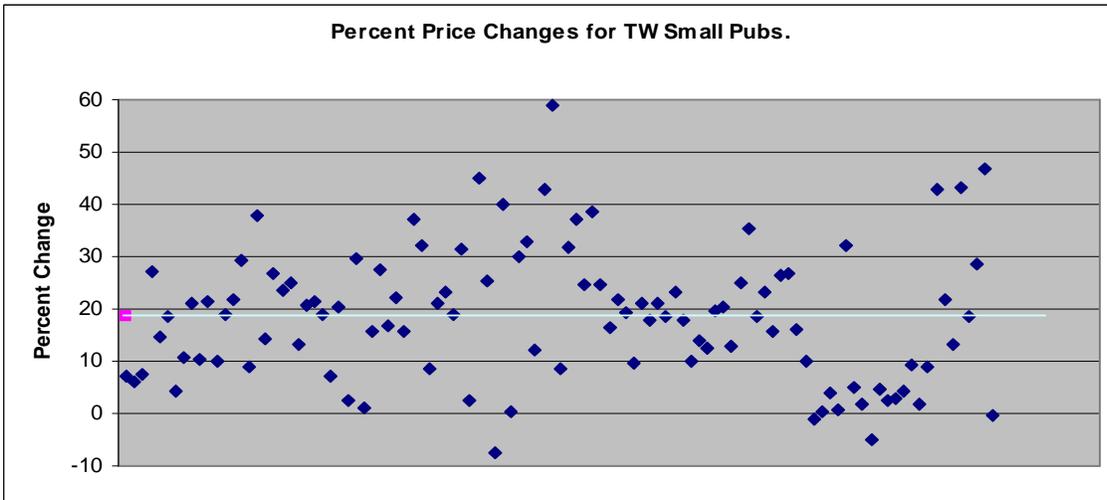


Figure 3: Percent Price Changes for MPA Small Publications

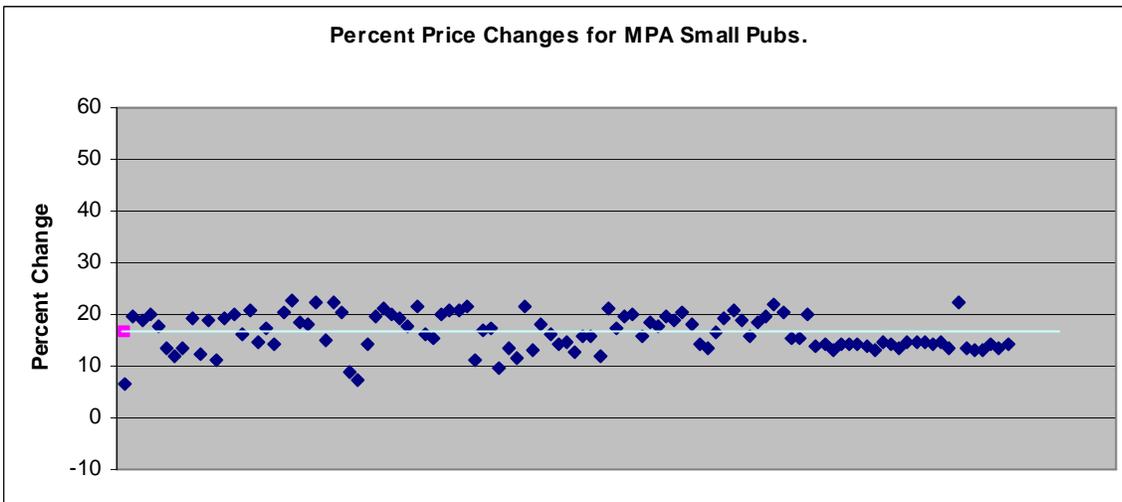


Figure 4: Percent Price Changes for USPS Medium Publications

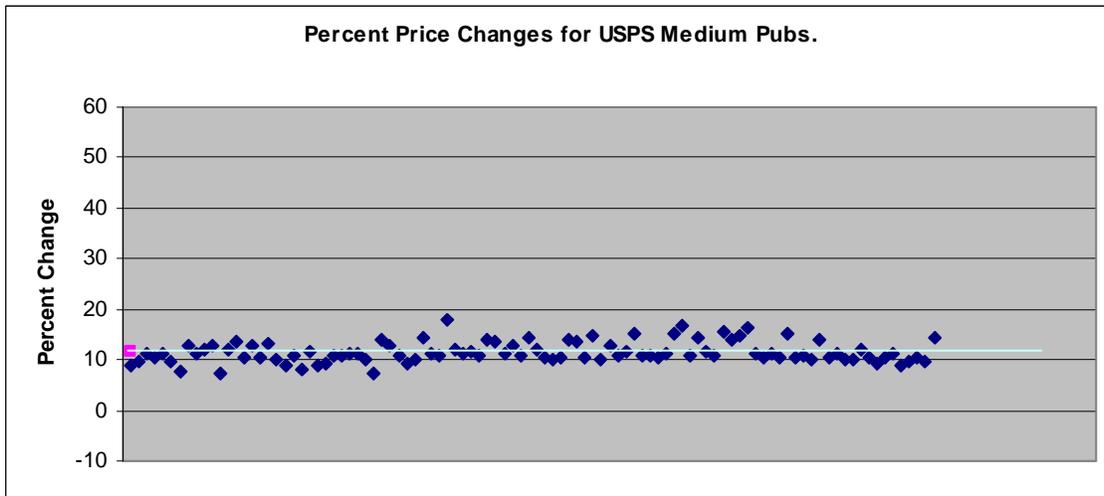


Figure 5: Percent Price Changes for Time Warner Medium Publications

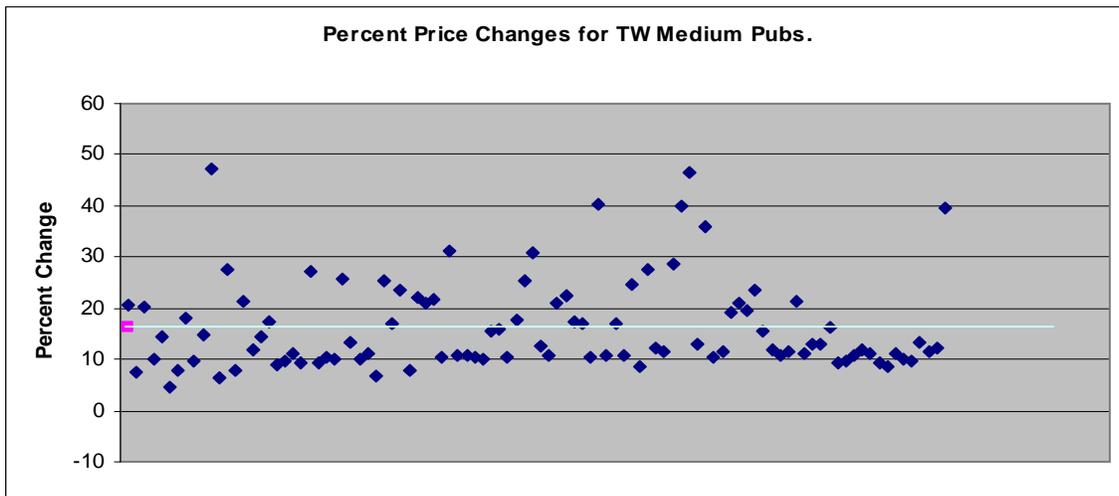


Figure 6: Percent Price Changes for MPA Medium Publications

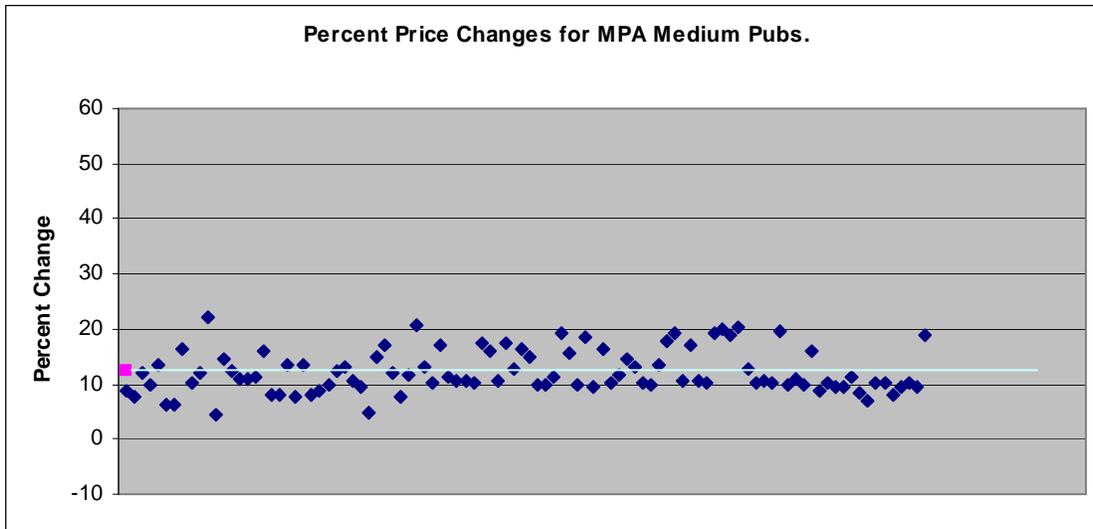


Figure 7: Percent Price Changes for USPS Large Publications

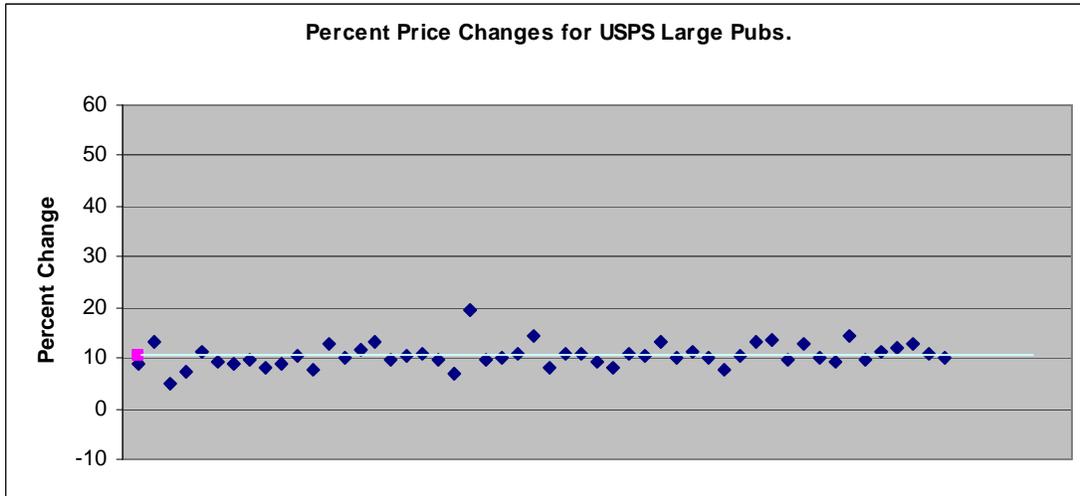


Figure 8: Percent Price Changes for Time Warner Large Publications

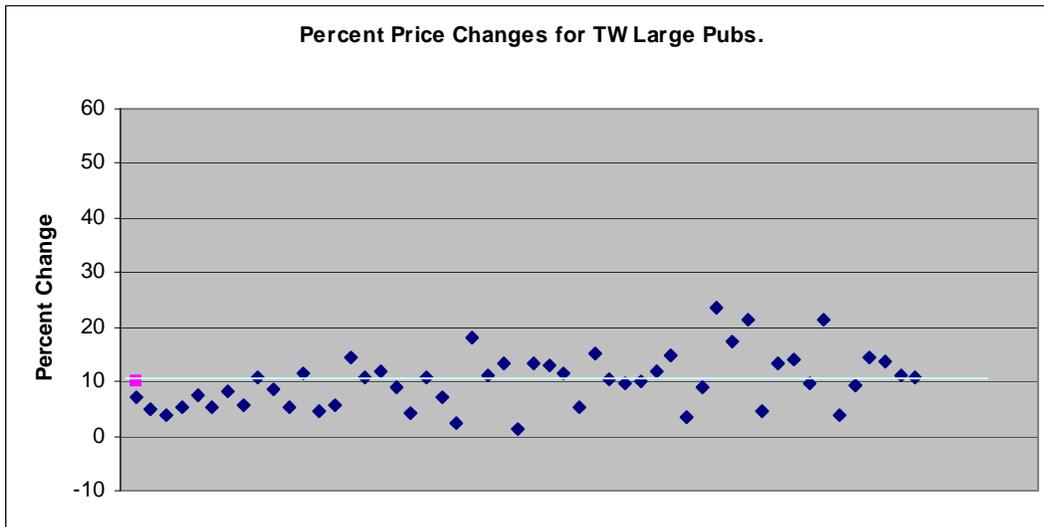
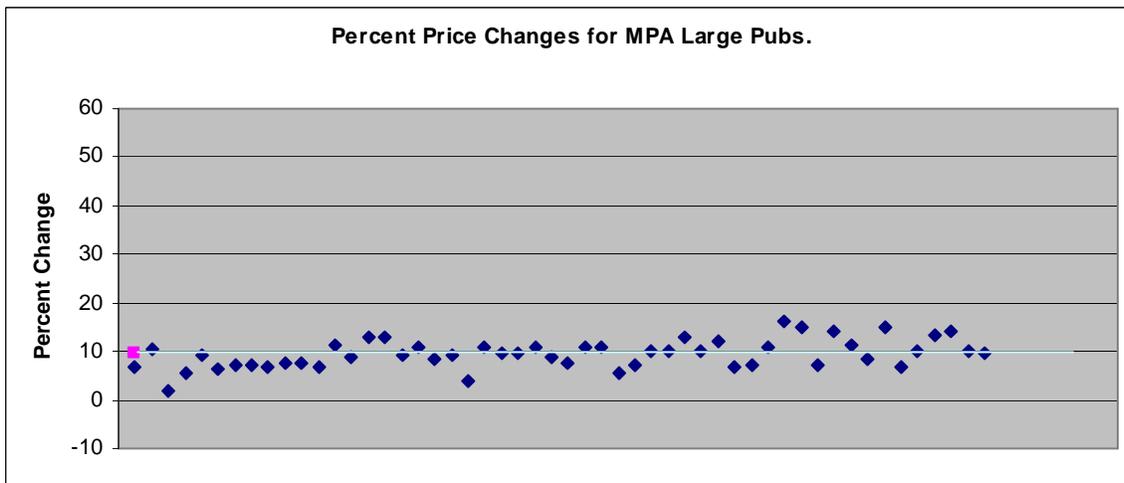


Figure 9: Percent Price Changes for MPA Large Publications



Ride-Along Piece Rate

The Ride-Along rate was originally designed and introduced by me. In Docket No. MC2000-1, I stated in my testimony (USPS-T-1) that:

Currently, Periodicals mailers face restrictions both on the amount and type of advertising that can be included either within the publication, or as a supplement. For example, commercially available products such as cosmetics and perfumes are prohibited from being mailed at Periodicals rates. So are contents which are not comprised of printed sheets such as cloth, leather, and other non-paper material. All advertising matter or other enclosures or attachments that do not meet the requirements for mailing at Periodicals rates can be attached to the publication or included as enclosures, but pay a separate Standard (A) rate ... [which is] prohibitively expensive ... (Page 2, lines 3 – 17)

....

The experimental “Ride-Along” classification change for Periodicals is expected to provide a cost-effective method to mail what are now Standard (A) supplements, including very small product samples, to targeted markets. (Page 4, lines 2 – 4)

As witness Tang said in her response to MPA/USPS-T35-2, “(a) Ride-Along piece has never been, and should not be, treated as an element of average Periodicals advertising pounds.” The Ride-Along rate was originally developed to respond to customer demand for a new, effective, and affordable advertising medium for Periodicals mailers. Its rate has been considerably cheaper than alternatives for mailing advertising materials (product samples, small catalogs, etc.) that were used by publishers prior to the introduction of Ride-Along rates. The Ride-Along weight is not included in the calculation of advertising pounds. The Ride-Along revenue, as intended when the rate was established, is to be included in the total Periodicals revenue and improve the overall class contribution.

The methodology witness Tang used to develop the proposed Ride-Along per-piece rate is consistent with the original approach described on page 5 of my testimony in Docket No. MC2000-1. While I understand that this approach leads, in this instance, to a higher-than-average increase, it nonetheless adheres to the original intent of the Ride-Along program. To

the extent another approach is used that would lead to a lower price, the negative revenue consequences would have to be addressed in the other Periodicals rate components to maintain the Periodicals cost coverage target.