

United States of America
POSTAL REGULATORY COMMISSION

Before:

Chairman Blair,
Vice Chairman Tisdale,
Commissioners Acton, Goldway and Hammond

Postal Rate and Fee Changes

Docket No. R2006-1

OPINION
AND
RECOMMENDED DECISION

VOLUME 1

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RECOMMENDED DECISION

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SUMMARY

In this decision the Postal Regulatory Commission responds to a United States Postal Service Request for rate increases designed to generate almost \$4 billion of additional annual revenue. In addition to rate increases, the Service asks the Commission to approve rate design changes for most categories of mail, including First-Class Letters and Sealed Parcels.

The Commission finds the Postal Service will need to increase rates in order to break even next year. The Commission also concludes that the rate designs for many postal products can and should be improved.

The rates recommended in this decision fully fund every expense the Postal Service identifies in its Request, including \$768 million for contingencies. However, the Commission has identified calculation errors in the Service's supporting financial documentation, and conceptual errors in the Service's proposed rates, that allow the Commission to recommend smaller increases than the Postal Service requested. The Commission recommends rates that increase, on average, 7.6 percent. The rates requested by the Postal Service equate to an 8.1 percent increase.

The Commission recommends an increase of 2 cents instead of 3 cents in the rate for First-Class one-ounce letters. The rate will go from 39 to 41 cents. The Commission also recommends an increase of 2 cents instead of 3 cents in the rate for postcards. That rate will go from 24 to 26 cents. On average, First-Class Mail rates increase 6.9 percent.

The Postal Service sought authority to offer a new “Forever Stamp” to ease the transition to new rates. Forever Stamps will be sold in reasonably limited quantities for the price of a First-Class one-ounce letter, and continue to be worth the price of a First-Class one-ounce letter even if that price changes. The Commission recommends this innovative proposal which will be a convenience for individual consumers, and reduce the costs of transitions to new rates.

The Postal Service also requested new, separate shape-based rate schedules within First-Class. Large or odd-shaped pieces are more expensive to process than letters, and the Service wants to be able to charge compensatory rates for such pieces. The Commission finds this step justified and recommends separate rate schedules for flats (large envelopes) and parcels. This refinement also allows the Commission to reduce the First-Class additional ounce rate from 24 to 17 cents. The Postal Service is urged to carry out a broad public education program before it begins to charge separate rates for letters, flats, and parcels.

In this case the Commission obtained comments and testimony from a cross-section of interested participants on how best to develop rate discounts for mailers who perform worksharing to reduce Postal Service costs. Most business mailers now participate in worksharing activities in order to earn postage discounts. The consensus was to apply the economic principle of Efficient Component Pricing. This results in the most productive use of the Nation’s resources.

The Commission has used Efficient Component Pricing to develop rates wherever possible. Many rates proposed by the Postal Service were not consistent with Efficient Component Pricing as they failed to reflect cost differences fully. Rates that more accurately reflect costs send proper price signals. Rates that send proper price signals result in more efficient processing and transportation practices, which in turn reduce costs, thereby allowing smaller rate increases, and less volume losses.

In First-Class, the Postal Service proposed to “de-link” single-piece from worksharing rates. This practice would abandon the principle that worksharing discounts should be based on the costs avoided by worksharing activities. As applied by the Postal Service in this case, it would expand discounts beyond avoided costs, and unfairly shift the burden of this rate increase on to single-piece mailers. The Commission believes that mailers who workshare should be rewarded, and recommends discounts that fully reflect the costs avoided by worksharing. Because the de-linking approach does not equitably balance the interests of all mailers within a subclass, and does not follow established principles of rate design including Efficient Component Pricing, the Commission does not adopt it.

Standard Mail consists entirely of bulk mailings with rates intended to reflect cost distinctions. The Postal Service proposes that new, separate shape-based rate schedules be added to Standard Mail to better reflect costs. The Commission recommends this improvement. Recommended Standard rates vary from those suggested by the Postal Service in that smaller increases are recommended for the more efficient (lower cost) pieces, while some less efficient pieces face larger increases. On average, Standard Mail rates increase 9.3 percent.

Several participants, including the Postal Service, propose new rate designs for Periodicals. Here, too, the goal is to better reflect costs, and send price signals that will encourage more efficient mailing practices. Periodicals’ costs have risen disproportionately in recent years, in part because current rates send such poor signals. For example, Periodicals is the only class where no rate penalty is applied to nonmachinable pieces.

The Commission recommends a new design that draws from the separate proposals of the Postal Service and Time Warner Inc. The recommended rates recognize only a limited portion of the costs associated with identifiable cost drivers in order to moderate the impact on mailers. Nonetheless, Periodicals mailers are extremely cost conscious, and the Commission expects that these rates will foster more efficient, less costly Periodicals mail. On average, Periodicals rates increase 11.8 percent.

The Postal Accountability and Enhancement Act of 2006 has altered the way postal rates will be set in the future. In particular, the Postal Service will have wide flexibility to set the rates for competitive products, so long as those products generate revenues sufficiently above costs. In recognition of that fact, the Commission has not recommended new rate designs for the Postal Service's competitive products. Rates for Express, Priority and Parcel Post include adjustments to better reflect costs, but otherwise are largely as suggested by the Postal Service.

This completes the last omnibus rate request filed prior to enactment of the 2006 legislative reform. The rates recommended by the Commission provide a sound foundation on which the Postal Service and the Postal Regulatory Commission will begin to exercise their new, important responsibilities under this legislation.

I. PROCEDURAL HISTORY

[1001] On May 3, 2006, the United States Postal Service filed a Request with the Postal Rate Commission for a recommended decision on proposed changes in domestic postage rates, fees and certain mail classifications. The Commission gave notice of the Request in Order No. 1464, issued May 5, 2006, and assigned Docket No. R2006-1 to this proceeding. The Commission heard the case *en banc*, initially with former Chairman George Omas and subsequently with Chairman Dan G. Blair serving as Presiding Officer. The 60 participants sponsored 139 pieces of testimony from 99 witnesses that were received during 34 days of hearings.

[1002] The Postal Service supports its Request with testimony that projects its costs forward from Fiscal Year 2005 (the base year), and estimates that at existing rates it will experience a revenue deficiency in Fiscal Year 2008 (the test year) of \$5.874 billion. It proposes rates calculated to generate additional revenues of \$3.983 billion, of which \$767 million will be used as a contingency against unforeseen financial adversities.

[1003] During this proceeding, the Commission issued three Notices of Inquiry directed to all interested participants. The first concerns the development of the Periodicals Within County markup; see Notice of Inquiry No. 1, issued June 5, 2006. The second addresses rate design methodology for Standard Mail; see Notice of Inquiry No. 2, issued July 21, 2006. The third deals with approaches to development of rates for First-Class Mail and Standard Mail; see Notice of Inquiry No 3, issued July 26, 2006. The latter two inquiries also address the role of Efficient Component Pricing in rate design. Participants provided significant responsive materials, which are discussed in Chapter IV, Section A.

[1004] The Presiding Officer issued 25 information requests most of which were directed to the Postal Service. Three of these information requests, focused on the issue

of City Carrier Street Time costs, raised one of the most prominent evidentiary issues in this case.

[1005] In the Opinion in Docket No. R2005-1, the Commission expressed significant concerns regarding data quality and its effect on econometric modeling in the City Carrier Street Time Study (CCSTS) sponsored by Postal Service witness Bradley in that case. PRC Op. R2005-1, ¶ 4011. In light of these concerns, the Commission urged the Service to analyze the issue carefully prior to the next rate proceeding. *Id.* at ¶ 4018.

[1006] The Postal Service's Request in this docket includes no new data or analysis of carrier street time costs. To shore up the resulting weaknesses in the record, the Presiding Officer issued three information requests seeking more recent CCSTS data and alternatives to the models proposed by the Service in Docket No. R2005-1. He subsequently designated responsive materials for inclusion in the evidentiary record.

[1007] Several participants objected to inclusion of these materials, noting that their production in the latter stages of the proceeding precluded an adequate opportunity to examine and respond to these complex and potentially significant additions to the record. In two Orders addressing these matters, we acknowledged participants' due process concerns, and limited the use of the materials to illustrative purposes. Order No. 1482, November 8, 2006; Order No. 1, December 22, 2006. Nonetheless, as noted in the Orders, we anticipate that this research could contribute to the objective of effectively modeling the variability of carrier street time costs in the future. It is described in Appendix K.

II. REVENUE REQUIREMENT

A. Bases of Test Year Cost and Revenue Estimates

[2001] The Postal Service estimates its future revenue needs in Commission rate cases by identifying a recently concluded fiscal year as a base period, adjusting its reported historical result through intermediate periods, and by rolling results forward incorporating the effects of numerous expense and volume factors to arrive at cost and revenue estimates in a selected test year. This process is described in the testimonies of witnesses Milanovic (USPS-T-9); Loutsch (USPS-T-6), Waterbury (USPS-T-10); and Page (USPS-T-23).

[2002] The Postal Service uses Fiscal Year 2005 as the base year from which to project costs and revenues. In USPS-T-9 and associated exhibits, witness Milanovic provides the base year Cost and Revenue Analysis and develops costs by class, subclass, and special service for each cost segment and component. His testimony also identifies a number of changes in cost treatment between the Fiscal Year 2004 Cost and Revenue Analysis and Base Year 2005 costs. USPS-T-9 at 4-7.

[2003] Witness Loutsch develops the cost change factors used to roll the base year costs forward to the test year, Fiscal Year 2008. His testimony also presents an overview of the financial status of the Postal Service. His testimony, together with supplemental information provided by the Service during the course of this proceeding,¹ provides the basis for the Postal Service's estimated revenue requirement of \$79.4 billion before rates in the test year.

¹ In response to Presiding Officer's Information Request No. 16, the Postal Service filed Library Reference L-196. The supplemental estimates and supporting documentation provided in the library reference update the estimates provided in witness Loutsch's revised testimony.

[2004] Using the roll forward model described in her testimony, witness Waterbury develops costs by class, subclass, and special service for the interim periods FY 2006 and 2007, and for Test Year 2008 both before and after proposed rate increases. Witness Page develops final adjustments for each year of the roll forward process in a portion of his testimony. The final adjustments he sponsors are intended to reflect cost changes not captured in the roll forward process, such as changes in volume mix due to migration of mail to more heavily workshared categories, and the impact of three negotiated service agreements. USPS-T-23 at 22-26.

[2005] Based on these analyses, the Postal Service projects that the rate and fee changes it proposes would produce test year revenues of \$77.6 billion, which would recover a total after-rates revenue requirement of \$77.5 billion, resulting in a test year revenue surplus of \$97 million.

B. Volume Models and Forecasting Methodologies

1. The Postal Service's Methodologies

[2006] As in the most recent previous omnibus rate proceeding,² the Postal Service's filing in this docket presents its test year volume forecasts in the testimonies of witnesses Thress (USPS-T-7) and Bernstein (USPS-T-8).

[2007] The testimony of witness Thress presents models for estimating the demand for domestic mail services and describes their underlying methodologies; identifies the factors affecting mail volumes; and projects these factors through the test period in order to develop a set of volume forecasts. In general, the approach witness Thress takes in forecasting test year volumes is familiar and well-established in Commission omnibus rate proceedings.³

[2008] The testimony of witness Bernstein focuses more narrowly on the subject of recent declines in First-Class Mail volumes. Supplementing witness Thress' treatment of the Internet and electronic diversion (USPS-T-7 at 22-29), witness Bernstein examines several sources of volume-related data and potential explanations for changes in historical volume trends. Based on these analyses, he concludes that the principal reason for First-Class volume declines is increased use of various technological alternatives, particularly electronic bill payment alternatives. USPS-T-8 at 2, 60-61.

2. Criticisms and Alternative Estimates

[2009] One intervenor in this proceeding, the Greeting Card Association (GCA), sponsors evidence that challenges the Postal Service's demand estimation procedures and the credibility of the Service's estimates of the own-price elasticities of First-Class

² See PRC Op. R2005-1, November 1, 2005, ¶¶ 3041-44.

³ See, e.g., PRC Op. R2000-1, November 13, 2000, ¶¶ 2042-44.

single-piece mail and workshared mail. GCA also sponsors a study that yields a coefficient indicating that First-Class Mail is more sensitive to price increases than the Postal Service estimates.

[2010] GCA witness Kelejian (GCA-T-5) focuses on the econometric procedures used by witness Thress in his model for estimating elasticity coefficients. He testifies that witness Thress did not use some of these procedures properly, thereby calling the results they yield into question. In other instances, he asserts, witness Thress used what he characterizes as intuitive procedures that have no formal basis in econometrics. For these reasons, he expresses serious doubt regarding the validity of the estimated elasticities used by the Postal Service. GCA-T-5 at 2-15.

[2011] GCA witness Clifton (GCA-T-1) also critiques the Postal Service's elasticity estimates for First-Class single-piece letters (GCA-T-1 at 26-43), and produces alternative estimates based on a different model he develops. *Id.* at 43-49. His estimate of own-price elasticity is -0.456, significantly higher than the -0.184 estimate developed by witness Thress.⁴ Witness Clifton further testifies that the own-price elasticity of First-Class single-piece letters exceeds that of Standard Regular mail — for which he estimates a coefficient of -0.254,⁵ in comparison with witness Thress' estimate of -0.296 — in the presence of diversion of the former to the Internet. *Id.* at 49-56.

[2012] GCA witness Martin (GCA-T-2) supplements the Clifton testimony with survey research he sponsors on emerging competitive substitutes to First-Class letter mail, particularly those that involve the rendering of billing statements and the associated payment process. GCA-T-2 at 1. In addition to examining the role of non-postal attributes on diversion of such transactions from the mail to electronic means, witness Martin addresses the potential impact of future postal rate increases on diversion. He concludes that potential postal rate increases are a significant behavioral trigger for

⁴ *Id.* at 50; Compare Appendix A at 3, Table A2 with Appendix A at 5, Table A4.

⁵ *Id.* at 54; Appendix A at 10, Table A9.

consumers and businesses to investigate electronic alternatives, and therefore for diversion to those alternatives. *Id.* at 2, 56.

[2013] In response to GCA's presentation, the Postal Service submitted the rebuttal testimony of witness Thress (USPS-RT-2) that addresses the analyses in witness Clifton's testimony. Witness Thress testifies that Clifton's economic analysis of the payments market, and the Postal Service's position in it, is flawed. USPS-RT-2 at 3-15. He also challenges witness Clifton's econometric analysis of the bill payments delivery market (*id.* at 16-36), and asserts that the own-price elasticity estimates Clifton develops for First-Class single-piece letters are fatally flawed. *Id.* at 37-67. For these reasons, witness Thress concludes that Clifton does not present a usable estimate of own-price elasticity, and submits that the extent of price competition for single-piece First-Class Mail is best reflected in his initial estimate. *Id.* at 67.

[2014] On brief, the Postal Service argues that its volume forecasts are based on the well-established methodology employed in previous omnibus rate proceedings, and disputes the merit of the challenges posed by GCA.⁶ For its part, GCA argues that the Service's elasticity estimates for First-Class are not credible, and fail the tests of technical rigor employed by the Supreme Court in its decision in *Daubert v. Merrell Dow Pharmaceuticals*, 509 U.S. 579 (1993).⁷

3. Commission Evaluation of Alternative Presentations

[2015] In view of the methodological challenges, and alternative estimates, presented by GCA, the Commission has conducted an independent analysis of volume

⁶ Postal Service Brief at 33-62; Postal Service Reply Brief at 34-72.

⁷ GCA Brief at 40-62. While noting that "[m]any factors will bear on the inquiry, and we do not presume to set out a definitive checklist or test[;]" 509 U.S. at 593, the Court suggested four touchstones of scientific validity for proffered reasoning or methodology: (1) "whether it can be (and has been) tested[;]" (2) "whether the theory or technique has been subjected to peer review and publication[;]" (3) "the known or potential rate of error[;]" and "general acceptance' [within] a relevant scientific community...." 509 U.S. at 593-94.

forecasting methodology in this case. This analysis is reported in Appendix I to this Opinion. In general, the Commission concludes that the Postal Service's well-established methodology, although flawed in certain respects, produces forecasts that are sufficiently reliable to be used for the purposes they are offered in omnibus rate proceedings.

[2016] Analysis of witness Thress' techniques reveals that his econometric practice is conventional, with the exception of several devices that have been adapted to deal with the special problems he confronts. Witness Kelejian correctly identifies several problematic features of witness Thress' techniques; however, it has not been shown that these errors will have more than a very minor impact on the volume forecasts his models produce. The claimed deficiencies in witness Thress' methodology admittedly are likely to cause bias in the estimates of own-price elasticities, as well as the other coefficients, in witness Thress' equation for First-Class single-piece mail. However, there is no reason to believe that such bias will necessarily result in an underestimate of own-price elasticity.

[2017] While witness Clifton's linear equations are simpler and somewhat easier to fit than those of witness Thress, his estimates are somewhat suspect on technical grounds. He has chosen a defective method for dealing with autocorrelated errors, and his estimate of the coefficient for the worksharing discount from his equation for First-Class single-piece letters has a sign that can not be correct. The latter flaw indicates that the equation is mis-specified. Consequently, witness Clifton's equations for First-Class single-piece and Standard Regular rate mail are not preferable to those of witness Thress.

[2018] There is little disagreement between the Postal Service and GCA witnesses regarding the negative impact of electronic diversion on First-Class single-piece volumes and the facilitating role of the Internet. However, witness Martin's testimony does not convincingly establish the influence of postage increases on this development. The questionnaire, data capture and sample designs for the consumer, and small business surveys referenced by witness Martin precluded an objective examination of "emerging

competitive substitutes to first-class letter mail.” GCA-T-2 at 1. The qualifications associated with the results of these studies should be noted carefully. While the data presented by witness Martin confirmed increased acceptance of technological advances accessible to the general consumer and a gradual shift toward more use of electronic alternatives to First-Class Mail, his efforts to provide data that support the hypothesis that knowledge of regularly scheduled increases in postage rates would “trigger” a switch or serious consideration of a switch to electronic methods of submitting billing statements and rendering payments were substantially deficient. His major conclusions were subjective and lacked statistical defensibility. For these reasons, the Commission rejects witness Martin’s testimony to the extent it attempts to modify the Postal Service’s elasticity estimates put forth by witness Thress.

[2019] The ultimate measure of the suitability of a volume estimation technique is the accuracy of its forecasts. The review in Appendix I indicates that forecasts made with witness Thress’ models appear to be unbiased and are highly accurate in the aggregate. However, the forecasts are less reliable for smaller subclasses and worksharing categories. Consequently, the Commission has used the estimates developed by witness Thress for the purpose of volume estimation in this case, but encourages the Postal Service to consider the methods for improving forecasts suggested in the Appendix.

C. Changes and Adjustments to Test Year Costs and Revenues

1. Supervisory Savings in Cost Reduction Programs

[2020] A coalition of mailers led by Direct Marketing Association, Inc. (DMA) asserts that the Postal Service has overestimated the revenue requirement by underestimating savings in supervisor costs in connection with its cost reduction programs.⁸ Witness Buc (DMA-T-1) devotes a portion of his testimony to supporting this argument.

[2021] Witness Buc cites the Postal Service's general recognition in USPS-LR-L-1 that changes in supervisory hours should reflect changes in craft hours, but that the "span of control" may change when new programs or technologies are introduced.⁹ He challenges the Service's use of the latter possibility as a ground for declining to make any reduction in supervisor costs in connection with Cost Reduction Programs in Fiscal Years 2006, 2007, and the test year, claiming such an approach is not credible. *Id.* at 2. While he did not attempt to develop a method for determining which cost reduction programs will change the work organization structure and which will not, he states that his examination of all of them indicates that many will not. *Id.* at 5-7. Based on the indications he cites, witness Buc testifies that the Commission should adjust the Service's Cost Reductions and Other Programs for FY 2006, 2007, and the test year after rates based on the estimated reductions for the crafts supervised. He also recommends that the Commission net out supervisor cost reductions in Breakthrough Productivity Initiatives (BPI) programs since these would now be reflected in the adjusted

⁸ Joint Brief Concerning the Revenue Requirement of Direct Marketing Association, Inc., Alliance of Nonprofit Mailers, Association for Postal Commerce, Continuity Shippers Association, DMA Nonprofit Federation, Dow Jones & Company, Inc., Magazine Publishers of America, Inc., The McGraw-Hill Companies, Inc., Mail Fulfillment Services Association, Mail Order Association of America, National Newspaper Association, Inc., National Postal Policy Council, Parcel Shippers Association, Pitney Bowes, Inc. at 4-8 (DMA, et al. Brief).

⁹ DMA-T-1 at 3, *quoting* USPS-LR-L-1 at 2-2.

Cost Reductions and Other Programs for supervisors. After making these adjustments, he states, the Commission should also adjust test year after-rates equity to reflect the fact that, with lower costs in FY 2006 and 2007, net income will be higher for each of these years and the test year. *Id.* at 7-8.

[2022] The Postal Service responded to witness Buc's proposals with the rebuttal testimonies of witnesses Lyons (USPS-RT-3) and Oronzio (USPS-RT-15). Witness Oronzio challenges witness Buc's conclusion that the Service's cost reduction programs fail to include supervisor cost savings, testifying that such savings are incorporated in their entirety as an implicit component of the BPI each year. While he concedes that, in theory and on average, there should be an accompanying change in supervisory hours when newly-acquired equipment reduces clerk and mail handler work hours, witness Oronzio states that any such supervisory efficiencies are accounted for in the difference between identified operating savings and the BPI target, which allocates funds to each operating area. USPS-RT-3 at 5-7. He also presents two charts which display craft and supervisory work hours for each year from 2000 through 2005, the second of which plots supervisory hours lagged by one year. Witness Oronzio testifies that the closer, albeit rough, alignment of the second chart "suggests that supervisory savings occur primarily in the next year, as might be expected from the way our budget system functions." USPS-RT-15 at 5.

[2023] Witness Lyons testifies that witness Buc fails to demonstrate — and that no other evidence proves — that cost reduction programs generate supervisory savings proportional to craft savings. According to witness Lyons, witness Buc also fails to recognize the approach to identifying and capturing supervisory cost reductions outlined in the testimony of witness Loutsch. He also cites the approach used by the Service to identify, plan and capture potential supervisory cost reductions described by witness Oronzio, with the result that reductions in supervisory costs are already reflected in program estimates or in the estimates of Breakthrough Productivity Initiatives and Local Management Initiatives (BPI/LMI). The effect of witness Buc's proposal, witness Lyons states, would be to increase cost reductions beyond the level predicted to occur in the

Service's rate filing and the FY 2007 operating budget, thereby adopting an unjustified overstatement of expected savings. USPS-RT-3 at 4-5.

[2024] The Commission last considered the issue of potentially "piggybacked" supervisory cost savings in Docket No. R2000-1. In that decision, the Commission maintained its conclusion, first adopted in Docket No. R97-1, that "[i]n the absence of better record evidence, the Commission will assume a stable supervisor to craft employee ratio[,]"¹⁰ and therefore made the adjustment suggested by witness Buc. It also acknowledged the argument made by Postal Service witness Patelunas regarding variances between actual versus estimated supervisor costs for FY 1998, but did not view the existence of variances to be probative evidence that rebutted the Buc hypothesis, and therefore retained the proposed adjustment. The Commission also invited the Service to produce a study isolating and retrospectively analyzing the actual effects of operational cost reduction programs for use in future proceedings.¹¹

[2025] No such study has been produced in this case, and the Postal Service does not dispute the basic proposition that programs that produce reductions in craft hours should lead, in principle, to associated reductions in supervisory costs. Witnesses Lyons and Oronzio offer assurances that any such costs make their way into program estimates or estimates in BPI/LMI, but provide no empirical documentation that this has occurred in prior periods.

[2026] Consequently, neither the Postal Service nor the DMA coalition has advanced a metric that could be used to quantify supervisory cost savings with reliability for the periods under scrutiny in this case. Additionally, witness Oronzio's charts of craft and supervisory costs indicate an apparent "lagging" correlation between craft hours and supervisory hours one year later, tending to support his hypothesis that supervisory savings associated with cost reduction programs occur primarily in the year following the program's implementation. If this hypothesis is accurate, it would be inappropriate to

¹⁰ PRC Op. R97-1, ¶ 2155.

¹¹ PRC Op. R2000-1, ¶ 2059.

impute supervisory cost savings as a proportion of current-year reductions in craft hours; some alternative approach based on “lagged” piggybacking would apparently be needed.

[2027] No such approach has been explored on the record, and the Commission is reluctant to devise a method of its own under these circumstances. Consequently, while the Commission maintains its conviction that cost reduction programs generate supervisory cost savings in some proportion to resulting reductions in craft hours, it is unable to recommend a reduction of the revenue requirement to accommodate this conclusion. The Commission once again encourages the Postal Service and other interested parties to study the actual effects of operational cost reduction programs in order to identify and capture supervisory cost savings.

2. Summary of Miscellaneous Changes and Adjustments

[2028] In arriving at a final estimate of the Postal Service’s revenue needs, the Commission has routinely included the effects of events that occur after the initial filing of the Postal Service’s Request that will produce “known and certain” effects on costs and revenues in the test year.¹² In this proceeding, there are two such events that will affect the revenue requirement.

[2029] First, the actual Cost of Living Adjustment (COLA) payment made in September 2006 was \$521 per year higher than the estimate included in the Postal Service’s direct case.¹³ The effect of recognizing this higher COLA is to increase the revenue requirement by \$472 million.

[2030] The second such event concerns health benefit premiums for Fiscal Year 2007. The actual increase in premiums, based on the current mix of Postal Service

¹² See, e.g., PRC Op. R2000-1, ¶ 2071.

¹³ Response of United States Postal Service Witness Loutsch to Presiding Officer’s Information Request Number 13, Question 1, Tr. 19/6767-68; see also Rebuttal Testimony of W. Ashley Lyons on Behalf of United States Postal Service, USPS-RT-3 at 8.

employees, is 2.3 percent, as compared to the initial estimate of 7.0 percent.¹⁴ The effect of this development is to reduce the revenue requirement by \$353 million.

¹⁴ Response of the United States Postal Service to Presiding Officer's Information Request No. 16, Question 7, Tr. 19/6769-70.

D. Provision for Contingencies

[2031] For purposes of estimating the Postal Service's total costs in an omnibus rate proceeding, 39 U.S.C. § 3621 explicitly includes "a reasonable provision for contingencies." In this docket, the Postal Service proposes a contingency of one percent of total cost segment expenses, including final adjustments, which equals \$768 million in the test year after implementation of proposed rates. USPS-T-6 at 62.

[2032] Witness Loutsch testifies that the contingency provision is designed to accommodate "the reality that events that affect the Postal Service's financial picture and the impacts of those events are, to varying and unknown degrees, unforeseen and unforeseeable." *Id.* Because of these unknown and unknowable events, he states, an adequate contingency provision is essential to the Postal Service's achievement of financial stability and breaking even in the long run.

[2033] According to witness Loutsch, some of these potentially adverse events relate to elements of the Postal Service's forecasts that involve significant unknowns. He identifies, as examples:

- Potential loss of interest income on the funds held in escrow as required by Pub. L. 108-18;
- Potential obstacles to capturing the entire \$2.9 billion in cost reductions projected for the Service's cost reduction programs through FY 2008;
- Uncertainty regarding labor costs arising from the expiration of contracts in FY 2007;
- Potential understatement of transportation and other energy cost-related components of the revenue requirement in the event of further fuel and energy cost increases; and
- Potential changes in workers' compensation liabilities and expense resulting from actuarial review of these accounts.

Id. at 62-63.

[2034] Witness Loutsch also mentions examples of unforeseeable risks with negative financial impact such as the terrorist attacks of September 11, 2001, the anthrax attack of the same year, and last year's hurricanes. *Id.* at 63.

[2035] DMA, et al. witness Buc testifies that the proposed contingency is excessive. According to witness Buc, a zero contingency would be more reasonable in view of the Postal Service's strong financial condition. He notes that the equity position of the Postal Service is substantially better than at any time since postal reorganization in 1970; that the Service's cash balance of \$3.8 billion is more than adequate to cover unforeseen events; and that the appreciated market value of real estate held by the Service further enhances the Service's financial condition. DMA-T-1 at 13-17. Witness Buc also cites the Service's anticipation of annual rate increases for commercial products as further proof that it needs no contingency. *Id.* at 17.

[2036] In his rebuttal testimony, Postal Service witness Lyons emphasizes the judgmental character of the selection of an appropriate contingency provision. He also notes that, with the exception of a zero percent contingency proposed in its Request in Docket No. R2005-1 to cover its escrow expense, the contingency has varied from 1.0 percent through 5.0 percent in omnibus rate filings. USPS-RT-3 at 10-11.

[2037] Witness Lyons also challenges witness Buc's rationales in favor of a zero contingency. Noting that the Postal Service's test year after-rates total equity is projected to equal \$2.247 billion — \$787 million less than the Federal Government's capital contribution of \$3.034 billion — witness Lyons asserts that offsetting the costs of an adverse event against the Government's capital contribution would be inconsistent with the concept of break even contemplated by the Postal Reorganization Act. He also disputes the basis of witness Buc's claim that the Service's cash balance cushion is approximately \$3.8 billion, stating that the figure should be the \$1.0 billion end-of-year cash level for FY 2008 reported in Library Reference LR-50. Finally, witness Lyons testifies that witness Buc's argument regarding the appreciated value of real estate and potential profits from sales ignores the legal and practical realities of postal operations, which require use of the real estate owned by the Service to operate and support its nationwide service network. *Id.* at 11-13.

[2038] On brief, DMA, et al. argue that witness Buc's testimony and the recent enactment of the Postal Accountability and Enhancement Act (PAEA) support a finding

that a zero percent contingency is reasonable. DMA, et al. Brief at 5-8. The Greeting Card Association similarly argues that passage of the PAEA reduces financial uncertainty and thereby alleviates the need for a one percent contingency. GCA Brief at 62-63. The Postal Service argues that witness Buc's arguments are based on misapprehensions and misjudgments,¹⁵ and have been mooted by subsequent record evidence and events — including the passage of the PAEA, the effects of which the Service characterizes as “financially challenging, rather than enriching.”¹⁶

[2039] Consideration of the record, together with precedent established in prior omnibus rate proceedings, leads the Commission to find the proposed one percent contingency to be reasonable in the circumstances of this case. As the Postal Service observes, the proposed amount is at the lower end of the range of contingency percentages recommended in ratemaking history. Only the Docket No. R2005-1 proceeding — which was devoted exclusively to recovery of the financial escrow mandated by the Civil Service Retirement Funding Reform Act of 2003 — featured a contingency provision of zero. Given the recognized purpose of the allowance — provision against unestimated and unforeseeable financial uncertainties — recommendation of a contingency provision of zero would require an extraordinary level of assurance that available Postal Service resources could accommodate financially adverse developments.

[2040] The record does not support such a conclusion. In addition to unforeseeable events, there are several identifiable sources of financial uncertainty. As witness Loutsch notes, there are significant uncertainties in energy and transportation costs, and the Service's ability to achieve the full level of savings projected in its cost reduction programs. Further, as witness Lyons notes, test year financial estimates would provide the Service with approximately \$1 billion in unrestricted cash to meet such needs — less than a two-week payroll disbursement. USPS-RT-3 at 12.

¹⁵ Postal Service Brief at 11-13.

¹⁶ Postal Service Reply Brief at 15.

[2041] While the passage of the PAEA affords the Postal Service more frequent opportunities to enhance revenues through rate increases, it also presents immediate financial challenges, as the Service anticipates. Specifically, one adverse consequence cited by witness Loutsch — the loss of investment income on amounts held in escrow under Pub. L. 108-18 — can be expected, for the reasons presented in the concluding section of this chapter. The Commission estimates the resulting reduction in investment income may amount to almost \$400 million in the test year following rate implementation, more than half the proposed \$768 million contingency amount.

[2042] Under these circumstances, the Commission concludes that the proposed one percent contingency provision is well within the zone of reasonability, and has included it in the estimated revenue needs of the Postal Service in this decision.

E. Potential Impact of the PAEA on Finances

[2043] Enactment of the PAEA, Pub. L. 109-435, on December 20, 2006, can be expected to result in both favorable and adverse financial consequences for the Postal Service during the periods under scrutiny in this proceeding. On one hand, section 802 of the PAEA eliminates the escrow requirement imposed by Pub. L. 108-18 and returns the obligation to fund the military service-related portion of postal employee retirement to the Treasury; on the other, section 803 of the PAEA establishes a Postal Service Retiree Health Benefits Fund and adopts a schedule of significant contributions to it by the Postal Service: \$5.4 billion no later than September 30, 2007, and an additional \$5.6 billion no later than September 30, 2008. Compliance with the latter requirements can be expected to require a recommitment of funds that will, at the least, eradicate anticipated investment income on the escrow, as noted above.

[2044] Coming, as it did, one day before the deadline for filing initial briefs in this docket, participants had little opportunity to consider the new law's potential impact on postal finances for ratemaking purposes and formulate comments on how they should be reflected in this proceeding. For the same reason, there was no opportunity to supplement the evidentiary record on these matters.

[2045] On brief, the Postal Service projects a consequent negative impact on test year income of \$662 million. The Service offers this calculation solely to rebut the merit of the zero contingency proposal of the DMA coalition,¹⁷ and otherwise states that its "understanding of the new law is that it is not intended to interfere with the litigation of present or future proceedings being conducted under the provision and rules associated with the previous...statutory regime."¹⁸ Other participants argue that the costs of the

¹⁷ Postal Service Reply Brief at 15-17.

¹⁸ *Id.* at 129. Had the Postal Service desired to recover additional revenues to compensate for the impact of the reform legislation in this proceeding — thereby revising its initial revenue requirement — accommodating this change in its Request would have required the Commission to supplement the record with the Service's detailed explanation of the costs involved, its proposed treatment of the costs as attributable or institutional, and the rates for which it proposed additional increases. It would also have been necessary to afford other participants an opportunity to respond to the Postal Service's presentation and to supplement the record with their proposed treatments of such amounts.

new Retiree Health Benefits Fund either should or should not be attributable to mail classes and subclasses to varying degrees.¹⁹

[2046] Because participants lacked any opportunity to supplement the record on the cost and revenue effects of the postal reform legislation and their appropriate recognition in rates, the Commission has not altered the revenue requirement in light of the new law's provisions. Accordingly, as the Postal Service has argued, it is neither necessary nor appropriate to consider whether certain cost elements should be treated differently in this case because of enactment of the Postal Accountability and Enhancement Act.

¹⁹ MPA-ANM Brief at 3, 31-33; MPA-ANM Reply Brief at 2-3, 25-33; McGraw-Hill Reply Brief at 2; UPS Reply Brief at 4, n.1.

III. COSTING

A. Mail Processing Variability

[3001] In this docket, the Commission evaluates for the first time three sets of econometric models of mail processing labor demand variability that rely on the instrumental variables estimating technique to mitigate the risk of bias from errors in the MODS piece handling data. One set was developed by the Postal Service, one sponsored by the Office of the Consumer Advocate (OCA), and one developed by United Parcel Service.

[3002] For reasons explained in depth in Appendix J and summarized here, the Commission concludes that this technique has not been effective in accomplishing its purpose. The Commission finds that the error-ridden MODS data remains a formidable obstacle to econometrically modeling mail processing variability despite the use of extensive data scrubbing and the use of instrumental variables estimation techniques. Appendix J discusses new categories of data that hold substantial promise of overcoming this obstacle.

[3003] OCA's presentation includes a well-developed theoretical component that the Commission generally endorses as making substantial headway toward the goal of estimating the marginal cost of mail processing labor. Using this theoretical structure to estimate marginal cost will require the development of plant-specific volume data disaggregated by relevant cost characteristics.

[3004] A group of Periodicals mailers²⁰ argues that the time required to change sort schemes is predominantly fixed, and therefore should be added to the small set of mail processing operations that the Commission now treats as entirely fixed. For reasons summarized here and explained in depth in Appendix J, the Commission finds that the

²⁰ Magazine Publishers of America, Inc., Alliance of Nonprofit Mailers, American Business Media, Dow Jones & Company, Inc., The McGraw-Hill Companies, Inc., and National Newspaper Association.

degree to which the time required to change sort schemes might be fixed is an issue that remains largely unresolved. Accordingly, the Commission adheres to its view based on engineering and operational analysis, that most mail processing operations vary in proportion to volume.

[3005] *Postal Service modeling approach.* In Docket No. R97-1, the Postal Service proposed a statistical model for estimating the variability of mail processing labor costs. The Commission rejected the proposal. It concluded that the quality of the underlying data was too poor to support a valid statistical model, that it did not reflect an articulated economic theory, and that the resulting variabilities (76 percent) were so low as to be counterintuitive. PRC Op. R97-1, ¶ 3013.

[3006] In Docket No. R2000-1, the Postal Service proposed a revised model. While it reflected a more identifiable economic theory, the theory required a number of restrictive assumptions that the Commission found to be unrealistic. Prominent among them was the assumption that each operation within a processing plant functioned as a stand-alone operation, unaffected by the volume of mail or productivity of any other operation. Another overly restrictive assumption, in the Commission's view, was that piece handlings affect work hours in exactly the same way that volume does. Perhaps more important, the quality of the underlying data was no better than that upon which the initial model was based. The resulting variability estimates were even lower (less than 73 percent), and as implausible as the initial model results. For these reasons, the Commission rejected those estimates.

[3007] In Docket No. 2005-1, the Postal Service acknowledged for the first time the possibility that poor data quality was biasing the results of some of its models. In 2002, Mark Roberts, working on behalf of the OCA, published a paper recommending the use of an Instrumental Variables estimator to reduce the risk of downward bias that errors in the measurement of output impart to the class of models that the Postal Service employs. In that docket, the Postal Service applied the Instrumental Variables technique recommended by Roberts to its models.

[3008] The resulting variability estimates for the automated processing operations were inconsistent. For some automated operations, the variability estimates rose sharply to well over 100 percent, while variabilities for the remaining automated operations dropped sharply with percentages in the 40's and 50's. Finding no operationally sensible interpretation of these results, the Postal Service concluded that they were not suitable for use in ratemaking. Docket No. R2005-1, USPS-T-12 at 57-58. The results for the non-automated cost pools were more consistent. The variabilities estimated for its manual sorting operations rose dramatically (each by roughly 20 percentage points). The Postal Service viewed these results as more reasonable and recommended their use in ratemaking. *Id.* This selective use of the Instrumental Variables estimation technique increased the Postal Service's estimate of overall mail processing variability to 83 percent.

[3009] By agreement of the participants to Docket No. R2005-1, the Commission did not rule on the merits of the cost attribution proposals presented there. Consequently, the Commission evaluates these revisions to the Postal Service's proposed models for the first time in this docket.

[3010] In this docket, the Postal Service uses essentially the same Instrumental Variables models that it used in Docket No. R2005-1, updated with data for FY 2005. The results are summarized in the table below. It changed its model for the DBCS operation, separating it into separate models for outgoing and incoming processing. For the AFSM 100 operation, it estimates separate variabilities for outgoing and the incoming processing in a single, multi-variate model. Of the 11 sorting operations modeled, seven yield variability estimates (those shaded) that are statistically indistinguishable from the overall variability that the Commission estimates based on engineering/operational considerations (which is 94.3 percent for the base year in this docket). *See* PRC-LR-2. In this docket, the Postal Service estimates that the overall variability of mail processing labor demand is 85 percent. USPS-T-12 at 3. The results are displayed in Table III-1.

[3011] *The modeling approach of OCA witness Roberts.* Also in this docket, for the first time, the Commission evaluates the approach to modeling mail processing labor

Table III-1

Postal Service Estimated Mail Processing Variabilities

Translog						
DBCS	DBCS Incoming	DBCS Outgoing	OCR	FSM 1000	AFSM 100	SPBS
0.88	0.823191 (0.068115)	1.0562 (.059433)	0.782744 (.054455)	0.718714 (.032568)	0.99295 (.078844)	0.86644 (.049220)

Instrumental Variables (IV)				
Manual Flats	Manual Letters	Manual Parcels	Manual Priority	Cancellation
0.936682 (.066975)	0.892369 (.092588)	0.797821 (.177479)	0.751602 (.087483)	0.50476 (0.067071)

costs recommended by OCA witness Roberts. He develops a different theory of production that defines output as real volume, i.e., the number of unique pieces of mail processed in the plant. The best available measure of volume in the plant is First Handled Pieces (FHP). He believes that modeling the effect of actual volume in the plant on work hours in the plant is the only way to estimate economically meaningful marginal costs.

[3012] Roberts' modeling approach avoids the use of cost drivers unique to each individual sorting operation, and avoids the need to speculate about how those cost drivers might relate to volume in the plant. His theory of production is that there are separate processes (sets of machines) for each major mail shape—letters, flats, and parcels. Based on his own observation of mail processing in plants, he theorizes that plant managers respond to changes in volume levels by adjusting the mix of sorting technology applied (among manual, older types of machines, and newer types of machines) within a shape stream in order to minimize costs or meet service obligations.

[3013] In order to capture the effect of that changes in volume (FHP) have on the mix of operations in a plant, his models for a particular operation include measures of the stock of capital equipment and the relative wage in related operations.

[3014] He recommends this general approach to the Commission, and illustrates it with specific variability models for letter sorting and for flat sorting.²¹ He concludes that his approach models the variability of letters reasonably well, but not that of flats. Witness Roberts observes that his variability estimates for flats have large standard errors and are not stable with respect to reasonable variants of his models. Accordingly, he does not recommend that his estimates of flat sorting variability be used for ratesetting. He attributes the instability of his results for flats to recent upheaval in the flat sorting process itself.²²

[3015] The Roberts' estimated variabilities for letter sorting are presented below. His estimates for flats, which he does not endorse, are presented for illustrative purposes.

[3016] His estimated variabilities for letter sorting operations are well above 100 percent, both in aggregate and for the individual letter sorting operations. Witness Roberts concludes that his estimated variabilities for letters are robust across reasonable variants of his models, are consistent in aggregate, and are consistently above 100 percent. OCA-T-1 at 39. The primary conclusion that he draws from his models is that

²¹ Roberts' recommendations are developed in a series of three papers. The first was published in May of 2002 and the second in March of 2006. These papers were made available on the OCA's portion of the Commission's website and discussed in a public seminars following their publication. Roberts presented testimony in this docket in September, 2006 which referenced his findings in the earlier papers and included additional research. These papers have been treated by Roberts and the participants in this docket as an integrated whole in discovery, oral cross-examination, and briefs. The Commission affords them similar treatment in evaluating the evidence in this docket.

²² In his March 2006 paper, Roberts presents graphs showing that the widespread deployment of the AFSM 100 appears to have caused an upheaval in flats sorting—transforming the roles that the Manual Flats and the FSM 1000 operations play that is reflected in his model results. See Appendix J, Figure J-4 . He suggests that the Postal Service's models do not exhibit comparable instability because they do not have a means of capturing the effect of changing relationships among operations.

Table III-2

OCA Recommended Letter Variabilities

	Letters			
	Manual Labor	OCR	Aggregate BCS	Total Letters
FHP _{IN}	.911 (.110)	.783 (.227)	.930 (.080)	.912 (.062)
FHP _{OUT}	.609 (.077)	.420 (.153)	.202 (.056)	.364 (.044)
FHP _{IN} and FHP _{Out}	1.520 (.075)	1.204 (.241)	1.132 (.091)	1.276 (.061)

OCA Flats Variabilities (not recommended)

	Flats			
	Manual Labor	OCR	Aggregate BCS	Total Letters
FHP _{IN}	-.140 (.289)	.177 (.504)	.448 (.073)	.242 (.134)
FHP _{OUT}	.415 (.313)	2.042 (.529)	.605 (.079)	.857 (.142)
FHP _{IN} and FHP _{Out}	.275 (.361)	2.219 (.595)	1.054 (.091)	1.098 (.162)

there is no evidence that the variability of letter processing is less than 100 percent. Id. at 40.

[3017] *Separability, proportionality, and exogeneity.* In this docket, the Postal Service elaborates on its theory that each mail processing operation should be modeled as a stand-alone process, unaffected by the status of other operations in the plant (the “separability” assumption). This means that one operation is never substituted for another, even if they perform closely related functions.²³

[3018] The Postal Service defines work effort in a sorting operation as Total Pieces Fed (TPF). TPF is the number of times that a piece of mail is fed into a machine. The Postal Service elaborates on its theory that work effort in a sorting operation, workload in

²³ For example, the OCR operation reads an address and translates it into a printed barcode. The OCR function can be performed in the other automated letter sorting operations and in all of the automated flat sorting operations. All automated operations within a shape stream sort mail, but they accommodate different mail characteristics, and have different productivity rates.

an operation, volume in an operation, and volume in the plant, all move in lock step, so that any of these measures can be a proxy for any other (the proportionality assumption).

[3019] It theorizes that the level of TPF in each operation is determined automatically, based on the physical characteristics of the mail, pursuant to an operating plan that remains unchanged over a rate cycle of several years. This assumption has important theoretical implications. It means that the work effort (TPF) observed in each operation is a pure “volume” effect, uninfluenced by other factors such as the discretionary decisions that a manager might make to deal with higher volume by shifting mail from one operation to another (for example, to sort mail on a machine, rather than by hand, because there is enough volume to cover the cost of setting up and sweeping down the machine or to hold non-pref mail for later processing). TPF is “exogenous” if it is a force that is imposed on a sorting operation from the outside. It is “endogenous” if it is partly determined by the voluntary choices of the plant manager seeking to reduce costs or meet service commitments. If it is exogenous, TPF represents a “pure” volume effect. It means that by modeling the effects of TPF, the Postal Service could, from a theoretical standpoint, obtain an accurate, unbiased estimate of volume variability.

[3020] In this docket, the Postal Service presented evidence and argument that the separability assumption, the proportionality assumption, and the exogeneity assumption were all true, or nearly true, or could be made true if variable costs were distributed to subclasses the right way. It uses mailflow diagrams that purport to show that the path of each piece of mail through a processing plant is hardwired, based only on the physical characteristics of the mailpiece. USPS-T-12 at 17 and 20. It also used statistical tests to support its view that the underlying process consists of autonomous sorting operations, with unique cost drivers, whose effects are indistinguishable from the effects that volume would have had on work hours. These demonstrations and tests are evaluated in Appendix J at 87-96.

[3021] Roberts, supported by UPS witness Kevin Neels, and ValPak witness John Haldi, argues that the Postal Service’s views on separability, proportionality, and exogeneity are true, if at all, only in the very short run. Roberts views the time frame over

which these assumptions hold as a single sorting day. Robert March 2006 at 34. They argue that over longer periods of time, such as the multi-year rate cycle, operating plans change as additional machines or machines with new technology are deployed and plant responsibilities in the network are adjusted. VP-T-2 at 21-22. In shorter time frames, Roberts describes the discretion that managers have to define sort schemes that are run and adjust them to fit such things as seasonal mailing patterns. He also discusses the discretion that managers have to send mail rejected in an automated operation to be run on older, less used machines in other operations before sending them to manual operations. Roberts March 2006 at 34-35.

[3022] The opportunities for discretionary allocation of workload among operations in the short run is particularly evident in flat sorting. The record shows that the boundaries between the operations there are less rigid because the productivity differences are less pronounced than for other mail shapes. Tr11/2902; Tr. 11/2753. A substantial share of total volume is still processed manually and diverting automation compatible flats to the manual operation is still a common tactic when capacity is reached or service commitments require it. USPS-T-42 at 19; Tr. 11/2902,2785.

[3023] As the Commission reads the record, the characteristics of mail processing described by these witnesses cause a degree of substitution of some operations for others over the rate cycle. This causes the ratio of TPF/operation to FHP/plant to change, contrary to the separability, proportionality, and exogeneity assumptions upon which the Postal Service's models depend.

[3024] The result of these substitution effects can be seen in the data. Tables 1 and 2 in Roberts March 2006 show that the ratio of TPF/operation to FHP/plant changes significantly, both from year to year, and across plants. Similarly, Neels shows that the mix of sorting technologies, which largely define MODS operations, changes significantly from year to year. These changes are to a substantial degree, a response to changes in volume, since sufficient volume is necessary to justify deployment of expensive, large footprint machines. UPS-T-1 at 39.

[3025] The Postal Service models, because they treat each operation as an autonomous process, do not capture the impact of volume on the mix of operations in the plant, and therefore, measure only a narrow category of volume variability. Roberts demonstrates econometrically the relationship between the variability that the Postal Service models capture (the response of hours in an operation to TPF in an operation) and the variability that his models capture (the response of hours in an operation to FHP in the plant).

[3026] He restructured his models to be consistent with the Postal Service's basic assumption of separability. He then separately estimated the response of hours in an operation to changes in TPF in an operation, and the response of TPF in an operation to changes in plant FHP. Roberts observes that the first of the two responses is what the Postal Service models measure. He shows that when the two responses are summed, they generally yield the overall variability of hours in response to changes in plant FHP that his models measure. Generally, when the two responses are summed, they yield higher variabilities than the Postal Service estimates.

[3027] Witness Roberts' restructured model has clarified the partial nature of the volume variability that is captured by the Postal Service's models. In doing so, he has identified one source of the downward bias in the Postal Service's variability estimates. Roberts used the results of his restructured models to statistically test the Postal Service's assumption that operation TPF varies in proportion to plant FHP. He found that this assumption is not valid for eight of the 11 operations that the Postal Service models. This test, and the Postal Service's rebuttal material are evaluated in Appendix J at 43-45.

[3028] *Data quality.* The Postal Service's Management Operating Data System (MODS) records work hours and piece handlings incurred in each mail processing operation in each mail processing plant. Like most self-reporting systems, MODS generates an enormous amount of observations at the level at which the data are first collected and reported. The downside to collecting data this way is that the data set may be quite inaccurate, since the quality controls exercised at the source are likely to be

minimal. The MODS reports are also susceptible to censorship and manipulation because the basic purpose of MODS is to enable management to evaluate the performance of the Service's mail processing plants. See PRC Op. R2005-1, Appendix I, at 23 of 62.

[3029] Since these data were first made the basis for econometric modeling of mail processing cost variability, the Commission has consistently concluded that they are too error ridden to produce estimates that are sufficiently free of bias to be relied upon for ratemaking. See PRC Op. R97-1 at 81-84; PRC Op. R2000-1 at 90, 97; PRC Op. R2005-1, Appendix I, at 29-33, 37, 52.

[3030] Measurement of the variables that are to be used as explanatory terms in the estimated variability models (TPF or FHP) must be substantially free of error. The Commission has warned since Docket No. R97-1 that the consequences that follow from using an explanatory variable measured with a substantial level of error can be severe. When fit to the sample, the model's estimated coefficients are likely to be biased and inconsistent. "Biased" means that the estimated coefficients aren't likely to be the true coefficients. "Inconsistent" means that the bias will remain even if the sample is large. PRC Op. R97-1 at 82-83.

[3031] In general, errors in an explanatory variable bias the estimated coefficient of that variable toward zero.²⁴ The greater the variability in the measurement error, the greater the downward bias. This is clear in the case of a model with a single explanatory variable, but in a multi-variable model, there is a general tendency for the set of estimated coefficients to collectively move toward zero.²⁵ This bias is magnified when estimators are used that difference the data, and thereby remove much of the cross-sectional variation in the panel. This is true of all of the models proposed in this

²⁴ This assumes that the errors are independent and identically distributed.

²⁵ Robert S. Pindyck and Daniel L. Rubinfeld, *Econometric Models and Econometric Forecasts*, 2nd ed, McGraw Hill, 1981, at 177.

docket, all of which use Fixed Effect estimators. See the relevant econometric literature summarized in Roberts 2002 at 50.

[3032] The dependent variable in the mail processing labor demand models under review is workhours in the sorting operation, or the plant as a whole. These hours are calculated from clock rings in which the worker is responsible for swiping a badge across the appropriate reader whenever he enters or leaves a MODS operation. Employees are sometimes not sufficiently motivated to ring in and out of an operation if changes in assignment are frequent or short term and their pay is not affected. Witness Neals demonstrates that misclocking is common in the MODS data, as indicated by the first-hand observations recorded by data collectors in the overlapping IOCS system. UPS-T-1 at 15.

[3033] If the measurement error in the dependent variable (work hours) is systematically related to the independent variable (output), then least-squares estimation methods can cause bias in the estimate of the output coefficient.²⁶ A systematic relationship between misclocking and output might plausibly occur, for example, if work hours are underreported by workers whose productivity is evaluated on that basis relative to other workers.

[3034] At the conclusion of Docket No. R97-1, the Commission observed “[e]conometricians are accustomed to using data as they find it, however the MODS data . . . are far below the common standard.” *Id.* at 82. Nothing has been done in the ten intervening years to cause the Commission to reconsider that observation.

[3035] The nature and extent of the errors in the MODS piece handling data were thoroughly documented in Docket Nos. R2000-1 and R2005-1, and again by witness Neals in this docket. In Docket No. R97-1, a study of MODS data quality by the Postal Inspection Service was cited which concluded that there were large variances between the piece handling figures contained in the MODS system and actual piece counts. See

²⁶ Jeffrey M. Woolridge, *Introductory Econometrics: A Modern Approach*, South-Western College Publishing, 2000, at 293.

PRC Op. R97-1 at 83. Most of this kind of error, however, is not extreme enough to be detected without a special study like that conducted by the Inspection Service. It is implicit, absent a specific study to quantify it.

[3036] Added to this implicit error are a wide variety of explicit error — error that is so obvious that it is self identifying upon inspection. Errors of this kind abound in the MODS data. They include hours or handlings with negative values, instances where hours are positive and handlings are zero (or vice versa), instances where First Handled Pieces are greater than Total Piece Handlings, and (for automated operations) instances where Total Piece Handlings are greater than Total Pieces Fed. There are also instances where the ratio of hours to handlings implies productivities that are either too low or too high to reflect actual operating conditions. There are numerous “drop outs” (periods when reporting of values intermittently ceases). The Postal Service does not distinguish reporting drop outs from valid zero observations (those that indicate that a relevant operation was temporarily shut down).

[3037] MODS data are collected by shift, and rolled up by day, week, Accounting Period, and Quarter. Errors that would be explicit at the shift level tend to be masked when rolled up into a daily count. The masking increases with the level of aggregation. The degree of masking can be considerable by the time that MODS data are rolled up into Quarters — the level at which it is used in the various models under review in this docket.

[3038] For MODS data compiled at the weekly level, the frequency of explicit errors is quite high. Tables constructed by witness Neels show that the frequency of observations with unrealistic productivities are extraordinarily high for a database to support valid econometric work. The Commission agrees with witness Neels that “[o]ne must wonder about the reliability of a data reporting system that produces obviously erroneous results up to 30, 40, or as much as 50 percent of the time.” UPS-T-1 at 26. These frequencies reflect only one of the half-dozen categories of explicit error in the MODS data. Such rates of explicit error must be regarded as symptomatic of a data measuring, recording, verifying, auditing, and archiving process that is broken.

[3039] Witness Bozzo argues that his screens are effective at removing explicit error in the MODS data, and implies that the implicit errors that remain are not significant. As evidence, he cites the results of a sensitivity check that he conducted, using his preferred models. Witness Bozzo reestimates his variability models using a sample constructed by using threshold and productivity screens at the weekly and Accounting Period level. He obtains a composite variability of 84 percent from his models with strict screens compared to the composite variability of 86 percent that he obtains from his model with quarterly screens. He concludes screening at the stricter level “[h]ad relatively little effect on most variabilities.” USPS-T-12 at 97.

[3040] Bozzo neglected to evaluate what his results show when Manual Priority variability is left in. Using weekly screens causes Manual Priority variability to triple to 228, manual parcel to rise from 80 to 97 percent, and cancellation to rise from 50 to 59 percent. The composite variability rises from 85 to 93 percent. *See id.* at 99 (Table 26).

[3041] When witness Neels developed his plant-level model of mail processing variability, he performed a sensitivity analysis similar to that of Bozzo’s. To be reliable, a plant-level model requires substantially error-free data for the entire plant. In preparing a database free of explicit error for the entire plant, Neels found that the cumulative effect of screening out explicit error at the weekly level is dramatic. As can be seen from Table J-6 in Appendix J, only 920 out of 10,304 records (about nine percent) were valid for the entire plant. At the quarterly level, the results of screening are less severe. At the quarterly level, 2,155 out of 10,304 records (about 21 percent) were valid for the entire plant.

[3042] The difference in screening level produced significantly different variability estimates. Neels model using data screened at the weekly level produced an aggregate plant variability of 114 percent. At the quarterly level, estimated variability was 103 percent. Neels points out that it is not possible to determine whether the differences in variability estimates are the result of eliminating the obvious errors from the data, or sample selection bias arising from the severely truncated sample. He concludes that the nature of the MODS data is such that there is no workable balance that can be struck

between using these data despite their obvious errors, or screening out the obvious errors and risking drastic sample truncation bias. UPS-T-1 at 26, 55.

[3043] The Commission agrees. The sensitivity analyses performed by Bozzo and Neels result in dramatic reductions in the size of their usable samples, and significant differences in their variability estimates. These results strongly imply that enough explicit error remains in the data when screened at the quarterly level to make the resulting estimates unreliable for ratemaking.²⁷

[3044] *Correcting for errors in the MODS data.* When it is not practical to count mail, the Postal Service weighs it and infers the number of pieces from national standard conversion factors. Bozzo and Roberts treat the set of factors that the Postal Service uses to convert pounds of mail to pieces as the major source of error in the MODS piece handling data. Conversion factors are inaccurate because they are not plant specific, and many years go by between updates. Conversion factors are needed to compute FHP in each operation. They are also the basis of TPH counts for the manual operations.

[3045] The data also shows that the average weight per piece of letters, flats, and parcels varies substantially by quarter. See Appendix J, Figures J-1 through J-3 . For letters and flats, it has also risen gradually over time. See Roberts 2002 at 49. These kinds of systematic error in the output variable present a substantial risk that the resulting estimates of output variability will be biased. All of the econometric witnesses acknowledge this risk, and all have turned to the use of Instrumental Variables estimators as a way of mitigating that risk.

[3046] *The need for instruments.* Instrumental variables are commonly used in econometric modeling to overcome the endogeneity of a regressor (the correlation of a regressor with the regression error term). Instruments are variables that partly cause the

²⁷ There are also serious errors in the data used to match capital equipment deployment (the PPAM/PEAS data) with work hours and output data that are likely to bias the econometric estimates of the mail processing labor variability under review. See Appendix J at 54-55.

endogenous regressor. This causal relationship can be used to recover an estimate of the endogenous regressor that is free of the measurement error that it contains.²⁸

[3047] All of the econometric witnesses agree that inaccurate weight-to-pieces conversion factors measure FHP with error. To the extent that it is inaccurately measured, variation in FHP transmits both the effect of variations in volume and the effect of measurement error to work hours. As explained above, mixing these effects is likely to bias the estimated response of work hours to volume downward. Roberts acknowledges that this is especially true for the Fixed Effect models under review. Fixed Effects models remove much of the variation in the volume variable that is available for modeling. This magnifies measurement error relative to the volume variation that remains, which greatly increases the risk of bias from measurement error. Roberts March 2006 at 50.

[3048] *Validity of instrumental variables used in this docket.* The theoretical requirements and the mechanics of using instrumental variables to estimate an economic relationship are briefly reviewed in an academic note in Appendix L. Their application by the econometric witnesses in this docket is evaluated in Appendix J at 56-76.

[3049] The conditions that instruments must meet in order to be valid are quite demanding. The basic idea of Instrumental Variables regressions is to find an instrument that causes or explains only the variation in the volume variable that is “true” volume variation, but is independent of the variation in the volume variable that represents other things—such as measurement error in that variable.

[3050] These are rigorous conditions. In order to be valid, the instrument must be exogenous to the underlying model, that is, it must affect work hours only through its

²⁸ The most common method of estimating the value of the endogenous variable without error is called Two-Stage Least Squares. The first stage of analysis is to take the right hand side variables in the model of interest and replace the endogenous regressor with the instruments. The endogenous variable in the regression of interest is regressed on the set of right hand side variables including the instruments. The fitted value of the endogenous variable that results is correlated measurement error, assuming that the instruments and the other right hand side variables are valid. The second stage of analysis is to insert the fitted value of the explanatory variable back into the regression of interest and to rerun the regression.

effect on the endogenous “volume” variable (FHP or TPH). It must not affect work hours directly.²⁹ (If the instrument affected work hours directly, it would belong in the set of control variables in the regression of interest). In addition, the instrument must be “relevant,” that is, it must cause or verifiably explain the portion of the variation in the endogenous “volume” variable that is not caused by omitted variables or by measurement error.³⁰ If it explains any of the erroneously measured part (if a factor that makes the measure of the “volume” variable erroneous also makes the measure of the instrument erroneous) the instrument will transmit the error in the “volume” variable through to work hours. This would defeat the instrument’s purpose.

[3051] As explained in Appendix L, it is impossible to demonstrate that an instrument is valid through a statistical test.³¹ To be credible, an assertion that an instrument actually eliminates endogeneity, such as that caused by measurement error, needs a convincing theory that identifies the cause of the endogeneity, and a convincing theory that explains why the instrument is independent of that cause. In addition, the instrument must capture the “true” variation in the “volume” variable, not just coincidental correlation. This also requires a sound theory as to why the instrument is a partial cause of the “volume” variable, rather than simply responding to common factors that cause them both.

²⁹ Holland, P.W., “Causal Inference, Path Analysis and Recursive Structural Equation Models,” *Sociological Methodology*, 18, 449-84, Angrist, J. and Imbens, G. “Estimation of Average Causal Effects,” *Journal of the American Statistical Society*, 91, 444-72.

³⁰ Angrist, J. and Kreuger, A., *Instrumental Variables and the Search for Identification: From Supply and Demand to Natural Experiments*, *Journal of Economic Perspectives*—15, No. 4 (Fall 2001), at 73. The causal effect must run from the instrument to the endogenous “volume” variable, not the other way. If some intervening force should change the value of the “volume” variable, it must not affect the instrument. See Rubin, D.B., *Statistics and Causal Inference: Comment: Which Ifs Have Causal Answers,* *Journal of the American Statistical Association*, 81, 961-962 (1986).

³¹ It is possible, of course, to increase one’s confidence that an instrument is relevant by testing the significance of the instrument’s coefficient in the First Stage of a Two Stage Least Squares regression and obtaining a high “t” value. That will indicate the strength of the correlation of the instrument with the endogenous explanatory variable, but it will not indicate whether the correlation is theoretically meaningful, or merely coincidence.

[3052] *Relevance of the instruments under review.* Although all three researchers have employed instrumental variables in their models, and their instruments differ,³² they basically borrow the theoretical justification for the validity of their instruments from witness Roberts. The Commission's conclusions with respect to the validity of the instruments that he uses generally apply to the instruments used by the others.

[3053] The following discussion illustrates Roberts' theoretical justification for believing that his instruments are relevant to his endogenous output variable (FHP/shape). Roberts uses the following as instruments for the FHP of letters: FHP flats/incoming, FHP flats/outgoing, quarterly dummy variables, and the number of destinating letters, flats, and parcels in a plant's service area. He asserts that

[a]ny exogenous source in the demand for mail services will lead to fluctuations in the FHP variables that are not correlated with the error term and, as a result, will be useful as an instrumental variable. In short, variables that measure fluctuations in the demand for mail services will be good instrumental variables (IVs) because they will be correlated with FHP but not correlated with the technology shocks or output measurement errors captured by the error terms.

OCA-T-1 at 28. These criteria are broad, vague, and conclusory. By themselves, they do not have the theoretical rigor required to provide reasonable assurance that variables that meet them would be valid instruments.

[3054] Roberts is a bit more specific with respect to why FHP/flats is a valid instrument for FHP/letters. He asserts that FHP/flats

reflect variation in the demand for mail services that can result from differences in the mix of business and household mailers in the plant's service areas, differences in population and its growth over time, and other sources of differences in demand across plants.

³² See Appendix J, Table J-7 which compares the instruments used by the various econometric witnesses.

[3055] *Id.* FHP/flats is much like true RPW flat volume. The volume of flats that arrives at a plant will certainly be a function of the mix of mailers, population trends, and other factors in the plant's service area, just as the volume of letters that arrives at a plant will be a function of these factors. It is not enough, however, that the the level of FHP/flats entering a plant and the level of FHP/letters entering a plant both are a function of local business conditions and consumer wealth characteristics. To be valid, an instrument for FHP/letters must not just be correlated with the FHP/letters, it must partially cause variation in FHP/letters.

[3056] It is not plausible to characterize variation in FHP/flats as a source of variation in FHP/letters. The plausible sources of variation in FHP/letters include such things as the profile of local business mailers (utility billers, credit card issuers, etc), the disposable income of local recipients of mail, the pace of local household formation, the price and availability of competing forms of communication and advertising, etc. The proximity of other postal facilities, and their capacity and function are also plausible causes of the amount and kind of mail that a plant receives. These are much the same as the plausible sources of variation in FHP/flats. This would make FHP/flats a spurious instrument for FHP/letters.³³ FHP/flats can not be used to extract the "relevant" portion of the variation in FHP letters that is free of confounding effects. It can only mimic FHP/letters. If one were to imagine an array of intervening forces that could affect

³³ An intuitive example of a spurious correlation would be sales of ice cream and sales of soda by local outdoor vendors. Both are likely to rise strongly in summer, as outdoor recreation increases. A statistical test would reflect the strong correlation. But sales of ice cream do not logically cause sales of soda. The true cause is the warm weather, which encourages both. Ice cream sales would be a spurious instrument to use to predict sales of soda, despite their close correlation. A true causal relationship likely exists between the quantity of chips and soda sold by outdoor vendors. Warm weather increases outdoor recreation, causing outdoor sales of both chips and soda to rise. But, because salty chips increase thirst, they independently encourage sales of soda. This correlation would be meaningful because there is a plausible causal theory to explain the correlation. For this reason, sales of chips (in an earlier period) might be a valid instrument for sales of soda.

In the mail processing context, the relationship between FHP flats and FHP letters is analogous to the relationship between sales of soda and sales of ice cream in the above example. They are correlated, but the correlation is not meaningful. They are spurious instruments for each other. The local business cycle is analogous to the weather in the above example. It is a plausible cause of variation in both FHP letters and FHP flats, and might make a theoretically relevant instrument for either.

FHP/letters (e.g., a local recession, a surge of home construction) most of them would be expected to affect FHP/flats as well. This means that FHP/flats is not a well-defined instrument for FHP/letters.³⁴ Instead of FHP/flats, plausibly valid instruments for FHP/letters would be the underlying causes of variation in both. These would include measures of the economic and business conditions in the service area of a plant described above.

[3057] For the reasons explained above, the Commission has concluded that while FHP of one shape may be correlated with FHP of a different shape, it is not plausibly a function of, or caused by, FHP of a different shape. Because the correlation stems from common latent causes, FHP of a different shape is a spurious instrument.

[3058] None of the econometric witnesses have provided a convincing theoretical rationale for believing that the instruments that they use are relevant to the endogenous output variable on which their models are based. If the instruments are not relevant, they can not serve their purpose. The theoretical relevance of the instruments used, and the relevance tests applied, are discussed in more depth in Appendix J at 59-68.

[3059] *Exogeneity of the instruments under review.* When output can not be counted, it must be inferred by weighing the mail and using a conversion factor to estimate the number of pieces. FHP counts are based on this process, as is the major portion of TPH in manual operations.³⁵ For reasons described earlier, using a national conversion factor that is seldom updated ensures that the piece count (FHP) inferred will be inaccurate.

[3060] Using instruments to overcome measurement error in the endogenous output variable (FHP or TPH) is based on the idea that a variable can be found that will extract that portion of the variation in FHP that is independent of measurement error (or any other source of non-volume variation). It is not necessary that the instrument itself

³⁴ See Rubin, D.B., Statistics and Causal Inference: Comment: Which Ifs Have Causal Answers," *Journal of the American Statistical Association*, 81, 961-962 (1986).

³⁵ TPH in manual operations consists of First Handling Pieces (FHP) and Subsequent Handling Pieces (SHP).

by free of error, just that its error be independent of the error in the FHP shapestream of interest. Roberts 2002 at 54, n.30.

[3061] Noting that different conversion factors are used for different shapes, Roberts reasons that FHP of a different shape will be free of the predominant source of measurement error in FHP of the same shape. The assumption that the error in the instrument is uncorrelated with the error in FHP can not be proven through statistical tests. Statistical tests can only indicate that this requirement is not met by particular instruments when they are tested. Therefore, a convincing theory that explains why variation in the instrument can be assumed to be independent of error in FHP/shape is needed to be assured that use of the instrument will lead to reliable estimates.

[3062] *Conversion error.* The fact that different weight-to-piece conversion factors are used for different shapes might not be sufficient to ensure that they are independent. As noted above, these are secular and cyclical variations in average weight per piece that may be correlated among mail shapes.

[3063] Witness Neels demonstrated that the average weight per piece changes substantially over time for classes of mail. Tr. 23/8528-31. This implies that it changes substantially over time for shapes of mail as well. Witness Oronzio observes that one reason that FHP data are not trusted by plant managers is that the composition of the mail changes by season. He remarks that even humid weather can alter the weight of the mail enough to induce conversion error. USPS-RT-15 at 12.

[3064] Systematic changes in weight per piece could cause corresponding changes in conversion error and the work hours required to process mail. (The ounce/rates and breakpoints common in postal rate schedules, in part, reflect the productivity of the equipment that can be used to process mail of certain weight characteristics). Therefore, there appears to be a significant risk that conversion error is correlated with work hours in the manner described. This provides reasons to doubt that opposite shape FHP can be assumed to be an exogenous instrument.

[3065] *Other sources of measurement error.* Even if conversion error in FHP of one shape were truly independent of conversion error in FHP of other shapes, there are

sources of significant measurement error in MODS output data that are not related to the conversion process whose effect is probably common to all shapes, and, therefore, correlated. These include the negative FHP counts, implausibly high or low productivity values, the pairing of zero hours with positive FHP and vice versa, and the discontinuities in the data that are treated as true zeros. If these errors are essentially failures to collect the data, to record them by the prescribed procedures, or to audit the data either at the source, or after aggregation, such failures are most likely to be the result of the administrative problems that are known to plague self-reporting data systems from which productivity can be inferred.

[3066] The tension that exists between allocating resources between mail processing and data collecting is reflected in the old MODS manual which authorizes the director of mail processing in the plant to “assign employees to other duties to ensure full utilization on assigned tours, providing that such assignment does not interfere with the accurate recording of mail volume....” Handbook M-32, dated 1987, Section 144.2(e). Conflicts of this kind would seem to be a particular problem at times when plants operate above capacity. Instead of carefully recording, compiling, and auditing MODS data, such conflicts might be resolved in favor of getting the mail out. Under high-volume conditions, the required reports might not be prepared, or be prepared but not audited. This would be all the more likely if, as Postal Service witness Oronzio asserts, plant managers no longer rely on MODS FHP data. USPS-RT-15 at 12-13. The resulting errors should have a similar effect on all shapes of mail (and therefore are likely to be correlated), which would violate a basic condition that instrumental variables of the opposite shape must meet if they are to avoid the bias associated with measurement error in the piece handling data.

[3067] As noted, the assumption that the error in the instrument is uncorrelated with the error in FHP must rest on a sound theory because it can not be proven through statistical tests. Statistical tests can only indicate that this requirement is not met by particular instruments when they are tested.³⁶ The Commission concludes that there is

³⁶ The tests that the econometric witnesses conducted of the hypothesis that the instruments that they used are exogenous are evaluated in Appendix J at 69-76.

no convincing theory that the opposite-shape output variables used as instruments in all three models are uncorrelated with the measurement error in the output variables of the same shape.³⁷

[3068] *Reasonableness of the model results.* In evaluating the models under review in terms of the reasonableness of their behavior and results, the overriding circumstance that should be borne in mind is that they all depend on error-ridden MODS data, and none of them have found valid and relevant instruments that overcome the risk of bias that results from errors in the definition and the measurement of volume. Consequently, none of the model results can be trusted to be unbiased, and none provide a suitable basis for estimating the variability of mail processing labor demand. The task here is to identify the model with the fewest infirmities.

[3069] The results of the various models under review are summarized in Appendix J in Table J-8 . These results bracket the approximate 94.3 percent variability that results from application of the Commission's engineering/observational assessment of the volume variability of mail processing labor demand. The shaded variability estimates are statistically indistinguishable from the Commission's overall estimate. The unshaded estimates fall above and below the Commission's overall estimate. Due to the formidable obstacle that MODS data quality presents to econometric modeling, none of these estimates is more reliable than the Commission's operational assessment of variable mail processing labor costs.

[3070] *Postal Service models.* The most significant properties of witness Bozzo's models that the Commission has not previously had an opportunity to evaluate are the results of using log-linear Instrumental Variables estimators. Bozzo investigates using these estimators for all 11 modeled operations, but recommends using the results only for manual and cancellation operations. Table J-8 in Appendix J shows the effect of

³⁷ It is theoretically plausible that the destinating-shape volume variables used as instruments are uncorrelated with measurement error in the FHP/TPH variables because they are obtained from an independent data collection system (ODIS/RPW). But they do not seem to add much explanatory power to any of the models under review.

applying log-linear Instrumental Variables estimators (row 2) and compares them to the results of using Bozzo's traditional translog Fixed Effects estimators (row 1).

[3071] Table J-8 shows that when Bozzo's traditional translog, Fixed Effect estimator is applied to manual and cancellation operations, it yields variability estimates below 50 percent for all but the Manual Flat operation. There is no plausible operational explanation for manual sorting variabilities this low, for reasons that the Commission explained in Appendix F to Docket No. R2000-1.³⁸

[3072] When the log-linear Instrumental Variables estimator is applied to the manual and cancellation operations, estimated variabilities consistently rise by astonishing amounts. Manual letter variability rises by more than 50 percentage points, Manual Parcels and Manual Priority rise by more than 30 percentage points, and Manual Flats rises by 17 percentage points. Bozzo interprets such results as verification of the Commission's suspicion that attenuation bias due to measurement errors in the FHP variable drive the Fixed Effects estimates downward. See Docket No. R2005-1, USPS-T-12 at 57.

[3073] The translog Fixed Effects estimator traditionally used by witness Bozzo yields less extreme results when applied to automated operations, but the variabilities are still less than 100 percent for all but outgoing DBCS and the AFSSM 100. When the Instrumental Variables estimator is applied to the same automated operations, estimated variabilities for three of the operations rise above 100 percent, while the estimated variabilities for the OCR and the FSM 1000 drop dramatically to 53 percent and 44 percent, respectively (levels that are operationally unexplainable for automated operations). There is little that could explain why some automated operations would be more than 100 percent variable, but others are half that.

³⁸ In this docket, Postal Service witness McCrery attempts to justify an estimated variability of 50 percent for the Cancellation operation by asserting that employees clocked into the operation are intermittently rotated to other activities during lulls in arriving mail, but that the employees seldom relock as the rules require. USPS-T-42 at 39. Such misclocking constitutes measurement error, since it allocates time spent outside the Cancellation operation to the Cancellation operation. If misclocking is the reason for the low variability estimated for the Cancellation operation, the estimate is invalid for that reason.

[3074] For many operations, the results from Bozzo's models are operationally implausible without using the Instrumental Variables estimator, but a different set become operationally implausible when the Instrumental Variables estimator is used. These results do not inspire confidence in the Bozzo models.

[3075] *Roberts' models.* The Commission views witness Roberts' modeling approach as being more sound from a theoretical standpoint than that of witness Bozzo. It endorses his definition of output (plant-level FHP by shape) as being much closer to an economically meaningful definition of volume than operation-level TPH, and it endorses the key assumptions that underlie it, including the assumption that volume levels affect the mix of operations within a plant. It also endorses his conclusion that categorizing output according to its cost-driving characteristics, and distributing the variable costs caused by each category to subclasses according to their true (RPW) volume share of that category would come closer to an economically meaningful product marginal cost, provided the data were available. The question then becomes whether Roberts' theoretically superior approach can be successfully applied, given the limitations of the data.

[3076] Roberts explores many variations of his models and is not strongly wedded to the results of any particular variation of his FHP/shape models that use a Fixed Effects, Instrumental Variables estimator. Like Bozzo, Roberts finds that output variabilites decline dramatically with the inclusion of a plant-specific Fixed Effects variable, and rise dramatically when an Instrumental Variables technique is used, suggesting that measurement error in the output variable has been causing substantial downward bias in the estimates. *See Roberts 2002, at 60-61.*

[3077] The results of Roberts evolving models are presented in Appendix J, Table J-8. In Roberts 2002 (row 7), Roberts modeled panel data for the period 1994-2000. In Roberts March 2006 (row 6) his model covered the 1999-2004 period. In Roberts September 2006 (row 5), his model covered the period 2002-2005.

[3078] For reasons explained in Appendix J, Roberts' aggregate letter variabilities could be viewed as stable or as rising significantly over time, depending on which

relatively minor model variations are considered. Another way to judge whether Roberts' letter models are robust is whether his estimated aggregate letter variabilities are stable across reasonable variants of his models. For reasons explained in Appendix J, his letter models are quite stable in this respect.

[3079] When Roberts disaggregates his output variable to distinguish between automated and non-automated categories, standard errors become very high. Some variability estimates lose their statistical significance (particularly for OCR) or become counter-intuitive (particularly FHP/in/non-automated). See OCA-T-1, Table 5, Panel D. This illustrates the practical limit of disaggregating the output variable, given the nature of the MODS data that are available.

[3080] Roberts has had more difficulty modeling the variability of flat sorting operations than letter sorting operations, particularly for the period that follows the introduction of the AFSM 100 technology. As described in Appendix J, his results for flats for that time period are unstable and sometimes counterintuitive. Most of the plausible explanations suggest that Roberts failure to produce robust and intuitively variability estimates for flats stem from numerous inherent obstacles to successfully modeling mail processing discussed in Appendix J at 96-106.

[3081] *Neels' models.* Witness Neels developed multi-variate models that estimate the response of work hours in the entire plant to changes in FHP for each of the major shapes—letters, flats, and parcels. He argues that the virtue of his models is that they capture cross-operation and cross-shape effects of volume, as well as within-operation effects. Any changes in the relationship of TPH to FHP have been reflected in his models' results. Neels contends that a plant-level model also provides a sound way to integrate allied operations and overhead activities into the model. It also tends to net out that portion of the errors in the MODS data that mismatch hours and volumes in specific operations. He essentially disavows his results, however, due to the risk of bias from the poor quality of the MODS data and from truncation bias arising from the drastic screening of the data that poor data quality requires.

[3082] Neels' models demonstrate that screening MODS data at different levels produces significantly different variability estimates. They are also valuable in the sense that they treat the processing plant as an organic whole where mail processing of all shapes is brought together to take advantage of economies of scope. Economies of scope are found in the sharing of allied and overhead costs (dock functions and staging and prepping activity) among the shape streams. His models illustrate how modeling might overcome the flaws in the Postal Service's approach, which artificially selects only 11 direct distribution operations to model and then extrapolates the results to the other two-thirds of mail processing that consists of allied and overhead activities. In the Commission's view, direct modeling of these activities is required, since there is reason to believe that the bulkier shapes of mail (flats and parcels) account for a greater proportion of such costs than of the costs of the direct sorting operations.

[3083] *Conclusions applicable to all models.* There are fundamental obstacles to obtaining economically meaningful marginal costs for mail processing labor through econometric modeling. The most important obstacle is that the Postal Service does not have data on the theoretically correct definition of volume--unique RPW pieces finalized to exit the mail processing system. The Postal Service does not have data that can track RPW pieces as they move through plants, or through operations in plants. The Postal Service's models appear not to be motivated by theory so much as by the ready availability of detailed data on total piece handlings, at least for the narrow set of operations that handle pieces of mail individually.

[3084] TPH is a measure of work effort—not production. TPH yields measures of work effort expended as it rises and falls at different points in the plant—a measure that can be disaggregated to a fine degree. What is needed, however, is a disaggregated measure of the burden that the volume of mail entering the plant imposes on the various activities throughout the plant.

[3085] Because TPH are not unique pieces, and can not be reliably converted to unique pieces, it is only meaningful within an operation. Dollars spent in one cost pool can be compared with dollars spent in another, but TPH incurred in one cost pool can not

be compared with TPH in another. TPH does not represent the same amount of work, or accomplish the same improvement in mail condition, from one pool to another. It therefore can not be used to measure how labor is being allocated among sorting activities. See Roberts 2002 at 10-14. TPH can not even be relied on to represent the same amount of work effort, or improvement in mail condition, within a cost pool from one period to another, because the technology that defines the cost pool often evolves, and the boundaries of the cost pool change.³⁹

[3086] Plant-level FHP is one level closer to true volume (RPW finalized pieces) than TPH. It measures the average propensity of a unique piece of mail entered into a plant to generate work hours finalizing a piece of mail, not the propensity of an intermediate handling to generate work hours, as TPH does. FHP is linked directly to volume in the plant, and therefore is a potentially more consistent measure of the plant-wide burden that a piece of mail imposes on the plant.

[3087] To be truly consistent, however, FHP must be disaggregated into incoming/outgoing, and machinable/non-machinable categories, etc. Roberts recognized this, but found that the estimates are not precise enough to be meaningful when the data are disaggregated to the required degree. Another flaw in using FHP as a proxy for volume is that it is endogenous in the sense that it will be partly determined by management decisions to balance workloads among plants.⁴⁰

³⁹ An example would be the OCR cost pool. The OCR function has gradually migrated away from the OCR pool itself into the AFCS and the D/BCS. More time is spent, and more improvement in mail condition occurs in the latter two cost pools when an address is read, and a barcode applied, prior to the actual sorting of the piece. Yet the TPH count in the operation won't change if a piece receives one aspect of this service, or all three. Differences in the work content of the TPH over time within a pool will result in a biased elasticity estimate, especially in a plant-specific Fixed Effect model, which focuses on variation over time. Other examples would be the gradual migration of DPS level sorting of letters, and carrier route sorting of flats, from the plant, to the delivery unit, and back to the plant as technology changes. When this occurs, it tacitly redefines TPH for the pools affected in terms of the improvement in mail condition that a TPH represents. This, too, will lead to biased estimates of the effect of TPH on work hours.

⁴⁰ The Managed Mail program shifts volume dynamically among plants according to the spare capacity of plants. It illustrates that there are volume effects that occur across plants that need to be reflected in valid models of mail processing variability.

[3088] This leaves those wishing to accurately model the variability of mail processing labor demand in a dilemma. The Postal Service has a wealth of data with which to measure TPH, disaggregated to the nth degree, but it is a localized, partial, and biased measure of the effect of true volume on work hours. On the other hand, the data required to disaggregate FHP to the necessary degree to find the marginal effect of variation in true volume on work hours are not available. Even if the data were to become available, there would still be bias when FHP is used to compare volume effects across plants. The bias inherent in TPH, and the lack of data that are sufficiently detailed to properly model with FHP, are partly to blame for the failure of econometric methods to reliably measure the variability of mail processing labor costs.

[3089] The lack of plant-specific data on true volume that has long prevented successful modeling of its effects on work hours could, however, be remedied in the near future by the Postal Service's "Intelligent Mail" program. Apparently, that program envisions applying a powerful, four-state barcode to all mail that can be passively scanned. The objective of the program is to be able to monitor the path of each RPW mailpiece through the mail processing network. This raises the prospect of being able to record the number of unique RPW pieces with relevant cost driving and subclass characteristics in a sorting activity and correlate it with work hours spent on that activity. This could provide a direct method of calculating the marginal cost of processing each postal product (or, at least, each postal product that is machinable). This method could be extended to the two-thirds of mail processing activity that currently is not modeled, since mail could be effectively tracked even when it is handled in bulk in containers.

[3090] True volume, however, is not the only data that are required in order to successfully model the variability of mail processing labor. Valid data on the capital stock by operation are needed, properly matched to the time of deployment and retirement. As Roberts has pointed out, the Postal Service data on its capital equipment does not accurately record the time of deployment and retirement of equipment. Since timing of deployment is a major factor in Fixed Effect models, errors of that kind

undermine the ability of such models to accurately capture the underlying production process.

[3091] For the reasons described above, econometric modeling of mail processing labor demand variability seems to have reached an impasse. Witness Bozzo has chosen to model partial, short-run effects of output (loosely defined) on a very detailed level and does not obtain stable or intuitively reasonable results. Witness Roberts has chosen to model longer-run, more comprehensive effects of output (more correctly defined) and does not obtain stable or intuitively reasonable results, at least at the operation level. He has also reached the limit of disaggregation of his output variable short of that which is necessary to estimate true marginal costs of subclasses. Witness Neels results, though intuitively reasonable, vary according to the level data screening, and require such massive truncation of the available data that Neels, himself, does not trust the results.

[3092] All three witnesses presenting econometric models grasp the serious risk of bias from relying on TPH and FHP data of poor quality and attempt to avoid that risk through the use of Instrumental Variables estimators. The instruments selected, however, are not valid, either because they are not supported by plausible theories that they are exogenous, or are not sufficiently relevant to effectively capture the variability of interest. This reflects the paucity of data that are available from which valid instruments could be fashioned.

[3093] If the system by which MODS piece handling data is collected is not reformed, or a comprehensive substitute measure of volume is not provided through the Intelligent Mail program, econometricians will have few alternatives but to continue to search for valid instruments. This search is not likely to bear fruit, however, unless a new category of data are made available for their use. Econometricians need to be able to access (with reasonable safeguards) the wealth of location-specific information that exists with respect to processing plants in the network. This would allow measures of local economic activity, and local business and consumer profiles that would be expected to drive mail volume, to be analyzed for their value as exogenous Instrumental Variables. See Appendix I.

[3094] Until data of the kind described are made available, the vacuum left by unsuccessful econometric models of mail processing variability will have to be filled with the estimate of approximately 94 percent variability that the Commission applies, based on engineering and operational assessment.

[3095] *Seasonal effects.* Mail volume varies substantially by quarter. In his March 2006 paper, Roberts examined in some depth the issue of whether that variation should be exploited by mail processing labor demand models or whether that variation should be swept out of such models in order to remove such non-volume-related influences on work hours as quarterly changes in the mix of mail or the composition of the work force. He recognizes that quarterly dummy variables have a statistically significant influence on work hours, and would cause omitted variables bias if left out of the model. At the same time, he is concerned about the amount volume variation that has already been removed from the model.

[3096] He notes that using a plant-specific fixed effect variable sweeps out the cross-plant effects of scale, essentially leaving only volume variation over time in the model. He also notes with concern that models such as Bozzo's already rely on a wide variety of dummy variables that "blindly" sweep suspect variability out of the models. He says that in such models, there is not much variability left but short-run "jitter" to model, which he doubts is economically meaningful. Roberts March 2006 at 53-60.

[3097] Witness Roberts theorizes that the time series movements in volume that remain in the Fixed Effect models basically reflect four sources of variation: 1) quarterly variation arising from mailer behavior, 2) technical change as generations of sorting machinery are phased in, 3) short-term change as new equipment is ramped up and old equipment is ramped down, and 4) high-frequency variation arising from day-to-day oscillation of mail volume, staff shortages, equipment breakdown, bad weather, etc.

[3098] Roberts' effectively makes the point that which kind of variation should be swept out of the model, and which kind should be left in, is a judgment call because of the trade-offs involved. Leaving in yearly dummies will de-emphasize the influence of gradual technological change, but will miss the effect of long-term trends in demand.

Leaving in quarterly dummies will de-emphasize the influence of changes in the mix of part- and full-time labor on work hours, but will miss the effect of the seasonal rise and fall of volume resulting from mailer behavior.

[3099] Roberts argues that there should be a debate about the use of quarterly variation in output in the model similar to the extensive debate that has occurred in prior dockets about the use of cross-plant variations in volume to model labor demand variability. Plant-level fixed effect variables and quarterly dummies both pass the test of statistical significance and would induce a degree of omitted variables bias if left out. Unlike Bozzo, who seems to imply that passing a test of statistical significance should end the debate, Roberts has analyzed the trade offs involved in terms of the sources of volume variation that will be emphasized or deemphasized and the non-volume variation that will be emphasized and deemphasized, and has provided theoretical grounds for choosing between them. See discussion in Appendix J at 82-86.

[3100] The Commission's tentative conclusion is that quarterly variation in output should be reflected in models of mail processing labor demand. Roberts has provided a well reasoned theory for believing that the models should reflect this variation, noting that it provides a large share of the total volume variation that is available for modeling, and is a consequence of mailer behavior. Such variation should not be excluded by the use of quarterly dummy variables. The solution to the omitted variables bias that this would entail is to find adequate statistical measures of important non-volume-related seasonal effects on work hours that would allow variables to be constructed that would explicitly control for them. The most prominent candidates would be seasonal changes in the proportion of mail that is difficult to process (e.g., non-machinable letter mail) and changes in the proportion of the workforce that is part- or full-time.

[3101] *Operational analyses of variability.* In support of its variability estimates that are substantially below 100 percent, the Postal Service says that this should be expected because all sorting operations must change sort schemes. Sort schemes, it argues, must be "set up" in order to run, and then be "torn down" in order to allow the next sort scheme to be installed, and the time it takes to set up and tear down a sort scheme is the

same regardless of the volume of mail sorted. It presented the testimony of operations witness McCrery who asserts that most sort schemes are incoming schemes which are unique to the set of destinations that they sort to, and must be run regardless of volume. Therefore, he argues, the set up and tear down time associated with most sort schemes is fixed.

[3102] Witness Elliott, on behalf of a group of Periodicals mailers, proposes that the engineering/operational analysis employed by the Commission to estimate variability be “augmented” by expanding the categories of activity that are presumed to be predominantly fixed to include set up and tear down time. This proposal is based on the belief that set up and tear down time is predominantly fixed, and the belief that it can be quantified by data from the Postal Service’s In Office Cost System. Adding set up and tear down time to those activities that are considered fixed per se, the group argues, implies that mail processing variability ranges from roughly 92 to 94 percent.

[3103] The Commission concludes that witness Elliott’s analysis of the variability of the time that it takes to change schemes on sorting machines is too superficial to reliably establish that it is predominantly fixed. The Commission notes that a certain percentage of schemes are run in parallel and are therefore volume variable. It further notes that an unknown but potentially substantial percentage of non-parallel schemes are logically volume variable, as well. *See Appendix J at 77-81.*

[3104] The Commission also analyzes anecdotal data from End of Run reports provided by the Postal Service that show that intervals between sort schemes for most machines cover a wide range of times, many as short as one minute. *See USPS LR-198.* This suggests that if the time associated with changing sort schemes is fixed, it is much shorter than reflected in the IOCS data, and that if it is variable, it varies over a surprisingly wide range. The Commission further notes that Postal Service witness McCrery has provided reasons for believing that set and tear down time as a general matter is volume variable to an unknown degree. *See Appendix J at 80.*

[3105] The degree to which set up and tear down time is volume variable is far from certain, based on the reasonable inferences available on the record. The record,

therefore, does not support witness Elliott's conclusion that set up and tear down time is predominantly volume variable, and, therefore, does not support his proposed augmented Commission method of estimating mail processing variability.

[3106] It is worth noting that even if the record had supported a finding that set up and tear down time is predominantly fixed, it would not necessarily undermine the econometric estimates of variability above 100 percent presented by witnesses Roberts, Neels, and, (for some operations), Bozzo. The Commission recognizes that true volume variability is unknown for the system as a whole, and for any given sorting operation. Its method of inferring from engineering and operational observation that work hours vary approximately in proportion to volume does not rule out that a reliable econometric estimate could come in higher.⁴¹

[3107] *Commission conclusions.* As in Docket No. R2000-1, the competing mail processing variability models in this docket bracket the estimate of approximately 94 percent that the Commission has traditionally applied to mail processing labor costs. Ninety four percent remains near the center of gravity of the array of statistical and the operational estimates of mail processing variability that have been presented on this and prior records. For this reason, the Commission adheres to its determination that most mail processing labor costs are 100 percent volume variable.

[3108] For more than a decade, the Commission has expressed concern that the quality of the MODS data upon which mail processing variability models depend is too poor to support valid econometric models. Over that time, the quality of that data has not improved in any discernable respect. This record has clarified the theoretical requirements of valid mail processing models. At the same time it illustrates that

⁴¹ For example, a recent empirical study in Great Britain by the LECG Consulting Group concluded that marginal costs in much of its mail processing network were greater than 100 percent. See LECG. Future Efficient Costs of Royal Mail's Regulated Activities, 2 August, 2005 at 365; [www.psc.gov.uk/postcom/live/policy-and-consultations/consultations/price-contrl/LECG efficiency review report excised. Pdf](http://www.psc.gov.uk/postcom/live/policy-and-consultations/consultations/price-contrl/LECG%20efficiency%20review%20report%20excised.Pdf). The conclusions of this study is of particular interest because it consciously avoids the use of the relevant self-reported data that was available to it on the ground that it was unreliable. In addition, it uses analytical methods that do not involve a need to resort to the use of instrumental variables of questionable validity.

resourceful data manipulation techniques have not been sufficient to overcome the obstacle to successful modeling that the error-ridden MODS data presents. The Postal Service should understand that unless the quality of the MODS data improves, or alternative data is developed, models that rely on such data have little prospect of being accepted by the Commission.

B. City Carrier Street Time Attribution

[3109] *Postal Service model.* In this docket, the Postal Service does not submit a new carrier delivery model. Rather, it relies upon the model and associated variabilities accepted by the Commission in Docket No R2005-1, to attribute accrued city carrier street time costs to mail shapes.⁴² These are subsequently distributed to mail services by class and subclass, which in turn are utilized by witness Kelley as part of his development of unit delivery costs (USPS-LR-L-67).

[3110] *OCA's 2002 CCSTS recommended model.* OCA witness J. Edward Smith sponsors new city carrier testimony that examines 12 full quadratic models and 12 restricted models of delivery costs he developed using the 2002 CCSTS data set. He adopts the model and variabilities witness Bradley proposed for parcels and accountables in Docket No. R2005-1. His recommended regular delivery model uses a full quadratic specification, similar to the one originally submitted by witness Bradley in Docket No. R2005-1, with two differences: it does not include a density variable; and it combines cased letters and flats into a cased variable, while limiting letters to those that are DPSed.

[3111] Several of the variabilities that result from this model differ significantly from those produced by witness Bradley's Docket No. R2005-1 restricted quadratic model as shown in the following table.

⁴² Appendix K discusses the Postal Service's response to Presiding Officer Information Request Nos. 4 and 16, which presented data similar to that collected in the 2002 City Carrier Street Time Survey, and performed various regression analyses on this data.

Table III-3
Comparison of OCA's and USPS's Mail Shape Variabilities

	OCA	USPS
Letters /1	16.8%	22.3%
Flats /2	16.7%	7.1%
Sequenced Mail	1.5%	1.3%
Small Parcels	0.5%	0.2%
Collection Mail	6.6%	8.9%
/1 DPSed only for OCA, /2 Cased letters + flats for OCA. Sources: OCA-T-3 at 10; Docket No. R2005-1, USPS-T-14 at 39.		

[3112] Specifically, the variability of flats significantly increases and that of letters significantly decreases compared to the Docket No. R2005-1 model.

[3113] *Explanation for excluding the density variable.* Witness Smith first argues that the density variable should be excluded from a model of carrier delivery because density is determined as part of the process by which management minimizes costs. Witness Smith states that “[d]ensity is an output of [this] process.” OCA-T-3 at 6. On brief, OCA explains that “...the density variable...is subsumed in some type of maximization or adjustment process for efficient City Carrier delivery....”⁴³ OCA Brief at 48.

[3114] OCA further claims that witness Bradley was unable to demonstrate the relevance of density to delivery time during his oral cross-examination. During

⁴³ One might characterize OCA's argument as stating that retaining density is akin to introducing simultaneity bias into the cost estimation. This would occur because one has not simultaneously accounted for the effect of prior management decisions that determined density by establishing ZIP Code areas that minimize costs. When an explanatory or independent variable is determined simultaneously with the dependent variable, simultaneity bias may arise. See Wooldridge, J., *Introductory Econometrics*, 3rd ed. at 557. The Commission presumes that OCA calls for the exclusion or “subsumption” of density because it believes density is completely determined by the variables remaining in its model, and no others. Carrying out this logic, there could be two equations: (1) cost = mail volume + delivery points + density, and (2) density = cost – mail volume – delivery points, where mail volume and delivery points operate as constraints on the minimization of cost. Substituting density from equation (2) back into equation (1) would yield a non-useful solution of costs = costs or 0 = 0. Under this logic, density would need to be excluded as a factor determining the volume of delivery costs.

cross-examination, OCA developed a hypothetical example in which the same density could be obtained for two routes that differed in length, and therefore delivery time, by altering the number of delivery points at each node of the route. *Id.* at 49. If the same density can co-exist with routes of different lengths and different delivery times, then density could not be a variable that explained the difference in delivery times for the two routes.

[3115] OCA also faults witness Bradley's citation of one article.⁴⁴ Tr. 34/11604. OCA argues that the article is critical, not supportive, of the use of the density variable. OCA Brief at 50. Finally, OCA argues that witness Bradley did not compute density correctly, because density changes from day to day in the CCSTS data set due to the failure of carriers to report their deliveries nearly every day of the study. OCA contends that if density is included in a model of carrier delivery, it should be constant from day to day, so as to operate as a situational variable that consistently measures congestion in the ZIP Code. *Id.* at 51. *See also* OCA-T-3 at 8.

[3116] *OCA's preference for a full quadratic model.* OCA next argues that a full quadratic model, which includes the interaction between different mail shapes, is operationally more accurate than a restricted model. For example, OCA states that

“[i]t appears that there is interaction in handling procedures by city carriers in delivering the various types of mail....The carrier's actions in the delivery of DPS letters and cased flats and letters also appear to be related to the handling of sequenced mail. Accordingly, it appears that interaction terms are drivers of carrier time and should be retained....”

OCA Brief at 52.

[3117] *Arguments against OCA's new mail shapes.* Witness Bradley argues that while he was not opposed to exploring an approach which limited letters to those that were DPSed, and combined cased letters and flats, he believed that during the time the

⁴⁴ See Roy, B. “Technico - Economic Analysis of the Costs of Outside Work in Postal Delivery” in *Emerging Competition in Postal and Delivery Services*, Crew, M. and Kleindorfer, P., eds., Kluwer 1999.

2002 CCSTS data were collected "...DPS was not as widespread as it is now, and there was still some casing of letters and flats." USPS-RT-4 at 19. He also criticizes witness Smith for failing to explain how the costs of the mixed letters and flats variable would be distributed to classes and subclasses. Witness Smith does not provide a distribution key for this new variable. *Id.* Witness Crowder believes that combining cased letters and flats is a contribution, and that it must be explored further in the future. MPA et al.-RT-1 at 10.

[3118] *Arguments In favor of retaining witness Bradley's density variable.* Several parties support the use of a density variable and reject OCA's arguments for excluding the density variable from a model explaining city carrier delivery time. Witness Bradley cites five other studies that supported the use of a density variable in modeling city carrier delivery. USPS-RT-4 at 2-5. Furthermore, he argues that ZIP Code density is not a function of the number of routes that management establishes to minimize costs. Rather, density is a function of the number of delivery points and the area served, and would be the same regardless of the number of routes. *Id.* at 7. Finally, he argues that dropping a significant variable, such as density, would bias witness Smith's econometric estimates. *Id.* at 17.

[3119] Witness Bradley criticizes witness Smith's definition of density as housing units per square mile. Witness Bradley also argues that witness Smith's density variable does not measure postal density and so is incorrect. Furthermore, the 2002 CCSTS data would have allowed witness Smith to calculate a constant postal density, but he did not do so. *Id.* He also argues that since he did not have the square miles served by the included and excluded routes, he attempted to "...account for the variation in the number of routes included," by including SAS code that weighted square miles "...by the number of routes included in that ZIP Code – day observation." Tr. 13/3788-89.

[3120] Witness Bradley also challenges OCA's criticism that because his measure of density was not constant from day to day it was incorrectly measured. He claims density is not constant from day to day even though ZIP Code square miles remain constant, because as the number of routes reporting delivery data vary from day to day,

delivery points do not stay constant. When all routes in a ZIP Code report, reported density is equal to the density actually served by carriers on that day. However, since some routes go unreported, the area actually served by carriers reporting on that day will be less than ZIP Code square miles. Thus, calculating density as the ratio of reported delivery points to ZIP Code square miles will not properly measure density unless some adjustment is made for the number of non-reporting routes. Tr. 34/11602.

[3121] Witness Bradley states that he did adjust his measure of ZIP-day density by weighting it by the number of routes reporting each day. *Id.* He also argues that weighting density by the number of routes reporting scales the density variable, and while this would affect the estimated coefficient of the density variable, it would not affect estimated coefficients of mail shapes, which are the variables of interest. *Id.* at 11603.

[3122] Witness Crowder argues that density is a key explanatory variable in a city carrier delivery model, and that excluding density "...ignores operational realities." MPA et al.-RT-1 at 8. She argues that when postal managers minimize costs, they respond to three workload variables: mail volumes; possible delivery points; and square miles in a delivery unit's service territory. Witness Bradley's density variable is "...just a combination of two of the primary workload variables: ZIP-code possible deliveries divided by ZIP-code square miles." *Id.* at 9.

[3123] Two briefs echo the arguments of witnesses Bradley and Crowder. MOAA Brief at 35, MPA et al. Brief at 17. MPA et al. criticize OCA's argument that density does not matter by showing a strict mathematical relation between density and route miles, namely: "as density decreases...total route mileage increases." MPA et al. Reply Brief at 16. Thus, an increase in route miles would reduce density, contrary to the example provided by OCA during oral cross-examination of witness Bradley.

[3124] MPA et al. also provide an example designed to illustrate witness Bradley's point that weighting density by the number of routes does not affect coefficients of interest. The day to day percentage change in the density measure is the same whether one calculates density by weighting it by the number of reporting routes, or calculates it as delivery points per square mile served by carriers reporting on any given day. Thus,

even though the latter measure, delivery points as a percent of square miles actually served by carriers on any given day is unknown, a route-weighted density measure, which is known, produces unbiased regression estimates, since “...for modeling purposes, relative variation is the only thing that matters.” *Id.* at 20.

[3125] *Criticism of witness Smith’s alleged ad-hoc and incomplete modeling technique.* A series of arguments against witness Smith’s CCSTS models may be considered variants of the criticism that he engaged in *ad hoc* or incomplete estimation.⁴⁵ Thus, for example, witness Bradley shows that witness Smith’s models vary depending on whether a density variable is included, whether letters are defined as DPSed, whether a collection variable is included and whether the parcel and accountable variables are combined. USPS-RT-4 at 15. Witness Crowder agrees that witness Smith’s choice of models were not guided by economic principles, but relies instead on pre-conceived notions of how well the models fit the data.⁴⁶ MPA et al.-RT-1 at 19.

[3126] *Commission’s analysis.* The Commission agrees with OCA that the use of a full quadratic equation is desirable because it is more firmly based in the operational reality that different mail shapes are delivered in tandem. The interaction variables among mail shapes capture this operational reality and strong efforts should be made to retain them. While a full quadratic model may cause individual variable coefficient estimates to appear to be not significantly different from zero, the important issue is whether the variabilities associated with each mail shape are significantly different than zero.

[3127] In the full quadratic model first presented by witness Bradley in Docket No. R2005-1, the variability of each shape is computed through a combination of the coefficients of all related shapes (i.e., the mail shape, its square, and the relevant interaction terms for that shape), each evaluated at appropriate mean volumes, and the

⁴⁵ See *e.g.*, MOAA Brief at 34, 35, MPA et al. Brief at 18, 20, Postal Service Reply Brief at 121, and MPA et al. Reply Brief at 10. See also USPS-RT-4 at 14, and MPA et al.-RT-1 at 6.

⁴⁶ See, Postal Service Brief at 121, MOAA Brief at 34, MPA et al. Brief at 18, 20. See also Postal Service Reply Brief at 121; MPA et al. Reply Brief at 10, 22.

value for delivery time at the mean values for volumes, delivery points, and density. Docket No. R2005-1, USPS-T-14 at 39. Consequently, a test of the joint significance of the vector of values associated with the terms making up the variability of each mail shape would determine whether the variability of each mail shape was significantly different from zero.⁴⁷

[3128] The Commission tested the number of shape variabilities that are significant for witness Smith's CC5A model (new mail shape, and no density variable); CC2A (new density definition and standard mail shapes); and CC1B (witness Bradley's restricted Docket No. R2005-1 model).⁴⁸ CC5A and CC2A are full quadratic models, while CC1B is the restricted model witness Bradley proposed in order to reduce the multi-collinearity exhibited in his full quadratic model. The following table summarizes, by model, which shape variables have variabilities that are significantly different from zero at a 95 percent level of confidence or greater. The table shows that CC5A and CC2A each have four out of five shape variables with significant variabilities (although CC2A does have a negative variability), while the restricted quadratic has three out of five shape variables with significant variabilities. Thus, eliminating all interaction terms does not necessarily improve the number of shape variables with significant variabilities. This practice should not be undertaken in the future without investigating whether their elimination actually improves the number of mail shapes with significant variability estimates.

[3129] In the future, analysts should seriously consider combining mail shapes if doing so would be both operationally accurate and reduce the number of main variables of interest. If so, this procedure would reduce the number of interaction terms, and possibly alleviate the reduced efficiency associated with multi-collinearity. In this regard, the Commission believes that even the 2002 CCSTS data set could have been used to create a cased mail variable and a DPSed letter variable. The Commission disagrees

⁴⁷ See Johnston, J. and DiNardo, J., *Econometric Methods*, 4th ed. at 91.

⁴⁸ See PRC-LR-5\Carrier\Variability Significance Test\CC5 CC2 Bradley Mixed Final!.sas which implements this significance test, using heteroskedastic-consistent standard errors. See also PRC-LR-5\Estimate Statement Explanation.pdf.

Table III-4
Significance of Variability by Shape

		CC5A**		CC2A		CC1B
Mail Shape	Coefficient	T-Value	Coefficient	T-Value	Coefficient	T-Value
Letters	.1683	6.43*	.2565	7.31*	.2227	6.39*
Flats**	.1670	7.44*	.1385	5.96*	.0712	2.90*
Sequenced	.0149	2.37*	.0153	2.37*	.0129	1.73
Small Parcels	.0052	0.26	-.0223	-1.14	.0158	0.82
Collection	.0659	6.04*	.0395	3.74*	.0881	7.35*

* Significantly different than zero at a 95 percent level of confidence.
** CC5A combines cased letters and flats, while letters are DPSed.

with witness Bradley that the process of delivery point sequencing had not progressed far enough in 2002 to warrant the use of new mail shapes with the 2002 CCSTS data set. The percent of letters DPSed according to the 2002 CCSTS was 66 percent, while it was 73 percent in the 2004 CCSTS submission.⁴⁹ The relatively modest degree to which delivery point sequencing increased in two years does not justify excluding a model with a DPSed-only letter shape that uses the 2002 CCSTS data set.

[3130] The defenses made for the validity of estimates in the presence of day to day variation in ZIP Code density proffered by witness Bradley and MPA et al., discussed above, are off the mark for several reasons. Witness Bradley claims he adjusted density for the number of reporting routes through the use of special SAS code. However, when the Commission ran witness Bradley's 2002 CCSTS program with and without this SAS code it found no difference between the two measures of density.⁵⁰ Witness Bradley's density variable, supposedly weighted by number of routes, is no different than the sum of delivery points in a given ZIP Code reporting on a given day, divided by an unchanging value of square miles per ZIP Code.

⁴⁹ See PRC-LR-5\2002 2004 DPS Data.xls.

⁵⁰ PRC LR-5\Carrier\Nrts Test\NRTS.sas.

[3131] The Commission also disagrees with the conclusions drawn in the Reply Brief of MPA et al., regarding the equality of day to day percentage differences in route-weighted density for a known ZIP Code area, and densities for areas that are unknown because routes may not report data on a given day. MPA et al. Reply Brief at 20. First, as explained above, witness Bradley does not perform a route-weighted density calculation. Second, the example is limited to a variation within a single ZIP Code during two days under the very unique assumptions that one route is being dropped and the area served by that route equals one square mile. In fact, the formula showing the across-day equality of the percentage difference of route-weighted densities and the densities served by routes, rests on a strict equality between the ratio of number of routes reporting on “day 1” to “day 2” and the ratio of route-area served in “day 1” to “day 2.”⁵¹ Finally, the Commission not only agrees with witness Smith that witness Bradley’s density variable is mis-measured due to day to day variations in reporting, but also that all variables of interest are mis-measured for the same reason. This mis-measurement would cause ordinary least squares estimates to be biased and inconsistent.⁵²

[3132] The Commission strongly urges the Postal Service to improve its city carrier data collection procedures associated with any carrier delivery studies submitted in the future. However, witness Smith’s density variable excludes delivery to commercial establishments. For this reason as well, it is measured incorrectly, and the estimates from his regression analyses that use this modified density variable are biased and inconsistent.

⁵¹ See PRC-LR-5\Density Explanation.doc for a mathematical proof of this conclusion.

⁵² The same conclusion applies with regard to witness Smith’s estimates. He too relies upon the 2002 CCSTS, so measures for variables other than his modified density variable are also mis-measured due to route attrition. See Johnston, J, and DiNardo, J., *Econometric Methods*, 4th ed., at 154. See also Kennedy, P., *A Guide to Econometrics*, 5th ed. at 169.

[3133] The Commission agrees with parties who assert that density is an important determinant of delivery time, and agrees that witness Smith should have included one.⁵³ The Commission confirmed the need for a density variable by testing whether witness Smith's density variables, including all density interaction terms, were jointly significantly different than zero. This test was performed on what witness Smith termed model CC2A: Recommended Case, Density Modified. The test shows that these density variables were jointly significantly different from zero at or above a 95 percent level of confidence.⁵⁴

[3134] The Commission agrees with those parties who criticize witness Smith for what they describe as employing alternate models uninformed by economic principles to achieve a desired result. Thus, for example, his recommended model eliminates the density variable, yet he arrives at his decision to exclude this variable on the basis of a completely different, although unspecified, model of delivery time. OCA-T-3 at 6.

[3135] Thus, the Commission does not accept witness Smith's recommended CC5A model because he did not develop a distribution key appropriate for the new mail shapes he employs; did not develop unit delivery costs consistent with those new mail shapes; and excluded density, a relevant variable for the explanation of carrier delivery time.⁵⁵ Had the data submitted by the Postal Service in Response to Presiding Officer's Information Request No. 4 been provided earlier in the rate case, it is possible that at least some of the issues for which witness Smith was criticized (*e.g.*, lack of a distribution key appropriate for the new mail shapes) might have been allayed. For these reasons, even though the Commission chooses to retain the current carrier delivery model and its

⁵³ See *e.g.*, Postal Service Brief at 122, MOAA Brief at 34, 35, and MPA et al. Brief at 17; Postal Service Reply Brief at 120; MPA et al. Reply Brief at 12-19. See also USPS-RT-4 at 1-9, and MPA et al.-RT-1 at 8, 9.

⁵⁴ See PRC-LR-5\Carrier\Density Significance Test\Smith Density Significant.sas.

⁵⁵ As discussed above, witness Smith possibly implies that the simultaneous determination of delivery cost and density may require an alternate delivery model, but he does not provide one.

associated variabilities, it expects to see the issues raised by OCA more fully litigated in the next rate case.

[3136] *OCA's 2002-2005 DOIS recommended model.* OCA witness Smith also presents testimony that examines 6 full quadratic models and 6 restricted models using 32 weeks of data, spanning 16 quarters, and 125 ZIP Codes, obtained from the Delivery Operations Information System (DOIS). See OCA-T-3. DOIS provides daily operational carrier route data for in-office time, delivery time, and delivery volumes.

[3137] Postal Service managers use DOIS to pivot routes with the intention of minimizing delivery costs. Collection mail or accountable volumes were not available from DOIS. Parcels are defined by size, not by whether they fit into a mailbox, so there is no small parcel variable in DOIS. DOIS provides data on the volume of Priority Mail, and witness Smith includes those volumes in his parcel variable. Tr. 22/8085.

[3138] Witness Smith recommends a full quadratic model with no density variable, similar to his recommended 2002 CCSTS model. OCA-T-3 at 19. However, when using the DOIS data, he does not combine mail shapes, and he substitutes type-of-route variables, such as curblines and neighborhood delivery collection box unit (NDCBU), for delivery points. *Id.* at 17. Table III-5 below, compares the variabilities of witness Smith's recommended DOIS model with those obtained from the current model.

**Table III-5
Comparison Of OCA's DOIS Model And Currently Adopted Model**

Mail Shape	OCA	Current
Letters	19.4%	22.27%
Flats	12.7%	7.12%
Sequenced	0.2%	1.29%
Small Parcels		1.58%
Collection		8.81%
Accountables	100%	25.0%
Parcels	3.6%	28.5%
Source: OCA-T-3 at 17, Model ND6, Full Quadratic.		

[3139] Witness Smith justifies excluding collection mail from his DOIS model, arguing that with the advent of carrier pickup “[t]he nature of collection volume has changed significantly.... Accordingly, the collection volume variability developed by witness Bradley appears now to be irrelevant.” *Id.* at 21-22. Witness Smith also argues that it is possible to use an unspecified ratio to determine volumes of collection mail. Tr. 22/8082.

[3140] Witness Smith also justifies his inability to econometrically estimate a variability for accountables by arguing that “...the extra time for accountables is an incremental cost and is therefore 100 percent attributable,” and he states that USPS-LR-L-1 identifies 5.1 percent of regular delivery time associated with parcels and accountables. *Id.* at 8122. In its brief, OCA proposes to identify the mean delivery time and mean volume of large parcels in the CCSTS. These values would then be applied to the DOIS data set to remove large parcel volumes and times.⁵⁶ OCA Brief at 58.

[3141] *OCA’s conclusions regarding DOIS models and DOIS data.* Witness Smith concludes that he has performed defensible regressions using DOIS data, for he states that “[m]y recommended equation is Equation ND6, which I believe is the preferable equation for addressing City Carrier costs.” OCA-T-3 at 23. Despite the lack of several variables, DOIS has the advantage of being a very large, routinely produced, database of carrier delivery times and certain mail shape volumes. *Id.* at 23-24. It is well known that a possible solution to multi-collinearity is an increase in sample size. Witness Smith finds that multi-collinearity is less of a concern with the DOIS data provided by the Postal Service. *Id.* Despite the presence of autocorrelated errors in his DOIS regressions, witness Smith concludes that provision of DOIS data on an ongoing basis could improve the modeling of city carrier delivery. *Id.* at 22, 24. Consequently, he proposes that the Commission ask the Postal Service to provide DOIS data for the ZIP Codes and time

⁵⁶ OCA does not explain further, but the Commission presumes that one would then be left with an approximation of the volumes of small parcels, and after removing accountables time, an approximation of the appropriate amount of regular delivery time would remain. This procedure could allow an estimate of the variability of small parcels to be performed.

periods they have already provided for two weeks over 16 quarters, on a daily basis, updated annually. He also urges the Commission to recommend that the Postal Service provide quarterly summations of daily DOIS data on an ongoing basis. Witness Smith contends that these requests would allow for easily updated data, which would "...set a basis for an improved understanding of City Carrier costs." *Id.* at 25.

[3142] *Criticisms of the unknown quality of DOIS data.* Several parties criticized OCA's modeling efforts using DOIS data because the DOIS data are of unknown quality.⁵⁷ The concerns raised include, but are not limited to, the following major points: setting missing values to zero, potentially creating biased and inconsistent estimates (USPS-RT-4 at 16), uncertainty regarding the quality of the data or the quality of controls the Postal Service applied to the collection of DOIS data (MPA et al.-RT-1 at 15), the deletion of 33 percent of observations in order to perform a regression (USPS-RT-4 at 15), and the failure to correct for autocorrelated errors. MPA et al. Brief at 19.

[3143] *Criticisms of omitting or incorrectly measuring collection, parcels, and accountables.* Witnesses Bradley and Crowder note that omitting or incorrectly measuring these variables would bias the DOIS-based estimates of witness Smith's remaining variables. USPS-RT-4 at 20, and MPA et al.-RT-1 at 15. Moreover, because these variables are missing, witness Smith is unable to develop either cost pools or distribution keys associated with them. USPS-RT-4 at 25, and MPA et al.-RT-1 at 16. Witness Bradley also defends the current relevance of the collection variable by noting that carrier pickup volumes are small, and "...collection activity is still dominated by collection of letters and flats." USPS-RT-4 at 26. Finally, the Postal Service notes that it may be impossible to separate accountables from parcels in order to develop a distinct cost pool for accountables, as proposed by witness Smith. This is so, the Postal Service argues, because a piece often may be both a parcel and an accountable, as these items may be delivered together, and thus accountables will not always appear as a fully

⁵⁷ See Postal Service Brief at 22, MOAA Brief at 36, and MPA et al. Brief at 22. See also Postal Service Reply Brief at 124.

separate item in the CCSTS. Postal Service Reply Brief at 23. MPA et al. also question the use of times and volumes contained in one data set, the CCSTS, to form cost pools and volumes for another data set, namely DOIS. MPA et al. Reply Brief at 24.

[3144] *Commission analysis.* The Commission finds the arguments against using OCA's DOIS-based carrier models convincing. Still, the Commission agrees with OCA that the volume of DOIS data may allow the reduction of multi-collinearity,⁵⁸ and this, along with additional variables such as route type and route miles, could improve future carrier delivery studies. The Commission suggests that interested parties continue to examine DOIS data, continue to learn about existing quality controls, and continue to examine the feasibility of adding the needed controls, explanatory material, and additional variables, so that if DOIS data are utilized in future studies, either those designed for attribution purposes, or those designed to assist the Commission fulfill its new regulatory responsibilities, they will be reliable.

C. Window Service Cost Attribution

1. Introduction

[3145] The Postal Service presents a new window service study which consists of matching operational Point-Of-Service ONE (POS ONE) volume data to time data collected by special data collectors for econometric estimation of window service variabilities. OCA witness Smith (OCA-T-2) submitted testimony regarding this study. Postal Service witnesses Bradley (USPS-RT-4) and Kelley (USPS-RT-6) submitted rebuttal testimony.

[3146] The established transaction variability study was submitted by witness Brehm in Docket No. R97-1. It defined the variability of window service transactions as

⁵⁸ It might be that a route-based, rather than ZIP-Code based, model would be able to more fully exploit the potential of DOIS observations to significantly reduce multi-collinearity.

the marginal increase in transaction time for a window service item, which he defined as the weighted average increase in single service transactions and multiple service transactions, divided by the estimated time for the single window service transaction in question. Docket No. R97-1, USPS-T-21 at 20-21.

[3147] This formula does not conform to the Commission's definition of variability. In the case of window service transaction, witness Bradley (USPS-T-17) states, variability would express the percentage change in time to purchase a window service due to a 1 percent change in the volume of that window service. USPS-T-17 at 10. One purpose of witness Bradley's testimony is to produce a model of window service variability that relies on a computational formula in keeping with the Commission's definition of variability. *Id.* at 1. In addition, the new study utilizes data from the POS ONE system and allows separate variability estimates of "weigh and rate" services for First-Class Mail, Priority Mail, and Parcel Post, where the previous study had a single, undifferentiated, "weigh and rate" variability estimate. *Id.* at 6.

2. Postal Service Window Service Study

[3148] *Sample selection of window service special study.* Witness Nieto (USPS-T-24) develops a sample design, and oversees the collection and matching of window service time and volume data to develop a window service database that witness Bradley uses in his econometric model to calculate window service transaction variabilities. The sample universe consists of more than 15,000 post offices that utilize the POS ONE system. USPS-LR-L-78 at 5. POS ONE sites were stratified according to nine geographic areas; then two large and one small post office were randomly selected from each geographic area, yielding a sample of 27 post offices. *Id.* at 6. The sample design essentially reproduces the one performed by witness Brehm in Docket No. R97-1. Tr. 5/712-15.

[3149] *Criticisms of the Postal Service's window service sample selection.* OCA witness Smith criticizes the sample selection performed by witness Nieto, arguing that

she fails to utilize sampling theory to determine appropriate sample size and the number of sites allocated to different geographic and size strata. OCA-T-2 at 5. He presents evidence that because of this failure, the sample size is too small, is not representative, and is therefore unsuitable for estimating the volume variabilities of window services. *Id.* at 14-16.

[3150] *Defense of witness Nieto's sample methodology.* Witness Kelley provides rebuttal testimony to defend the validity of the sampling methodology utilized by witness Nieto. See USPS-RT-6. He argues that witness Nieto did employ commonly utilized statistical practices such as analyzing the sample frame; determining the coverage of the universe to be sampled; employing a stratified sample; and randomly selecting post offices from each stratum. *Id.* at 4. Witness Kelley disputes witness Smith's claim that the sample size is too small, arguing that witness Smith incorrectly employs a standard statistical formula to compute sample size. *Id.* at 13. Using an alternate formula, witness Kelley shows that a much smaller sample size for one window service (passports) would be needed than was claimed by witness Smith. *Id.* at 14. Moreover, he argues that it would be impossible to develop a sample that produces the correct sample size for each transaction "in which the transactions to be observed are not known in advance. . . ." *Id.* at 15.

[3151] Finally, witness Kelley argues that since the study and the resulting database were not designed to produce point estimates of the mean of each type of transaction, but merely to "...provide the data needed to update the econometric model...constructing (such mean level transaction estimates) ...would not have been useful." *Id.* at 4. He argues that it was sufficient to reproduce the basic coverage, stratification, and magnitude of the previously performed window service study. *Id.* at 16. OCA responds that although witness Kelley's sample size formula would require a reduced sample size for a single service, the sample size is still too small for passports and many other window services for a proper statistical analysis. OCA Brief at 78-81.

[3152] *Commission analysis.* The Commission recognizes that developing and implementing special data collections can be expensive, yet reliable data are an

essential component of reliable variability estimates. The Postal Service should have utilized standard statistical techniques to determine an appropriate sample size. The Commission agrees with witness Kelley that it would have been sufficient to identify several key window service transactions and then compute a sample size large enough so that at least key transactions would probably yield the desired number of observations within an acceptable margin of error. This procedure balances the trade offs between the preferred margin of error and the cost of collecting data from an extensive sample. USPS-RT-6 at 14. Unfortunately, the Postal Service did not follow this procedure.

[3153] The Commission agrees with OCA that a measure of the statistical properties of the data set (such as the coefficients of variation associated with key variables) is needed as part of the evaluation of the reliability of the econometric estimates of window service variabilities estimated from the collected data set. The Commission urges the Postal Service to improve its sampling procedures in the future.

[3154] *Window service data collection and database development.* The study was conducted between April 18 and May 7, 2005. Data were collected for two days at each of the 27 selected post offices. USPS-LR-L-78 at 7. Special study personnel recorded the time at which various events occurred, such as: (1) a customer beginning to walk to the window; (2) a customer arriving at the window; or (3) a clerk finishing the transaction. The study defined the time difference between a – b as “walk-time,” and between b – c as “transaction time.” Study personnel also recorded the time at which a customer would leave the window to obtain forms, and the time at which the customer returned to the window with completed forms. The difference between these two times was considered as “nested transaction time.” *Id.*, Attachment A, at 5. Except for non-POS ONE transactions such as “hold-out,” Regular window service clerks also recorded most, but not all, services in the POS ONE system, where they were electronically entered into the POS ONE database, and received a time of sale and type of service record.

[3155] Faulty event codes were identified and deleted if they could not be corrected. Because non-transaction events, such as timekeeper breaks, were recorded by study personnel, these event times did not identically match time entries associated

with sales recorded by the POS ONE system. Consequently, time data were manually matched to transaction data where possible. Where matching was not possible, transactions were deleted. The final data set consisted of 7,915 transactions.

[3156] OCA notes that special data collectors had difficulty tracking nested transactions: 57 out of 190 nested transactions were dropped due to data collection problems, constituting approximately 30 percent of nested transactions. OCA-T-2 at 10. In addition, witness Smith notes that 1,535 out of 9,459 observations, over 16 percent of all eligible data, were dropped because it was not possible to accurately match the time data collected by special study personnel with transaction data obtained from the POS ONE system. USPS-LR-L-78 at 13-14.

[3157] The Postal Service justifies dropping this amount of data because the remaining data set was a bit larger than the previous window service study data set. Tr. 5/722. Witness Smith counters that even if the new database may be better than the previous one, witness Nieto has not established the validity of the new data set for use in econometric estimation. OCA-T-2 at 16.

[3158] *Defense of witness Nieto's data collection and database development procedures.* Witness Kelley responds to criticism by OCA that a large percent of eligible observations were deleted by stating that precisely because time data that could not be matched with transaction data were deleted, the remaining data set contained highly accurate and verified data. USPS-RT-6 at 11.

[3159] *Commission analysis.* The Commission accepts the sampled data for the purpose of estimating witness Bradley's window service model. The Commission finds that although matched data may be accurate, this fact does not address the nature of the dropped observations. If the dropped data were not random, their absence would bias witness Bradley's econometric results. The Postal Service does not report having made an attempt to determine whether dropped transactions were randomly distributed, yet the type of each dropped transaction should have been available to the Postal Service. In the future, the Postal Service should take the time to consider, analyze, and present the potential impacts of its data collection and database weaknesses. While the sampling

and data collection procedures should be improved in the future, the Commission accepts the sampled data because it allows for a more detailed econometric estimation of window service variabilities estimated in witness Bradley's improved window service model.

[3160] *Witness Bradley's formula to calculate window service variability.* Witness Bradley develops a window service variability formula by treating the cost-generating process as a linear combination of the time associated with processing a window service transaction and the non-processing time associated with that transaction. He chose a linear form because the processing part of a transaction (as opposed to non-processing part, where one may be conversing with a clerk) is such that processing one piece of mail takes one-half the time as does two pieces, stating that: "[i]f I do three [pieces] of that activity it takes three times as much [time as] if I did one of those activities." Tr. 5/849. He also stated that "[l]inearity implies that the product-specific cost pools are additively separable and the total window service transaction time can thus be exactly decomposed." USPS-T-17 at 16. Finally, he argues that additive separability is implicitly assumed by IOCS which establishes the costs of individual window services by identifying the product specific times uniquely associated with those activities. Tr. 5/850. Witness Bradley derives a formula that meets the Commission's definition of variability using his assumption that the cost generating process for different services can be distinctly decomposed into the separately identifiable costs of each service.⁵⁹ USPS-T-17 at 17-18.

[3161] *OCA's criticism of witness Bradley's window service variability formula.* OCA was critical of the linear model utilized by witness Bradley because it always results in 100 percent volume variabilities for products such as Certified Mail and Registered Mail that are only purchased in conjunction with the mailing of another service such as Priority Mail. OCA-T-2 at 25. This occurs because such transactions do not have what witness Bradley refers to as "core transaction time;" they only have time associated with processing the transaction itself. Since the model is linear with no intercept, this means that additional pieces take the same amount of time, resulting in variabilities of 100

percent for these services. Tr. 5/853. OCA believes a non-linear model, such as a quadratic model, should be used.⁶⁰ OCA-T-2 at 25.

[3162] *Postal Service's defense of witness Bradley's variability formula.* The Postal Service does not directly rebut the validity of using a non-linear model. Nor does it rebut the implied assertion that its model is inappropriate because it causes services such as Certified Mail to obtain variabilities of 100 percent. Rather, it refers to witness Bradley's statements that "...a linear functional form is appropriate here." Postal Service Reply Brief at 116.

[3163] *Commission analysis.* The Commission is not convinced that services such as Registered Mail do not have core transaction time. When a person wants to mail a package and obtain some proof of mailing, proof of delivery, or some reimbursement when a delivery is lost, he or she may be uncertain which combination of these services may serve them best, and may need to discuss the various possibilities with the clerk. This is not solely core time associated with the package, for it involves core time

⁵⁹ The final formula used to calculate the variability of a window service cost pool is:

$$\epsilon_k = \frac{\partial Y_k \cdot X_k}{\partial X_k \cdot Y_k} = \frac{(\beta_0 \rho_k + \beta_k) \bar{X}_k}{(\rho_k + \delta_k) \beta_0 + \beta_k \bar{X}_k}, \text{ where}$$

ϵ_k = the variability of window service k ,

β_0 = the non-processing time associated with the transaction,

ρ_k = single quantity purchases of service k where service k is the only item in the transaction, as a share of all window service transactions,

β_k = the change in time due to transaction k ,

\bar{X}_k = the mean volume of window service k , and

δ_k = multiple quantity purchases of service k where service k is the only item in the transaction, as a share of all window service transactions.

With this formula, the only place transactions that are not "single item" transactions are considered is in the estimation of each β_k in the regression equation. Thus, for a service such as Certified Mail,

$\rho_k = 0$, and $\delta_k = 0$, so $\epsilon_k = 1$

discussing some sort of guarantee, namely its certification, registration, return receipt, or insurance. The Commission believes a model that accounts for the non-additive separability of such products ought to be considered, even if a linear model is easier to develop and collect data for its econometric estimation.

[3164] The Commission can not determine, on this record, whether it is feasible to collect the data necessary to estimate variabilities for a non-linear model. For now, it accepts witness Bradley's use of a linear model. As the Postal Service evaluates how to improve its understanding of window service costs, it should strive to also measure the quality of window service. This issue will be a new area for Postal Service and Commission interaction under the Postal Accountability and Enhancement Act (PAEA).

[3165] *Witness Bradley's econometric estimates of window service variabilities.* In witness Bradley's analysis, transaction time was the dependent variable, and transaction volumes of various window services were the explanatory variables. The 27 post office sites were considered location dummy variables, and methods of payment and the number of different services or "items" present in each transaction were also included as control variables.

[3166] Witness Bradley deleted nine observations he considered obvious outliers. USPS-T-17 at 23-24. He also deleted observations with large negative regression residuals. *Id.* at 25, 31. The regression produced heteroskedastic standard errors, which were corrected by applying a heteroskedastic-consistent covariance matrix. *Id.* at 26. Witness Bradley's recommended model appears free of the problems associated with multi-collinearity, as 23 of 25 variables are significant at a level of confidence exceeding 95 percent.⁶¹

[3167] *OCA's econometric estimates of window service variabilities.* OCA witness Smith recommends a linear model similar to that of witness Bradley with the exception that he includes walk time in his measure of transaction time. Walk time is the time from

⁶⁰ Presumably, this option is proposed so that the services discussed immediately above could obtain less than 100 percent variability.

when the customer is called to the window by a clerk and time of arrival at the window. Witness Smith argues that this time should be included in transaction time because the clerk indicates a readiness to serve a customer. Since the clerk is not available to perform work other than transaction work at the window, witness Smith includes walk time in his measure of transaction time. OCA-T-2 at 18-20.

[3168] *Arguments against including walk time.* Witness Bradley (USPS-RT-4) rebuts witness Smith's assertion that walk time should be included in the measure of window service transaction time. He argues that differences in walk time are not related to differences in transaction volumes. Because walk time can not influence volume variability, it can not improve the model estimating volume variability of window services. USPS-RT-4 at 40. He also argues that a clerk may be involved in another activity while a customer is walking to the window and is not ready to serve the customer for at least part of what would be considered walk time. Consequently, walk time should not be included in transaction time. *Id.* at 39.

[3169] Moreover, as Table III-6 shows, variabilities are essentially unchanged by including walk time. *Id.* at 40.

[3170] *Commission analysis.* Witness Bradley's strongest argument against including walk time is that differences in walk time do not cause differences in transaction volumes. His contention that a clerk may signal a customer to approach the window, but then become engaged in another activity, is not persuasive. The special data collectors should have excluded such periods from walk time, since witness Nieto explained that:

⁶¹ Witness Bradley also performed four other plausible regressions including using only a single intercept, rather than using 27 location dummy variables; dropping observations with very short transaction times; dropping observations with large positive residuals; and including a term for transactions not included in normal POS ONE transactions. *Id.* at 30-36. The single intercept version was rejected because site dummies were found to be jointly significantly different from zero. *Id.* at 30. Dropping observations with short transaction times was rejected because it did not improve the fit of the model (*e.g.*, more variables were not found to be significantly different from zero). *Id.* at 32. Dropping observations with large positive residuals was rejected because most of the change in estimated coefficients was the result of a single transaction, and while the transaction was not typical, it was not implausible. *Id.* at 34. Finally, including a variable to account for non-POS ONE transactions was rejected because more variables were not found to be significant and estimated coefficients were nearly identical to those of his recommended model. *Id.* at 36.

Table III-6
Comparison of Window Service Variabilities:
Walk Time Included and Excluded

Product	Variability Including Walk Time	Walk Time Included and Excluded
Bulk Stamps	40.80%	41.00%
Non-Bulk Stamps	68.10%	68.00%
Priority Mail	69.90%	70.20%
First-Class Mail	64.00%	64.20%
Parcel Post	74.90%	75.30%
Other Weigh and Rate	67.10%	67.50%
Express Mail	66.00%	66.40%
Money Order	64.40%	64.70%
Certified Mail	100.00%	100.00%
Insurance	100.00%	100.00%
Registered Mail	100.00%	100.00%
International Mail	78.20%	78.50%
PO Box	77.20%	72.50%
COD	100.00%	100.00%
Other Special Services	95.10%	95.20%
PVI	59.20%	59.60%

“[p]ure waiting time can only occur if a clerk is not performing additional activities, such as completing paperwork, filling out orders, or processing mail.” USPS-LR-L-78, Attachment A at 5.

[3171] The Commission notes that the IOCS includes walk time in wait time. USPS-LR-L-21 at 6-79. Walk time is distributed to all services in the B-workpapers. Distributed wait time is subsequently multiplied by a window service variability specific to each subclass or class of service. USPS-LR-L-5, B-workpapers, cs03.xls.” Consequently, walk time (which is included in wait time) receives its variability indirectly from another source, and should not be used to directly estimate window service variabilities. The Commission, therefore, accepts the window service methodology

provided by witness Bradley with minor computation corrections to his computed window service variabilities.⁶²

D. FedEx Day-Turn Network Costs

[3172] In 2001, the Postal Service contracted with Federal Express Corporation (FedEx) for transportation of mail by air.⁶³ In the fall of 2001, the Postal Service complied with a directive of the Federal Aviation Administration to limit mail that could be transported on commercial passenger aircraft, resulting in a substantial increase in the cubic volume of mail flown on the FedEx Day-Turn network. UPS-T-1 at 58; USPS-T-15 at 2. As a result, the parties renegotiated the contract and included, at the Postal Service's behest, a declining block rate structure in lieu of a flat rate structure for purposes of calculating the non-fuel transportation charge on the FedEx Day-Turn network. Postal Service Brief at 131-32; Tr. 18D/6658.⁶⁴

[3173] In Docket No. R2005-1, Postal Service witness Bradley addressed the issue of how to calculate volume variability of costs incurred under a declining block rate structure. Witness Bradley concluded that volume variability of these costs would be less than 100 percent. Docket No. R2005-1, USPS-T-31 at 15.

⁶² The Commission found several minor errors due to rounding and incorrect calculation of SIMQ, SISQ counts in witness Bradley's variability estimates, which slightly affect overall window service variabilities utilized in USPS-LR-L-5, B-workpapers, CS03.xls, "3.2.1." These differences are explained in PRC-LR-6. Witness Bradley did not provide a file or program calculating the number of single-item single-quantity transactions, and single-item multiple-quantity transactions for each window service. The Commission's calculations were made in the SAS program entitled "Window Bradley Reproduce Recommended.sas" in PRC-LR-6, and are confirmed in the file entitled simq sisq calcs final!.xls, which uses the formula supplied in the Response of Postal Service Witness Bradley To Presiding Officer's Information Request No. 11, Questions 1a and 1b. Tr. 18A/5310-11.

⁶³ UPS-T-1 at 58. Under the initial contract, the Postal Service paid a fixed per-unit fee for handling and scanning of items, plus a fuel charge and non-fuel transportation charge based on a per-cubic foot of capacity purchased.

⁶⁴ Under the declining block rate structure,⁶⁴ once a certain capacity threshold is reached, the non-fuel transportation charge for additional capacity decreases by a fixed amount to a lower rate per cubic foot, and steps down further as additional higher thresholds are achieved. See USPS-T-15 at 2.

[3174] The Commission did not evaluate the merits of this treatment as Docket No. R2005-1 was resolved through a settlement which by its terms had no precedential effect. In this proceeding, witness Kelley concludes, based on witness Bradley's theoretical construct, that the base year volume variability of the non-fuel transport costs associated with the FedEx Day-Turn network ranges from 72.29 percent to 75.83 percent, depending on the quarter. USPS-T-15 at 3-4. The Postal Service proposes to treat the balance of these network costs, the non-volume variable costs, as institutional. As a result, it proposes to attribute 83 percent of FedEx Day-Turn network costs, with the balance, \$226 million, treated as institutional.⁶⁵

[3175] UPS argues that all of the FedEx Day-Turn network costs should be attributed. UPS Brief at 10-12. On behalf of UPS, witness Neels offers two rationales for attribution of the FedEx Day-Turn network costs. First, he cites Postal Service testimony that the FedEx Day-Turn network was sized specifically for Priority Mail and First-Class Mail, with 75 percent of capacity allocated to Priority Mail and 25 percent allocated to First-Class Mail. Noting that charges under the contract are incurred based on cubic volumes and that the two subclasses have equal access to the network, he contends that the non-volume variable costs should essentially be treated as specific to Priority Mail and First-Class Mail and, therefore, should be attributed to them in proportion to their relative cubic volumes. UPS-T-1 at 61-62. Alternatively, witness Neels proposes that the costs of the FedEx Day-Turn network be attributed to all classes of mail in proportion to their respective capacity usage.⁶⁶ *Id.* at 63.

[3176] On brief, UPS does not contest witness Bradley's theoretical construct. It does, however, contend that reliance on it in this instance is flawed, asserting that attribution is based on causation, not merely volume variability. UPS Brief at 11-12. To that end, it argues that the FedEx Day-Turn costs are caused by each additional cubic

⁶⁵ The Postal Service includes the non-volume variable costs in the incremental costs of First-Class Mail and Priority Mail because the FedEx Day-Turn network was created for the transportation of that mail. *Id.* at 4.

⁶⁶ The network carries small amounts of mail other than Priority Mail and First-Class Mail.

foot of mail flown on the network and that the Postal Service knows the cubic volumes by subclass that are flown. UPS urges the Commission to attribute FedEx Day-Turn network costs on the basis of cubic volumes transported by subclass. *Id.* at 12.

[3177] *Commission analysis.* The Commission recognizes that under a declining block rate structure volume variability is less than one. Nonetheless, this conclusion does not mean that the non-volume variable costs are not attributable. In response to the Supreme Court's opinion in *National Association of Greeting Card Publishers v. U.S. Postal Service*, 462 U.S. 810 (1983) (*NAGCP IV*), the Commission has held that "the [*NAGCP IV*] decision makes it plain that the Commission is not restricted to volume variability as a basis for attribution, but may in addition employ such non-volume-related causal relationships as it is satisfied are reliable." PRC Op. R84-1, Appendix J, CS IX, ¶ 0010, citing *NAGCP IV* at 830-32.

[3178] The cause of non-fuel transportation costs incurred on the FedEx Day-Turn network is not reasonably open to debate. Each additional cubic foot of capacity used incurs a charge. See Tr. 13/3828. Furthermore, cubic volume by subclass is known. Consequently, under the circumstances, the FedEx Day-Turn non-fuel transportation costs are properly attributed to the subclasses transported in proportion to their respective cubic volume. To do otherwise would improperly treat the \$226 million of non-volume variable (non-fuel transportation) costs as though they were fixed, when demonstrably they are not. The Commission has treated all previous air transportation contracts as fully attributable. Accordingly, the Commission rejects the Postal Service's proposal to treat the FedEx Day-Turn non-volume variable costs as institutional. To adopt that position would unfairly burden other subclasses, principally those subject to the Postal Service's monopoly, while ignoring causation.

IV. PRICING

A. Role of Efficient Component Pricing

[4001] The Commission's approach to ratemaking in general and rate design in particular has evolved over 36-plus years. Throughout this period, however, the requirement of section 3622(b)(3) that rates recover costs has been the starting point for Commission analysis. Thus, it is fair to say that the Commission has practiced cost-based ratemaking.

[4002] The rate structures for the various classes and services varied widely prior to the Postal Reorganization Act of 1970. The Postal Service has generally designed its rate proposals to meet the needs of mailers, and to avoid major changes that might cause economic dislocation to industries that rely on its services. As a result, the rate structures for various classes of mail remain distinct, although the processing and delivery of different classes follow certain similar patterns.

[4003] During this period the Postal Service, with the strong support of the Commission, has implemented innovations such as workshare discounts that have simultaneously recognized economic principles and spurred market growth. These changes tended to be implemented on a class-by-class basis, so discounts were designed to fit into the differing rate structures of the various classes.

[4004] In Docket No. MC95-1, the Commission provided a clear rationale for worksharing, explaining why workshare discounts were in the nation's best interest, and how the amounts of workshare discounts should properly be developed. This rationale was premised on the concept of Efficient Component Pricing (ECP).

[4005] Since that case, broad support has grown for applying that principle in the development of mail processing workshare rates. Indeed, in every subclass that has worksharing discount rates, both the Postal Service and the Commission strive to obtain an ECP outcome, i.e., a one-hundred percent passthrough of the avoidable cost savings. The ECP principle has now been applied to more workshare activities, such as the costs

saved as a result of mailer dropshipping. Although consideration of the pricing factors and other policies of the Act sometimes prevent attainment of a full set of ECP rates, it does provide a unifying principle across subclasses for worksharing rates.

[4006] While the Commission continues its commitment to and preference for cost-based workshare rates, there continues to be inconsistency in rate design methodologies from subclass to subclass because there is no unifying pricing principle for other mail characteristics, *e.g.*, weight and non-dropship transportation. These issues came into sharp focus in this case as a result of certain pricing practices followed by the Postal Service in preparing its Request.

[4007] At the beginning of this rate case, the Commission identified substantial changes in rate design methodology used by the Postal Service, some of them presented with a cogent rationale, others with no rationale provided. These included changes in the costs recognized as workshare-related, de-linking workshare rates in First-Class from the bulk metered mail benchmark, and changes in the treatment of shape.

[4008] Furthermore, there continued to be proposals to treat similar costs savings activities differently in different subclasses without any rational explanation. For example, in Standard Regular, the Postal Service proposes discounts recognizing only avoidable mail processing costs, while in Standard ECR, it bases discounts on avoidable mail processing and delivery costs. The Postal Service does not provide in its direct testimony any discussion of why these worksharing discounts should recognize different categories of avoidable costs by subclass.

[4009] In Docket No. MC95-1, the Commission determined that worksharing discounts properly should recognize both mail processing and delivery costs. The Postal Service might have good reason for using different workshare calculations subclass by subclass; however, the Commission concluded that further on the record discussion of the Postal Service workshare rate proposals was necessary. The Commission decided to use the Postal Service's proposed changes as an opportunity to gain insight into rate design generally by asking for help from both the Postal Service and the postal

community. For these reasons, the Presiding Officer issued Presiding Officer's Information Request No. 5, Question 3, which asked the Postal Service to explain more fully why it had altered its workshare rate discount development methodology and how it had determined that the specific discounts proposed were reasonable. Shortly thereafter, the Commission issued two Notices of Inquiry on rate design approach.

[4010] Presiding Officer's Information Request No. 5, Question 3, included a fairly extensive predicate providing background on worksharing discount rate development for Standard Mail in previous cases. In Notice of Inquiry No. 2, the Commission explained its thinking about rate design and sought comments from all participants on how rates might best be designed in Standard Mail. In Notice of Inquiry No. 3, additional discussion was sought with regard to First-Class Mail rate design. The Commission encouraged participants to respond directly to the NOIs, but also to prepare and submit relevant testimony to assure that a complete evidentiary record was available to inform the Commission's development of recommended rates.

[4011] Presiding Officer's Information Request No. 5, Question 3 and Notice of Inquiry No. 2 included questions about the use of a presort tree for developing and explaining rates. The potential benefits of using a presort tree are discussed in the rate design section on Standard Mail. Notice of Inquiry No. 3 focused primarily on the Postal Service's de-linking proposal in First-Class Mail. This is discussed in the rate design section for First-Class. In this chapter, the Commission focuses on broad rate design issues that have more general applicability.

[4012] The Postal Service and the postal community responded with extensive comments and testimony. These responses enabled the Commission to clarify its thinking on rate design in general, as well as on how best to reflect workshare cost avoidances in rates. This discussion is offered in the expectation that analysis on these topics will continue, and that better application of economic principles in the future will lead to rates that are both fair, and able to foster efficiencies and thereby make inexpensive postal products even more widely available.

[4013] This discussion must begin by revisiting the purpose of rate design. The first step in recommending rates is to determine the attributable cost for each subclass. The second step is to assign an institutional cost burden to each subclass based on the pricing factors of the Act. The third step is to design rates for each subclass that will cover the attributable cost and assigned institutional cost burden.

[4014] In R2000-1, the Commission observed that “[r]ate design for a subclass can be thought of as setting the implicit percentage markups for each rate category.” PRC Op. R2000-1, ¶ 5533. Thus, the outcome of any rate design is essentially a distribution of institutional cost among the rate categories and rate cells. This allocation follows appropriate recognition that rates must be cost based.

[4015] Historically, Standard Mail institutional costs have been included in the subclass revenue requirement and then essentially apportioned to rate categories on a per-piece basis. In describing the rate design methodology for Standard Mail in R97-1, the Commission explained that “each rate is comprised of both volume variable and institutional cost; but the difference between the rates of any pair of rate categories equals the difference in the avoided cost between the categories, assuming 100 percent passthrough of avoided cost.” PRC R97-1, ¶ 5373. All of the Standard Mail rate categories are worksharing categories, and both the Postal Service and the Commission attempt to pass through 100 percent of the avoidable cost savings.

[4016] This approach is consistent with Efficient Component Pricing. Efficient Component Pricing rates are those where the difference between the rates of any two worksharing categories will equal the difference in avoidable worksharing cost between the categories assuming 100 percent passthrough of avoidable cost savings. Similarly, the ECP rate between a non-workshare category and a workshare category will equal the difference in costs due to the specific workshare activity to be recognized in the rate.

[4017] In First-Class Mail, a substantial portion of the Letters and Sealed Parcels subclass is not workshared. Workshare discounts have been developed to pass through to mailers the savings to the Postal Service when they presort their mail. To the extent possible, discounts reflect costs the Postal Service will avoid if candidate mail is

presorted, or conversely, the costs the Postal Service will incur if presorted mail returns to the single-piece mailstream.

[4018] Currently, not all subclasses have rates designed to achieve this equality of rate differences and cost differences. For example, the rates in each weight and zone cell in inter-BMC Parcel Post are computed in accordance with the following formula:

Weight and zone rate = piece-related cost x subclass cost coverage + weight-related cost by zone and pound cell x subclass cost coverage.

[4019] There is only one cost coverage used in this formula. Institutional costs are distributed to each rate cell in proportion to the attributable costs associated with that rate cell. Thus, rate differences do not equal cost differences. Because costs for each rate cell are increased by a percentage coverage factor rather than an equal per-unit amount, the difference between rates in each rate cell will exceed the corresponding cost difference. Although this approach does not equate rate differences with cost differences, it does produce rates that are non-discriminatory.

[4020] According to Professor George Stigler's standard text on pricing, price differences do not necessarily indicate discrimination. There are two situations where there is no price discrimination.⁶⁷ No price discrimination exists when the ratio of price to marginal cost is the same for two products. This embodies a proportional approach to allocating institutional burden to rate categories or rate cells. The other instance when price discrimination does not exist is when the absolute difference between price and marginal cost for two products is equal. This latter approach embodies the Efficient Component Pricing.

[4021] This review and evaluation of existing postal ratemaking practice has led the Commission to question whether rate differences unrelated to worksharing should more frequently equal cost differences within every subclass. This prompted the following question which appeared in both Notices of Inquiry 2 and 3.

⁶⁷ See Stigler, George J., *The Theory of Price*, 3rd ed. (1966), at 209.

1. Does the principle of Efficient Component Pricing (ECP) require that the difference between any two rates within a subclass equal the difference in avoidable cost between the two rate categories? Consider that Baumol and Sidak define the efficient component price as the input's direct per-unit incremental cost plus the opportunity cost to the input supplier of the sale of a unit of output.

a. How does ECP apply to worksharing?

b. How does ECP apply to shape?

c. How does ECP apply to other cost causing characteristics?

Notice of Inquiry No. 2 (July 21, 2006) at 7 (footnote omitted); Notice of Inquiry No. 3 (July 20, 2006) at 6.

[4022] Most parties addressing this question agreed that ECP applies to worksharing only and that worksharing does not include shape.⁶⁸ In commenting on the issue of shape, witness Sidak observed that ECP was developed in an environment where access to an incumbent firm's network was to be granted to another firm competing for inputs that it could provide more cheaply than the incumbent firm. Tr. 26/9139. According to Sidak, if cost savings do not arise from competition for inputs, ECP does not apply. In the case of the Postal Service, mailers and third-party providers compete with the Postal Service to provide mail processing and transportation, but not shape conversion. In other words, the Postal Service does not offer a service to convert flats to letters, therefore there is no competition for shape conversion and Sidak concludes that ECP does not apply to shape. NAA-T-1 at 11-12. The Postal Service

⁶⁸ See Response of United States Postal Service to Notice of Inquiry No. 2 (August 17, 2006) at 4; Response of United Parcel Service to Notice of Inquiry Nos. 2 and 3, *supra*, at 2; Comments of Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. in Response to Notice of Inquiry Nos. 2 and 3 (August 17, 2006) at 5-7; *see also* testimony of NAA witness Sidak, NAA-T-1 at 9-12.

agrees. See Response of the United States Postal Service to Notice of Inquiry No. 2, *supra*, at 4–5.

[4023] No party except Pitney Bowes, through witness Panzar (PB-T-1), addresses mail characteristics beyond shape. Panzar contends that mailers have some control over mail characteristics, *e.g.*, shape and weight. He further notes that mailers can minimize end-to-end costs when postal rates reflect cost behavior, *i.e.*, that rate differences equal cost differences. Tr. 26/9239. This approach, he argues, promotes productive efficiency.

The basic economic argument in support of cost-based rate differentials is the same as that for avoided cost worksharing discounts. Mailers can act to minimize end-to-end costs only if the difference in rates for mail with differing characteristics reflects differences in the costs incurred by the Postal Service.

PB-T-1 at 45-46.

[4024] The Commission finds Panzar's argument persuasive. The virtue of ECP or an ECP approach beyond worksharing is that it continues to promote productive efficiency. Just as ECP should produce the least cost mail by incentivizing a mailer or third party to workshare if it can perform mail processing or transportation more cheaply than the Postal Service, so too it should provide appropriate incentives to minimize costs in the case of shape and other mail characteristics. An example of the latter is provided in Docket No. MC2005-3, the Bookspan NSA, wherein Bookspan is expected to convert flat-shaped advertising pieces to letter-shaped pieces in exchange for a lower letter rate. PRC Op. MC2005-3, ¶ 4094. The Bookspan NSA demonstrates that mailers have some choice over mail characteristics.

[4025] Obviously, not all cost-causing characteristics can, or should, be reflected in rates. Public policy factors such as the importance of a widely available, affordable postal network that provides a variety of services to bind the nation together may militate against de-averaging in certain instances. Nonetheless, it is clear that over time de-averaging has helped maintain a healthy Postal Service to the benefit of all mailers.

In this case, the Commission is giving increased recognition in Periodicals rates to the costs caused by bundles, sacks and pallets.

[4026] ECP rates send effective price signals and, as noted above, also have the virtue of being non-discriminatory. A proportional approach to the allocation of institutional costs within a subclass, although non-discriminatory, does not equate rate differences with cost differences and thus will not promote end-to-end cost minimization.

[4027] In this recommended decision, the Commission has used ECP to design rates in those subclasses that contain mostly pieces over which the Postal Service has a market dominant position. This should produce fair rates that promote economic efficiency. ECP has not been applied to Bound Printed Matter because, as explained in Chapter V, Rate Design, to do so requires volume data not now collected by the Postal Service.

[4028] The Commission recognizes that where subclasses contain substantial volumes of competitive products, market and value pricing considerations are important; significant rate redesign might cause extensive dislocation to mailers that have developed businesses in reliance on existing structures. *See* § 3622(b)(4). For these reasons, among others, the Commission continues to distribute institutional costs on a proportionate basis for most subclasses that include significant volumes of pieces with wide variations in weight.

[4029] During cross-examination, Postal Service questioning evidenced concern that extending ECP to other mail characteristics, specifically weight, might result in a per-piece contribution in certain subclasses that is relatively large for light pieces and relatively small for heavy pieces. When confronted with this outcome, witness Panzar confirmed that this is the intended outcome of the ECP approach, that rate differences equal cost differences. Tr. 26/9196-97, 9238-39, 9261-62. No evidence has been offered that a heavy piece increases fixed cost as compared to a light piece. Thus, there seems to be no cost basis to charge a higher-per-piece contribution as weight increases as long as the attributable costs imposed on the Postal Service by the heavier weight

pieces are accurately identified and recognized in the rate design, for example through a per-pound charge.

[4030] In Priority Mail, Express Mail, and Parcel Post, the Postal Service generally uses a cost coverage factor to allocate institutional cost within the subclass. In previous rate cases, the Commission has also recommended rates for those subclasses embodying that approach, i.e., proportional cost coverages within a subclass. In R2000-1, the Commission explained that it begins the rate design process by assuming equal implicit markups because this is a neutral starting position which seems to be implied by §3622(b)(1), a fair and equitable schedule. The decision to recognize worksharing by creating worksharing discounts results in unequal cost coverage, but equal per-piece contribution. The Commission further noted that rate design involves recognizing other mail characteristics (*e.g.*, weight, shape, and machinability) and that in a subclass without worksharing cost differences, rates would be based on an implicit cost coverage, i.e., the neutral starting position. PRC Op. R2000-1, ¶¶ 5533-37.

[4031] The evidence in this case has given the Commission reason to rethink that policy. The Commission has long promoted productive efficiency as a worthy goal of rate regulation. This goal is supported by Panzar.

...the promotion of postal sector productive efficiency, the reduction of the Postal Service's end-to-end costs, and lower postal rates for mail users is a policy objective worth pursuing.

Tr. 26/9171.

[4032] There are many cost drivers over which mailers may have some control, for example, shape, machinability, and containers. Witness Panzar has provided the insight that if cost differences equal rate differences then mailers can make informed choices which minimize net end-to-end mailing costs. Moreover, it seems to be fundamentally fair that mailers pay the costs they impose upon the Postal Service plus the same contribution per piece that all the mailers make within the same subclass. This is the definition of an ECP price. For all these reasons, and contrary to what the Commission

articulated in R2000-1 about the neutral starting position for rate design, the Commission now believes, and with good evidence, that the neutral starting position should equal the per-piece contribution because this promotes productive efficiency.

[4033] Of course, a neutral starting position is by its own terms, only a starting position, and not the end of any analysis. It is essential that subclasses contain rational groupings of mail with similar cost and demand characteristics. *See id.* at 9259-60 (Panzar).

[4034] In Parcel Post, the straightforward application of ECP would be inappropriate, as Parcel Select has been shown to have a substantially higher own-price elasticity in absolute value terms than inter- and intra-BMC. ECP can be applied within a subclass, and promotes productive efficiency reasonably well, if mail within the subclass has roughly the same own-price elasticity. *Id.* at 9164. The elasticity for Parcel Select suggests that it should have a different (lower) contribution per piece than inter- and intra-BMC. Therefore, a single per-unit contribution should not be used to allocate institutional cost within this subclass. Given the existence of substantially different elasticities, and given that Congress has already determined that Parcel Select should be treated as a separate product following implementation of the PAEA, if the Postal Service files another rate case, it should propose a separate subclass for Parcel Select. At that time, the Commission can evaluate whether it is appropriate to use ECP to develop rates for single-piece parcels.

[4035] Priority Mail also may contain a combination of two types of pieces with distinct cost and demand characteristics, although the record on variations within that subclass is not so well developed. At the very least, before the ECP approach could be applied to Priority Mail, the cost of flats would have to be de-averaged from the cost of parcels; otherwise, the per-piece handling costs for flats would be overstated, while the per-piece handling costs for parcels would be understated. This would distort rate-cost signals to mailers.

[4036] Although the Act provides pricing factors and policies, it does not prescribe a rate setting methodology. That is left to the judgment of the Commission. For

thirty-six-plus years, the Commission's thinking on ratemaking and rate design has evolved, and it will almost certainly continue to evolve. Sometime in the future economists may well develop new pricing methods that will better serve mailers and the national economy. The Commission finds in this case that ECP is a sound starting point from which to make adjustments to satisfy the pricing factors and policies of the Act.

[4037] Finally, the Commission turns to the calculation of worksharing costs. None of the Postal Service's responses to Presiding Officer's Information Request No. 5, Question 3 provides a conceptual rationale for varying the calculation of worksharing avoidable cost by subclass. In Docket No. MC95-1, the Commission determined that presort/barcode worksharing costs should include both mail processing and delivery costs. PRC Op. MC95-1, ¶¶ 4292-93. The Commission reaffirmed this in PRC Op. R97-1, ¶ 5374. Lacking evidence to the contrary, the Commission reaffirms that presort/barcoding worksharing cost should be based only on mail processing and delivery. Consistent with previous decisions, delivery costs underlying the workshare rates in this Recommended Decision reflect differences in delivery point sequencing by rate category. The rate design section on First-Class Mail discusses this in more detail.

[4038] Strictly speaking, shape is not a workshare attribute. Nonetheless, it is evident that, particularly in Standard and First-Class Mail, some flats and even a few parcels might well be transformed into different shape pieces if postage rates provided accurate price signals. Where adequate cost data exist, ECP principles also should be used to develop shape-based rate differences to further the goal of efficient pricing within a subclass. For a number of cases the Commission has urged that rates should better reflect the costs of shape. In this case, the Commission recommends rates that move in that direction, although some shape-based rate increases have been moderated.

B. Assignment of Institutional Cost

[4039] This is the 14th and perhaps final omnibus rate proceeding conducted under the Postal Reorganization Act of 1970 (PRA or Act). Subsequent to the hearings in

Docket No. R2006-1, the PRA was amended, substantially revamping, among other things, the rate setting process. See Postal Accountability and the Enhancement Act (PAEA), Pub. L. 109-435. The modern system of ratemaking required under the PAEA will take effect no later than June 20, 2008.⁶⁹ In the interim, the Postal Service's current rate request (and any subsequent request) are subject to subchapter II of Chapter 36 of the PRA, which, in sections 3621 and 3622, details the current ratemaking standards.⁷⁰

[4040] Section 3621 imposes a break-even constraint on the Postal Service. Thus, the Commission's recommended rates and fees are designed to generate sufficient revenues to recover, as nearly as practicable, total estimated test year costs. 39 U.S.C. § 3621. Section 3622(b) sets out the nine ratemaking (or pricing) factors on which the Commission's recommended rates are based.⁷¹ In addition, the PRA identifies certain public policy considerations, which, within the Commission's discretion, may color its rate recommendations. See, e.g., §§ 101(d) and 403(c).

[4041] Section 3622(b) reads as follows:

- (b) Upon receiving a request, the Commission shall make a recommended decision on a request for changes in rates or fees in each class of mail or type of service in accordance with the policies of this title and the following factors:
 - (1) the establishment and maintenance of a fair and equitable schedule;
 - (2) the value of the mail service actually provided each class or type of mail service to both the sender and the recipient, including but

⁶⁹ See Postal Accountability and Enhancement Act, Pub. L. 109-435, § 201(a), 120 Stat. 3201.

⁷⁰ Pursuant to the PAEA, new section 3622(f) provides that, until December 19, 2007, the Postal Service may request a recommended decision on changes in rates in accordance with subchapter II of Chapter 36 as in effect prior to enactment of the PAEA. See also new section 3632(c).

⁷¹ The Commission's authority under section 3622 also extends to fees. For purposes of this discussion, the term "rates" encompasses fees as well. In addition, unless otherwise indicated, references to section 3622 in this Recommended Decision refer to 39 U.S.C. § 3622 of the PRA prior to enactment of the PAEA.

not limited to the collection, mode of transportation, and priority of delivery;

- (3) the requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to that class or type plus that portion of all other costs of the Postal Service reasonably assignable to such class or type;
- (4) the effect of rate increases upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters;
- (5) the available alternative means of sending and receiving letters and other mail matter at reasonable costs;
- (6) the degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service;
- (7) simplicity of structure for the entire schedule and simple, identifiable relationships between the rates or fees charged the various classes of mail for postal services;
- (8) the educational, cultural, scientific, and informational value to the recipient of mail matter; and
- (9) such other factors as the Commission deems appropriate.

[4042] The Commission's ratemaking process is well-established, in large part, because in each rate case the Commission has explained its pricing decisions, taking care to distinguish circumstances that may have a particular bearing on the recommended rates. The pricing factors are quite broad, but only one, factor 3, is a requirement. *National Association of Greeting Card Publishers v. United States Postal Service*, 462 U.S. 810, 820 (1983).

[4043] Recommended rates are developed in a two-step process. First, recommended rates for each class or type of mail must be adequate to recover "the direct and indirect postal costs attributable to that class or type [of mail]." The Commission satisfies this requirement by recommending rates that recover attributable costs. Thus, attributable costs form the floor for the Commission's recommended rate levels.

[4044] Second, to enable the Postal Service to break even, the recommended rates must also be sufficient to recover “all other costs of the Postal Service,” i.e., institutional costs. To recover that portion of the institutional costs “reasonably assignable to such class or type,” the Commission applies a cost coverage to each subclass’ (or service’s) attributable costs based upon its consideration of the remaining pricing (non-cost) factors and policies of the Act.⁷²

[4045] Historically, attributable cost levels, particularly as relates to mail processing and delivery, have generated considerable controversy. This proceeding is no exception. *See, e.g.,* OCA-T-1, UPS-T-1, USPS-T-12, USPS-RT-5, VP-T-2, and MPA et al.-RT-2. The Commission’s conclusions regarding costing are contained in Chapter III.

[4046] In this proceeding, perhaps more than most, the issue of institutional cost burdens has been hotly contested with parties advocating significant shifts in institutional cost responsibilities between classes and within classes of mail. *See e.g.,* GCA-T-1; NAA-RT-2, USPS-T-31, and VP-T-1. In evaluating these proposals, the Commission weighs the evidence presented, including any changed circumstances underlying the proposals, against its historical consideration of the non-cost factors. On numerous occasions, the Commission has commented on the breadth of the non-cost factors, noting that they encompass both standards of efficiency and equity and indeed that they serve sometimes-conflicting objectives. *See, e.g.,* PRC Op. R84-1, ¶ 4000; PRC Op. R87-1, ¶¶ 4093-96; PRC Op. R90-1, ¶ 4001; PRC Op. R94-1, App. F at 17, ¶ 149, and PRC Op. R97-1, ¶ 4004. (“The [pricing] objectives of the Act, suggest, in one form or another, virtually every standard for equity and efficiency found in economic theory. Many of the objectives of the Act can conflict[.]”) In summary, it is the Commission’s practice to consider the evidence related to each pricing factor, exercising its informed judgment to balance the competing objectives of the Act in a manner that will result in fair and equitable rate recommendations.

⁷² Cost coverage is the ratio of subclass test year after-rate revenues to attributable costs. The term markup is sometimes used in lieu of cost coverage. Markup is the ratio of subclass contribution to institutional costs to its attributable costs.

[4047] Because the factors are broad and necessarily entail the exercise of judgment, the Commission has developed several tools to measure the relative institutional cost burdens borne by the various subclasses. The Commission has measured the relative institutional cost burden of each subclass in the following ways: cost coverage, unit contribution, markup index, and share of total contribution. The Commission employs these measures not only to provide a means for assessing relative burdens in particular cases, but also as they may shift over time. None by itself is an entirely satisfactory measure of contribution to institutional costs. In combination, however, they serve the Commission well.

[4048] Each case provides an opportunity for the Commission to evaluate the continued efficacy of these tools. As with rate design, the Commission's thinking on pricing continues to evolve. In this proceeding, the Commission has put renewed emphasis on unit contribution as well as total contribution in establishing fair and equitable rate levels.

[4049] The principal tool has been cost coverage, which, compared to the system average coverage, provides a useful measure of the each subclass' relative institutional cost burden in a specific case.⁷³ It is less useful as a relative measure over time because, as the Commission has previously commented, cost coverage may change from case-to-case due to exogenous factors, such as changes in costs, mail classification, and mail mix. For those reasons the markup indices, which are derived from cost coverage, have not proven to be as reliable a long-term gauge of relative burdens as was initially hoped when they were first introduced in Docket No. R87-1. Comparing markup indices over time, without accounting for the changed circumstances during the intervening period, may have only slightly more probative value than pure cost coverage comparisons.

⁷³ A drawback of this measure is that the attributable cost level may not be a reliable indicator of the extent to which a subclass should be assigned an institutional cost burden.

[4050] Unit contribution appears best suited to be used as a complementary measure both in any particular case and over time. In a specific proceeding, reference to unit contribution can be used to review cost coverage relationships to avoid unreasonable results. Illustratively, if two subclasses have similar coverages, but dissimilar unit contributions, it may (or may not) signal the need to adjust cost coverages. Over time, unit contribution is a useful measure because changes in attributable cost levels should not necessarily cause unit contributions to fluctuate widely. Thus, for example, if worksharing increases, cost coverage may be affected, but unit contributions should not change dramatically because of it.⁷⁴

[4051] Finally, total contribution by subclass is reviewed as a comparative measure in individual cases to avoid unfair results and may be useful as a longer term gauge.

[4052] The Commission has long-employed these relative measures of burden. See, e.g., PRC Op. R80-1, ¶0610; and PRC Op. R84-1, ¶4005. The Commission's greater reliance on unit contribution in this docket is a change in emphasis in assessing relative subclass burdens. The goal however, remains the same — to assure a fair and equitable assignment of institutional cost recovery.

[4053] Ratemaking is an iterative process, initially involving target coverages stated generally relative to the average, e.g., slightly below or above the average. The analysis begins with reference to the existing, presumptively reasonable rate structure. That task is complicated in this proceeding because the current rates (and the rates prior to that) were adopted pursuant to settlements. Several parties, e.g., UPS, PostCom, and Amazon, argue that the Commission's pricing analysis should begin with the rates recommended in the last litigated rate case, Docket No. R2000-1. The Commission does not disagree. However, this does not require the Commission to ignore intervening events, including current circumstances, when evaluating the Postal Service's and participants' proposals.

⁷⁴ This is not to suggest that unit contribution might not be affected by another non-cost factor, e.g., a change in value of service.

[4054] The Commission has carefully considered the Postal Service's and participants' rate proposals based on the record before it and the factors and policies of the Act. The Commission's recommended rates are designed to yield revenues for the four major classes approximately equal to the Postal Service's requested rate levels but based upon improved rate designs structured to achieve a more efficient mailstream.

[4055] In evaluating potential rate levels to achieve the Postal Service's break-even requirement, the Commission begins its deliberations with the First-Class Mail first-ounce letter (or basic) rate. It has good reason for doing so. Notwithstanding recent First-Class volume declines, the basic rate is essential to meeting the Postal Service's revenue requirement. That rate is designed in whole integers and all First-Class letter rates are tied to it. A one-cent change in the basic rate equals roughly \$750 million. To put this figure in perspective, the Postal Service's rate request seeks nearly \$4.0 billion in additional revenues.

[4056] Several parties propose alternatives to the Postal Service's proposed 42-cent first-ounce letter rate, some of which have systemwide implications.⁷⁵ Greeting Card Association (GCA) witness Clifton's 41-cent rate is predicated on his contention that the price elasticity for single-piece First-Class Mail is substantially higher than the Postal Service believes. GCA-T-1 at 48, 58; GCA Brief at 40-61. Witness Clifton proposes that the revenue shortfall occasioned by his proposal be shifted entirely to Standard Regular. GCA-T-1 at 59.

[4057] Independent of any specific First-Class rate proposal, witness Sidak, on behalf of the Newspaper Association of America (NAA), proposes an unquantified shift of institutional costs from First-Class Mail to Standard Mail. NAA-RT-1 at 22.

[4058] Against this backdrop, the Commission first evaluated the Postal Service's 42-cent basic rate, employing, as noted above, ECP principles passing through 100

⁷⁵ The merits of these alternate First-Class rate proposals are addressed below in Chapter V, Section B.

percent of the avoided cost savings to establish workshare discounts.⁷⁶ This exercise produced revenues significantly greater than proposed by the Postal Service. Thus, the Commission rejected this result since it would have increased First-Class Mail's contribution to institutional costs excessively, while concomitantly reducing, consistent with the Postal Service's break-even constraint, the contribution from other subclasses.

[4059] Next, the Commission considered a 41-cent first-ounce letter rate. This exercise produced test year First-Class letters revenues (\$35.7 billion) virtually identical to the Postal Service's proposal (\$35.8 billion) with the same unit contribution (22.1 cents). For the subclass, this set of rates generates a below average rate increase of 7 percent.

[4060] Finally, a 40-cent basic rate was considered but ultimately rejected because it would entail a substantial shift of institutional costs to other subclasses, a result not shown to be justified on this record. For NAA, witness Sidak proposes a shift of an unquantified portion of institutional costs from First-Class Mail to Standard commercial mail. NNA-RT-1 at 19, 22.⁷⁷ His suggestion is premised on: (a) the argument that First-Class Mail volumes, but not Standard, have declined due to substitution to electronic communications, and (b) that volume trends since 1995 indicate that institutional cost burdens should be shifted from First-Class Mail to Standard Mail. *Id.* at 16-22.

⁷⁶ Regarding this process, two prefatory comments are in order. First, as more fully discussed below, the Commission rejects the Postal Service's de-linking proposal. Second, in each of its First-Class rate iterations, the Commission passed through 100 percent of the cost savings (or differences) in evaluating First-Class rate levels. Its recommended rates adhere to that practice, except where exceptions are specifically discussed.

⁷⁷ By First-Class Mail, witness Sidak (and NAA) refer to the subclass Letters and Sealed Parcels, consisting of Single-Piece, Presort, and Automation rate categories. For purposes of this discussion, the phrase "First-Class letters" will be used to refer to the subclass, with "single-piece" and "workshare" (or "workshared") used to refer to the separate rate categories. It is not entirely clear what witness Sidak means by "Standard Commercial mail," but presumably the term means both Standard Regular and ECR. If by the word "commercial" he intends to exclude Standard non-profit mail, it is not clear how that could be accomplished under the Act given the manner in which non-profit rates are calculated.

[4061] The record is clear that electronic diversion exists. The parties, however, are not in agreement regarding the extent to which First-Class volumes are being diverted to broadband communications. See GCA-T-1 at 6-14; USPS-RT-2 at 66-67, and NAA-RT-1 at 16. In any event, since FY 2000 through FY 2006, single-piece First-Class Mail has declined from 52.7 billion to 42.1 billion. Even assuming that the entire decline is due to diversion to broadband, witness Sidak's suggestion is not a solution to the problem. A reduction in the first-ounce letter rate to 40 cents has not been shown likely to staunch diversion to electronic communications. As noted by witness Bernstein, the two products do not appear to be competing primarily on price. Relative to the price of postage, the price of technological alternatives i.e., broadband, has declined rapidly and has advantages, such as convenience and speed, that First-Class Mail can not match regardless of its price. Tr. 32/10890-91. Since witness Sidak's solution does not solve the issue of electronic diversion, it fails as an imperative to shift institutional cost responsibilities.⁷⁸

[4062] On brief, NAA argues that the Commission should reduce the institutional cost burden on First-Class Mail and shift a greater share of institutional costs to Standard Mail. NAA Brief at 31-37. It suggests this could be accomplished by adopting either GCA's or APWU's 41-cent first-ounce letter rate. *Id.* at 36-37. The Commission rejected the Postal Service's proposed 42-cent first-ounce letter rate, in favor of the recommended 41-cent rate, precisely because of concerns about disparate contributions among the classes.

[4063] In support of its proposal, NAA offers several statistical comparisons intended to show that First-Class Mail bears an excessive burden and that Standard Mail

⁷⁸ Furthermore, witness Sidak does not indicate how he would assign the additional institutional cost responsibility between Standard Regular and ECR subclasses and did not assess his proposal in light of the pricing factors of the Act.

bears too little.⁷⁹ NAA begins with a comparison of markup indices from 1996 to 2008. *Id.* at 25-27. In discussing changes in the mailstream, NAA notes that significant changes have occurred since 2000. *Id.* at 24. In FY 2000, single-piece first class volumes were 52.4 billion; by FY 2006, that figure dropped to 42.1 billion; on a test-year after rates (TYAR) basis, volumes drop further to an estimated 37.5 billion. Over the same period, workshared First-Class Mail increased by about 2 billion pieces, going from 45.7 billion in FY2000 to 47.8 billion TYAR. This change in mail mix, with workshared mail becoming a majority of the rate category, is the principal reason for the increase in the markup indices for First-Class Mail. In contrast, all of Standard mail is heavily workshared with the gradual increase in the Regular indices and decline in ECR indicative of the trend that continues in this proceeding.

[4064] Second, NAA argues that under the Postal Service's proposal First-Class Mail bears an excessive share of institutional costs when measured on a unit basis or in the aggregate. *Id.* at 32. NAA's conclusion rests on a simple TYAR comparison. Viewed longer term, however, the facts dispel its conclusion. As noted above, the Commission's analysis begins with Docket No. R2000-1, the last litigated case. In that docket, Standard Mail's unit contribution was 5.92 cents; on a TYAR basis in this proceeding, it is 9.52 cents, representing an increase of 61 percent. By comparison, in Docket No. R2000-1, the unit contribution for the First-Class letters was 15.74 cents; on a TYAR basis in this proceeding, it is 22.1 cents, an increase of 40.4 percent. As a consequence, the relative difference in unit contribution between First-Class letters and

⁷⁹ In discussing institutional cost burdens, NAA's analysis focuses solely on Standard Mail. Notably missing is any specific suggestion that the contribution of Periodicals, which essentially makes no contribution to institutional costs and has an own-price elasticity below Standard Regular, should be increased meaningfully.

Standard Mail shrinks from 1.66 to 1.32 times, indicating that the relative burden on First-Class Mail is declining, while Standard Mail is increasing.⁸⁰

[4065] Finally, a comparison of total contributions over the relevant time period shows, contrary to NAA's claim, that First-Class Mail's share has steadily declined while Standard's mail has risen. In Docket No. R2000-1, First-Class letters' share of total contribution to institutional costs equaled almost 62 percent of the total. On a TYAR basis at recommended rates, its share falls to 55.3 percent. For the same period, Standard Mail's share of the total increases from 20.5 percent to 30.2 percent. The Commission finds these shifts both appropriate, and adequate to meet the concerns raised by NAA.

[4066] For the most part, cost coverage considerations by subclass are addressed below in Chapter V. Particularly when cost coverage is disputed, unit contribution assumes a prominent role. *See, e.g.*, Priority Mail, Chapter V.B.6; Parcel Post, Chapter V.E.1.; and Bound Printed Matter, Chapter V.E.2. For purposes of this discussion, two examples will suffice.

[4067] At recommended rates, the average rate increase for the First-Class letters is 7 percent, which corresponds with a cost coverage of 211.6 percent, a result heavily influenced by the implicit coverage of workshared letters. Superficially, this appears to be a relatively large increase in coverage from Docket No. R2000-1. The unit contributions prove otherwise. In Docket No. R2000-1, the single-piece unit contribution was 14.94 cents; for workshared letters, it was 16.63, a difference of 1.69 cents. At recommended rates, that difference narrows slightly to 1.62 cents. The rate relationship

⁸⁰ Data for comparisons are from Appendix G of the relevant dockets. Comparing the First-Class single-piece and workshare rate categories with Standard Mail subclasses individually does not alter the conclusion. The former both increase by about 40 percent, whereas the increases in unit contribution for Regular, 98 percent, and ECR, 23.4 percent, reflect a rebalancing of intra-class unit contributions in this case.

between the two rate categories has remained stable, and the putative increase in coverage notwithstanding, the relative burdens are fair and equitable.⁸¹

[4068] In Standard Mail, too, unit contributions prove to be a particularly useful gauge. Valpak witness Mitchell argues that institutional cost burdens for ECR should be reduced and that for Regular increased. VP-T-1. He reviews the history of the two subclasses and addresses the non-cost factors of the Act. His proposal, however, relies principally on differences between the own-price elasticity of each subclass, with ECR having a substantially higher (in absolute value) elasticity. He contends that Standard ECR should have a lower cost coverage than Standard Regular to properly reflect this difference.

[4069] At recommended rates, the average increase for Regular is 9.3 percent, with a cost coverage of 170.8 percent; the comparable figures for ECR are 6.9 percent and 206.3 percent, respectively. Analysis should not end at this point. The Commission recommends Standard Mail rates that incorporate the Postal Service's proposed shape-based initiatives and the application of ECP principles. The recommended rates send appropriate price signals to mailers because they better reflect costs, including differences caused by shape. As a consequence, the mailstream will become more efficient as mailers opt for lower cost mailing alternatives, a result ultimately reflected in the unit contribution of each subclass.

[4070] A unit cost comparison demonstrates that the relative rate levels for the two subclasses are reasonable. At recommended rates, the unit contribution for Regular is 9.54 cents; for ECR, it is 9.47 cents. The slightly lower contribution for ECR relative to Regular is appropriate given the demand distinctions between the two subclasses.⁸² Based on an assessment of the non-cost factors of the Act, the Commission concludes

⁸¹ As discussed above, this conclusion is further corroborated by a comparison of unit and total contributions made by First-Class Mail and Standard Mail from Docket No. R2000-1 to the TYAR in this proceeding.

⁸² This relationship is not achieved by the rates proposed by the Postal Service, using corrected cost attribution.

that the unit cost contributions represent a fair and equitable distribution of burdens both as between the two subclasses and relative to the system as a whole.

Docket No. R2006-1

V. RATE DESIGN

A. Express Mail

1. Introduction

[5001] Express Mail is a premium expedited service offering guaranteed overnight, second day, or, in certain circumstances, second delivery day delivery for mailable matter weighing up to 70 pounds, but not exceeding 108 inches in length and girth combined. Generally, postage will be refunded if delivery does not occur as specified by the Postal Service.⁸³ Express Mail is sealed against postal inspection.

[5002] Express Mail rates are unzoned with rates based on the weight of the mailpiece and service (rate schedule) selected by the mailer. The first two rate blocks are 1/2 pound and 1 pound, and then in one-pound increments above 1 pound (up to 70 pounds). An exception is the Flat Rate Envelope which is charged the one-half pound rate regardless of weight.

[5003] Three services are included in Express Mail without additional charge: document reconstruction insurance and merchandise insurance both of which protect against loss, damage, or rifling up to \$100; and tracking, which provides information on the acceptance, arrival at the destination office, and delivery of the mailpiece.

[5004] There are five Express Mail rate categories as follows:

- Post Office-to-Post Office (Next Day and Second Day) — provides guaranteed delivery to designated post offices by 10 A.M. on the next day, second day, or, in certain instances, the second delivery day.

⁸³ Witness Berkeley identifies several *force majeure* events that relieve the Postal Service of its refund obligation. USPS-T-34 at 6. Refunds for Express Mail military service are subject to several additional exceptions. *Id.* at 10.

- Post Office-to-Addressee (Next Day and Second Day) — provides guaranteed next day delivery to an addressee from designated originating locations to designated 3-digit Zip Code destinations. Second Day Post Office-to-Addressee service provides second day (or, in some instances, second delivery day) service to any address to which Next Day service is not available from a particular originating location.
- Custom Designed Service — provides for a customized schedule for the pickup and delivery of Express Mail based on a service agreement between the mailer and the Postal Service.
- Military Service — is available between the U.S. and designated APOs and FPOs to provide Department of Defense personnel stationed overseas, and others eligible to use APO and FPO mailings, with guaranteed two- to three-day delivery to or from the United States; and
- Same Day Airport Service — (currently suspended for security reasons).

Express Mail may also be used to dropship other classes of mail between domestic postal facilities. *See id.* at 5.

2. Postal Service Proposal

[5005] Witness Berkeley sponsors the Postal Service's proposed Express Mail rates. She proposes a 12.5 percent overall rate increase based upon witness O'Hara's target cost coverage of 191 percent. *Id.* at 13; *see also* USPS-T-31 at 23. Increases for individual rates range from 3.7 percent to 27.7 percent. Currently, the same rate is charged for both one- and two-pound parcels. She proposes separate one-pound and two-pound rates. USPS-T-34 at 1, 13. No classification changes are proposed.

3. Rate Design

[5006] On brief, the Postal Service indicates that, with two exceptions, witness Berkeley's rate design generally follows the design she used in Docket No. R2001-1.

Postal Service Brief at 270. She begins with the Post Office-to-Addressee one-half pound rate, which represents almost 84 percent of total Express Mail volumes.

USPS-T-34 at 21. She develops the proposed rate, \$16.25, by increasing the current rate by 12.5 percent and applying a \$0.25 rounding constraint, in lieu of the \$0.05 used in Docket No. R2001-1.

[5007] In a change from the pre-existing rate design, she develops separate rates for one- and two-pound parcels by first developing the two-pound rate to achieve an increase approximating the average rate increase. The proposed one-pound rate essentially splits the difference between the proposed one-half pound rate and the proposed two-pound rate. To develop rates for 3 to 9 pounds, she applies a per-pound increment of \$3.10. Similarly, from 10 pounds through 70 pounds, she adds a per-pound increment of \$2.15. *Id.* at 22.

[5008] Proposed rates for the Post Office-to-Post Office and Custom Designed rate categories are based on rate differentials from the proposed Post Office-to-Addressee rates. To develop the proposed Post Office-to-Post Office rates, witness Berkeley marks up a cost differential, \$1.22, developed by witness Page (USPS-T-23) representing the cost difference between Post Office-to-Addressee and Post Office- to-Post Office service, by 96.36 percent and rounds the result up by \$0.05, resulting in a \$2.40 rate differential. To develop proposed Custom Designed rates she reduces the foregoing differential by \$0.30, resulting in a \$2.10 rate differential. *Id.* at 22-23.

[5009] Witness Berkeley indicates her rate design is intended to be responsive to concerns expressed by the Commission in Docket No. R2005-1 about the development of Express Mail rates. In particular, the Commission commented that the use of minimum and maximum constraints “causes deviations from cost based rates and creates an uneven application of markup.” PRC Op. R2005-1, ¶ 6009. Witness Berkeley asserts that because the range of cost coverages (by rate cell) is narrower than in Docket No. R2001-1, her rate design represents an improvement. *Id.* at 23-24.

[5010] No party challenges the proposed Express Mail rates or raises any rate design issue.

[5011] *Commission analysis.* Two preliminary observations are in order. The Postal Service's claim that, with two exceptions, witness Berkeley's rate design generally adhered to the rate design she used in Docket No. R2001-1 is dubious. The proposed rates are simply layered upon the current Express Mail rates, which were accepted as part of the Docket No. R2005-1 settlement, and which, in turn, were derived by uniformly increasing the then-current Express Mail rates, which were accepted as part of the Docket No. R2001-1 settlement. So, in some limited technical sense, the proposed rates can trace their lineage to Docket No. R2001-1. But this tenuous connection is not synonymous with using the same rate design.⁸⁴

[5012] Furthermore, while the Commission appreciates witness Berkeley's attempt to be responsive to its rate design concerns, the result, a narrowing of cost coverages compared to Docket No. R2005-1, is scarcely an indication that proposed rates are any more cost based, particularly given the manner in which the rates are developed.⁸⁵

[5013] As it did with every subclass, the Commission developed preliminary Express Mail rates based on Efficient Component Pricing principles. The Commission found it impractical to develop recommended rates on that basis. The preliminary rates were, for certain rate cells, substantially greater than the Postal Service's proposed rates. With nearly 84 percent of total Express Mail volume in the Post Office-to-Addressee one-half pound rate, it may be fairly assumed that this rate cell reasonably reflects the subclass elasticity. Since Express Mail's price elasticity, -1.65, is the highest (in absolute value) of any subclass, any increase substantially above the

⁸⁴ In Docket No. R2001-1, witness Berkeley used a traditional passthrough approach with Post Office-to-Addressee serving as the benchmark category. Volume variable costs were distributed to Post Office-to-Addressee rate cells and a markup was applied. Then minimum and maximum constraints were applied. Then rate differentials, which were calculated the same way as in this proceeding, were applied to develop rates for the other rate categories.

⁸⁵ In Docket No. R2001-1, proposed Express Mail rates were somewhat dependent upon the costs, whereas in this proceeding the rates are premised on existing rates on the apparent assumption that cost relationships remain unchanged.

Postal Service's proposed rates would not only affect mailers adversely, but also cause a potentially precipitous drop in after-rate volumes.⁸⁶

[5014] The Commission sees no benefit in developing recommended rates by imposing rate caps on the one-half pound rate (or other light-weight rate cells). The lack of volumes at other weight increments would essentially preclude recovery of any shortfall occasioned by the rate caps. More importantly, the PAEA identifies expedited mail as a competitive product. Express Mail rates shortly will be established by the Governors pursuant to subchapter II of Chapter 36 and section 3633 of Title 39. Thus, the Commission finds no compelling reason to adopt a rate design other than the Postal Service's, a conclusion further supported by the absence of any challenge to the Postal Service's proposed rates, and by the uncertain impact of any alternate rate design.

[5015] The Commission finds that the proposal to eliminate the uniform rate for one and two pounds in each rate category in favor of separate rates for the one-pound and two-pound rate cells to be reasonable. The change better aligns Express Mail's rate structure with Priority Mail, Parcel Post, and the express delivery market as a whole.

[5016] Finally, the Postal Service urges the Commission to maintain Same Day Airport service in the Domestic Mail Classification Schedule (DMCS) even though service is currently suspended for security reasons and there are no rates proposed. USPS-T-34 at 6-7. No party commented on this proposal. The Commission will accede to the Postal Service's request and maintain the service in the DMCS.

a. Custom Designed Delivery Stop

[5017] Express Mail Custom Designed service items are subject to an additional fee, currently \$13.25, for each delivery stop. The Postal Service proposes to increase

⁸⁶ On an after-rates basis, Express Mail volumes decline by about 15 percent, based on an average rate increase of 12.5 percent. An increase nearly 50 percent greater than the Postal Service's proposed half-pound rate would have a more deleterious effect on mailers and Express Mail after-rate volumes.

this fee from \$13.25 to \$14.25. There is no opposition to the proposed fee. Based on its costs, the Commission recommends a Custom Designed delivery stop fee of \$14.25.⁸⁷

4. Cost Coverage

[5018] For the Postal Service, witness O'Hara proposes an Express Mail cost coverage of 191 percent, yielding an average rate increase of 12.5 percent. O'Hara supports his proposed coverage by evaluating the pricing criteria of the Act, concluding that the proposed rate level is fair and equitable. USPS-T-31 at 23-24. No party contests the Postal Service's proposed rate level.

[5019] The Commission approves the proposal for an above-average rate increase of 12.5 percent. The projected Express Mail cost coverage is 170.4 percent. The recommended rates recover attributable costs (\$467.2 million) and make a reasonable contribution to institutional costs (\$329.1 million). At recommended rates, Express Mail's unit contribution to institutional costs is approximately \$7.71, by far the highest of any subclass.

[5020] Express Mail has a high intrinsic value of service due to its delivery priority, extensive air transportation, service guarantee, and additional features, *e.g.*, tracking and insurance, provided at no additional charge. On the other hand, it has the lowest economic value of service (in absolute terms) of any subclass. The above-average rate increase will have an effect on mailers. Alternative expedited delivery services, however, are available. By the same token, the above-average rate increase, particularly given Express Mail's relatively small market share, should not affect competitors in the expedited delivery market unfairly.

⁸⁷ Express Mail is eligible for Pickup On-Demand service. The fees for Pickup On-Demand services are developed by witness Scherer and are discussed in Priority Mail, section B.6.

[5021] No party has raised any substantive issue regarding Express Mail rates or rate level. The Commission concludes that its recommended rates are fair and equitable.

B. First-Class Mail

[5022] *Introduction and summary.* In this proceeding, the Postal Service proposes a 3-cent increase in the rate for single-piece First-Class Mail letters weighing one ounce or less, thereby raising the price of the First-Class stamp from 39 cents to 42 cents. Applying the Commission's rate design methodology, the Commission recommends a 41 cent rate for the first ounce of single-piece letters. This rate and the associated First-Class Mail rates recommended by the Commission generates First-Class Mail revenue essentially equivalent to that requested by the Postal Service.

[5023] The Postal Service also proposes a 3-cent increase for single-piece cards, increasing the rate from 24 cents to 27 cents. The Commission recommends a 2-cent increase, which raises the single-piece cards rate to 26 cents. At this rate, single-piece cards remain an economical means of communication.

[5024] For the convenience of single-piece First-Class Mail rate payers, the Postal Service proposes the creation of the Forever Stamp. The Forever Stamp would serve as postage equivalent to the first ounce of single-piece First-Class Mail letters prevailing at the time of its use. It would retain this value regardless of its price when purchased. The Commission recommends the Postal Service's proposal to create the Forever Stamp. The initial rate for the Forever Stamp shall be equivalent to the newly recommended rate for the first ounce of single-piece First-Class Mail letters. The Forever Stamp is a forward-looking initiative that should benefit both the mailing public and the Postal Service. It will reduce the public's inconvenience when transitioning to new rates, and reduce printing and window service costs associated with the need for "make-up" stamps.

[5025] The Postal Service proposes a fundamental change within the Letters and Sealed Parcels subclass to recognize shape as an important element of rate design. The proposal requires the development of rates specific to letter-, flat-, and parcel-shaped mail. The Commission recommends the Postal Service's proposal to

move towards shape-based rates. Shape-based rates send appropriate signals to mailers by better aligning rates to the costs imposed on the postal system.

[5026] Additional ounce rates traditionally are used to recover the costs imposed on the postal system by both the weight and shape of a mailpiece. By recognizing shape-related costs with shape-based rates, the additional ounce rates can be refocused on the costs imposed by weight. The Postal Service proposes, and the Commission recommends lower additional ounce rates. Letter-shaped mailpieces weighing more than one ounce will actually realize a net reduction in the price of postage as a result of these changes. Rates for heavier flat- and parcel-shaped mailpieces are also mitigated.

[5027] The shape-based rate proposal includes several other related proposals: a maximum 3.5 ounce weight for single-piece letter-shaped mail; the establishment of a new bulk business parcels rate category with three presort tiers; the elimination of the letters and cards carrier route discounts; the elimination of parcel-shaped mailpieces from the non-automation presort category; changes in minimum sort requirements within the non-automation presort category; and the elimination of the heavy piece discount. The Commission recommends these classification proposals. The accompanying rate-related recommendations are discussed below.

[5028] The Postal Service also proposes the elimination of the nonmachinable surcharge from the current rate categories, and the creation of a new nonmachinable surcharge within the new business parcels category. The Greeting Card Association (GCA) submits an alternative proposal to retain the surcharge for certain low-aspect ratio letter-shaped mailpieces rather than having these mailpieces treated as flats for rating purposes under the Postal Service's shaped-based rate proposal. The Commission recommends elimination of the nonmachinable surcharge from the automation flats category, and the creation of a new nonmachinable surcharge within the new business parcels category as suggested by the Postal Service. However, the Commission recommends temporarily retaining the nonmachinable surcharge for nonmachinable letter-shaped mailpieces to mitigate rate shock.

[5029] Concurrent with the shaped-based rate proposal, the Postal Service also proposes a fundamental shift in the methodology that it uses to develop rates for First-Class Mail. It proposes de-linking workshared mail rate design from single-piece rate design. Separate revenue requirements would be developed for workshared mail and for single-piece mail. The Postal Service proposes a goal of establishing similar unit contributions, on average, from each category.

[5030] Four participants, APWU, GCA, MMA, and Pitney Bowes propose alternatives to various aspects of the rate design methodology proposed by the Postal Service. APWU proposes an alternative rate schedule with a 41-cent first-ounce single-piece rate for First-Class Mail letters based on previously recommended concepts and methodologies, including use of the bulk metered mail benchmark. GCA proposes a 41-cent first-ounce single-piece First-Class Mail letter rate based on its analysis of mail volume elasticities. The proposal includes suggestions for workshare rates based on whether or not the Commission recommends the Postal Service's de-linking proposal. MMA generally supports the Postal Service's rates including the de-linking proposal, and it separately analyzes worksharing costs. Finally, Pitney Bowes proposes an alternative rate schedule for First-Class Mail workshared letters based on an independent estimate of avoided costs.

[5031] The Commission continues application of Efficient Component Pricing (ECP) as its basic methodology for designing rates that reflect costs. It recommends rates using a single bulk metered mail benchmark as established by precedent. This Commission finds that with minor adjustments necessary to give proper recognition to other policy considerations, this approach results in recommendations that are fair and equitable, and that balance the considerations of all mailers within a subclass. It also results in rates that send appropriate pricing signals, and meet revenue targets.

[5032] The Postal Service also proposes reductions in the discounts for Qualified Business Reply Mail (QBRM) letters and cards. Time Warner and MMA submit alternative proposals to either increase or to not reduce the current discounts. The Commission recommends a uniform 3.0 cent discount for QBRM letters and cards.

[5033] Two participants, OCA and Pitney Bowes, present additional proposals in this docket. OCA proposes an alternative rate schedule for the First-Class Mail Letters and Sealed Parcels subclass which features four-ounce rate increments for letter-, flat-, and parcel-shaped mail. The Commission finds merit in further study of this proposal, but does not recommend this proposal at this time. Pitney Bowes proposes a 0.1-cent discount for single-piece First-Class Mail letters with evidence of first-ounce postage purchased through alternative sales channels, limited to mail bearing PCPostage, permit, or meter indicia. The Commission does not recommend this proposal.

[5034] The recommended First-Class rates reflect an average class-wide increase of 6.9 percent, based on increases of 7.0 percent for letters and 6.1 percent for cards. These rates are expected to generate revenues that are 212 percent of attributable costs for letters and 155 percent of attributable costs for cards.

[5035] Preliminary issues applicable to First-Class Mail are discussed in section B.1.

[5036] Rate design and classification issues specific to the Letters and Sealed Parcels subclass are discussed in section B.2.

[5037] The four-ounce increment rate design proposal presented by OCA, and the indicia discount proposal presented by Pitney Bowes are separately discussed in section B.3.

[5038] The Postal Service's Forever Stamp proposal is discussed in section B.4.

[5039] Rate design and classification issues specific to the Cards subclass are discussed in section B.5.

[5040] Rate design and classification issues pertinent to the Priority Mail subclass are discussed separately in section B.6.

1. Preliminary Matters

[5041] Postal Service witness Taufique presents the Postal Service's Letters and Sealed Parcels subclass and Cards subclass rate and classification proposals. See *generally* USPS-T-32.⁸⁸

[5042] Witness Taufique sponsors two significant changes to the Letters and Sealed Parcels subclass. First, he proposes the establishment of shape-based rates. Second, he proposes the de-linking of workshare rate design from single-piece rate design. Several participants in this case discuss the applications of Efficient Component Pricing and the use of benchmarks specific to First-Class Mail rate design. The Commission reviews these topics in order. The section concludes with a discussion of issues related to appropriately determining worksharing costs and cost avoidances.

a. Shape-Based Rate Design

[5043] The current First-Class Mail Letters and Sealed Parcels subclass rate and classification structure recognizes shape and weight characteristics that impose costs on the postal system through the application of first-ounce rates, additional ounce rates, nonmachinability surcharges, and a heavy piece discount. Understanding the interrelationship of the rates, surcharges, and the discount is not straightforward. For example, the first-ounce rates do not specifically reflect the impact of shape, and the additional-ounce rates compensate for both the shape and the weight of a mailpiece.

⁸⁸ Witness Taufique's testimony relies on the testimony of several other Postal Service witnesses beginning with the First-Class Mail revenue requirements presented by witness O'Hara (USPS-T-31). Witness Waterbury (USPS-T-10) provides the roll forward costs for the Letters and Cards subclasses, as well as for single-piece and presort First-Class Mail within the Letters and Sealed Parcels subclass. Mail processing cost estimates for presort letters and cards are provided by witness Abdirahman (USPS-T-22) and for flat- and parcel-shaped pieces by witness Miller (USPS-T-20). Witness Kelley II (USPS-T-30) provides delivery costs by shape, and witness Smith (USPS-T-13) provides mail processing costs by shape. Witness Loetscher (USPS-T-28) provides revenue, pieces and weight (RPW) data by shape and weight, witness Berkeley (USPS-T-39) provides the test year fee revenue, and witness Thress (USPS-T-7) provides the test year volume forecast.

[5044] In this case, the Postal Service proposes to re-align rates to better reflect the costs imposed by mailpiece shape and weight. The Postal Service proposes to reflect the impact of the shape of a mailpiece with distinct first-ounce rates. The additional-ounce rates are proposed to reflect weight, with a de-emphasis on shape. These changes make the nonmachinable surcharges and the heavy piece discount no longer necessary. USPS-T-32 at 17-20.

[5045] The proposal is consistent with the realities of modern mail processing where mailpiece shape becomes more significant than the class under which the mailpiece is sent. For a mailpiece of the same shape, Standard Mail is processed much the same as First-Class Mail. Mail is segregated into shape-based letter, flat, and parcel mail flows. Each mail flow is processed on mail processing equipment specialized to handle that shape of mail. The specialized mail processing equipment imposes distinct costs on each mail flow. The shape-based rate proposal allows the Postal Service to align the rates paid by mailers with the specific costs imposed on the system by the unique mailflows. See Docket No. N2006-1.

[5046] Within the single-piece rate category, the Postal Service proposes the introduction of different rates for single-piece letters, flats, and parcels designed to specifically recognize the shape of the mailpiece as part of the first-ounce rate. This allows the Postal Service to propose elimination of the single-piece nonmachinable surcharge, and a reduction in the additional-ounce rate. Letter-shaped mail that does not meet the length, height, width, thickness, rigidity, variation in thickness, or aspect ratio letter machinability criteria will be rated as a flat. The Postal Service proposes that mailpieces weighing greater than 3.5 ounces, regardless of dimension, be rated as either a flat or a parcel. The Postal Service also proposes that under certain circumstances, where a mailpiece is too rigid for example, that the mailpiece be rated as a parcel.

[5047] The Postal Service proposes first-ounce rates for the automation letters and automation flats categories to better reflect whether the mailpiece is letter- or flat-shaped. The Postal Service also proposes reductions in the additional-ounce rates, and the elimination of the heavy-piece discounts within both the automation letters and

automation flats categories. It further proposes elimination of the nonmachinable surcharge from the automation flats category.

[5048] The Postal Service also proposes rates to better recognize shape in the non-automation presort category. Different rates are proposed for letter- and flat-shaped mailpieces. A corresponding reduction in the additional ounce rate, the elimination of the nonmachinable surcharge, and the elimination of the heavy piece discount also are proposed as the first-ounce letter and flat rates are designed to encompass these cost characteristics.

[5049] Parcel-shaped mailpieces no longer will be eligible for non-automation presort rates. Instead, the Postal Service proposes the introduction of a new business parcel category. The new business parcels category would apply to bulk-entered pieces that do not meet the machinability criteria for letters or flats. The Postal Service proposes ADC, 3-digit, and 5-digit rate tiers, and an additional-ounce rate within this category. It also proposes a limited application of the nonmachinable surcharge for certain parcels that are non-barcoded, less than two ounces, or nonmachinable.

[5050] *ABA position.* ABA supports the Postal Service's shape-based rate proposal. Noting that the Postal Service's proposal only passes through 55 percent of the cost differences between letters and flats, ABA comments that this is acceptable given the potential rate shock that a 100 percent passthrough would create.

[5051] Looking to the future under the new postal reform legislation, ABA argues that shape should not be recognized in a worksharing discount, but should be recognized either through different rate elements or through discounts that recognize intrinsic cost differences. ABA Brief at 8-12; *See also* Discover Brief at 2-3.

[5052] *Carlson position.* Carlson opposes the recommendation of shape-based rates. Although he states that he supports shape-based rates philosophically and economically, he raises serious practical concerns about this proposal's effect on the general public. He believes that the public's capacity to learn the definitions of letters, flats, and parcels quickly is unclear. He contends that the Commission should require

evidence concerning the effect of this proposal on the public before recommending this change. Carlson Brief, § III at 12-14.

[5053] *GCA position.* GCA argues that the Postal Service's proposal for separate letter, flat, and parcel rates based on shape makes excellent sense, deserves consideration, and should be recommended, with one exception. GCA contends that a nonmachinable surcharge should apply to a subcategory of certain single-piece low aspect ratio letters, rather than charging the single-piece flat rate as proposed by the Postal Service. See chapter V.B.2; GCA Brief at 65-81.

[5054] *MMA position.* Witness Bentley supports the Postal Service's shape-based rate proposal. For the single-piece First-Class Mail category, witness Bentley argues that the shape-based proposal allows rates to better track costs. He asserts that this sends the appropriate economic signals to mailers. For example, he states that the proposed rates will provide an incentive for mailers to replace flats (which have higher processing and delivery costs than a letter of the same weight) with letters, whenever possible. He also expresses support for the Postal Service's shape-based proposals within the worksharing categories, including the new business parcels category. MMA-T-1 at 22-24.

[5055] Witness Bentley comments that the Postal Service has missed an opportunity, however, by failing to consider volume as a significant cost driver within bulk First-Class Mail. He discusses the efficiencies exhibited by mailers who send large mailings, and suggests that such characteristics could justify a small discount to mailers who send large mailings and a small increase to mailers who send out small mailings. He urges the Commission to direct the Postal Service to also consider volume as a specific cost driver to be reflected in rates. MMA Brief on Issues Regarding First-Class Presort Rates at 58-61 (hereinafter MMA Presort Brief).

[5056] *NAPM & NCCP position.* NAPM & NCCP argue that recognition of shape is a step toward greater economic efficiency and sending better price signals to mailers. NAPM & NCCP Brief at 29-30.

[5057] *OCA position.* OCA supports the Postal Service's shape-based rate proposal arguing that rates should be more nearly aligned with mail cost characteristics. However, OCA cautions that the proposal will dramatically increase the complexity of the rate schedule, and require mailers to understand the differences between letters, flats, and parcels, as well as pay particular attention to weight. OCA Brief at 92-93.

[5058] *PSA, PostCom, and MFSA position.* Witness Glick argues that the Postal Service's shape-based rate design proposals have gone too far. He contends that the Postal Service is proposing enormous rate increases based on inadequate data, without giving due consideration to rate impact. He concludes that the rate increases for First-Class Mail parcels should be reduced. PSA/PostCom-T-1 at 14-15.

[5059] PSA suggests implementing the classification changes proposed by the Postal Service, but basing rates upon less than full passthroughs. PSA contends that this will allow the Postal Service to develop better information on the costs and characteristics of First-Class Mail parcels without inducing rate shock. PSA Brief at 23-29.

[5060] *Popkin position.* Popkin comments on the additional steps a mailer must take in evaluating a mailpiece to determine the appropriate postage given shape-based rates. He expresses concern that the Postal Service must realize the confusion and extra work that may be imposed on mailers, and attempt to make the transition to shape-based rates as smooth as possible. Popkin Brief at 10-11.

[5061] *Commission analysis.* The Commission recommends the Postal Service's proposal of rates that better reflect the mail processing and delivery costs imposed on the postal system by the shape of the mailpiece. Rates that reflect costs send appropriate pricing signals to mailers and lead to a more efficient use of postal resources. Record evidence demonstrates that shape is an important cost driver in both mail processing and delivery. Thus, it is appropriate for this cost driver to be reflected in the First-Class Mail rates.

[5062] The Commission is concerned about the actual implementation of these rates. Shape-based rates represent a significant departure from the current rate and

classification structure that will require the re-education of mailers. The Commission strongly encourages the Postal Service to develop and disseminate materials to educate all mailers as to what constitutes a letter, a flat, and a parcel, and what rates are applicable to each mailpiece shape.⁸⁹

[5063] Some mailers will face substantial rate increases as a result of shape-based rates. Consumer education by the Postal Service can help in this area too. It can and should be explained to mailers that shape-based rates better reflect actual Postal Service costs, and that adjusting mailpiece shape can result in substantial postage reductions. The specific rate and classification issues associated with shape-based rates are further discussed in section B.2 below.

b. De-Linking of First-Class Mail Rate Design

[5064] Witness Taufique explains that since Docket No. MC95-1, workshare rates have been determined by applying discounts to first-ounce single-piece rates. The discounts are based on estimates of costs avoided through various types of workshare activity relative to a representative workshare benchmark. USPS-T-32 at 12-17.

[5065] Taufique states that this approach has generated controversy and opposition because workshare mailers contend that this methodology may ignore cost-causing characteristics that, while not expressly associated with a worksharing activity considered in the development of discounts, nevertheless may be associated with their mail. He notes that the Cost and Revenue Analysis (CRA) and the roll forward model report separate estimates of costs and revenue for the single-piece category, and for the combined non-automation and automation presort category. He explains that the single-piece and combined presort costs do not simply reflect the avoided costs when a mailer chooses to perform worksharing activities, but reflect the full range of cost differences between the two sets of mail. He proposes that the rates for the single-piece

⁸⁹ The Postal Service is encouraged to continue to explore the experiences of Royal Mail, which recently implemented similar changes, in the United Kingdom.

category and the combined non-automation and automation presort category be developed independently of each other (de-linked) based on the separate CRA cost estimates.

[5066] The Postal Service identifies other benefits of the de-linking methodology. It argues that this methodology is reproducible from one case to the next, it is verifiable, it is transparent, it potentially could reduce much of the rate case controversy concerning worksharing that has occurred in the past, and it relies on a robust and well-established data source (the Cost and Revenue Analysis system). Postal Service Brief at 200; Postal Service Reply Brief at 157-158.

[5067] As part of the de-linked approach to rate design, the Postal Service proposes to establish separate revenue requirements for the single-piece category and the combined non-automation and automation presort category. The revenue requirements would be developed with the goal of obtaining similar unit contributions from single-piece in the aggregate and from presort in the aggregate. It is not the Postal Service's objective that each piece of mail provide the same unit contribution as every other piece of mail. Although the Postal Service notes its intent to equalize unit contribution from the two categories, it asserts that in the future other rate design and rate impact considerations may require deviation from this goal.

[5068] *ABA position.* Witness Kent argues that the Postal Service's de-linking proposal is logical, fair and equitable, and consistent with the Efficient Component Pricing rule. He disagrees with OCA's assertion that a discount rate based upon the avoided costs measured for bulk and single-piece First-Class Mail together should be the appropriate basis for a discount for First-Class workshare mail. See ABA-RT-1.

[5069] Witness Kent contends that the nature of First-Class Mail has changed during the last 30 years. He argues that the days of large mass conversion from single-piece mail to presort mail are largely over. He believes that mail prepared as bulk mail now is very different from mail prepared as single-piece mail. He asserts that there is approximately an 18-cent cost difference between bulk and single-piece First-Class Mail, yet only approximately 8 cents of costs are recognized as avoided costs by the

current rate process. Witness Kent contends that where rates fail to reflect significant cost differences, they tend not to be fair and not to encourage economic efficiency.

[5070] ABA further states that the Postal Service finally recognizes that single-piece and bulk First-Class Mail no longer are the same species of mail and each has separate cost characteristics. It argues that de-linking will allow recognition of cost differences based on actual CRA data. It contends that the proposal puts aside the appropriate benchmark controversy and instead allows reliance on actual data. ABA does not believe that Efficient Component Pricing principles bar de-linking so long as in establishing a discount a clear distinction is made between avoided costs and intrinsic non-avoided costs. ABA Brief at 13-17.

[5071] *APWU position.* APWU opposes the Postal Service's de-linking proposal. It argues that de-linking would shift costs to single-piece letters and result in excessive presort discounts. APWU contends that de-linking also would circumvent the Commission's Docket No. MC95-1 decision and disregard the policy considerations enunciated therein (the Docket No. MC95-1 decision rejected a Postal Service proposal to create separate Automation and Retail subclasses within First-Class Mail). APWU Brief at 5-15; APWU Reply Brief at 1-5, 8-10.

[5072] APWU witness Kobe, in developing an alternative rate proposal, explains that the Postal Service's de-linking approach would change current First-Class Mail policies, change the rate relationships between single-piece and presorted mail, and create a template for further change. She contends that by de-linking, the Postal Service is de-averaging single-piece and presorted letters, and finds it problematic that "[d]ifferences in per unit costs based on a difference in the total CRA costs for Presort mail and Single Piece mail may reflect a whole range of characteristics that do not relate to the cost avoidances for workshare activities." APWU-T-1 at 6-7. Witness Kobe asserts that de-linking can result in: identical First-Class letters making different contributions to overhead depending solely on whether or not the piece is workshared; discounts that exceed costs savings; and rates that violate the statutory policy of uniform rates for First-Class letter mail. She states that the Postal Service did not provide any

convincing rationale for this change in methodology or for the change in its policies on cost averaging. *Id.* at 4-8.

[5073] APWU also argues that de-linking would violate the requirements of § 3623(d) of the Act which specifies, in part: “The Postal Service shall maintain one or more classes of mail for the transmission of letters sealed against inspection. The rate for each such class shall be uniform throughout the United States, its territories, and possessions.” APWU Brief at 12, citing 39 U.S.C. § 3623(d). APWU asserts that the “proposal to de-link single-piece rates from presort rates, with the effect of permitting cost-shifting from large volume presort mailers to individuals and small businesses would violate this requirement of uniform rates within First-Class Mail service.” *Id.* at 14.

[5074] *GCA position.* GCA opposes the Postal Service’s de-linking proposal. It argues that de-linking is inherently inefficient and inconsistent with Efficient Component Pricing because it fails to distinguish between costs avoided by mailers performing functions the Postal Service otherwise would perform, and differences in the cost of a function that the Postal Service still must perform resulting from certain intrinsic characteristics of the mail. It contends that de-linking would be unfair and inequitable because it allocates the benefits of lower-cost mail among mailer groups. Finally, de-linking results in a “thinly-disguised but effective bifurcation of First-Class Letters into the same separate subclasses” as rejected by the Commission in Docket No. MC95-1. GCA Brief at 7, 10-23.

[5075] *MMA position.* Witness Bentley supports the Postal Service’s de-linking proposal. He sees benefit in the proposal because he believes it will simplify the Postal Service’s workshare rate/discount presentation, and should end the Postal Service’s tactic of proposing discounts that appear to be greater than estimated cost savings. He further asserts that de-linking of rates from derived cost savings also will eliminate inherent problems associated with mail flow models that attempt to compare unit costs on an absolute basis. However, he questions the relevance of equal contributions in the aggregate from each of the First-Class Mail categories. MMA-T-1 at 6-8; MMA Presort Brief, at 11-19.

[5076] *OCA position.* OCA opposes the Postal Service's de-linking proposal. It contends that the Postal Service's proposal "may encourage worksharing, but it does so at the expense of First-Class single-piece mailers." OCA Brief at 103; *see also* OCA-T-4 at 3-4. OCA supports continued use of the bulk metered mail benchmark and developing presort rates based on the costs avoided by the activities of mailers that justified the creation of the discount. OCA Brief at 98-107; *see also* OCA-T-4 at 13.

[5077] OCA draws parallels between the Postal Service's de-linking proposal and the Docket No. MC95-1 proposal for creation of separate Automation and Retail subclasses within First-Class Mail. OCA concludes by stating: "The OCA requests that the Commission again reject the Postal Service's request for special treatment for First-Class presort mailers on the grounds of fairness and equity and § 101(a), whereby the Postal Service is charged with binding the nation together." OCA Reply Brief at 28-30.

[5078] *Pitney Bowes position.* Pitney Bowes supports the de-linking proposal. It views de-linking as a means of decreasing the problems associated with First-Class Mail heterogeneity. PB-T-1 at 39. It also believes that de-linking improves modeling because all costs, not only workshare related costs, are considered. PB-T-2 at 11-12.

[5079] *Commission analysis.* The Commission does not adopt the Postal Service's proposal to de-link single-piece from worksharing rates within the First-Class Mail Letters and Sealed Parcels subclass.

[5080] The Postal Service argues that de-linking will reduce controversy because it eliminates identification of a single benchmark, and it eliminates discussion concerning whether certain costs are related to worksharing.

[5081] The Commission evaluates the merits of reducing "controversy" starting with the presumption that the First-Class Mail Letters and Sealed Parcels subclass is a single subclass. The Postal Service has not proposed bifurcation of this subclass. The Commission recognizes that First-Class Mail, and First-Class mailers exhibit diverse characteristics. Considering the interests of diverse mailer populations, and heterogeneous mail characteristics may naturally involve controversy. However, this

does not prevent the Commission from developing recommendations that are fair and equitable.

[5082] Similarities between the Postal Service's de-linking proposal and the Postal Service's proposal in Docket No. MC95-1 are noted by APWU, GCA, and OCA. In Docket No. MC95-1, the Commission considered a Postal Service request to replace the Letters and Sealed Parcels subclass and the Postal and Post Cards subclass with an Automation subclass and a Retail subclass. The Postal Service expressed a rate design goal of "contribution neutrality," i.e., the Automation and Retail subclasses would retain their implicit cost coverages from Docket No. R94-1.

[5083] The Commission did not recommend the proposal in the absence of evidence of distinct differences in demand characteristics between the proposed subclasses. Although the Commission recognized cost differences, it concluded that there were more similarities than differences between content and other characteristics across the proposed subclasses. Furthermore, the proposed subclasses were not naturally disjunctive, i.e., Courtesy Envelope Mail which is fully automation compatible, would be considered Retail, and combining the Cards and the Letters subclasses would destroy the homogeneity of Cards. Finally, the Commission could not ignore the reasonable foreseeable consequence of rate impact on the Retail subclass in future rate cases.

[5084] The Postal Service is not proposing to establish separate subclasses for single-piece and worksharing mail in this case, and the conceptual goal of "contribution neutrality" has been replaced with a goal in this rate case of equal unit contribution in the aggregate.

[5085] The Commission recognizes the differences between Docket No. MC95-1 and the current proposal. However, both the Docket No. MC95-1 proposal and the present de-linking proposal raise concerns over the reasonable foreseeable consequence of rate impact in future rate cases on single-piece mailers.

[5086] The de-linking methodology allows many costs that are not worksharing related to be avoided by worksharing mailers. The full burden of these costs are shifted

to the single-piece mailers. The Commission believes that these non-worksharing-related costs should be shared by all mailers within the subclass.

[5087] De-linking dissolves the rate relationships between single-piece and worksharing mail. The Postal Service states a goal of equal unit contribution, in the aggregate, is to create a link between single-piece and worksharing mail. However, the Postal Service states that it may or may not adhere to this goal in the next rate case. The tentative nature of this goal is not reassuring. The Postal Service further notes that it is not an objective that each mailpiece provide equal unit contribution under the de-linking proposal. Thus, this change in methodology runs counter to the economic principles that support designing rates within a subclass that utilize Efficient Component Pricing.

[5088] An undesirable feature of the de-linked, equal aggregate unit contribution approach is demonstrated by the effects of an interim (August 24, 2006) revision to USPS-LR-L-129. As a result of this revision, the difference between the aggregate unit contribution of single-piece and presort increased from 0.1 cents to 1.2 cents. This change was primarily the result of the removal of an adjustment to account for the migration of single-piece parcels to the new business parcel categories. Tr. 19/6839.

[5089] Letters make up the large majority of the subclass, and the price signals sent by letter worksharing discounts are very important drivers of efficiency in the postal sector. The above example shows how revenues and costs associated with parcels, which make up about 1 percent of single-piece volume, can significantly impact aggregate unit contributions. For this reason and others, targeting equal aggregate unit contributions in the absence of equal unit contributions across shapes is unlikely to result in the most efficient price signals.⁹⁰ A comparison of pieces that are similar, except for worksharing, is the approach most likely to accurately isolate the savings due to

⁹⁰ Differences in additional ounce and other non-piece revenue also distort the relationship between the aggregate unit contribution of single-piece and presort.

worksharing, and therefore allow for the development of discounts that encourage efficient mailer behavior and minimize costs to society.

[5090] De-linking the rate design does not fairly and equitably balance the interests of all First-Class mailers within the subclass, does not follow established principles of rate design including Efficient Component Pricing and does not fairly allocate costs unaffected by worksharing. The Commission does not accept the Postal Service's de-linking proposal.

c. Efficient Component Pricing

[5091] The Commission sought comments on the applicability of Efficient Component Pricing to rate design in this rate case. This is thoroughly discussed in Chapter IV, section A.

[5092] The Commission's First-Class Mail rate analysis applies the principles of Efficient Component Pricing. However, the Commission's final rate recommendations must consider all factors of the Act. The rates that might reflect strict application of Efficient Component Pricing sometimes must be moderated to obtain rates consistent with the requirements of the Act. This is an issue in First-Class Mail rate design.

[5093] Witness Taufique proposes First-Class Mail rates that balance a number of factors, other than economic efficiency, that allow rates to deviate from economically efficient rates. *See* USPS-T-32 at 30, 42. Postal Service witness Robinson, when considering several intervenor proposals, concludes: "A mechanistic assertion that 'discounts should always equal costs avoided' or that 'only economically efficient rates should be adopted' fails to consider the myriad of factors that must be considered in constructing postal rates that are both fair and equitable and consistent with the Act." USPS-RT-10 at 5-6, (footnote omitted). As an example, the Postal Service criticizes the APWU proposal for an overemphasis on Efficient Component Pricing. Postal Service Brief at 219-20.

[5094] The principle of Efficient Component Pricing significantly influences the Commission's First-Class Mail recommendations. However, the Commission agrees that this principle should not be blindly applied, and that the impact of potential rates must be evaluated with regard to the policy factors of the Act.

[5095] The Commission's recommendations analyze rates within a framework of Efficient Component Pricing. The rates are then weighed against the factors of the Act and appropriately adjusted where necessary. Generally, the rates recommended for Letters and Sealed Parcels are consistent with both Efficient Component Pricing and the requirements of the Act. Notably, the parcel-shaped rates are not fully consistent with Efficient Component Pricing. They have been adjusted because of consideration of the factors of the Act.

d. Benchmark

The Commission has recommended a bulk metered mail benchmark as the starting point for establishing First-Class Mail worksharing discounts since Docket No. MC95-1. Docket No. MC95-1, ¶ 4302; *see also* Docket No. R97-1, ¶ 5089. The Commission most recently described the application of the bulk metered mail benchmark in Docket No. R2000-1.

The Commission continues to accept bulk metered mail as the appropriate benchmark for determining the worksharing cost savings for First-Class Mail. The Postal Service provides evidence that at least some BMM does exist in the mailstream. The Commission also views a benchmark as a 'two-way street'. It represents not only that mail most likely to convert to worksharing, but also, to what category current worksharing mail would be most likely to revert if the discounts no longer outweigh the cost of performing the worksharing activities.

Docket No. R2000-1, ¶ 5089.

[5096] The Postal Service's de-linking proposal does not require use of a single benchmark. The proposal effectively creates two benchmarks within the Letters and

Sealed Parcels subclass. Within single-piece, the first-ounce single-piece letters rate would act as the benchmark from which all single-piece shape-based rates and related charges would flow. Within the worksharing categories, the first-ounce automation letters Mixed AADC rate would act as the benchmark from which all shape-based rates, worksharing discounts, and related charges would flow.

[5097] *APWU position.* APWU witness Kobe proposes an alternative to the Postal Service's rate design, which supports the bulk metered mail benchmark approach to developing First-Class Mail workshare mail rates.

When looking at a very heterogeneous pool of mail, such as that of First Class letters, [using the BMM letter benchmark] is the only way to make certain that two mailers with identical pieces of mail are paying the same contribution to overhead costs, irrespective of whether they workshare.

APWU-T-1 at 15. She states that it is unlikely that the mail converting to presort mail is equivalent to average collection mail, which she infers is witness Taufique's position from his proposal.

[5098] Generally, APWU argues in favor of the current practice of using a single benchmark. It contends that "use of the BMM benchmark is the appropriate way to ensure that identical pieces of mail pay identical rates for the same service." APWU Reply Brief at 7. It contests the notion that bulk metered mail does not continue to exist and the contention that there is evidence that collection mail is being converted to presort mail in significant numbers. Moreover, APWU asserts that there is no record basis in this case to adopt any benchmark other than bulk metered mail. APWU Brief at 15-21; APWU Reply Brief at 6-8.

[5099] *MMA position.* Witness Bentley contends that the appropriate benchmark is single-piece metered mail letters. He asserts that there is no basis to assume that bulk metered mail letters are the most likely mail to shift from single-piece to bulk, citing the proliferation of presort bureaus as proof that most single-piece mail that theoretically could convert already has. He believes that workshare mailers have already been

successful in converting residual mail to worksharing mail. He states that bulk metered mail severely discounts other significant mail preparation activities undertaken by workshare mailers that provide cost savings, such as sleeving, strapping, pre-labeling trays, and presorting on pallets. Finally, he notes that there are no direct CRA costs available for bulk metered mail, and proxies must be used based on metered mail letters.

[5100] Witness Bentley's preference would be to use the average cost for all First-Class Mail single-piece letters as the benchmark as witness Taufique has suggested. However, he is concerned with the perception that some portion of single-piece letters is dirty, and workshared discounts previously have not reflected cost savings due to cleanliness. Therefore, he endorses the metered mail letters benchmark, which is made up of clean single-piece letters generally sent by non-households that are normally not pre-barcoded, not properly faced, and not placed in trays. MMA-T-1, Appendix I at 2-6.

[5101] *NAPM position.* Witness Bell (NAPM-RT-1) testifies in response to assertions made by APWU witness Kobe concerning the characteristics of mail processed by the presort mailing industry and the work performed by presort bureaus. Witness Bell is the owner and chief executive officer of Access Mail Processing Services, Inc. (Access), a small to medium-sized presort bureau that processes approximately 145 thousand pieces of mail per day. She relates her experiences with the mail received by Access from its customers and describes the effort undertaken by Access to prepare the mail for delivery to the Postal Service. She concludes that the mail received by presort bureaus needs considerable processing before it can be tendered to the Postal Service. Witness Bell contends that based on her experience "the single-piece First-Class Mail most likely to convert to presort mail has the physical and cost characteristics typical of collection mail, not Bulk Metered Mail ('BMM')." She asserts that she has never seen bulk metered mail. NAPM-RT-1.

[5102] Upon cross-examination, witness Bell clarifies that she has never seen bulk metered mail coming in from a new customer. However, by the time she has educated her customers, she states that hopefully her customers are presenting Access with bulk

metered mail. She further contends that the most likely source of bulk metered mail received by the Postal Service is from presort bureaus. Tr. 38/12999-13001.

[5103] Witness Bell disagrees with witness Kobe's contention that the Commission should adopt bulk metered mail as the benchmark for calculating presort "to make certain that two mailers with identical pieces of mail are paying the same contribution to overhead costs, irrespective of whether they workshare." NAPM-RT-1 at 10, quoting APWU-T-1 at 15. Witness Bell asserts that the single-piece mail currently available to convert to presort is dirtier and more costly to process than bulk metered mail. Thus, she contends that basing discounts on the bulk metered mail benchmark will cause the average piece of presort First-Class Mail to pay a higher contribution to overhead costs than the average piece of single-piece mail. NAPM-RT-1 at 10.

[5104] *NAPM & NCCP position.* NAPM & NCCP contends that the relevant benchmark is single-piece mail at the margin of conversion. It argues that this mail has the cost characteristics of collection mail, not bulk metered mail. NAPM & NCCP Brief at 7-25; NAPM & NCCP Reply Brief at 3-10.

[5105] *OCA position.* OCA supports the use of a bulk metered mail benchmark and uses it in developing its four-ounce increment proposal. See OCA 4-Ounce Increment Proposal, subsection 3.b (below).

[5106] *Pitney Bowes position.* Witness Panzar discusses setting worksharing discounts given First-Class Mail heterogeneity.

In a recent paper, I analyzed the choice of the appropriate discount in a simple model that incorporated mail heterogeneity and one level of worksharing. The basic theoretical result was that an efficient allocation of mail processing activity between the Postal Service and mailers requires a worksharing discount equal to the average Postal Service processing cost of the type of mail just at the margin of being profitable for mailers to workshare. This suggests that the previous methodology of basing discounts based upon the avoided processing cost of mail most likely to be work-shared, is likely to lead to discounts too low to result in an efficient allocation of mail processing activity. However, the primary practical implication of my analysis was that in the presence of Postal Service mail

processing cost heterogeneity, any discount policy will lead to some mail being processed inefficiently.

PB-T-1 at 36-37 (footnote and emphasis omitted.).

[5107] *Postal Service response.* Witness Abdirahman (USPS-RT-7) contests the metered mail letters benchmark proposed by MMA witness Bentley and the rejection of the bulk metered mail benchmark by Pitney Bowes witnesses Panzar and Buc. He states that the Commission previously rejected the metered mail letters benchmark for presort letters costs, and that nothing has been added to the argument to warrant its reconsideration.

[5108] Although witness Abdirahman believes the de-linking approach is superior to using a single bulk metered mail benchmark, he notes the precedent of the bulk metered mail benchmark and the lack of field observation substantiation for the positions of the other intervenors. USPS-RT-7 at 4-6. When asked whether the Commission should continue to use a bulk metered mail benchmark if the Commission does not recommend the de-linking proposal, he states:

Yes, that's why I explained my testimony; that the BMM is still there; and I, myself, observed their existence. And if the Commission decides not to accept the de-linking proposal, the only alternative that I see is the BMM, and that's as a costing witness.

Tr. 35/11968-9; *see also* 12050-51.

[5109] *Commission analysis.* The Commission, having determined not to de-link First-Class Mail rate design, continues to use the bulk metered mail benchmark in developing worksharing rates. The Commission accepts that this benchmark is not perfect due to First-Class Mail heterogeneity and the need to use a proxy in developing bulk metered mail costs. However, the Commission finds that no better alternative to bulk metered mail has been persuasively argued on this record. The Commission continues to believe that this benchmark “represents not only that mail most likely to convert to worksharing, but also, to what category current worksharing mail would be

most likely to revert if the discounts no longer outweigh the cost of performing the worksharing activities.” Docket No. R2000-1, ¶ 5089.

e. Worksharing Mail Costs and Cost Avoidances

[5110] The Postal Service cost methodology relies on both CRA mail processing unit costs and model-based mail processing unit costs to develop mail processing unit cost estimates by rate category. This methodology generally parallels the approach taken in past cases, and is modified to accommodate the de-linking proposal.

[5111] The Postal Service explains that it has made several methodological changes from previous rate cases. The Postal Service’s models now use a single, combined CRA cost for automation and non-automation presort letters. The models no longer use bulk metered mail unit costs in the letters mail processing cost analysis. One CRA adjustment factor is used in place of the two previously used. The previous cost pool classifications: proportional, worksharing-related fixed, and non-worksharing related fixed, are replaced with proportional and fixed cost pool classifications. Thus, the distinction between worksharing-related and non-worksharing-related cost pools is eliminated. Proportional cost pools contain costs for tasks that are actually modeled and fixed cost pools represent tasks that have not been modeled. The Postal Service explains that it classifies a cost pool as proportional only when the associated mail processing activities identified within that cost pool are understood to vary in known ways by presort level.

[5112] The Postal Service also changes the way in which it produces rate category delivery unit cost estimates in this case. In the last rate case, separate delivery unit cost avoidance estimates by rate category were derived by applying delivery point sequence percentages by rate category to the delivery costs. The Postal Service rejects this methodology asserting that there is no conclusive basis for determining that the delivery point sequence percentages actually vary among machinable rate categories. The

Postal Service now contends that machinability is the one characteristic of a mailpiece that has a quantifiable impact on delivery unit costs. Thus, it does not develop distinct delivery unit costs for each rate category.

[5113] *APWU position.* APWU is opposed to the Postal Service's changes in methodology due to the de-linking proposal. Witness Kobe proposes First-Class Mail rates based on what she asserts is "the concept and general methodology that has been used by the Postal Service and the Postal Rate Commission for many years." This includes the use of the bulk metered mail letter benchmark. APWU-T-1 at 3.

[5114] Witness Kobe develops bulk metered mail benchmark and presort worksharing-related costs by approximating the methodologies used in previous rate cases. For example, she allocates costs pools into three categories: workshare-related proportional, workshare-related fixed, and non-workshare-related, and she uses non-automation presort letters for the proxy for bulk metered mail unit delivery costs. Witness Kobe uses the costs that she develops to support her position that the discounts proposed by the Postal Service (except for non-automation presort) are not justified by avoided costs.

[5115] Witness Kobe then develops rates basing discounts on avoided costs. She assumes the single-piece letter rate of 42 cents proposed by the Postal Service as a starting point. She notes that the rates that she develops in some cases result in increases 10 percentage points or more beyond the rates proposed by the Postal Service. Thus, she believes that these rates are not a viable alternative for this case because they are likely to result in rate shock, and with no other adjustments, would cause the revenue requirement to be exceeded.

[5116] Consequently, witness Kobe proposes an alternative set of rates for the Commission to consider. The alternative rates represent only a partial adjustment of the discounts towards the avoided costs, and keep the presort letter rate increases down to single-digit percentages. She suggests that the remaining adjustment should be phased in during subsequent proceedings.

[5117] In addition to her First-Class Mail letters proposal, witness Kobe proposes lowering the single-piece flat rate proposed by the Postal Service to maintain a 20-cent differential between flats and letters. She proposes lowering the single-piece parcel rate proposed by the Postal Service to mitigate rate shock, and she also readjusts the rate difference between presort letters and flats. She does not propose changes to the rates proposed by the Postal Service for business parcels. Witness Kobe estimates that revenues as a result of her proposals are virtually unchanged from those proposed by the Postal Service.

[5118] *GCA position.* GCA does not comment on the Postal Service's rate design methodology, but instead criticizes the unit contributions that result from the Postal Service's proposals. Witness Clifton proposes an increase in the unit contribution made by Standard Regular mail sufficient to reduce the rate increase on First-Class single-piece letters from 42 cents to 41 cents. If First-Class Mail rate design remains "linked," he further proposes reducing each first-ounce letter workshare rate by one cent. If the Commission recommends the de-linked approach to First-Class Mail rate design, he proposes the workshare rates proposed by the Postal Service. GCA-T-1 at 59.

[5119] Witness Clifton's rate proposals are based on his criticisms of Postal Service witness Thress's elasticity analysis. Witness Clifton contends that "witness Thress' approach to competing substitutes in his First-Class single-piece demand equation fails to capture the impact of the Internet on single-piece mail, especially its impact on alternative electronic bill payment methods to the mail." *Id.* at 49.

[5120] Witness Martin presents testimony on competitive substitutes to First-Class Mail letters, particularly those involving the rendering of billing statements and the process for their payment. His testimony incorporates research and analysis from multiple sources and includes analysis and conclusions drawn from two national telephone surveys of customers and small businesses, and from a series of interviews with firms involved in the billing process. In summary, witness Martin concludes that postal rate increases will likely have a significant impact on the diversion of payment and statement mail, which will be applicable to both businesses and consumers. He

contends that postal rate increases are a “triggering device” that causes consumers and businesses to examine and turn to the competitive electronic alternatives for First-Class Mail. GCA-T-2 at 2. His presentation is more fully reviewed in Appendix I.

[5121] Witness Clifton’s independent analysis indicates that in the face of Internet diversion, the elasticity of Standard Regular mail is becoming more inelastic and the elasticity of First-Class single-piece mail is becoming less inelastic. He notes that the elasticity of Standard Regular mail is less than his estimate for single-piece First-Class Mail letters. GCA-T-1 at 54.

[5122] He asserts that volume growth is healthy for Standard Regular, unlike that for single-piece First-Class Mail letters, and his elasticity estimate indicates that Standard Regular can absorb higher rate increases than those proposed by the Postal Service. He states that “[i]t is in many instances self-defeating for the Postal Service to raise First-Class single piece rates at this time.” *Id.* at 3. The conclusion witness Clifton draws, and the underlying basis of his 41-cent first-ounce single-piece First-Class Mail rate proposal, is that Standard Regular mail should be looked to first as a source of extra revenue when there is a general revenue deficiency, and single-piece First-Class Mail letter should be looked to last. *Id.* at 3, 58.

[5123] *DMA position.* Because of the availability of alternative marketing channels for mailers that utilize Standard Mail and their marketing decision process, witness Buc (DMA-RT-1) does not agree with GCA witness Clifton’s estimates of elasticity for First-Class Mail and his contention that Standard Regular Mail is becoming increasingly inelastic because of Internet diversion. Witness Buc discusses various marketing channels available to Standard Mailers in general, and banks in particular. The alternative marketing channels, he contends, have important ramifications on elasticity. Witness Buc explains that while the Internet is an alternative for bill payment, marketers and advertisers also are more frequently using the Internet. He further explains that marketing mailers make marketing decisions based on what is cost effective. Thus, he asserts that witness Clifton’s suggestion that the Internet could result in demand for

single-piece First-Class Mail becoming more elastic, while Standard Mail becomes less elastic, is counterintuitive. See DMA-RT-1.

[5124] *MMA position.* Witness Bentley supports the specific workshare rates proposed by the Postal Service under de-linking. However, he asserts that the Postal Service's cost methodology improperly disregards important cost differences. Thus, he independently develops cost savings estimates, and concludes that his methodology provides even more support for the Postal Service's discount proposals than provided by using the Postal Service's cost savings methodology. He separately derives mail processing cost savings and delivery cost savings, and then combines both to derive total workshare-related cost savings. MMA-T-1 at 5-19, Appendix I.

[5125] Witness Bentley's mail processing cost savings estimates use PRC attributable costs, and an attributable cost methodology that generally assumes 100 percent cost variability. He uses metered mail letters as a benchmark, and he re-classifies cost pools into modeled and proportional, nonmodeled but proportional, and nonmodeled and fixed categories. He assumes that there are no non-workshare-related cost pools. He uses a method similar to what the Postal Service uses in combining CRA-derived unit costs for automation and non-automation letters, and uses mail flow models to de-average the combined presort level costs into separate automation and non-automation estimates. Unlike the Postal Service, he uses separate CRA adjustment factors for non-automation and automation. Finally, he uses DPS percentages that vary with presort level.

[5126] To estimate delivery cost savings due to worksharing, he estimates unit delivery costs for each presort level and then compares them to a non-workshared letter-shaped benchmark. He relies on the Postal Service's delivery cost study that derives unit costs by shape. The estimation process includes removal of collection costs from single-piece delivery costs, de-averaging single-piece letter delivery costs into stamped, metered, and other categories, using an "all single piece letters combined" benchmark, de-averaging automation delivery costs into presort categories, and derivation of delivery costs per delivered letter. *Id.* at 21.

[5127] Combining the mail processing cost savings and the delivery cost savings, witness Bentley asserts that his estimates show greater costs savings both on an absolute and on an incremental basis than the cost savings developed by the Postal Service. Using his estimate of costs savings, he calculates passthroughs for each rate category on both an aggregate and an incremental basis, and shows that in each case the passthroughs are less than 100 percent. From this, witness Bentley concludes that the Postal Service's discount proposals are justified.

[5128] MMA sponsors the testimonies of witnesses McCormack and Gorham in opposition to the proposals presented by APWU and OCA.

[5129] Witness McCormack (MMA-RT-1) is employed by Verizon Corporate Services Corp. She contends that adoption of APWU's approach to setting First-Class Mail worksharing discounts will have an adverse impact on First-Class presort mailers and the Postal Service. She asserts that reducing workshare discounts, as would happen through adoption of APWU's proposals, would disrupt the First-Class workshare mail industry. MMA-RT-1.

[5130] Witness McCormack explains that Verizon primarily uses First-Class Mail to invoice customers, including use of pre-barcoded Courtesy Reply Mail envelopes to expedite return of payment. Her testimony outlines the steps Verizon takes to mail approximately 40 million mailpieces per month, including additional tasks undertaken by Verizon that save the Postal Service costs but that are not specifically reflected in the discounts.

[5131] Witness McCormack estimates that the discounts proposed by APWU will lead (in two stages) to discounts 34 percent lower on average than the discounts proposed by the Postal Service. She estimates that APWU's discounts also are 28 percent lower on average than the discounts currently in effect. She contends that the reduced discounts "will greatly change the dynamics of worksharing and the monetary benefits earned by mailers." *Id.* at 9. She further asserts that the lower discounts proposed by APWU "will severely curtail Verizon's incentive and ability to fund its

worksharing program.” *Id.* at 10. Thus, she opposes adoption of APWU’s proposals, and supports the Postal Service’s discount proposals which increase discounts.

[5132] Witness Gorham (MMA-RT-2) is the Manager, Postal Services for CSG (CSG) Systems, Inc. He explains that CSG is a provider of outsourced billing, customer care, and print and mail solutions and services supporting the North American converged broadband and direct broadcast satellite markets. He states that CSG utilizes First-Class Mail to send tens of millions of monthly statements. The billing statements include Courtesy Reply Mail envelopes. Witness Gorham explains the investment made by CSG in its mailing operations, and the steps CSG takes in preparing its mail. He states that CSG also provides its customers with alternative electronic bill presentation and payment solutions. MMA-RT-2 at 2-4.

[5133] Witness Gorham estimates that the worksharing discounts proposed by APWU would be 17 to 20 percent lower than the discounts proposed by the Postal Service. He comments that the discounts proposed by the Postal Service essentially maintain existing rate relationships. However, the discounts proposed by APWU “would disrupt these existing rate relationships and severely strain the equilibrium that both the Postal Service and workshared mailers have worked so hard to attain,” and “send entirely the wrong signal to First-Class workshare mailers such as CSG about the value of their worksharing efforts.” *Id.* at 8. He states that his conclusions about the adverse consequences of adopting APWU’s proposal also apply to OCA’s proposal. *Id.*

[5134] MMA believes that APWU’s alternative rate proposal is “patently irresponsible” for moving discount levels back to those that existed more than a decade ago, and for being “technically flawed.” MMA contends that the likely volume impact of the proposal has not been studied and criticizes the proposal for using the Postal Service’s attribution cost methodology instead of the Commission’s attribution cost methodology. MMA concludes that the proposal disregards the likely impact on presort mailers and the postal system in general. MMA Presort Brief at 47-55.

[5135] *Pitney Bowes position.* Witness Buc contends that the cost avoidance estimates presented by the Postal Service are flawed because they understate

workshare-related cost avoidance estimates, and are inadequate to develop rates using Efficient Component Pricing. He independently develops estimates of cost avoidances, and presents rates for automation letters that he argues balance important policy objectives, better comport with Efficient Component Pricing, and satisfy the rate-setting factors of the Act. *See* PB-T-2.

[5136] Witness Buc first discusses improvements the Postal Service has made to its cost methodology. He approves of the approach to combining the non-automation and automation letter IOCS costs, and de-averaging the combined First-Class Mail presort letter costs with the Postal Service's cost model. He approves of reclassifying certain worksharing-related fixed cost pools as proportional, and asserts that this has improved the cost model. Finally, he approves of the Postal Service's proposal to de-link presort rates from single-piece rates. *Id.* at 10-12.

[5137] However, he criticizes the Postal Service for removing delivery costs from its cost model. He does not find the Postal Service's explanation compelling, and states that excluding delivery unit costs is inconsistent with the approach it uses to measure mail processing cost avoidances for the automation rate categories. *Id.* at 12-13.

[5138] Buc contends that the chief deficiency in the Postal Service's cost model is the improper classification of cost pools. The Postal Service shows 14 cost pools as proportional, representing 64.7 percent of mail processing costs, and 49 cost pools as fixed, representing 35.3 percent of mail processing costs.

[5139] Witness Buc asserts that the Postal Service provides no evidence that cost pools classified as fixed actually are fixed with respect to presort level. Thus, he independently reviews each cost pool and classifies it as either proportional or fixed. He classifies a cost pool as proportional if he determines that the Postal Service has classified it as proportional, the pool is anomalous, or operational and mail flow analysis shows the pool to be proportional. He apparently classifies a cost pool as fixed if he determines that the operational analysis absolutely shows it to be fixed, or the available data were not sufficient to complete an operational analysis. Witness Buc concludes from his analysis that 52 cost pools are proportional, representing 90.4 percent of costs,

and 11 are fixed, representing 9.6 percent of costs using the PRC methodology. *Id.* at 13-31.

[5140] He assumes that the costs of the newly classified proportional pools vary among presort levels in exactly the same way as do the modeled pools, which he asserts is consistent with the attribution and distribution theory of the Postal Service. He then calculates costs, cost avoidances, and passthroughs for automation letter mail, both with and without delivery cost avoidance estimates. He states that his calculations use PRC volume variability and delivery unit costs and cost avoidance from USPS-LR-L-147. From his analysis he concludes that the Postal Service's calculated cost avoidances are inappropriately small, and the true cost avoidances are substantially larger. *Id.* at 31-32.

[5141] Witness Buc develops Efficient Component Pricing rates based on his estimates of cost avoidances. He determines that fully-Efficient Component Pricing rates produce less revenue compared with the Postal Service's rate proposal. Thus, he adopts the 33.1 cent 3-digit rate proposed by the Postal Service as a starting point, and passes through a uniform 100 percent of the cost avoided to develop alternate rates. He calculates that these rates result in \$39 million of revenue leakage when compared with the Postal Service's proposal.

[5142] *ABA position.* ABA opposes the APWU, GSA, and OCA alternative rate design proposals. It argues that the interests of single-piece mailers have been more than adequately accounted for, *e.g.*, by offering the Forever Stamp, and opposes proposals that would further lower or favor rates for single-piece mailers. ABA contends that raising the rates on bulk First-Class Mail would have an adverse effect on volumes and revenue. It further argues that the Commission should recognize "non-cost avoided" cost differences in First-Class Mail as it does in Periodicals and Standard Mail. Finally, it contends that higher rates would have an adverse effect on the price sensitive advertising component of First-Class Mail. ABA Brief at 21-24.

[5143] ABA submits that the First-Class Mail 3-digit automation letters passthrough should be set at 100 percent. ABA contends that the Postal Service has set the passthrough at 80 percent, assuming the Postal Service's proposed rates and the

Commission's costing methods. It states that 3-digit automation letters is a major market component within the First-Class Mail business mailstream, with projected after rates volume of 23 billion pieces or 48 percent of First-Class presort letter mail. Thus, ABA contends that "it is especially important that this mail be priced efficiently to reduce the overall cost of mail service to society." *Id.* at 28. ABA notes that a 100 percent passthrough is consistent with Efficient Component Pricing, and argues that the other factors of the Act do not justify a deviation from a 100 percent passthrough. *See* ABA Trial Brief; ABA Brief at 28-31.

[5144] *NAPM & NCCP position.* NAPM & NCCP argue that the Postal Service repeatedly underestimates presort cost avoidances, in part, because of its failure to model all cost pools affected by the degree of presortation. NAPM & NCCP note that APWU witness Kobe and OCA witness Thompson only adopt limited changes to the cost pool classifications developed by the Postal Service. In contrast, NAPM & NCCP contend that the presort cost avoidance estimates developed by Pitney Bowes witness Buc and MMA witness Bentley are well supported. NAPM & NCCP state that witness Buc's comprehensive new analysis shows that many of the pools not modeled by the Postal Service in fact contain costs that vary with presort level and thus should be classified as proportional, and that witness Bentley has arrived at similar conclusions. NAPM & NCCP Brief at 26-28.

[5145] NAPM & NCCP conclude that a comparison of the cost avoidances developed by witnesses Buc and Bentley with the presort discounts proposed by the Postal Service demonstrates that the proposed discounts are reasonable, and quite conservative. *Id.* at 28-29.

[5146] *Postal Service reply.* The Postal Service opposes APWU witness Kobe's rate design proposal. Witness Taufique comments that witness Kobe's proposed discounts pass through greater than 100 percent of cost avoidance at each presort level. He criticizes witness Kobe for not articulating reasons for these choices of passthroughs. He states that it seems unfair that Kobe proposes the highest rate increases, and the highest implicit cost coverage for the finest presort mail within the subclass, which has

had some of the lowest cost increases over nine years. He asserts that this sends the wrong price signals and would encourage a reduction in automation compatible mail and an increase in non-automation presort mail volume. Witness Taufique also discusses the bulk metered mail benchmark used by APWU. He asserts that bulk metered mail certainly is representative of one type of mail that is a candidate for migration from single-piece to presort, but he contends there also are other types of single-piece mail that are potential candidates for conversion. USPS-RT-18 at 1-9.

[5147] The Postal Service criticizes the APWU proposal for failing to consider many of the factors that the Postal Service must consider when designing rates, and for over-emphasizing economic efficiency. It contends that APWU's proposal results in greater-than-average price increases for a customer group (presorted First-Class Mail customers) that has perhaps the most stable costs. Postal Service Brief at 219-22.

[5148] The Postal Service opposes the GCA proposal asserting that it relies on a "fatally flawed" economic model. See discussion of elasticities, Appendix I. The Postal Service further contends that GCA does not adequately consider other ratemaking factors, but focuses only on value of service as measured by elasticities. The Postal Service asserts that GCA fails to recognize that Standard Mail Regular already bears an above-average percentage increase under its proposal, and that a further increase is not warranted. *Id.* at 222-25.

[5149] Witness Abdirahman disagrees with the cost pool classifications proposed by Pitney Bowes witness Buc and MMA witness Bentley. He also disagrees with OCA witness Thompson's use of separate auto and non-auto cost pool classifications based on USPS-LR-L-141 in support of her proposals. He believes that the Postal Service cost pool classifications in this docket are consistent with previous Commission recommended classifications, and that they accurately reflect the costs that may be modeled to reflect differences in costs among presort levels. USPS-RT-7 at 9-12.

[5150] Witness Abdirahman explains that cost pools are classified as proportional because the activities, and the costs thereof, captured within those cost pools are understood to vary in known ways with the presort level. *Id.* at 10-11. He comments that

witness Buc classifies the vast majority of cost pools as proportional without providing supporting evidence, and that witness Bentley's approach also classifies most cost pools as proportional. He contends this results in a distortion of the cost relationships between rate categories.

[5151] Witness Abdirahman contests the use of delivery costs estimates by MMA, Pitney Bowes, APWU, and OCA because he believes that there are not reliable data indicating that delivery unit costs differ by presort category. He states that "[s]eparate delivery unit cost estimates by rate category are no longer provided because there is no conclusive evidence to suggest that the DPS percentages actually vary among the machinable rate categories." *Id.* at 6-9.

[5152] Witness Abdirahman rebuts the MMA criticism of the Remote Bar Code System (RBCS) stating that Postal Service data show that the system has consistently improved over time. He explains that when first employed in 1992, the finalization rate was 25 percent. It is now approaching 80 percent. He contends that witness Bentley's criticisms about how certain RBCS costs are over- or under-stated inappropriately relies on dissecting RBCS costs at the component level. Witness Abdirahman argues that when costs are examined at the operational level, the model's under- or over-statement of costs is not clear-cut. Finally, witness Abdirahman is critical of witness Bentley's use of the bulk metered mail CRA unit cost data to make adjustments to non-automation presort letters costs because it has not been previously used by either the Commission or the Postal Service, and it relies on unsupported assumptions that the RBCS costs are unreliable. *Id.* at 15-18.

[5153] Witness Robinson generally criticizes the alternative rate proposals put forth by APWU and GCA for not adequately considering the impact of their proposals on other ratepayers. Furthermore, she contends that APWU and GCA have not adequately considered all of the factors of the Act in their proposals. USPS-RT-10 at 1-15.

[5154] *Commission analysis.* For the reasons explained above, the Commission retains the use of a "linked" approach to rate design, and it continues to view the bulk

metered mail benchmark as the appropriate starting point for the estimation of cost avoidances.

[5155] The Commission also finds it appropriate to continue the practice of including estimated delivery costs by rate category in the calculation of cost avoidances for discounted letter rates. Differences in delivery costs between letter categories arise from differences in the percentage of each category that are sorted in automated Delivery Point Sequencing (DPS) operations. The Postal Service asserts that the use of average acceptance rates in the mail flow models yields misleading DPS percentages by rate category because pieces are very likely to be successfully processed on downstream operations after they have been successfully processed once.

[5156] The validity of this argument is undermined by the existence of significant non-zero reject rates for the second pass of the two-pass automated incoming secondary sort which, by definition, consists of mail that has been successfully sorted on automation equipment at least once. Also, it would be inconsistent to find that the use of average acceptance rates produce reliable estimates of mail processing unit costs, but the same acceptance rates produce unreliable DPS percentages for use in calculating unit delivery costs. The two outputs of the models are both dependent on the same inputs, including acceptance rates.

[5157] The inclusion of delivery costs in the estimates of cost avoidances for letters requires the selection of a delivery cost proxy for the bulk metered mail benchmark. The Commission accepts the use of the estimated delivery costs of non-automation machinable Mixed AADC (NAMMA) letters as a proxy.

[5158] Significant empirical differences in the cost of casing non-DPS single-piece letters and presort letters exist, but these differences are due to characteristics unrelated to worksharing. The only delivery cost differences that are appropriately ascribed to worksharing are those caused by the DPS percentage differences that result from machinability and presort level. Worksharing by a mailer can, through improved DPS percentages, avoid casing costs by avoiding casing. However, the record does not provide evidence that worksharing activities affect the casing costs of mail that must be

cased (i.e., non-DPS mail). The mail flow models estimate the same DPS percentage for bulk metered mail and for NAMMA. Therefore, using the delivery costs of NAMMA as a proxy for bulk metered mail properly isolates the worksharing related delivery cost savings.

[5159] The Commission accepts the use of a single CRA cost estimate that combines the costs of non-automation and automation presort. The use of the bulk metered mail benchmark, which has a separate CRA cost estimate, leads the Commission to retain the system of classifying MODS pool costs into three groups (proportional, worksharing-related fixed, and non-worksharing related). The Commission employs an approach to assigning costs to the three groups that falls between the Postal Service proposal and the analysis proposed by Pitney Bowes.

[5160] The Commission finds the Postal Service's assumption that the cost of non-modeled operations are not affected by worksharing to be insufficiently supported. The majority of the costs that MMA and Pitney Bowes claim are inappropriately treated as fixed are in mail processing activities that support other mail processing activities, including piece sortation. It is reasonable to assume that these supporting costs are at least indirectly affected by worksharing.

[5161] In the letter mail processing cost model, the Commission assigns the letter sorting cost pools as proportional, consistent with the Postal Service and intervenors.⁹¹ The pools that witness Buc assigns as fixed are assigned as either worksharing-related fixed or non-worksharing related, as appropriate.⁹² The remaining costs, which are largely allied and support costs, are distributed to the three groups in the same proportions as the directly assigned pools. The allied and support pools support all mail processing operations, and so it is reasonable to assume that they are affected by

⁹¹ Similarly, the flat sorting operations are treated as proportional in the flat mail processing cost model.

⁹² Pools associated with mailgrams and special services are non-worksharing related.

worksharing to the same extent as the proportional and fixed operations they support. The cost avoidances for First-Class letters are presented in PRC-LR-12.

2. Letters and Sealed Parcels Rates and Classifications

[5162] The Letters and Sealed Parcels subclass consists of First-Class Mail weighing 13 ounces or less that is not mailed within the Cards or Priority Mail subclasses.

[5163] Table V-1 presents a comparison of current, proposed and recommended First-Class Mail Letters and Sealed Parcels rates.

Table V-1
Summary of Rates for First-Class Mail Letters and Sealed Parcels

	Current	Proposed	Recommended
LETTERS AND SEALED PARCELS			
Single Piece			
First Ounce	39.0¢	N/A	N/A
First Ounce - Letters	N/A	42.0¢	41.0¢
First Ounce - Flats	N/A	62.0¢	80.0¢
First Ounce - Parcels	N/A	100.0¢	113.0¢
Additional Ounces	24.0¢	20.0¢	17.0¢
Nonmachinable Surcharge	13.0¢	N/A	17.0¢
Qualified Business Reply Mail	35.8¢	39.5¢	38.0¢
Presorted			
First Ounce	37.1¢	N/A	N/A
First Ounce - Letters	N/A	40.0¢	37.3¢
First Ounce - Flats	N/A	51.9¢	69.9¢
Additional Ounces	23.7¢	20.0¢	17.0¢
Nonmachinable Surcharge	5.8¢	N/A	17.0¢
Heavy Piece Deduction	4.3¢	N/A	N/A
Automation Letters			
Mixed AADC Letters	32.6¢	34.6¢	36.0¢
AADC Letters	31.7¢	33.5¢	34.1¢
3-Digit Letters	30.8¢	33.1¢	33.4¢
5-Digit Letters	29.3¢	31.2¢	31.2¢
Carrier Route Letters	29.0¢	N/A	N/A
Additional Ounces	23.7¢	15.5¢	12.5¢
Heavy Piece Deduction	4.3¢	N/A	N/A
Automation Flats			
Mixed ADC Flats	35.9¢	46.5¢	68.6¢
ADC Flats	35.1¢	43.3¢	56.7¢
3-Digit Flats	33.9¢	42.3¢	48.4¢
5-Digit Flats	31.8¢	39.8¢	38.3¢
Additional Ounces	23.7¢	20.0¢	17.0¢
Nonmachinable Surcharge	5.8¢	N/A	N/A
Heavy Piece Deduction	4.3¢	N/A	N/A
Business Parcels			
ADC Business Parcels	N/A	72.7¢	89.1¢
3-Digit Business Parcels	N/A	71.7¢	83.7¢
5-Digit Business Parcels	N/A	64.3¢	70.4¢
Additional Ounces	N/A	20.0¢	17.0¢
Nonmachinable/Non-barcoded (ADC and 3-Digit) Surcharge	N/A	5.0¢	5.0¢

a. Single-Piece Rate Design

[5164] The current rate schedule provides one rate, 39 cents, for the first ounce of single-piece letters, flats, and parcels. A nonmachinable surcharge of 13 cents also is applicable to mailpieces weighing less than one ounce that can not be readily handled by letter sorting machines. For administrative ease, and to avoid unnecessary complexity, the Postal Service proposes retail rates in whole cent increments. USPS-T-32 at 21-24.

[5165] As part of its shape-based rates proposal, the Postal Service proposes individual rates for each shape of mailpiece. The Postal Service proposes a letter rate of 42 cents, a flat rate of 62 cents, and a parcel rate of 100 cents. Witness Taufique explains that the flat rate is designed to pass through 55 percent of the 37.1 cent estimated cost difference between a single-piece letter and a single-piece flat. He also explains that the parcel rate is designed to pass through 50 percent of the 117.0 cent estimated cost difference between a single-piece letter and a single-piece parcel. He selected percentage passthroughs to mitigate the rate impact on lighter weight flat- and parcel-shaped mailpieces.

[5166] *Commission analysis.* The Commission recommends shape-based rates. The Commission ties all piece rates to a single-piece first-ounce letter rate of 41 cents. This is accomplished through a process that generally adheres to Efficient Component Pricing, uses a single bulk metered mail benchmark, and balances all factors of the Act. Because of the rate relationships that this process creates, the 41-cent rate is selected to meet the revenue goals of First-Class Mail. A higher rate would cause the First-Class Mail subclass to exceed its revenue goal, and would generate excess revenue. For example, a 42-cent rate would generate more than \$750 million of additional contribution.

[5167] The single-piece flat and parcel rates are developed by estimating average mail processing and delivery unit cost differences between a single-piece letter and a single-piece flat, and between a single-piece flat and a single-piece parcel. Adhering to Efficient Component Pricing and setting rates close to 100 percent of the cost difference

would result in a rate of 80 cents for a one-ounce single-piece flat, and 164 cents for a one-ounce single-piece parcel. This would represent a 54 percent increase for a one-ounce single-piece flat, and a 215 percent increase for a one-ounce single-piece parcel.⁹³ The Commission recommends the 80-cent first-ounce single-piece flat rate. However, the Commission believes that a 215 percent increase for parcels is excessive especially as this is a new rate classification, and that further experience should provide more accurate cost and volume information. Thus, the Commission recommends passing through 40 percent of the cost difference, and recommends a first-ounce rate of 113 cents for single-piece parcels.

b. Non-automation Presort Rate Design

[5168] The current rate schedule provides one rate, 37.1 cents, for the first ounce of non-automation presort letter-, flat-, and parcel-shaped mail. A nonmachinable surcharge of 5.8 cents also is applicable to mailpieces weighing less than one ounce that can not be readily handled by letter sorting machines. A heavy piece discount of 4.3 cents is applicable to certain mailpieces weighing more than two ounces.

[5169] As part of the shape-based rates proposal, the Postal Service proposes individual rates for letter- and flat-shaped mailpieces within non-automation presort. It proposes to eliminate eligibility of parcel-shaped mail from non-automation presort, as a portion of this mail is expected to migrate to the newly-proposed business parcels category. It also proposes to change the presort requirement for machinable letters in this category from 3-digit to AADC sortation. *Id.* at 19-20, 37-38.

[5170] Witness Taufique explains that he proposes a letter rate to preserve the rate relationship between non-automation presort letters and single-piece letters, and between non-automation presort letters and Mixed AADC automation letters. He passes

⁹³ Currently single-piece flats and parcels weighing one ounce or less pay a surcharge of 13 cents. That charge will be eliminated. Reduction of the additional ounce rate from 24 cents per ounce to 17 cents per ounce eases the impact of shape-based rates on heavier pieces.

through 290 percent of the 1.866 cent cost difference between non-automation machinable letters and automation letters Mixed AADC (the de-linking benchmark) and proposes a non-automation presort letter rate of 40.0 cents.

[5171] Witness Taufique proposes a 51.9-cent rate for non-automation presort flats. He explains that this rate is derived by adding 11.9 of the 30-cent cost difference to process and deliver a presort flat versus a presort letter to the automation letters Mixed AADC rate.

[5172] *Commission analysis.* The Commission recommends elimination of parcel-shaped mail from non-automation presort, and changing the presort requirement for machinable letters in this category from 3-digit to AADC sortation as proposed by the Postal Service. Neither proposal was opposed by any participant in this rate case. The parcel-shaped mail that would have been mailed in the non-automation presort category can be mailed either as single-piece or within the new business parcels category.

[5173] The estimated cost avoidance for machinable non-automation presort letters is 5.6 cents. Increasing the discount to fully reflect the avoided costs would represent a very large change from the current 1.9-cent discount. To mitigate the potential disruptions, the Commission recommends a discount of 3.7 cents. This discount is halfway between the current discount and the full 5.6-cent estimated cost avoidance, and results in a recommended rate of 37.3 cents for non-automation presort letters.

[5174] The rate for non-automation presort flats is developed by first estimating the unit mail processing and delivery cost difference between an average presort letter and an average presort flat. Then, 100 percent of this cost difference is added to the rate for non-automation presort letters. The result is the recommended rate of 69.9 cents for non-automation presort flats.

c. Automation Letters Rate Design

[5175] The automation letters category includes five rate tiers: Mixed AADC, AADC, 3-digit, 5-digit, and carrier route.

[5176] The Postal Service proposes the elimination of the carrier route rate tier from the automation letters category. Witness Taufique explains that the volume of this rate tier has declined by more than 16 percent over the last two years because fewer delivery units have Carrier Sequence Bar Code Sorter (CSBCS) equipment, and the discount has decreased. He asserts that presortation to the carrier route level has little or no value to the Postal Service, given that the current and future processing of letter-shaped mail requires delivery point sequencing at destinating processing and distribution centers. He further explains that this mail will migrate to 5-digit when the remaining CSBCS equipment is removed. He contends that elimination of the rate tier will not cause a large rate impact, and that any rate impact will be mitigated for mailers that have used carrier route by the greater than 100 percent passthrough proposed for 5-digit automation letters. USPS-T-32 at 20-21.

[5177] Witness Taufique adopts an automation letters Mixed AADC benchmark developed within the framework of presort workshare mail consistent with the Postal Service's de-linking proposal. He uses neither the bulk metered mail benchmark, nor the first-ounce single-piece rate in the development of rates for automation letters. *Id.* at 29-33.

[5178] He explains that he proposes discounts and rates to balance several goals, including: achieving the cost coverage target; recognizing the value of worksharing; avoiding unduly disruptive rate impacts; acknowledging the importance of mailer barcoding and presortation; and recognizing that automation letters are a low-cost, high-contribution mailstream. He estimates costs savings between the Mixed AADC, AADC, 3-digit, and 5-digit rate tiers, and passes through 100 percent, 100 percent, and 146 percent respectively of the estimated cost savings to arrive at rates. He explains that the 146 percent passthrough selected for the 5-digit discount is meant to mitigate the rate impact on 5-digit mailers and on mailers that use the carrier route rate tier that he proposes to eliminate. His proposal results in rates of 34.6 cents for Mixed AADC, 33.5 cents for AADC, 33.1 cents for 3-digit, and 31.2 cents for 5-digit.

[5179] *Commission analysis.* Although the Commission believes that cost savings can still be realized by preparing mail at the carrier route level, no participant offers support for retaining this rate tier. The proposal is consistent with the Postal Service's stated goal of transferring incoming secondary distribution to DBCS equipment, even though it is unclear when the Postal Service plans to take the remaining CSBCS equipment out of service. Tr. 11/3021. The Commission recommends elimination of the carrier route rate tier from the automation letters category.

[5180] The Commission recommends automation letters rates which adhere to the principles of Efficient Component Pricing by passing through 100 percent of avoided costs subject to a 0.1-cent rounding constraint. The cost avoidances are referenced to a bulk metered mail benchmark. The Commission recommends automation letter rates of 36.0 cents for Mixed AADC, 34.1 cents for AADC, 33.4 cents for 3-digit, and 31.2 cents for 5-digit.

d. Automation Flats Rate Design

[5181] There are four rate tiers within automation flats: Mixed ADC, ADC, 3-digit, and 5-digit. Witness Taufique estimates that average presort flats costs 30 cents more to process and deliver than letters. He adds 40 percent of this cost difference (11.9 cents) to the proposed automation letters Mixed AADC rate (the de-linking benchmark) to arrive at his proposed 46.5-cent rate for automation flats Mixed ADC. He then estimates costs differences between the Mixed ADC, ADC, 3-digit, and 5-digit rate tiers, and judgmentally passes through 44 percent, 20 percent, and 40 percent respectively of the estimated cost savings to arrive at rates. He proposes rates of 46.5 cents for Mixed ADC, 43.3 cents for ADC, 42.3 cents for 3-digit, and 39.8 cents for 5-digit. *Id.* at 33-34.

[5182] *Commission analysis.* The Commission recommends automation flats rates which generally adhere to the principles of Efficient Component Pricing by passing through 100 percent of avoided costs subject to a 0.1-cent rounding constraint. The Commission estimates the unit mail processing and delivery cost difference between an

average presort letter and an average presort flat. It then adds 100 percent of this cost difference to the automation letters Mixed AADC rate in developing the recommended Mixed ADC rate. The Commission further estimates mail processing cost avoidances between each subsequent rate tier and passes through 100 percent of these costs differences. The Commission recommends automation flats rates of 68.6 cents for Mixed ADC, of 56.7 cents for ADC, 48.4 cents for 3-digit, and 38.3 cents for 5-digit.

e. Business Parcels Rate Design

[5183] The Postal Service proposes the creation of a new business parcels rate category with three rate tiers: ADC, 3-digit, and 5-digit. Mailings would have to contain a minimum of 500 pieces. Bulk-entered pieces that do not meet the machinability criteria for letters or flats may qualify as business parcels. The dimensions of business parcels are limited to mailpieces that are 3.5 to 18 inches in length, 3 to 15 inches in height, and 0.05 to 22 inches in width. USPS-T-32 at 19-20, 36-37.

[5184] Witness Taufique proposes an ADC rate of 72.7 cents, a 3-digit rate of 71.7 cents and a 5-digit rate of 64.3 cents. He develops the ADC rate by adding 15 percent of the average cost difference between a parcel and an automation letter mailpiece to the proposed automation letters Mixed AADC rate. He judgmentally develops the 3-digit and the 5-digit rates by passing through 10 percent and 28 percent respectively, of the estimated cost savings between rate tiers. *Id.* at 36-37.

[5185] The Postal Service also proposes a 5-cent nonmachinable surcharge for ADC and 3-digit business parcels that do not exhibit a 5-digit barcode, that are less than 2 ounces, or are nonmachinable on the Automated Package Processing System equipment. *Id.* at 20.

[5186] *Commission analysis.* The Commission recommends the creation of the business parcels rate category, including the creation of the ADC, 3-digit, and 5-digit rate tiers, and the 5-cent nonmachinable surcharge.

[5187] To recommend rates for this new category, the Commission estimates the mail processing and delivery cost differences between an average presort flat and an average presort parcel. Forty percent of this cost difference is added to the automation flat Mixed ADC presort rate in developing an intermediate (not recommended) Mixed ADC rate. The Commission then estimates mail processing cost avoidances between each subsequent rate tier and passes through 33 percent of these costs differences. The Commission recommends business parcels rates of 89.1 cents for ADC, 83.7 cents for 3-digit, and 70.4 cents for 5-digit.

[5188] Business parcels is a new rate category with limited available cost and volume information. Thus, the Commission recommends rates that pass through less than 100 percent of avoided costs. The selection of passthroughs also takes into consideration the need to maintain logical rate relationships with flats rates. The Commission expects the Postal Service to develop accurate cost and volume data for this category so that future rates can more closely track costs.

f. Additional Ounce Rate Design

[5189] The additional-ounce rate for non-automation presort, automation letters and automation flats currently is 23.7 cents. Single-piece has a 24 cent additional-ounce rate, and business parcels as a new classification has no existing rate.

[5190] The Postal Service proposes a uniform additional-ounce rate of 20 cents for single-piece, non-automation presort, automation flats, and business parcels, and a 15.5-cent rate for automation letters. Witness Taufique justifies the lower rate for automation letters by asserting that shape is not an issue in this category because all mailpieces meet the letter dimension requirements including the aspect ratio, and the 3.5 ounce maximum weight requirement. USPS-T-32 at 4-5, 25, 38-39; Postal Service Brief at 205-6, 214.

[5191] Witness Taufique explains that traditionally additional-ounce rates were used as a mechanism to reflect costs caused by weight, and indirectly shape. The additional-ounce rate also is an important source of revenue, and is used as a tool to manage the overall revenue requirement of First-Class Mail. With the shape-based rate proposal, the costs associated with shape are partially being recognized in the one-ounce rates. Thus, the cost-causing characteristics of shape recovered through the additional ounce can be reduced, allowing for lower rates.

[5192] *ABA position.* ABA supports the Postal Service's assessment that the additional-ounce rate should be lowered and argues that rates generally should track costs. It asserts that lowering the additional-ounce rate takes away the incentive for mailers to "mail to one ounce" as described by witness Resch (DFS & MSI-T-1 at 3-6) and also could ameliorate the diversion of bulk First-Class Mail to electronic delivery. ABA Brief at 18-20; *see also* Discover Brief at 1.

[5193] *DFS & Morgan Stanley position.* Witness Resch testifies in support of the Postal Service's proposal to reduce the additional-ounce rate. Her testimony is intended to provide perspective on the potential impact of the Postal Service proposal on industry. She states that DFS has always managed its mail to one ounce because of the high price of First-Class additional ounces. She argues that lowering the additional-ounce rate will create business opportunities that should result in a transformation of the nature of DFS's mailing statements by adding a significant marketing component to the mailings. Mailers will be able to enclose one or more marketing pieces with their statements resulting in greater use of heavier First-Class Mail. She further contends that the additional marketing component should slow the rate of electronic diversion for statement mail. She believes that DFS's reaction should be typical of companies that mail bills and statements. *See* DFS & MSI-T-1.

[5194] *MMA position.* Witness Bentley supports the Postal Service's proposal to reduce the additional-ounce rate. He asserts that the proposal is consistent with witness

O'Hara's revenue requirement and consistent with reaching a First-Class Mail cost coverage that is fair and equitable. He contends that the proposed lower presort additional-ounce rate is more in line with costs, and will provide some disincentive for mailers to continue the practice of mail splitting.⁹⁴ This lowers the mailer's postage costs, but may result in higher costs for the Postal Service. MMA-T-1 at 24-26; MMA Presort Brief at 57-58.

[5195] *NAPM & NCCP position.* NAPM & NCCP support the Postal Service's proposal to de-emphasize weight as a rate determinant. They argue that the proposal is consistent with the principle that when a mail characteristic has only a limited effect on cost, the rate element incorporating the mail characteristic should not exceed the cost differential. Furthermore, they argue that the reduction in the additional-ounce rate for bulk letters would allow First-Class Mail to compete more effectively with the Internet, and attract volume from Standard Mail by encouraging mailers to insert more solicitation matter within their First-Class mailing. NAPM & NCCP Brief at 30-31.

[5196] *Commission analysis.* The Postal Service's proposal to reduce the additional-ounce rates is consistent with the Commission's recommendation to move toward shape-based rates. The Commission concurs that the focus of the additional-ounce rates should be on the weight of the mailpiece, with the effect of shape de-emphasized. Lowering the additional ounce rates in the direction of actual costs imposed on the system is fair and equitable, and will send a clearer price signal to mailers.

[5197] The Postal Service attempts to justify a lower additional-ounce rate for automation letters than for the other rate categories by arguing that the automation letters mailstream is more uniform, i.e., shape is not an issue and the mailpieces all meet the 3.5 ounce maximum weight limit. This argument may become tenuous in the near future as there should be little difference between a single-piece letter running on

⁹⁴ Mail splitting is the practice of separating First-Class content from Standard content into two separate mailpieces to take advantage of lower Standard automation rates.

automation equipment and an automation letter running on automation equipment. The Commission suggests that after implementation of the shape-based rate system, the Postal Service further study the costs imposed by additional ounces by shape and by how the mailpiece enters the system (*e.g.*, single-piece, presort, automation letter or flat, business parcel), and present the results to the Commission at a future date.

[5198] The Commission recommends rates that are slightly lower than those proposed by the Postal Service. This will benefit mailers of heavier-weight mailpieces, and substantially mitigate the effect of the first-ounce mailpiece rate increases. Although the Commission strives to recommend additional-ounce rates to reflect costs, these rates continue to be a significant source of revenue for the Postal Service and are employed as a tool in meeting the First-Class Mail revenue requirement. The Commission recommends an additional-ounce rate of 17.0 cents for single-piece, non-automation presort, automation flats, and the new business parcels, and it recommends a 12.5 cent additional-ounce rate for automation letters.

g. Nonmachinable Surcharge Proposals

[5199] The Postal Service currently imposes a nonmachinable surcharge within the single-piece, non-automation presort, and automation flats categories on mail weighing one ounce or less, if the aspect ratio of the mailpiece does not fall between 1 to 1.3 and 1 to 2.5, or if the mailpiece exceeds 11.5 inches in length, 6.125 inches in width, or 0.25 inches in thickness. The nonmachinable surcharge also is imposed on letter-size mailpieces that do not meet the machinability requirements of the Postal Service, or when manual processing is requested.

[5200] Witness Taufique proposes the elimination of the nonmachinable surcharge arguing that it is no longer needed with the introduction of shape-based rates. In place of the surcharge, he proposes to subject single-piece letters that are nonmachinable to the single-piece flats rate. He further proposes that certain single-piece letter-shaped

mailpieces and flat-shaped mailpieces that fail machinability requirements, rigidity for example, be rated as single-piece parcels.⁹⁵ USPS-T-32 at 19, 45.

[5201] *GCA counter-proposal.* GCA proposes to retain the nonmachinable surcharge for certain low aspect ratio letter-shaped mailpieces, rather than assessing these mailpieces the flats rate. It sponsors the testimonies of witnesses Morrissey (GCA-T1) and Liss (GCA-T-4) in support of this proposal.

[5202] Witness Morrissey describes the methodology, implementation, and results of an experiment intended to determine the degree to which square single-piece First-Class Mail letters (greeting cards) are successfully processed by Postal Service automation equipment. The experiment consists of mailing 504 square-shaped mailpieces and 504 rectangular-shaped mailpieces from several regions of the country. The received mailpieces indicate that 80.45 percent of the square-shaped mailpieces versus 91.84 percent of the rectangular mailpieces were cancelled on an AFCS (the percentages exclude a set of mailpieces that showed no indication of cancelling). The mailpieces further indicate that 95.24 percent of the square-shaped mailpieces versus 100 percent of the rectangular mailpieces were successfully sorted on automation equipment.

[5203] Witness Morrissey concludes that the observed machinability differences do not support the rate increase that would be imposed by assessing low aspect ratio mailpieces the flats rate as proposed by the Postal Service. He further contends that the existing 13-cent surcharge may be too high, or perhaps not necessary. He is concerned about moving low aspect ratio mailpieces into the flats category even though they are processed as letters, given the associated costs differences of processing and delivering letters versus flats. GCA-T-3 at 1-10.

⁹⁵ Witness Taufique proposes a new “nonmachinable” discount for the proposed business parcels category. This surcharge is independently defined, i.e., it is not the same as the nonmachinable surcharge discussed in this section. Discussion of the business parcels nonmachinable surcharge appears in section B.2.e.

[5204] Greeting Card Association witness Liss analyzes the square mailing piece from the perspective of standard design principles and consumer appeal. She asserts that “[b]ecause a square size is not the standard, designers find it to be an effective tool in helping their designs to stand out from the crowd of bills and direct mailpieces in the mailbox.” GCA-T-4 at 6. Her concern is that while customers may hesitate to use square mailpieces given the existing 13-cent nonmachinable surcharge, they will not mail square mailpieces if the extra cost is increased to 20 cents (the effect of the flat rate proposed for square envelopes). *Id.* at 13-14.

[5205] *Postal Service response to GCA proposal.* The Postal Service opposes GCA’s proposal. Witness Laws explains that low aspect ratio mailpieces are not always successfully oriented on an Advanced Facer Cancellor System (AFCS) because of limitations with the Edging Channel function, and because of the potential for low aspect ratio mailpieces to tumble. USPS-RT-16 at 6-7. He asserts that even if low aspect ratio mailpieces complete their processing on automation equipment, such pieces often require more handlings because an AFCS on average will not be able to properly orient one-half of the square mailpieces. *Id.* at 7.

[5206] Witness Laws contends that the GCA experiment should not be relied upon because the experiment only observed the mailpieces when sent and when received, but not during mail processing. *Id.* at 8. Thus, the experiment could not reveal whether or not additional costs (such as manual handling) were incurred while processing the mail, or provide useful insight into any additional steps necessary to process low aspect ratio mailpieces on automation equipment.

[5207] Witness Laws concludes by describing a second test performed by the Postal Service at the behest of GCA two months before witness Morrissey conducted his experiment. GCA provided 7,640 envelopes of varying sizes, aspect ratios and readability characteristics to the Postal Service. The prepared samples were processed through a Dual Pass Rough Cull System and an AFCS, and observations were made whether the test piece was accepted or rejected. Witness Laws asserts that of the samples with aspect ratios of one (square pieces), 48.39 percent were successfully

cancelled and processed. He further concludes that since low aspect ratio pieces may be returned for automation processing after some manual handling, the fact that the mailpiece have been cancelled using the AFCS does not mean that the mailpieces did not incur additional costs. *Id.* at 12.

[5208] *Commission analysis.* The experiment that the Postal Service performed with the help of GCA thoroughly exemplifies the mail processing issues that arise with low aspect ratio mailpieces in the initial steps of automated mail processing. The experiment independently performed by GCA is limited because it does not provide useful insight into handling during mail processing. The Commission concludes that low aspect ratio mailpieces indeed impose additional mail processing costs on the postal system. Furthermore, the Commission is not persuaded that low aspect ratio mailpieces should be treated differently because of their alleged aesthetic value.

[5209] The nonmachinable surcharge is not consistent with the Postal Service's proposal for shape-based rates. Thus, where shape is the dominant issue, *e.g.*, with flat- and parcel-shaped mail within the single-piece, non-automation presort, and automation flats categories, the Commission recommends elimination of the nonmachinable surcharge. The first-ounce rate recommendations for this mail incorporate the cost characteristics previously recognized by the nonmachinable surcharge.

[5210] The Commission's considerations are more involved when considering the nonmachinable surcharge applicable to letter-shaped mailpieces within the single-piece and presort categories. The surcharges in these cases predominately address the machinability of the mailpiece, and not shape. For single-piece, the Postal Service proposes to rate these nonmachinable pieces as flats, which would result in an effective

surcharge of 20 cents. This surcharge is consistent with long-term shape-based goals, simple to implement and understand, and might be fair and equitable.

[5211] However, under the rates recommended by the Commission, charging a nonmachinable letter-shaped mailpiece the flat rate would result in an effective surcharge of 39 cents. Given the existing surcharge is 13 cents, tripling the surcharge in one rate cycle with no prior warning is excessive. The Commission must consider the impact to mailers unprepared for this change that this may cause. Thus, the Commission recommends a scaled-back retention of the nonmachinable surcharge, limited to nonmachinable letter-shaped mail weighing one ounce or less within the single-piece and non-automation presort categories.

[5212] The Commission recommends a rate of 17 cents, the same as the recommended additional-ounce rate. Because this recommendation might not be consistent with the way the Postal Service will be processing mail in the future given a shape-based mailstream, the Commission provides notice that this surcharge might not be justified in the future. The Commission has recommended changes to the DMCS to define the transitions between shapes and the application of the recommended nonmachinable surcharge.⁹⁶

h. Heavy-Piece Discount Proposal

[5213] The Postal Service proposes elimination of the heavy-piece discount as part of its shape-based rate proposal. The discount currently is applicable to non-automation presort, automation letters and automation flats mailpieces weighing more than two ounces. The cost effects of the heavy-piece discount are to be reflected in the new shape-based first-ounce mailpiece rate. USPS-T-32 at 45.

⁹⁶ The changes include incorporation of the 3.5 ounce weight maximum for letter-shaped mail. This appears consistent with the Postal Service's intent to apply this requirement to all rate categories within First-Class Mail. See 71 FR 565793 (September 27, 2006).

[5214] With the recommendation of shape-based rates that better align rates with costs, there no longer is a need for the heavy-piece discount. The Commission recommends its elimination.

i. Qualified Business Reply Mail

[5215] The Postal Service offers a discounted rate for Qualified Business Reply Mail (QBRM). QBRM is described as clean, pre-approved, pre-barcoded, automation-compatible Business Reply Mail that incurs less cost than non-barcoded single-piece mail.

[5216] Witness Abdirahman estimates QBRM costs savings of 1.495 cents applicable to both letters and cards. USPS-T-22 at 21. His cost analysis is limited to costs incurred up to the point each QBRM piece receives its first barcoded sortation on a Bar Code Sorter (BCS). *Id.* at 16.

[5217] Witness Taufique proposes increasing the QBRM letters rate from 35.8 cents to 39.5 cents. This reduces the current QBRM discount relative to the single-piece rate from 3.2 cents to 2.5 cents. USPS-T-32 at 24-25.

[5218] *MMA position.* Witness Bentley urges the Commission to reject the Postal Service's proposal to reduce the QBRM letter discount to 2.5 cents, and alternatively proposes that the QBRM letters discount be increased to at least 4.0 cents. MMA-T-1 at 26-28, Appendix II; MMA Reply Brief at 26-30.

[5219] MMA explains the cost analysis supporting the QBRM discount as last approved by the Commission in Docket No. R2000-1. The methodology compares QBRM letter processing costs with a similar letter that is hand-addressed. Cost savings are based on all processing operations from acceptance through the incoming secondary sortation operation, and reflect the RBCS costs of barcoding hand-addressed letters and the higher percentage of hand-addressed letters compared to QBRM letters that must be processed manually throughout the mailstream. MMA Special Service Brief at 6.

[5220] Witness Bentley contends that the Postal Service's new methodology for deriving QBRM cost savings is flawed because it models QBRM and HAND (hand-addressed) letters only so far as the first outgoing sortation, and ignores additional savings after that point in processing. He further asserts that the Postal Service applies the wrong CRA proportional adjustment factor to the QBRM model-derived unit cost, thereby understating the derived cost savings. Correcting for these flaws, witness Bentley estimates a QBRM unit cost savings of 6.75 cents. He argues that this cost savings supports an increase in the discount to at least 4.0 cents. MMA-T-1 at 26-28, Appendix II at 1.

[5221] *Time Warner position.* Witness Mitchell proposes an increase in the QBRM discount for letters from its current level of 3.2 cents to 4.0 cents and an increase in the QBRM discount for cards from its current level of 2.9 cents to 3.5 cents, and urges that in no instance should either discount be reduced. TW-T-3 at 1. He lauds the merits of QBRM mail, including a possible multiplier effect, and argues that QBRM should continue to be recognized in a meaningful way.⁹⁷

[5222] Witness Mitchell requests that the Commission consider the following in QBRM costing and rate setting:

- the decision to not include window service costs in cost avoidance;
- the Commission's Docket No. R2000-1 model, which recognizes that QBRM pieces receive fewer sortations by hand after the first automated sort than do handwritten pieces;
- the fact that QBRM pieces almost never have to be returned or forwarded;
- the fact that QBRM pieces have an exceptionally strong multiplier effect;
- BRM sent out in automation rate mailings must be automation compatible and ZIP + 4 barcoded, which is in effect a requirement that QBRM be used; and

⁹⁷ Multiplier effect refers to the propensity of a mailpiece to generate future additional mailpieces.

- CRA adjustment factors presented by witness Bentley when examining cost estimates.

Id. at 11-13.

[5223] He also reviews the changes in QBRM cost avoidance methodology from Docket No. R97-1 through the instant docket, and cites a Postal Service cost avoidance estimate of 4.14 cents using the method last approved by the Commission in Docket No. R2000-1. *Id.* at 10. He believes that the cost avoidance of QBRM is adequate to support increasing the discount for letters to 4.0 cents and for cards to 3.5 cents.

[5224] *Postal Service reply.* Witness Abdirahman argues that Bentley's and Mitchell's proposals to expand the scope of the QBRM cost analysis should not be adopted. He explains that large volumes of QBRM (to any given mailer) are likely to be isolated in upstream operations, whereas small volumes are likely to be isolated in downstream operations. Assuming that a given mailer did not provide QBRM mailpieces to its customers, the point at which a hand-addressed mailpiece is isolated would be the same as where the QBRM mailpiece would have been isolated. Witness Abdirahman asserts that this is because mail volume dictates the amount of mail processing required before isolation. Thus, he argues that the only processing cost avoided by QBRM mailpieces is the application of a POSTNET barcode by the RBCS to the hand-addressed mailpieces. USPS-RT-7 at 12-15.

[5225] *Commission analysis.* The central difference between the two models used to estimate QBRM cost avoidance is the number of sorts performed by the Postal Service before reply mail is isolated. The more times a reply piece must be handled, the greater the savings generated by the use of QBRM instead of handwritten reply pieces. As witness Abdirahman points out, the number of required sorts can vary depending on the volume of reply pieces destined to each recipient.

[5226] None of the cost estimates presented on this record reflect this reality. By ending its analysis after the first barcoded sort, the Postal Service's model fails to capture the costs generated by those pieces that require additional sorts to isolate. Conversely, the cost avoidance estimates presented by Time Warner and MMA

overstate the true savings by assuming that every QBRM piece must be processed through the incoming secondary.

[5227] Lacking more specific information about how frequently QBRM mail is isolated after each sortation, the Commission is reluctant to recommend significant changes to the QBRM discounts. The Commission recommends a 3-cent discount for QBRM letters and QBRM cards. This falls between the 1.495-cent savings estimated by the Postal Service and the 4.14-cent savings estimated using the method approved by the Commission in the last fully litigated rate case (Docket No. R2000-1). It is also the same discount that was recommended in that case. A 3-cent discount results in a QBRM letter rate of 38 cents, and a QBRM card rate of 23 cents.

j. Consideration of Rate and Classification Factors

[5228] The Commission finds that the recommended rates for First-Class Mail in the Letters and Sealed Parcels subclass are consistent with the factors set out in § 3622(b). Based on the Commission's projected test year after-rates volume, First-Class Letters and Sealed Parcels revenue will exceed estimated attributable costs by \$18.8 billion. Thus, recommended rates will recover all attributable costs, in compliance with § 3622(b)(3).

[5229] Postal Service witness O'Hara notes First-Class Mail is sealed against inspection and receives forwarding, or return-to-sender, at no additional charge. It receives a high priority of delivery relative to other non-expedited classes of mail. It also benefits from an extensive collection system, and may travel by air when the distance between sender and recipient warrants it. Thus, he concludes it has a high value of service (§ 3622(b)(2)). USPS-T-31 at 17-18. Carlson contends that reductions in collections have diminished this value (DFC-T-1 at 36-50), but the Commission concludes that the existing level of collection service, including the alternative methods available for entering mail into the system, is consistent with the conclusion that First-Class Mail provides a high level of service.

[5230] The impact of the recommended rate changes is modest (§ 3622(b)(4)). The first-ounce single-piece letter rate increase is limited to two cents. Although the move towards shape-based rates has caused substantial increases for mailers of light weight flat- and parcel-shaped mailpieces, the rates more accurately reflect costs. These increases are balanced by reductions in the additional-ounce rate, which significantly benefit mailers of heavier mailpieces. Limiting or eliminating the applicability of the nonmachinable surcharge for most mailpieces further benefits mailers. The recommended Qualified Business Reply Mail discount of 3 cents should have little adverse impact and provide incentive to continue use of this type of mail. The average increase for the Letters and Sealed Parcels subclass is 7.0 percent, which is below the systemwide increase of 7.6 percent.

[5231] Available alternatives are somewhat limited for mailers in the Letters and Sealed Parcels subclass (§ 3622(b)(5)). Nevertheless, witness O'Hara notes that non-postal alternatives are available. These include growing access to the Internet, and the increasing availability of electronic payment options. USPS-T-31 at 18-19.

[5232] The recommendations recognize mailers' worksharing efforts, in accordance with § 3622(b)(6), through presorting and pre-barcoding discounts. In most cases, the recommended letters and cards automation discounts pass through close to 100 percent of the recognized cost savings.

[5233] The recommendation of shape-based rates, including the new business parcels rate category, has added to the complexity of the First-Class Mail schedule (§ 3622(b)(7)). However, the elimination of the heavy-piece discount, limited application of the nonmachinable surcharge, and elimination of the carrier route rate tiers has simplified the schedule. The Commission finds this acceptable, given the more accurate pricing signals that shape-based rates should send to mailers.

[5234] The Commission finds that recommended rates appropriately reflect § 3622(b)(8) considerations, which relate to the informational value of business and personal correspondence, as well as the cultural value of greeting cards. The

Commission's overall conclusion is that the recommended rates are fair and equitable (§ 3622(b)(1)).

[5235] The Commission also finds that the recommended classification for First-Class Mail in the Letters and Sealed Parcels subclass are consistent with the factors set out in § 3623(c) using much of the same rationale as cited when analyzing § 3622(b) above. Two classification proposals, however, stand out. The first is the new classification recommending a Forever Stamp. See § 3622(b)(4). The second is the adoption of shape-based rates. These initiatives further the objectives established in § 3623(c)(2) and (5), by meeting the needs of mailers and the Postal Service, and the requirement that classifications be fair and equitable for all mailers (§ 3623(c)(1)).

3. First-Class Mail Alternative Proposals

[5236] OCA and Pitney Bowes present alternative rate and classification proposals that warrant separate treatment. OCA proposes an alternative classification schedule featuring four-ounce increments for the Letters and Sealed Parcels subclass. Pitney Bowes proposes a 0.1-cent discount applicable to single-piece First-Class Mail letters with evidence of first-ounce postage purchased through alternate sales channels.

a. OCA Four-Ounce Increment Proposal

[5237] Witness Thompson suggests an alternative rate schedule for the First-Class Letters and Sealed Parcels subclass which features four-ounce weight increments for letter-, flat-, and parcel-shaped mail. Thompson simplifies the rate schedule by reducing the number of rate cells, and proposes rates, with one exception, in multiples of 42 cents. She incorporates the Postal Service's shape-based rate categories, and uses the Commission approved bulk metered mail benchmark when calculating First-Class Mail presort and automation discounts. She also eliminates the First-Class Mail additional

ounce rate for all categories except for the new business parcel rate category. The proposal does not adopt the Postal Service’s de-linking methodology. See OCA-T-4.

[5238] Witness Thompson asserts: “The virtue of the four-ounce rate proposal is a dramatic simplification of the First-Class rate schedule. Yet, the OCA’s rate proposal yields Test Year After Rate revenues that are virtually the same as those forecast by the USPS.” In addition to simplifying the rate schedule and minimizing the need to weigh each and every mailpiece, she explains that mailers would only need to maintain one type of stamp — 42 cents. *Id.* at 3. An example of the proposed rate schedule, for single-piece, is shown in Table V-2.

Table V-2
OCA Proposal First-Class Mail Single-Piece Rates

Single-Piece Letters, Flats, and Parcels	0 to 4 oz.	4 to 8 oz.	8 to 13 oz.
Letters	\$ 0.42	N/A	N/A
Flats	\$ 0.84	\$ 1.68	\$ 2.52
Parcels	\$ 1.68	\$ 2.52	\$ 2.79
Additional Ounces	N/A	N/A	N/A
Nonmachinable Surcharge	N/A	N/A	N/A
QBRM	\$ 0.395	N/A	N/A

[5239] Witness Thompson also proposes rates for the worksharing categories. For the automation letters category, she suggests one rate for each sortation tier. Each rate encompasses the full range of automation letter weights. Thus, an additional-ounce rate is not necessary. For automation flats, she proposes rates in four-ounce increments designed to reflect the mail processing and delivery unit cost difference of approximately \$0.298 between processing an automation letter and a flat. The 4 to 8 ounce flat rates are 80 cents higher than the 0 to 4 ounce flat rates, and the 8 to 13 ounce flat rates, are 80 cents higher than the 4 to 8 ounce flat rates. *Id.* at 7.

[5240] Witness Thompson also proposes rates for the new business parcels rate category. Because she considers this category similar in nature to an experimental classification, she does not propose four-ounce increments, but continues the practice of proposing rates in one-ounce increments and accounting for weight differences with an additional-ounce rate. *Id.* at 24-25.

[5241] Witness Thompson estimates that her rate proposal will have negligible impact on the revenue requirement, increasing revenue by \$2.8 million over the Postal Service's estimate. *Id.* at 26.

[5242] *ABA position.* ABA opposes OCA's alternative-rate design proposal. It argues that given the nature of the recently enacted postal reform legislation, it does not see how the Commission could recommend such a drastic change unless the Postal Service accepted it. ABA Brief at 21-24.

[5243] *MMA position.* MMA opposes OCA's alternative rate proposal, asserting that the proposal is "patently irresponsible" for moving discount levels back to those that existed more than a decade ago, and for being "technically flawed." MMA is critical of the proposal for shifting approximately \$500 million to workshare mailers. MMA contends that OCA has not studied the heavy-weight letter market in regard to presorted letters or the likely volume impact of the proposal. MMA also criticizes the proposal for relying upon USPS-LR-L-141, a workshare cost analysis that no witness sponsored. Furthermore, MMA argues that the proposal disregards the likely impact on presort mailers and the postal system in general, and would disrupt longstanding rate relationships. MMA Presort Brief at 47-55.

[5244] *Postal Service position.* Witness Taufique opposes witness Thompson's rate design proposal. He estimates that the proposal will result in rate changes ranging from negative 62.2 percent to positive 223 percent within the single-piece Letters and Sealed Parcels subclass. He asserts that the Postal Service is sensitive to extraordinary rate impacts, and that witness Thompson's proposal would subject mailers to even higher percentage increases than those proposed by the Postal Service. He contends that the range of rate changes proposed by witness Thompson is bound to lead to

changes in mail mix, and that the financial and operational consequences of the changes in mail mix requires examination before the proposed rate design is considered.

USPS-RT-18 at 9-10.

[5245] *Commission analysis.* OCA proposes an interesting approach to simplifying the First-Class Mail rate structure. With the recommendation of shape-based rates adding to the complexity of the First-Class Mail classification schedule, the Postal Service is encouraged to consider alternative approaches to again simplify the rate structure, especially for single-piece mailers.

[5246] Although the idea of First-Class Mail weight increments greater than one ounce is intriguing, it requires further study before it can be recommended. OCA has not provided any information indicating whether single-piece and/or worksharing mailers would be receptive to its proposal. In addition to a thorough examination of the proposal's affect on volume, a more comprehensive cost and revenue analysis should be undertaken.

[5247] The Commission is not opposed to considering ideas to significantly revamp rate structures, even if some mailers may be disrupted by the proposals, if the benefits can be demonstrated. The Commission does not recommend the OCA proposal at this time. However, the Commission encourages the Postal Service and mailers to further explore the potential benefits of this innovative approach to improving First-Class Mail.

b. Pitney Bowes Single-Piece Indicia Discount Proposal

[5248] Witness Buc proposes a discount for single-piece First-Class Mail letters with evidence of first-ounce postage purchased through retail sales channels that avoid the transaction costs incurred by stamps sold directly by Postal Service employees at Postal Service owned or leased facilities. He proposes a 0.1 cent per-piece discount limited to mail bearing PCPostage, permit, or meter indicia. He characterizes this as a form of worksharing which would promote economic efficiency by moving expensive stamp sale transactions away from the Postal Service retail window. Witness Buc further

suggests that the Postal Service study the cost of stamp sales and the cost of other forms of postage evidencing such that over time retail access discounts can be expanded, and better reflect costs. See PB-T-3.

[5249] Pitney Bowes considers this proposal as a worksharing discount. Unlike worksharing discounts that require substantial volumes, Pitney Bowes argues that this discount would be available to users of the mail with small mail volumes and would help democratize worksharing discounts. Pitney Bowes Brief at 26-28.

[5250] *Postal Service position.* The Postal Service opposes Pitney Bowes' single-piece indicia discount proposal. The Postal Service contends that the proposal does not adequately address important issues related to the costs of implementation, revenue leakage, and revenue protection. Furthermore, it argues that the proposal makes little sense because the proposed benefit is so small (0.1-cents), that it does not provide incentive for single-piece mailers to change their behavior. Moreover, the Postal Service contends that the discount would reward business mailers that already use alternate postage evidencing devices, without requiring them to change their behavior at all. Postal Service Brief at 225-29.

[5251] *Commission analysis.* The Commission does not recommend adoption of the Pitney Bowes single-piece indicia discount proposal. This proposal is similar in many respects to the Pitney Bowes one-cent meter technology discount proposal presented, but not recommended, in Docket No. R2000-1. See PRC Op. R2000-1, ¶¶ 5196-5221.

[5252] In Docket No. R2000-1, the Commission explains that it previously has not recognized cost avoidance associated with stamp manufacturing and distribution as worksharing related, and that although metered mail may save the Postal Service stamp costs, these costs are not in the same category as historically recognized worksharing costs. The Commission further comments on the potential for a metered mail discount to

discriminate between different single-piece First-Class mailers (those with the means to afford metering technology versus those that can least afford technology), and the possibility that further de-averaging First-Class Mail rates that would compound this problem.

[5253] In Docket No. R2000-1, the Commission also expressed concern over the potential for the discount to reduce Postal Service revenue that would have to be recouped through burdening other types of mail. Although the current proposal offers a modest 0.1-cent discount, arguably representing less potential revenue loss, questions remain on the proposal's actual revenue impact especially when considering the potential either to expand the discount in the future to the full cost avoided; or to logically expand the discount to the sale of stamps at non-Postal Service sites or to include permit indicia mail.

[5254] The Postal Service is encouraged to explore alternatives to the current practices of selling stamps that will lead to greater customer satisfaction and convenience, and as a related benefit, reduce Postal Service costs. However, as described in Docket No. R2000-1, the Commission does not consider stamp-related costs to be associated with worksharing in the traditional sense, or to warrant the further de-averaging of First-Class Mail rates to the detriment of those least able to afford it. The Commission considers the costs associated with the manufacture and distribution of stamps as part of the cost of providing First-Class Mail universal service, and thus should be shared by all First-Class Mail users.

4. Forever Stamp

[5255] The Postal Service proposes a classification change to introduce a stamp that will be valid for First-Class Mail first-ounce postage for single letter-shaped pieces, regardless of the prevailing first-ounce rate. The stamp will hereinafter be referred to as the "Forever Stamp." The proposal is designed to create a means for typical households and small businesses to avoid the inconvenience associated with future changes in

postal rates by creating a non-denominated, non-expiring, stamp valid regardless of future rate changes. The proposal is presented by witness Taufique. See USPS-T-48; USPS-T-32 at 26-27.

[5256] The Postal Service has undertaken market research in support of its Forever Stamp proposal. See USPS-LR-L-152. Witness Taufique asserts that the research shows that customers do not perceive usual rate changes as a major inconvenience, but they still take measures to prepare for the change such as special trips to purchase make-up stamps. USPS-T-48 at 7. He asserts that households and businesses would be receptive to the concept of the Forever Stamp, but would be less likely to favor the stamp if charged a premium over the established rate. Witness Taufique further concludes that the research indicates the Forever Stamp may add to the positive image of the Postal Service, and possibly help slow the downward slide of single-piece volume. *Id.* at 16.

[5257] The Postal Service also has reviewed the experiences of foreign posts with non-value-indicated stamps and concludes that the Forever Stamp will further the objective of making the transition to new rates less burdensome for the average user of single-piece letter mail. See OCA-LR-L-1.

[5258] Witness Taufique contends that the Forever Stamp proposal is fully justified under the classification criteria of § 3623(c). He highlights factor 5, “the desirability of special classifications from the point of view of both the user and of the Postal Service[.]” and factor 1, “the establishment and maintenance of a fair and equitable classification system for all mail.” USPS-T-48 at 18. He argues that it is desirable for the user because it eases the transition to new rates, and it is desirable to the Postal Service because it should simplify retail transactions around the time of rate changes. He

contends the proposal is fair and equitable because the stamp would be widely available to all users.

[5259] Witness Taufique asserts that the Forever Stamp will have no effect in the test year on the finances of the Postal Service because the stamp will not reflect a rate different from the rate implemented as a result of Docket No. R2006-1. Any financial effect will be experienced at the time of subsequent rate changes, assuming that a Forever Stamp purchased at the Docket No. R2006-1 rate is used for postage at the subsequent rate. Nevertheless, witness Taufique raises several long-range financial effects that should be considered. Early purchases prior to the subsequent rate change could provide a benefit by adding cash reserves, and generating investment income. However, early aggressive purchases could have a negative effect by negating the financial impact on the Postal Service of a subsequent higher rate if users do not purchase stamps at the higher rate. Finally, some foreign posts utilizing similar stamp programs have reported a negative impact on philatelic programs.

[5260] Witness Taufique proposes careful monitoring of the implementation and usage of the Forever Stamp. He envisions monitoring the revenue obtained from the sale of the Forever Stamp utilizing a separate account identifier code for sales. He also envisions monitoring stamp usage by evaluating "Postage in the Hands of the Public" and through the ODIS-RPW system. *Id.* at 24.

[5261] The Postal Service's Forever Stamp proposal has developed through extensive discovery. The intended use of the Forever Stamp is for single-piece First-Class Mail letters weighing up to one ounce. Tr. 19/6928. However, the Postal Service anticipates that the Forever Stamp will be used for other than its intended purpose and such use will be "tolerated." *Id.* at 6929. The Postal Service "intends" to give credit when the Forever Stamp is used for other than its intended purpose at the applicable First-Class Mail single-piece one-ounce letter rate. Tr. 40/13630, 13643; see *also* Postal Service Brief at 190-92.

[5262] *Carlson position.* As the Postal Service's position on the Forever Stamp has developed over the course of this proceeding, witness Carlson's concerns have

changed. Before the submission of witness Carlson's testimony, the Postal Service considered establishing the value of the Forever Stamp at the "forever" value if the stamp were to be used on a one-ounce single-piece First-Class Mail letter, and at the purchase price if used on any other type of mailpiece.

[5263] Witness Carlson, in his testimony, contends that such restrictions would cause public confusion as many people would place the stamp on flats and parcels, and those customers who understand the restrictions will have to keep two different types of stamps on hand. He asserts that this requires customers to know the original purchase price of every Forever Stamp (with the assumption that the Forever Stamp will not show a denomination). He further contends that "[t]he 'Forever Stamp' proposal will not be successful, and will not increase customer convenience, unless the stamp is valid for postage on all mail at the prevailing rate for single-piece, one-ounce First-Class letters." DFC-T-1 at 28.

[5264] In summary, witness Carlson does not oppose the "Forever Stamp" concept, but expresses concern that the implementation not introduce unnecessary inconvenience, confusion, and complexity, and result in unfairness to customers. He speculates that the Postal Service remains concerned about the potential financial impact of public behavior such as hoarding. *Id.* at 31.

[5265] Witness Carlson's testimony, and the discovery process, influenced the Postal Service to modify its position to tolerate the use of Forever Stamps on pieces of mail other than the first ounce of single-piece First-Class Mail letters, and to give credit at the forever value. On brief, witness Carlson comments that the proposed revisions permitting customers to use Forever Stamps on all mail at the "forever" value have eliminated his remaining opposition to the Forever Stamp proposal, subject to two conditions. Carlson Brief at 1-7.

[5266] First, witness Carlson suggests that the Commission should adopt his proposed DMCS language to avoid a perceived ambiguity of the Postal Service's DMCS language. In response to DFC/USPS-82 which queried whether the Postal Service's

proposed DMCS language could be interpreted to permit customers to use the Forever Stamp on First-Class letters only, the Postal Service responded:

Not if read in conjunction with the record in this docket, the proposed DMM language and other materials that the Postal Service intends to publish in conjunction with the implementation of the Forever Stamp, if it is recommended and approved as proposed.

Tr. 40/13648. Witness Carlson believes that “[t]he Commission should recommend DMCS language that clearly articulates the parameters of the ‘Forever Stamp’ proposal, not language that is clear only when read in conjunction with the record in this proceeding and DMM implementation language.” Carlson Brief at 4.

[5267] Second, witness Carlson suggests that the Commission should not recommend the Forever Stamp if the Postal Service intends to sell the Forever Stamp for 42 cents while the First-Class Mail letters rate remains at 39 cents. He argues that the public would be confused over the purpose of the Forever Stamp if it were to be sold at 42 cents while the prevailing postage rate were still 39 cents. He further contends that the Postal Service can not legally sell Forever Stamps for a price higher than the prevailing one-ounce First-Class rate. As an alternative, he proposes that the Postal Service sell a non-denominated stamp at 42 cents in advance of the rate increase, and then after the new rate comes into effect, announce that the non-denominated stamp is actually the Forever Stamp. *Id.* at 30-31.

[5268] *OCA position.* OCA gives its full support for the proposed Forever Stamp classification. It suggests that the Postal Service proceed with caution in the early years to limit financial exposure, and hopes that successful use of the stamp may eventually lead to opportunities to use the stamp on a wider variety of mailpieces. OCA Trial Brief at 1-2; OCA Brief at 142-57; OCA Reply Brief at 41-46.

[5269] OCA agrees with witness Carlson that the Postal Service's proposed DMCS language "is not a model of clarity." OCA Brief at 152, quoting DFC-T-1 at 21. It argues that in the absence of clarification the proposed DMCS language is ambiguous and could lead to inconsistent enforcement in conflict with the Postal Service's stated intent. This could be unfair to individual and smaller mailers, create the perception of discriminatory treatment, and confuse clerks, mailhandlers, and mailers. OCA Brief at 152-56.

[5270] To rectify this ambiguity, OCA suggests that the Commission recommend the DMCS language proposed by witness Carlson. OCA further asserts that it is critical for the Commission's recommendation to clarify the various weights and classes of mail on which the Forever Stamp may be used and resolve any ambiguities in the DMCS language in favor of the convenience to individual and smaller mailers.

[5271] *Popkin position.* Popkin reviews the issues raised through discovery concerning the Forever Stamp and provides support for the position that the DMCS language proposed by the Postal Service should be modified. He characterizes the Postal Service's position that use of the Forever Stamp on mail other than on single-piece, one-ounce First-Class Mail letters will be "tolerated" as abhorrent. He states that "[e]ither something is permitted to be mailed under certain conditions or it is not." Popkin Reply Brief at 2. Otherwise, the possibility exists that Forever Stamped mail may not be accepted for one of its tolerated uses. Popkin further suggests that the current 39-cent stamp be utilized for a period of time as a Forever Stamp during the transition to the new First-Class Mail letter rate. *Id.* at 1-10; *see also* Popkin Reply Brief.

[5272] *GCA position.* GCA supports recommendation of the Forever Stamp. GCA comments on Carlson's position on the applicable use of the Forever Stamp and the sale of the Forever Stamp prior to the rate change. It disagrees with Carlson that the Postal Service's positions are unlawful, but would support either the Postal Service's or Carlson's proposals regarding the treatment of implementation issues from a policy perspective. GCA Brief at 8-10.

[5273] *Postal Service reply.* The Postal Service asserts that the issues regarding the permitted uses of the Forever Stamp raised by witness Carlson have been resolved.

However, it contends that the Postal Service's originally proposed DMCS language best reflects the intent of the Forever Stamp proposal. The Postal Service also disputes witness Carlson's assertion as to the timing of when the Postal Service may begin selling stamps that ultimately could be used as Forever Stamps. Postal Service Brief at 236-43.

[5274] The Postal Service stresses its opposition to expanding its proposal from creating a stamp intended to benefit basic rate First-Class Mail users, to creating a stamp intended for use on all classes of mail at a postage value equivalent to the basic First-Class Mail letter rate prevailing at the time of use. It asserts that the positions and proposals presented by witness Carlson would undesirably expand the Postal Service's proposal. It asserts that an expanded proposal could have unknown financial consequences, and if negative, could undermine goodwill by requiring the Postal Service to modify (restrict) its Forever Stamp policies in the future. The Postal Service also supports its concept of tolerating unintended uses of the Forever Stamp by citing to other instances, such as the use of Priority Mail flat rate stamps affixed to Parcel Post packages, where it tolerates the unintended use of a Postal Service item. Postal Service Reply Brief at 186-87.

[5275] *Commission analysis.* The Commission recommends the implementation of the Forever Stamp. The Forever Stamp has the potential to benefit all single-piece First-Class Mail users by alleviating the need to purchase stamps at the time of rate changes. This is both convenient for mailers, and economical for the Postal Service as it should reduce the demand for window service when rates change. It could eliminate the need for printing non-denominated stamps, which pose difficulties of their own, as both customers and postal employees must remember the value of the non-denominated stamps. With the prospect of yearly rate changes on the horizon as a result of the PAEA, the goodwill developed through the Forever Stamp could be considerable.

[5276] The Forever Stamp will have no substantive impact on Postal Service revenues during this rate cycle as it will be sold at the recommended single-piece first-ounce First-Class Mail rate. The Commission concurs that the Postal Service should track sales and usage of the Forever Stamp to better estimate its financial impact

during subsequent rate cycles. Limiting the sales of the stamps to reasonable quantities as described by witness Taufique, should reduce the possibility of negatively affecting revenues through misuse.

[5277] The Commission sees no legal impediment to the Postal Service selling the Forever Stamp at the new recommended rate prior to the implementation date for the new rates. The Postal Service has sold non-denominated stamps at rates differing from the current rates in the past, and presently sells stamps valued at greater than 39 cents. There is nothing inherently wrong with the Postal Service's suggestion that it could inform customers in advance of the effective rate change of the Forever Stamp's classification, and that stamps sold at the new recommended rate prior to the effective date will convert to Forever Stamp status on the effective date. The Postal Service, in any event, is encouraged to develop and make available materials explaining the Forever Stamp initiatives prior to the first sale of the Forever Stamp to reduce the possibility of public confusion.

[5278] The concerns over the Forever Stamp DMCS language proposed by the Postal Service as expressed by Carlson, OCA and Popkin are shared by the Commission. The Postal Service asserts the Domestic Mail Manual, and other materials, will further delineate the application of the Forever Stamp. However, the parameters of an initiative designed for use by the general public should be clearly described in the DMCS, without the need to refer to other documents. The Postal Service's concern about expanding the scope of Forever Stamp usage through more permissive DMCS language is noted, but outweighed by the ill will that may ensue if the public views usage of the Forever Stamp as overly cumbersome or complicated. Through development and dissemination of educational materials, the Postal Service has the ability to reduce instances of unintended use.

[5279] The Commission recommends the DMCS language to be included in the First-Class Mail Classification Schedule as proposed by the Postal Service. Although witness Carlson provides a viable alternative that more clearly represents the overall intent of the Forever Stamp, the language proposed by the Postal Service is specific to

First-Class Mail. When read in this specific context, the Postal Service's language sufficiently describes the intent of the Forever Stamp as applicable to First-Class Mail. The recommended language follows:

241 Forever Stamp

Postage for the first ounce of a First-Class Mail single-piece letter may be paid through the application of a Forever Stamp. The Forever Stamp is sold at the prevailing rate for single-piece letters, first ounce, in Rate Schedule 221. Once purchased, the Forever Stamp may be used for first ounce letter postage at any time in the future, regardless of the prevailing rate at the time of use.

[5280] The Commission recommends the addition of footnote 5 to First-Class Mail Rate Schedule 221 as proposed by the Postal Service, with the change of the word "price" to the word "rate".

The rate for single-piece, first ounce letters also applies to sales of the Forever Stamp at the time of purchase.

[5281] The Commission recommends modifications to DMCS § 3030 based on language proposed by the Postal Service. The Commission's recommendation specifies the Postal Service's intended use of the Forever Stamp, and removes the inference that the Forever Stamp only may be used for the first-ounce of single-piece First-Class Mail letters. This modification is intended to address the concerns raised by intervenors that the Forever Stamp, without ambiguity, also may serve as postage for mail other than the first ounce of single-piece First-Class Mail letters. This language is intended to allow the Postal Service to develop and disseminate educational material on the intended use of the Forever Stamp as applicable to the first ounce of single-piece First-Class Mail letters, and leave it clear that alternative usage will be allowed. The modifications to § 3030 (renumbered as § 3031) recommended by the Commission are underlined.

3030 Payment of Postage and Fees

3031. Postage Payment. Postage must be fully prepaid on all mail at the time of mailing, except as authorized by law or this Schedule. The Forever Stamp, described in section 3032, is intended for the prepayment of postage for the first ounce of First-Class Mail single-piece letter mail, and otherwise may be used for the prepayment of postage. Except as authorized by law or this Schedule, mail deposited without prepayment of sufficient postage shall be delivered to the addressee subject to payment of deficient postage, returned to the sender, or otherwise disposed of as specified by the Postal Service. Mail deposited without any postage affixed will be returned to the sender without any attempt at delivery.

[5282] Finally, the Commission recommends the addition of a description of the Forever Stamp to the payment of Postage and Fees section of the DMCS. This general description, originally proposed by witness Carlson for use in the First-Class Mail section, is intended to convey the intended sale and use of the Forever Stamp as developed during the litigation of this rate case.

3032 Forever Stamp. The Forever Stamp is sold at the prevailing rate for single-piece letters, first ounce, in Rate Schedule 221. The Forever Stamp is an adhesive stamp within the meaning of section 3040. Once purchased, the Forever Stamp may be used for postage equal to the prevailing rate, at the time of use, for single-piece letters, first ounce, in Rate Schedule 221.

5. Cards Rates and Classifications

[5283] The First-Class Mail Cards subclass consists of stamped cards and postcards. Stamped cards are purchased through the Postal Service as a special service. See DMCS § 962. Postcards are privately printed mailing cards of uniform thickness that do not exceed 6 inches in length, 4-1/4 inches in width, or 0.016 inches in thickness. In FY 2005, cards generated approximately \$1.2 billion, or 3.3 percent, of First-Class Mail revenue, and represented about 5.7 percent of First-Class Mail volume.

Over the past five years, cards volume has increased by slightly over 2 percent, with volume growth in the automation category, and volume loss in the single-piece and non-automation presort categories. USPS-T-32 at 9, 39-44.

[5284] First-Class Mail cards may be mailed within regular, presort, and automation rate categories. The regular category includes single-piece cards and Qualified Business Reply Mail (QBRM) cards. The presort rate applies to qualified bulk mailings that are not automation compatible. The automation category consists of five rate tiers based on the level of mail preparation performed by the mailer: Mixed AADC, AADC, 3-digit, 5-digit, and carrier route. In this docket, the Postal Service proposes elimination of the carrier route rate tier from the current automation categories.⁹⁸

[5285] The Postal Service proposes increasing the current 24-cent rate for single-piece cards by 3 cents, paralleling the increase in First-Class letters. Single-piece cards account for approximately 51 percent of cards revenues. A 3-cent increase retains the 15-cent gap with the single-piece letter rate and represents a 12.5 percent increase above the current single-piece cards rate.

[5286] The Postal Service proposes increasing the discount rate of 21.1 cents for QBRM cards to 24.5 cents. This is a reduction from the current 2.9 cents discount for QBRM cards, and is equal to the 2.5 cents discount for QBRM letters. Witness Abdirahman calculates a QBRM cost avoidance of 1.495 cents for both letters and cards. USPS-T-22 at 21. A 2.5-cent discount passes through roughly 167 percent of the calculated cost avoidance.

[5287] A 1.8 cent increase (an 8.1 percent increase above the current rate) is proposed for non-automation presort cards, changing the non-automation presort cards rate from 22.3 cents to 24.1 cents. This increases the current 1.7-cent gap between the single-piece cards rate and the non-automation presort cards rate to 2.9 cents, and is greater than the proposed 2.0 cents difference between the single-piece letter rate and the non-automation presort letter rate. *Id.* at 22.

⁹⁸ Discussion of the elimination of the carrier route rate tier appears in chapter V, section B.2.c.

[5288] Witness Taufique reports a cost avoidance of 1.4 cents between non-automation presort cards and Mixed AADC automation cards. He proposes a 1.9 cent discount between non-automation presort cards and Mixed AADC automation cards, which passes through 134 percent of estimated cost savings. This results in an increase in the Mixed AADC automation cards rate from 20.4 cents to 22.2 cents.

[5289] Witness Taufique states that the calculated cost savings for the AADC, 3-digit, and 5-digit automation tiers are smaller than the current discounts for these tiers. Thus, if the discounts were tied strictly to avoided costs, the discounts would have to be reduced. Instead, he selects discounts and passthroughs to balance several other goals, including: achieving the Postal Service cost coverage target; recognizing the value of worksharing; acknowledging the importance of mailer barcoding; and avoiding discount level changes which result in disruptive rate impacts. As a result, witness Taufique proposes to increase each automation rate tier by 1.8 cents above their current levels. Applying a 1.8 cent increase to all other rate tiers maintains the current automation discount differentials and results in proposed rates of 21.5 cents for AADC, 21.1 cents for 3-digit, and 20.4 cents for 5-digit. USPS-T-32 at 42.

[5290] *Commission analysis.* The Commission finds the record supports a single-piece cards rate of 26 cents. The recommended rate continues to help ensure that there is at least one relatively inexpensive postal category that can be widely used by the general public, businesses, and organizations. It mirrors the 2-cent increase in single-piece letters, thereby retaining the 15-cent difference between single-piece letters and single-piece cards. Furthermore, the recommendation reflects the Commission's determination that the whole-cent integer constraint continues to be a significant consideration in establishing appropriate single-piece rates.

[5291] The Commission recommends a 3-cent discount for QBRM cards. This is the same discount recommendation as for QBRM letters and is based on similar cost avoidances. A 3.0-cents discount results in a 23-cent QBRM cards rate.

[5292] The Commission recommends a 24.1-cent rate for non-automation presort cards. This increases the current 1.7 cent difference between single-piece cards and non-automation presort cards to 1.9 cents.

[5293] With no participant advocating the retention of the carrier route rate tier, the Commission recommends its elimination. The Commission recommends cost-based rates for the remainder of the worksharing tiers based on the avoided costs. The recommended rates continue to acknowledge the importance of mailer barcoding, but also recognize the increase in avoided costs between automation 3-digit and 5-digit cards. To make rate increases as small as possible, the recommendations are based on a cost avoidance passthrough as close to 100 percent as possible, given a 0.1-cent rounding constraint.

[5294] The Commission estimates avoided costs of 2.1 cents between non-automation presort and Mixed AADC cards, 1.2 cents between Mixed AADC and AADC cards, 0.4 cents between AADC and 3-digit cards, and 1.3 cents between 3-digit and 5-digit cards. The Commission passes through close to 100 percent of avoided costs which results in rate recommendations of 22.0 cents for Mixed AADC, 20.8 cents for AADC, 20.4 cents for 3-digit, and 19.1 cents for 5-digit.

[5295] The Commission's recommended rates for the Cards subclass reflect an average increase of 6.1 percent. This is lower than the First-Class letters increase of 7.0 percent and lower than the systemwide average increase of 7.6 percent. Based on the Commission's projected test year after-rates volume, First-Class cards revenue will exceed estimated attributable costs by \$477 million. Thus, cards rates cover attributable costs, as required by § 3622(b)(3). The Commission's recommended 26-cent postcard rate reflects consideration of the somewhat more limited value of service that cards offer, especially in terms of privacy (§ 3622(b)(2)). No record evidence suggests that the recommended rates may have an unduly negative impact on mailers (§ 3622(b)(4)).

[5296] The recommended cost-based rates appropriately recognize the worksharing efforts of mailers presenting bulk presorted or pre-barcoded cards (§ 3622(b)(6)). The rate schedule for cards generally provides identifiable relationships.

The recommended 23-cent rate for QBRM cards is equal to the discount recommended for QBRM letters. (§ 3622(b)(7)). Overall, the Commission finds that the cards rates it recommends are fair and equitable (§ 3622(b)(1)). The markup index for cards is 0.698. This is somewhat higher than the Docket No. R2000-1 recommended markup index of 0.561.⁹⁹ The Commission finds the markup index for cards appropriate on this record.

[5297] Table V-3 provides a comparison of the current, proposed, and recommended rates and fees for the First-Class Mail Cards subclass.

Table V-3
Comparison of Current, Proposed, and Recommended
Rates and Fees for First-Class Mail Cards

CARDS	Current	Proposed	Recommended
Single-Piece Cards	24.0¢	27.0¢	26.0¢
Qualified Business Reply Mail	21.1¢	24.5¢	23.0¢
Non-automation Presort Cards	22.3¢	24.1¢	24.1¢
Mixed AADC Cards	20.4¢	22.2¢	22.0¢
AADC Cards	19.7¢	21.5¢	20.8¢
3-Digit Cards	19.3¢	21.1¢	20.4¢
5-Digit Cards	18.6¢	20.4¢	19.1¢
Carrier Route Cards	17.9¢	N/A	N/A

6. Priority Mail

a. Introduction

[5298] Priority Mail represents an extension of First-Class Mail for mailable matter weighing more than 13 ounces and up to 70 pounds. Priority mailpieces may not exceed 108 inches in length and girth combined. At the mailer's option, Priority Mail may also be used to mail matter weighing 13 ounces or less. In addition to providing expedited handling, this option enables mailers to elect service features, *e.g.*, Delivery Confirmation, otherwise not available to certain items under the Letters and Sealed

⁹⁹ Modification by the Governors changed the markup index for Cards to 0.629.

Parcels subclass of First-Class Mail.¹⁰⁰ Priority Mail contains both matter that is subject to the Private Express Statutes as well as items that may be carried outside the mail without restriction.

[5299] Priority Mail competes in the two- to three-day document and package delivery market. It receives expeditious handling and transportation, and includes value-added features such as Delivery Confirmation, which in the electronic option, is available at no additional charge; and Signature Confirmation, Return Receipt, and Pickup service for which additional charges apply. Private enterprise carriers in this very competitive market enhance their product offerings with features such as day-certain delivery and minimum insurance in the base rate not offered by Priority Mail. See USPS-T-33 at 7.

[5300] Generally, Priority Mail rates vary by weight and zone. Exceptions include Priority Mail weighing one pound or less, which is currently charged a uniform \$4.05; and Priority Mail sent in either the Flat Rate Envelope or Flat Rate Boxes provided by the Postal Service. The Flat Rate Envelope is subject to the one-pound rate regardless of weight or destination. The current rate for a Flat Rate Box, an experimental classification which the Postal Service proposes to make permanent in this proceeding, is \$8.10 regardless of weight or destination. Priority Mail envelopes and boxes, including the flat rate products, are available without additional charge.

b. Postal Service Proposal

[5301] On behalf of the Postal Service, witness Scherer (USPS-T-33) proposes Priority Mail rates that produce an average rate increase of 13.6 percent which corresponds with witness O'Hara's (USPS-T-31) target cost coverage of 163 percent. USPS-T-33 at 6, 61. Witness Scherer also proposes three classification changes, none of which is contested. Each is addressed below.

¹⁰⁰ Delivery Confirmation is limited to parcel-shaped Letters and Sealed Parcels mail.

c. Proposed Classification Changes

(1) Dimensional Weight Pricing

[5302] Dimensional weight (dim-weight) pricing is a pricing method, applicable to parcels, that considers the density (weight in relation to cubic volume) of the parcel. *Id.* at 13. Witness Scherer proposes dim-weight pricing in Zones 5-8 for parcels exceeding one cubic foot for a certain density threshold. Parcels destinating in Zones 5-8 generally receive air transportation. Dim-weight pricing considers the density of packages and charges low density parcels based on density and high density parcels based on weight. Witness Scherer testifies that “dim-weight” pricing will apply to an estimated 2.3 percent of Priority Mail volume. *Id.*

[5303] Witness Scherer advances several reasons in support of the classification change. First, he indicates that the underlying air transportation costs of Priority Mail are incurred mostly on a cubic foot basis: 96 percent are cube-related and only 4 percent are weight-related. USPS-LR-L-39 at 11. He asserts that Priority Mail is currently losing money on lightweight, bulky parcels. For test year purposes, he estimates that parcels eligible for dim-weighting would lose \$32.1 million. USPS-T-33 at 17. Dim-weighting redresses this problem incorporating cubic volume as a pricing determinant.

[5304] Second, dim-weighting is the industry standard for pricing of air freight, including parcels. It is used by all major U.S. carriers, including UPS, FedEx, and DHL. *Id.* at 13-15.¹⁰¹

[5305] Third, Scherer contends that dim-weighting will send appropriate price signals to customers, providing an incentive to make better choices in what packaging materials they use and whether to send parcels by air or ground transportation. *Id.* at 26.

[5306] Finally, dim-weighting will increase contribution to institutional costs, by staunching acceptance of money-losing parcels, and provide a measure of relief to

¹⁰¹ Scherer believes that FedEx implemented dim-weighting in 1989, followed by UPS in 1994. Both now, along with DHL, apply dim-weighting to all parcels regardless of cubic volume. *Id.* at 14, n.7, 15.

shippers of heavier, more dense parcels whose current rates are somewhat inflated to offset losses on lightweight, bulky pieces. *Id.*

[5307] *Commission analysis.* No party opposes the proposed dim-weighting pricing classification proposal. Witness Scherer's analysis is thorough and his support for the proposed change is compelling. The Commission finds that the dim-weight pricing proposal satisfies the criteria of section 3623 of the Act. In particular, the Commission concludes that dim-weight pricing is fair and equitable. It results in more cost-based rates, sends appropriate price signals to mailers of lightweight, bulky parcels, and provides some rate relief to mailers of heavier, denser Priority Mail.

(2) Balloon Rate

[5308] Complementing the dim-weighting proposal, witness Scherer proposes to eliminate the 15-pound balloon rate for Zones 5-8, contending that dim-weighting renders the balloon rate largely redundant in those zones. He also asserts that eliminating the balloon rate will avoid potential confusion over which rate is applicable. *Id.* at 21.

[5309] In addition, Scherer proposes to increase the balloon rate in Local and Zones 1-4 from 15 pounds to 20 pounds. *Id.* at 32. The balloon rate, which applies to parcels measuring more than 84 inches in length and girth combined, is uniformly used in the ground transportation industry. The increase in the balloon rate weight increment to 20 pounds, the first since Docket No. R76-1, will bring the Postal Service's oversized rate more in line with other carriers' oversized parcel rates. *Id.* at 21, 32.

[5310] *Commission analysis.* As the impetus for the proposal, witness Scherer states that, on average, balloon parcels are barely covering their costs, implicitly, at 15 pounds. *Id.* at 32. Since the weight increment has not been increased since Docket No. R76-1, this conclusion is reasonable. Scherer notes that UPS, FedEx, and DHL all charge a 30-pound oversize rate for balloon-rated parcels. *Id.* at 21. No party challenges the proposed balloon rate increase. The Commission finds the proposal to

be reasonable and, therefore, recommends that the balloon rate be increased to 20 pounds.

(3) Flat Rate Box

[5311] The Postal Service proposes to make the Priority Mail Flat Rate Box, approved on an experimental basis in Docket No. MC2004-2, a permanent classification. See PRC Op. MC2004-2. The Flat Rate Box is available in two shapes, but both have the same internal capacity of 0.34 cubic feet. USPS-T-33 at 52; see DMCS § 223.41. In addition, the Postal Service has customized Flat Rate Boxes for several mailers, but has maintained the standard size (0.34 cubic feet), while altering the dimensions. The current rate is \$8.10 and, as the name suggests, does not vary by weight or zone.

[5312] Witness Scherer addresses the risk factors identified in Docket No. MC2004-2: revenue leakage and customer overpayment. He concludes that revenue leakage has been more than offset by contributions from some pieces buying-up and from new Priority Mail volumes. For FY 2005, he estimates an \$8 million net increase in contribution. *Id.* at 54-55.

[5313] Witness Scherer also concludes that the risk is minimal that customers might “overpay” for service using the Flat Rate Box instead of zone-rated Priority Mail when it is less expensive. *Id.* at 55. According to witness Scherer, customers are generally not substituting the Flat Rate Box for the weight- and zone-rated option, but instead are using both options. He notes that there is a disclaimer on the Flat Rate Box advising consumers that other Priority Mail options may be less costly, *id.* at 53, and contends that it can be presumed that most customers are making rational economic decisions in purchasing Priority Mail products. *Id.* at 55.

[5314] Scherer proposes to increase the rate to \$8.80, an increase of 8.6 percent. He derives the rate by equating the implicit cost coverage of the Flat Rate Box and Flat Rate Envelope because they offer similar convenience and ease of use. At the proposed

rate, the implicit Flat Rate Box coverage is 179 percent, 16 percentage points above the subclass average. *Id.* at 57-58.

[5315] *Commission analysis.* The proposal to make the Flat Rate Box a permanent classification satisfies the Act's classification criteria. 39 U.S.C. § 3623(c). By all accounts, the experiment has been successful. The Flat Rate Box serves customers well, offering a convenient and easy-to-use mailing option without any restrictions on alternative choices. 39 U.S.C. § 3623(c)(2) and (5). By the same token, the Postal Service has realized increased volumes, with the Flat Rate Box trending towards 3 percent of total Priority Mail volumes, and increased contribution. 39 U.S.C. § 3623(c)(5). At the recommended \$9.15 rate, the implicit cost coverage of 169 percent is above the subclass average, which is appropriate given the added value features of the service. Moreover, at that level, the proposed rate should not adversely affect any carriers in the private sector. In any event, no party contests the classification change or the proposed rate. Accordingly, finding the proposal to be fair and equitable, the Commission recommends that the Flat Rate Box classification be made permanent.

d. Rate Design

[5316] Witness Scherer develops Priority Mail rates by separating test year before-rates volume variable costs into per-piece, per-pound, and per-cubic foot unit cost elements and then applying the subclass cost coverage to generate per-piece, per-pound, and per-cubic foot rate elements. USPS-T-33 at 32-35. The development of the per-piece and per-pound rate elements is consistent with previous Priority Mail rate design.¹⁰² The per-cubic foot rate element is new to the Priority Mail rate design. Witness Scherer explains that the per-cubic foot rate element varies by weight (due to

¹⁰² The per-piece rate element is derived solely from "nontransportation" costs and is the same for each rate cell. The per-pound rate element, which is derived from both transportation and nontransportation costs, varies by weight and zone. *Id.* at 35.

the positive correlation between weight and cubic volume) and varies by zone (because some transportation costs are distance related). *Id.*

[5317] Witness Scherer also introduces several structural changes to the Priority Mail rate design intended “to more accurately reflect cost incurrence.” *Id.* at 6. These include the following changes:

- Distributing weight-related costs for the 3-70 pound weight increments based on the midpoint of the weight interval instead of using postage pounds or the upper limit of weight increments. *Id.* at 35-36.
- Distributing a portion of distance-related ground transportation costs to Zones 5-8 in recognition that such costs are incurred in connection with air transportation. *Id.* at 40-41.
- Distributing air transportation costs, which under the FedEx contract has no specific distance-related element, based on an economic cost adjustment factor reflecting an implicit distance-related element. *Id.* at 41-44.
- Establishing a separate rate for Zone 3 by de-averaging the Local zone and Zones 1-3. *Id.* at 31-32.

[5318] Witness Scherer also updates the Local share of surface transportation costs. Since Docket No. R90-1, an estimate of 12.35 percent of total Local and Zones 1-3, by weight, (postage pounds), has been used. Using data from POS One terminals as a proxy for all Priority Mail, Scherer found that 7.65 percent of all Priority Mail in Local plus Zone 1 in FY 2005, by weight, was Local. This percentage equates to 4.81 percent of the total in Local plus Zones 1 and 2, which is used to distribute surface transportation costs (based on cubic feet) to the Local zone. *Id.* 44-45. No party contests the Postal Service’s Priority Mail rate design.

[5319] *Commission analysis.* The various rate design and structure changes proposed by witness Scherer represent improvements in developing Priority Mail rates. Generally, the changes are intended to reflect cost incurrence more accurately than the existing rate design. Witness Scherer has done a commendable job explaining and

supporting the various changes. The Commission's recommended Priority Mail rates are developed using the Postal Service's rate design. Recommended rates differ from Postal Service proposed rates because the Commission substituted its attributable costs into the rate design spreadsheets.¹⁰³

(1) Distribution of Ground Transportation costs to Zones 5-8

[5320] Prior to this proceeding, Priority Mail rate design distributed all distance-related ground transportation costs to Zones 1-4, the zones in which trucks are typically used for end-to-end transportation. In this docket, the Postal Service sponsors the testimony of witness Nash, who estimates the percentage of distance-related ground transportation costs incurred in connection with air transportation.¹⁰⁴ USPS-T-16 at 9-10. Witness Scherer uses this percentage (14.13 percent) to distribute distance-related ground transportation costs to Zones 5-8.

[5321] On brief, based on his experience with two Priority Mail parcels, limited participator Carlson warns the Commission that the distribution of ground transportation costs to Zones 5-8 may be based on unreliable information. Carlson Brief, § IV at 14-15.

[5322] The Postal Service responds that Carlson's conclusion is unsubstantiated. Postal Service Reply Brief at 260. It contends that the information used by Nash represents the best available data. It further asserts that deviations from the Network Operations scheme would imply a longer haul than what was modeled. *Id.* at 260-61.

[5323] *Commission analysis.* Carlson does not contest the premise that some ground transportation costs should be distributed to Zones 5-8. Instead, he cautions that

¹⁰³ In particular, the per-piece and per-cubic foot attributable costs increased due to the Commission findings on attribution of mail processing costs and FedEx Day-Turn network costs. In replicating the Postal Service's rate design, the Commission found that witness Scherer's development of the Flat Box Rate differed slightly from his description (USPS-T-33 at 57-58), requiring an adjustment in the recommended rate to be consistent with the Priority Mail rate level.

¹⁰⁴ In an interrogatory, Carlson sought the mapping data used by witness Nash to identify the FedEx facility serving each origin SCF. Following protracted motions practice, the Postal Service was directed to provide the mapping file subject to protective conditions. See P.O. Ruling R2006-1/59, August 28, 2006.

the data on which witness Nash's estimate of interconnectivity is based may be suspect. The record contains no other estimate of interconnectivity; nor does Carlson suggest an alternative. The new distribution of ground transportation costs to Zones 5-8 represents an improvement over the status quo which assumes that there is no interconnectivity. The Commission's recommended rates reflect Nash's distribution of ground transportation costs to Zones 5-8.

(2) Pickup On-Demand Service

[5324] Pickup On-Demand service is available for Express Mail, Priority Mail, and Parcel Post on an on-call or scheduled basis. The current fee per pickup stop is \$13.25. Witness Page develops test year costs for on-call and scheduled of \$12.96 and \$11.70, respectively. Witness Scherer develops a test year weighted-average cost of \$12.95. He proposes to increase the pickup fee to \$14.25, yielding a cost coverage of 110.1%. USPS-T-33 at 60.

[5325] *Commission analysis.* An increase in the pickup fee is justified. No party contests the proposed increase. The Commission recommends that the Pickup On-Demand fee be set at \$14.25.

e. Cost Coverage

[5326] Witness O'Hara, the Postal Service's rate level witness, proposes a cost coverage for Priority Mail of 163 percent, which corresponds to an average rate increase of 13.6 percent. He reviews the non-cost factors of the Act, finding, among other things, that Priority Mail has a high intrinsic value of service given its handling and transportation (relative to First-Class Mail), plus the availability of Delivery Confirmation on pieces of all shapes. On the other hand, witness O'Hara observes that the economic value of service for Priority Mail is much lower than for First-Class Mail. Priority Mail has a much higher (in absolute value) price elasticity of -1.02 than either single-piece (-0.18) or workshare (-0.13) First-Class Mail. USPS-T-31 at 21.

[5327] Witness O'Hara analyzes factor 4 (effect on mailers) and factor 5 (alternatives available) in tandem, concluding that although the proposed 13.6 percent increase will adversely effect mailers, competitive alternatives are readily available to business mailers. He also notes that the general public has increasing access to competitive alternatives, citing the availability of UPS Stores and FedEx/Kinko's centers. *Id.*

[5328] Regarding the impact of the proposal on private sector enterprises engaged in delivering nonletter mail matter (factor 4), witness O'Hara argues that the above-average increase and the difference between test year revenues (\$5,189 million) and test year incremental costs (\$3,434 million) assure that the proposed rates are not unfair to competitors. *Id.* at 22-23.

[5329] On behalf of United Parcel Service (UPS), witness Geddes advocates a cost coverage for Priority Mail of 163 percent, which yields an average rate increase of 23.6 percent. UPS-T-3 at 12. Although the cost coverage is the same as proposed by the Postal Service, UPS's proposal is based on the Commission's costing methodology from Docket No. R2000-1. *Id.* at 9. Witness Geddes focuses principally on three of the non-cost factors of the Act, including value of service, impact on competitors, and the availability of alternatives. More specifically, he references witness O'Hara's comment that Priority Mail has a high intrinsic value of service. *Id.* at 16. Based on a review of Priority Mail volumes since 1990, he contends that recent data (for 2005 and 2006) suggest that Priority Mail has sufficiently high value that its volume can recover from events earlier in this decade that caused decline in volumes. *Id.* at 16-18.

[5330] Witness Geddes compares the markup indices for First-Class Mail and Priority Mail over time.¹⁰⁵ His analysis shows that beginning with Docket No. R97-1 the Priority Mail markup index has steadily declined, first falling below the systemwide average in Docket No. R2001-1, a settled case, and subsequently to only slightly above

¹⁰⁵ The markup index compares the markup for each subclass, i.e., the ratio the subclass' test year contribution to institutional costs to its attributable costs, to the systemwide markup of 1.0.

half the systemwide average as a result of the settlement in Docket No. R2005-1. Based on this analysis, he argues that “the danger [of the current Priority Mail markup index] appears to be rates that are excessively low, thus harming competitors.” *Id.* at 15.

[5331] Witness Geddes echoes witness O’Hara’s observation that Priority Mail operates in a highly competitive market. Given this competition and the general public’s access to the alternatives, he contends that an increase in the markup for Priority Mail will not unduly harm users. *Id.* at 15-16.

[5332] Finally, witness Geddes argues that the Priority Mail markup index should exceed the systemwide average. He recognizes, however, that goal may not be attainable in one rate case. Thus, he recommends adopting the Postal Service’s markup, 63 percent, as a first step in a process of increasing the markup over time. *Id.* at 20-21.

[5333] In response, the Postal Service submitted the rebuttal testimony of witness Robinson, who contends that witness Geddes’ proposed rate increase is unreasonable. USPS-RT-10 at 16. She takes issue with his argument that recent growth in Priority Mail volumes supports a greater rate increase. She notes that from FY 2000 to FY 2005, Priority Mail volumes declined by 27 percent, from 1,222 million to 887 million. Further, witness Robinson asserts that, assuming continuation of the FY 2005 annual growth rate of 5 percent, Priority Mail volumes would not achieve their FY 2000 levels for almost another seven years. In contrast, she points to UPS’s experience for the period 2000 to 2004, indicating that its combined deferred and ground volumes increased by 2.1 percent. *Id.* at 17.

[5334] In addition, Robinson criticizes Geddes’ recommended cost coverage, 163 percent, because it fails to adequately consider the various pricing criteria in light of the different cost bases that underlie the Postal Service’s and UPS’s coverage proposals. *Id.* at 18-19. She concludes that, notwithstanding that cost coverage may provide useful

guidance, “the Commission’s obligation is not simply to recommend cost coverages.” *Id.* at 19.

[5335] *Commission analysis.* The Commission recommends an average rate increase of 13.6 percent which results in a Priority Mail cost coverage of 149.8 percent. The recommended rates satisfy § 3622(b)(3) — they recover attributable costs (\$3.5 billion) and make a reasonable contribution to institutional costs (\$1.7 billion). In total, its contribution exceeds that made for all but three subclasses. On a unit basis, Priority Mail’s contribution is more than nine times that of First-Class Mail and 4.4 times greater than Parcel Post. The Priority Mail’s relatively greater contribution also is evident based on a unit attributable cost comparison. Parcel Post’s test year after-rates unit attributable cost is \$3.41. Its per-piece contribution to institutional costs, \$0.47, represents 13.8 percent of its unit attributable cost. In contrast, Priority Mail’s per-piece contribution, \$2.08, represents almost 50 percent of its unit attributable cost, \$4.18.

[5336] Witness Geddes’ starting point is Docket No. R2000-1, the last litigated rate case. On brief, UPS urges the Commission to return to its pre-Docket No. R97-1 approach for setting a robust Priority Mail cost coverage in this case. UPS Brief at 3. The arguments advanced by UPS (and its witness) are not unreasonable. In the Commission’s view, however, they do not fully consider the effects of intervening changes.

[5337] First, the own-price elasticity of Priority Mail has changed since Docket No. R2000-1, increasing from -0.81 to -1.02. *Compare*, Docket No. R2000-1, USPS-T-32 at 6 *with* Docket No. R2006-1, USPS-T-31 at 11.¹⁰⁶ The increase doubtless reflects both competitive alternatives and, to some degree, service distinctions between Priority Mail and offerings by private delivery firms, *e.g.*, no minimum insurance in the base rate and day-certain delivery. *See* UPS Brief at 5-6; Postal Service Reply Brief at 140. For pricing purposes, the consequences of the higher elasticity can not be ignored. Value of

¹⁰⁶ In Docket Nos. R97-1 and R2001-1, it was -0.771 and -0.754, respectively. *See* Docket No. R97-1, USPS-T-30 at 5; Docket No. R2001-1, USPS-T-28 at 6.

service (factor 2) is one of the non-cost factors considered by the Commission in determining reasonable cost coverage levels.

[5338] Second, Priority Mail volumes peaked in FY 2000 at 1.22 billion.¹⁰⁷ The average annual growth for the period FY 2000 through FY 2006 is -3.5 percent. UPS notes that recent data indicate positive annual growth. UPS-T-3 at 16-17. Nonetheless, FY 2006 Priority Mail volumes of 924 million are still almost 25 percent below their FY 2000 peak. In fact, the FY 2006 volumes do exceed volumes from any prior annual period until FY 1995, when they were 869 million.

[5339] On a test year before-rates basis, Priority Mail volumes are approximately 949.6 million. At the recommended rates, equaling an average rate increase of 13.6 percent, Priority Mail volumes decrease to an estimated 829.0 million. At UPS's proposed increase, 23.6 percent, Priority Mail after-rate volumes would drop rather precipitously to approximately 726 million.

[5340] The recommended rates reflect an above-average rate increase, which under the circumstances, is appropriate. Although the increase will affect mailers adversely, competitive alternatives are available for that portion of Priority Mail not subject to the Private Express Statutes. The latter does warrant some tempering of the coverage. At UPS's proposed rates, excessive Priority Mail volumes would be driven out of the system and thus have a substantial effect on the Postal Service.¹⁰⁸

[5341] While witness Geddes believes that Priority Mail's markup index should exceed the systemwide average, he recommends something less, implicitly recognizing the dislocation his recommendation would cause. UPS-T-3 at 20-21. The factors that are cited in support of both his current proposal and longer term objective of a markup

¹⁰⁷ Volume data from revenue, pieces and weight reports for relevant fiscal years.

¹⁰⁸ On brief, UPS warns against rates designed to preserve the Postal Service's market share and argues that Priority Mail should bear a greater portion of institutional costs. *See, e.g.*, UPS Brief at 3, 5. The above-average rate increase recommended for Priority Mail precipitates nearly a 13 percent decline in Priority Mail volumes in a market which by all accounts is expanding and can not fairly be characterized as protecting the Postal Service's market share.

index in excess of the systemwide average are “robust volumes,” available alternatives, improved access to the alternatives, and the “substantial value provided by Priority Mail[.]” *Id.* at 21. The Commission has closely considered these contentions and is not persuaded that they reflect existing circumstances to an extent that supports a rate increase in excess of 13.6 percent.¹⁰⁹

[5342] Third, UPS discusses Priority Mail’s cost coverage, citing the settlements in Docket Nos. R2001-1 and R2005-1 as causing the “precipitous decline in the share of institutional costs paid by Priority Mail.” UPS Brief at 3. UPS’s contention is not compelling.¹¹⁰ Cost coverage has value in assessing the relative burdens borne by the various subclasses within a particular proceeding. It has less value as a barometer of relative burdens across cases because from case-to-case many factors may influence coverage for a particular subclass, *e.g.*, changes in mail mix, attributable cost levels, and markets.¹¹¹ Beginning with Docket No. R2000-1, Priority Mail’s cost coverage has declined due in large measure to substantial increases in attributable costs, precipitating volume declines in reaction to substantial price increases.

[5343] Comparing cost coverage trends for Priority Mail and First-Class Mail, UPS asserts that “the cost coverage for monopoly First-Class letters increased steadily and substantially since Docket No. R97-1, with a dramatic increase resulting from Docket Nos. R2001-1 and R2005-1 settlements. UPS Brief at 4. Its claim underscores the peril of relying on coverage as indicative of relative burdens. In fact, since Docket No.

¹⁰⁹ UPS points to the proposed Within County rate increase of 24.4 percent as a measure of the reasonableness of its proposal. The comparison is misplaced. That some individual rates or even those for a subclass may increase substantially is no indication of the reasonableness of an unrelated proposal. The Postal Service’s proposed Within County increase is predicated upon underlying subclass cost increases, an issue not present in Priority Mail.

¹¹⁰ Furthermore, the premise is somewhat problematic. By their terms, the settlements which led to recommended rates in Docket Nos. R2001-1 and R2005-1 have no precedential effect. Thus, citing the outcomes as a basis for considering the merits of the Postal Service’s proposed rates (or alternatives to them) is misplaced.

¹¹¹ For similar reasons, reliance on markup indices without taking into account exogenous factors can be misleading.

R2000-1, First-Class letters contribution, as a percentage of the total, declined in each proceeding, including Docket No. R2005-1. That trend continues in this proceeding as well, with First-Class letters contributing an historic low of 55.3 percent of total contribution. In contrast, not only is Priority Mail's contribution as a percent of the total above Docket No. R2005-1 levels, it is also some 30 percent greater in total than the prior docket.¹¹²

[5344] In accepting the settlement in Docket No. R2005-1, the Commission signaled its intent to examine closely cost and rate relationships. PRC Op. R2005-1, ¶ 5032. It has done so, for example, employing ECP principles to design rates whenever feasible. Priority Mail has been affected in at least two ways — the attribution of the FedEx Day-Turn costs and the continued treatment of mail processing costs as essentially 100 percent volume variable. Furthermore, although the Priority Mail rate design is by no means perfect, the latest iteration includes improvements designed to follow costs more closely, *e.g.*, dim-weighting, and distributing transportation costs based on cubic volume.

[5345] Finally, although the Commission will not adopt UPS's proposed cost coverage, its recommended rates, corresponding with a coverage of 149.8 percent, represent in important ways a significant increase in Priority Mail's institutional cost burden. At recommended rates, Priority Mail's unit contribution increases to \$2.08, an increase of nearly 34 cents over the last litigated case.¹¹³ This level represents an historic high and is more than nine times the unit contribution of First-Class letters. The Priority Mail markup index increases to .63. Although this is less than UPS would prefer, it does represent an increase over the status quo and is reasonable based on the record in this proceeding.

¹¹² To make any meaningful conclusion regarding Priority Mail's share of institutional costs in comparison with Priority Mail contributions from earlier dockets would necessarily have to account for the variations in Priority Mail volumes. Even if one were to conclude that the share has declined, that would only be a factor for the Commission to consider rather than, as UPS implies, dispositive that coverage must be increased to historic levels.

¹¹³ The unit contribution in Docket No. R2005-1 was \$1.57, 51 cents per piece lower.

[5346] For all of the foregoing reasons, the Commission concludes that the recommended Priority Mail rates are fair and equitable and consistent with the factors and policies of the Act.

C. Standard Mail

1. Introduction

[5347] Standard Mail consists primarily of advertising circulars, catalogs, and product samples. However, any item with content not unique to the recipient can be mailed as Standard Mail. It contains four subclasses: (1) Regular; (2) Nonprofit; (3) Enhanced Carrier Route (ECR); and (4) Nonprofit Enhanced Carrier Route (NECR). It is a bulk class requiring a permit and a minimum of 200 pieces or 50 pounds per mailing. Each piece must weigh less than one pound and must meet minimum preparation and sorting requirements.¹¹⁴

[5348] The Standard Regular and Nonprofit subclasses currently reflect the same rate structure as well as the same presort, pre-barcode, and dropship categories. Both also contain rate distinctions for letters, flats, and residual shape pieces.¹¹⁵

[5349] Similarly, the rate structures are the same for ECR and NECR. Both subclasses contain the same density (basic, high-density, and saturation), pre-barcode, and dropship categories. Both contain rate distinctions for letters, flats, and residual shape pieces. The ECR subclasses contain a nonmachinable surcharge for letters.

[5350] Nonprofit and NECR rates are subject to 39 U.S.C. § 3626(a)(6)(A) which requires that the average revenue per piece for Nonprofit and NECR mail be equal to 60 percent of the average revenue per piece for the corresponding commercial subclass.¹¹⁶

[5351] First, the Commission traces the history of the Standard Mail subclasses. Next, the Commission evaluates the appropriate cost coverages and institutional cost burdens for the Standard Mail subclasses based on that history and other relevant

¹¹⁴ USPS-T-36 at 8.

¹¹⁵ Residual shape pieces pay a residual shape surcharge.

¹¹⁶ Specifically, the average revenue per piece must be calculated using TYBR volumes and recommended rates.

factors. It then addresses the proposed classification changes for the Regular and ECR subclasses, including the shape-based changes. After that, the Commission considers the appropriate rate design methodology to use as well as the various rates proposed by the participants. Subsequently, rate proposals for the nonprofit subclasses are discussed. Finally, the Commission presents its recommended rates for the Standard Regular and ECR subclasses.

2. History of Standard Mail Subclasses

[5352] Prior to Docket No. MC95-1, Standard Mail (then called third-class) contained three subclasses: Single Piece, Bulk Rate Regular, and Bulk Rate Nonprofit. In Docket No. MC95-1, the Postal Service proposed to divide the Bulk Rate Regular subclass into several new subclasses. In its recommended decision, the Commission noted that “[t]he driving factor for the definition of the subclass ... is the perceived differences in demand as well as costs, and the corroborating evidence of Postal Service and mailer support.” PRC Op. MC95-1, ¶ 5481. As a result of a successful evidentiary showing of such differences, the third-class Bulk Rate Regular subclass was divided into two new subclasses, Commercial Regular and Commercial ECR.¹¹⁷ In recommending the creation of these subclasses, the Commission found:

Of the new subclasses proposed by the Postal Service, only Enhanced Carrier Route has been shown on this record to exhibit sufficiently distinct market characteristics from the remainder of the subclass within which it currently is found to warrant treatment as a separate subclass for rate design purposes.

PRC Op. MC95-1, ¶ 4208. The Commission’s Opinion in MC95-1 went on to say that “the only benefit of disaggregating subclasses further would be the ability to reflect differences in demand or other non-cost factors of the Act in separate markups.” *Id.* at

¹¹⁷ In the later Docket No. MC96-2, the Nonprofit (Regular) and Nonprofit ECR subclasses were created.

¶ 4253. Appropriate markups were not addressed in Docket No. MC95-1 due to the proposal’s goal of being “contribution neutral.”¹¹⁸ Nonetheless, the Postal Service’s pricing witness for Standard Mail stated that “except for constraints such as contribution neutrality, they would have reduced coverages to the new, ‘efficient’ subclasses while shifting additional institutional cost coverage to the ‘regular’ mail.” PRC Op. MC95-1, ¶ 2129.¹¹⁹ (Footnote omitted.)

[5353] In Docket No. R97-1, the Postal Service proposed a rate increase for Standard ECR mail that was somewhat lower than the systemwide average increase. This was to “reflect[] the Service’s efforts to lower the very high cost coverage of this subclass.” PRC Op. R97-1, ¶ 5533. (Citation omitted.) Nevertheless, the Postal Service did not believe that a lower cost coverage than proposed was appropriate since (1) a lower cost coverage for ECR mail would impose higher cost coverages on other subclasses, and (2) a lower ECR cost coverage would have made it difficult to design rates resulting in a Regular automation 5-digit rate below that of ECR basic, which encourages movement of ECR letters into the automation mailstream. *Id.* at 5535. The Commission ultimately recommended in No. R97-1 a slightly lower percent increase than that proposed by the Postal Service, concluding that “even though several of the statutory factors might indicate a low ECR cost coverage, on balance the record supports an ECR cost coverage that is well above average.” *Id.* at 5547-50.

[5354] In Docket No. R2000-1, the Postal Service proposed a cost coverage for Standard ECR of 209 percent resulting in an average increase of 4.9 percent, somewhat below the proposed system average. *See* PRC Op. R2000-1, ¶¶ 5415, 5440. The Commission “accept[ed] the basic rate design methodology that underli[ay] the Service’s ECR proposal.” *Id.* at 5450.

¹¹⁸ The Postal Service’s reclassification proposal in Docket No. MC95-1 was designed to be “contribution neutral,” that is, have no effect on Postal Service finances.

¹¹⁹ *See also* Docket No. MC95-1, USPS-T-18 at 7 (“If not for the desire to avoid major rate relationship changes, I would propose a lower cost coverage for Enhanced Carrier route.”).

[5355] Docket Nos. R2001-1 and R2005-1 were largely settled cases and did not result in most issues relating to Standard Mail being fully and fairly litigated.

3. Cost Coverage

[5356] A number of participants have reviewed the history of the Standard Mail subclasses and conclude that the Commission has failed to adequately recognize the subclasses' distinguishing characteristics. The appropriate relationship between the cost coverages for Standard ECR and Standard Regular has been subject to significant dispute.¹²⁰ The Postal Service's proposed rates result in coverages of 169.7 percent for Standard Regular and 208.8 percent for Standard ECR under accepted costing methodology. Several intervenors argue that the proposed cost coverage for ECR is too high. Valpak also argues that the proposed Standard Regular cost coverage is too low. The Flute Network argues that the value of service for Standard Nonprofit Regular letters is low which should result in lower rates.¹²¹ These proposals are discussed below.

a. Standard ECR Subclasses

[5357] *Postal Service's Standard ECR cost coverage proposal.* The Postal Service proposes rates with an average increase of 8.9 percent, USPS-T-31 at 29-31, which

¹²⁰ This section only discusses the cost coverages and allocation proposals within the Standard Mail subclasses. The allocation of institutional costs between the Standard Mail class and other subclasses is discussed in Chapter IV: Pricing.

¹²¹ NAA witness Ingraham argues that witnesses Mitchell's and Prescott's reliance on Postal Service witness Thress's ECR elasticity estimates is inappropriate since the point estimate is subject to "sufficient statistical uncertainty as to undermine the validity of their conclusion[s]" since at a 95 percent confidence interval, Thress's elasticity range contains both elastic and inelastic values. NAA-RT-2 at 7. While this observation may be technically correct, this does not help the Commission choose an appropriate elasticity to estimate changes in mail volumes or help measure value of service. A point estimate for elasticity is necessary to make such calculations, and a better estimate has not been presented on this record. In fact, witness Ingraham conceded that Thress's estimate is the "the best guess" for ECR volume. Tr. 35/11870. Accordingly, the Commission uses Thress's elasticity estimate to measure volume and to help determine the value of service under 3622(b)(2).

results in a cost coverage of 208.8 percent under accepted costing methodologies. The proposed increase is just above the systemwide average of 8.5 percent. Witness O'Hara believes that this slightly above-average increase, and cost coverage indicates that competitors are not unfairly targeted by this increase. *Id.*

[5358] The characteristics of Standard ECR mail, according to Postal Service witness O'Hara, are similar to those of Standard Regular – a “relatively low” value of service, due to the fact that ECR lacks access to the collection system, uses ground transportation, and is subject to deferred delivery. *Id.* While the Postal Service attempts to meet mailer needs for specific delivery dates, this requires regular planning and coordination by the mailer, especially for high-density and saturation rate categories. *Id.* ECR has a very high degree of preparation by the mailer – the basic category must be line-of-travel sequenced and the high-density and saturation categories are walk sequenced.

[5359] ECR's price elasticity is about -1.1, which is much higher¹²² (in absolute value) than that of Standard Regular, First-Class Mail letters and cards, or Periodicals, which suggests, according to O'Hara, a “rather low” economic value of service. Due to their use of geographic targeting, ECR mailers have a “relatively high” number of alternatives, including alternative delivery firms and newspaper inserts.

[5360] Witness O'Hara notes that while these criteria might appear to indicate a cost coverage lower than actually proposed, it is important to keep in mind that as mailer preparation increases, volume-variable costs shrink, but institutional costs are not directly effected. ECR should provide a reasonable contribution per piece, according to O'Hara. He notes that the contribution per piece is about the same for both ECR and Standard Regular, despite the different cost coverages. *Id.*

[5361] *Participants' ECR cost coverage proposals.* In Docket No. R97-1, the Commission noted, “In subsequent cases, as more information specific to Standard A

¹²² The elasticity for Nonprofit ECR is about -0.3, but witness O'Hara believes that since Commercial ECR makes up about 83 percent of total ECR volume, the commercial elasticity provides a good indicator of the economic value of service for the subclasses as a whole.

Regular and ECR becomes available, these relative coverage levels may be adjusted as warranted.” PRC Op., R97-1 ¶ 5512. In this case, MOAA, SMC-Advo, and Valpak argue that the cost coverage for the Standard ECR subclasses is too high and should be reduced.¹²³

[5362] Valpak witness Mitchell argues that the cost coverage for Standard ECR should be decreased, while the coverage for Standard Regular is too low and should be increased.¹²⁴ He proposes a cost coverage for ECR of 177.0 percent under the accepted costing methodology.¹²⁵ This would result in a rate decrease for ECR of 8.47 percent. Valpak argues in support of its proposed rates that: (1) Docket No. MC95-1 de-averaged the third-class Bulk Rate Regular into separate ECR and Regular subclasses with the understanding that the markup for ECR should decrease, while the markup for Regular should increase; (2) the newly passed Postal Accountability and Enhancement Act (PAEA) calls for adjustments of “some magnitude” since it establishes a regime of price caps which may limit the ability to alter these rates in the future; and (3) due to the prior settlements, the cost bases for the current rates go back as far as eight years and do not take into account changes in postal operations and mail preparation.

¹²³ SMC-Advo agrees with MOAA and Valpak that the cost coverage for ECR is too high, but believes that the downward adjustment should be “moderate[] with the understanding that the cost coverage issue will need to be fully and finally resolved in the next (and likely) final rate case under current law.” SMC-Advo Brief at 19.

¹²⁴ The total contribution from the four subclasses of Standard Mail is approximately the same as that proposed by the Postal Service under witness Mitchell’s proposed rates. Witness Mitchell notes that due to P.L. 106-384, the cost coverages of the commercial and their corresponding nonprofit subclasses are linked, making the choice of cost coverages of these subclasses extremely important so that the burden of subsidizing nonprofits falls upon *all* mailers; not just the mailers in the associated commercial subclasses. VP-T-1 at 61-62.

¹²⁵ Witness Mitchell notes that “[i]f, at the time the Commission is formulating its recommendation, it seems clear either that statutory rate caps are not a possibility, in the near future, or that another rate case under the current rules will occur, the Commission could decide to accommodate the changes needed in two steps.” VP-T-1 at 97. In that event, he recommends a cost coverage for ECR of not more than 192 percent. Since the passage of the legislation is now known to have occurred, Valpak stated on brief “[i]f it appears that the Postal Service will file such [another] rate case, the step to a rational rate relationship between coverages for Standard ECR and Standard Regular could be made into two steps.” Valpak Brief at I-19.

[5363] In designing his proposed rates, Mitchell explicitly addresses all the relevant non-cost factors found in § 3622(b) in detail and how they apply to both the Standard subclasses.¹²⁶ These considerations, and especially the relative elasticities, cause him to conclude that a fair and equitable cost coverage for ECR should be “somewhat” below the coverage on Standard Regular. VP-T-1 at 94-97.¹²⁷

[5364] MOAA witness Prescott also reviews the reasons for establishing the Standard Mail ECR subclass and its subsequent rate history and cost coverages. MOAA-T-1. He notes that ECR volumes have declined by 6 percent since Docket No. MC95-1, from 34.1 billion pieces in 1998 to 32.0 billion pieces in 2005. See MOAA-T-1 at 19.¹²⁸ He then argues that the pricing factors of the Act do not support the Postal Service’s proposed ECR cost coverages; they instead support a cost coverage for ECR significantly below that for Regular. He believes this is appropriate for the following reasons: (1) the ECR subclass was created to give the Postal Service the ability to develop market-based pricing and preserve or increase mail volumes, which has not yet happened; (2) relative contributions per piece for Regular and ECR should not be considered;¹²⁹ and (3) the Postal Service’s past actual cost coverages for ECR have

¹²⁶ See VP-T-1 at 67-94. Witness Mitchell does not believe that factors (b)(7) and (b)(8) are applicable to Standard Mail. *Id.* at 67. In contrast to witness O’Hara, Valpak argues that a high degree of mail preparation should not be a sound justification for a high cost coverage on ECR. It believes that the logic behind (b)(6) is to recognize that through competition, low costs should mean low rates. Valpak Brief at I-10.

¹²⁷ Valpak also argues that an excessive cost coverage on ECR tends to create higher rates for local nonprofits, as compared to national nonprofit mailers (who tend to mail at lower-density Nonprofit Regular rates).

¹²⁸ The Postal Service argues that this decline reflects, in part, a migration of mail to the Regular subclass that was assumed to take place because of the elimination of automation basic ECR rate. Postal Service Reply Brief at 142.

¹²⁹ Postal Service witness O’Hara notes that the Postal Service’s proposed rates result in a contribution per piece for Standard Regular and Standard ECR mail where “both round to 10.0 cents.” USPS-T-31 at 30; Tr. 17/5076. MOAA witness Prescott argues that a comparison of the contribution per piece between the two Standard mail subclasses is inappropriate, and that the Commission should not rely on the comparison of contribution per piece when determining the institutional cost burden for Standard ECR. Valpak makes a similar argument. Valpak Brief at I-1-2; Valpak Reply Brief at I-8.

been considerably higher than those projected. However, MOAA does not suggest that lower ECR rates should be achieved by shifting institutional cost burden to Regular. Such a drastic change to the Regular subclass rates would “undoubtedly result in rate shock” for those mailers. MOAA Brief at 10; *see also* SMC-Advo Brief at 19.

[5365] NAA witness Sidak rebuts the Mitchell and Prescott testimonies and argues against a lower institutional cost contribution for Standard ECR. Witness Sidak contends that there has been a “fundamental change in the composition of the mailstream” since Docket No. MC95-1 that invalidates the premise underlying their proposals. In support of his analysis, he argues that the decline in the volume of First-Class Mail means that the Postal Service’s business model can no longer presume, as it has in the past, that growth in First-Class Mail volume will be sufficient to fund the growth of the Postal Service’s network. This decline is based in part on the tremendous growth in broadband deployment in recent years as a viable substitute for First-Class Mail. Further, he contends that witness Thress has likely underestimated the true effect of electronic diversion on First-Class Mail volumes, citing the use of the one-year lagged measure of broadband subscribers. In contrast, he argues that there is no evidence that Standard Regular or ECR has experienced a significant diversion due to electronic communications. In fact, broadband appears complementary to Standard Mail. Witness Sidak believes that Standard Mail should bear a portion of the institutional costs currently borne by First-Class Mail and that this fundamental change should result in the institutional cost contributions of Standard ECR increasing, rather than decreasing as proposed by witnesses Prescott and Mitchell.

[5366] On brief, MOAA argues that witness Sidak’s rebuttal testimony does not appropriately acknowledge the differences between the Standard Regular and Standard ECR subclasses. In particular, it points out the vast differences in elasticities in those subclasses and the fact that ECR volumes have declined since 1998 while Regular

volumes have risen. MOAA Brief at 17.¹³⁰ MOAA also argues that electronic diversion can impact the Standard Mail subclasses.

[5367] NAA argues that witnesses Mitchell's and Prescott's arguments for lowering the institutional burden on ECR are incorrect since (1) their premise is wrong – the relative contribution of Standard ECR (relative to other classes) has declined since Docket No. MC95-1; (2) they place unwarranted reliance on the Postal Service's elasticity of demand for ECR; (3) they marginalize the concept of value of service to little more than own-price elasticity of demand; and (4) they fail to consider unit contributions, total contributions, and relative contributions (including markup indices) in addition to cost coverage.¹³¹ NAA Brief at 42-44.

[5368] On rebuttal, Postal Service witness Kiefer testifies that Mitchell's approach does not adequately take into account current rate relationships or the impact on mailers. He argues that even if Docket No. MC95-1 and subsequent rate cases intended to lower Standard ECR's cost coverage, circumstances, both within and outside Standard Mail, have changed, and those changes must be taken into consideration. Postal Service witness Robinson criticizes Mitchell for not considering the effects of his recommendations on other subclasses and the revenue requirements of the Postal Service as a whole. USPS-RT-10 at 21.

[5369] On brief, the Postal Service argues that Valpak's cost coverage arguments are "longing for the rate level relationships of yester-year." Postal Service Brief at 158. It also contends that even if one were to accept Valpak's argument that the ECR cost coverage is too high, it would be unfair to shift that entire burden to Standard Regular and would instead require a complete reconsideration of cost coverages for all the subclasses. Additionally, the Postal Service argues that Standard ECR has no "special status" and should not be any more entitled to a pre-reform "nip/tuck" before PAEA is in

¹³⁰ Valpak and SMC-Advo make similar arguments. SMC-Advo Brief at 22; Valpak Reply Brief at I-6.

¹³¹ As the Postal Service notes, "all else being equal, the cost coverage on workshared mail is higher than that of comparable non-workshared mail because the unit cost of workshare mail is lower." Postal Service Brief at 159.

full effect than any other subclass. It notes in passing, however, that the Postal Service has generally proposed price increases for ECR that were below those proposed for Standard Regular, meaning that the cost coverage of ECR relative to the systemwide average has been declining (and the current docket follows that trend).

[5370] The Postal Service also contests MOAA's argument that Standard Mail ECR cost coverages have repeatedly turned out higher than previously predicted by the Postal Service. It argues that MOAA has identified no systematic bias in estimating ECR revenues or costs and the current forecasts have not been challenged. Accordingly, it believes that this "string of higher coverages than estimated should have no more predictive value than, for example, three consecutive coin tosses coming up heads have with regard to a fourth coin toss." Postal Service Reply Brief at 142. The Postal Service also believes that MOAA is misconstruing witness O'Hara's testimony regarding the relative unit contributions of ECR and Regular. It argues that "MOAA has turned this simple observation into a policy for pricing ECR," when, in fact, O'Hara never claims that equality of contributions is the basis for his rate levels. *Id.* at 143-44.

[5371] On reply, Valpak contends that the relative size of First-Class Mail volume has had nothing to do with cost coverage decisions in the past and relative volumes are not relevant to ratesetting.¹³² Instead, the factors of the Act should be used to determine cost coverage. Valpak also criticizes the Postal Service's argument that, with respect to the passage of the PAEA, Valpak has taken the position that ECR has "special status." Valpak clarifies that it believes that all subclasses should be at appropriate cost coverages going into any price cap regime.

[5372] On reply, Association of Alternate Postal Systems (AAPS) argues that Valpak's premise with respect to the impact of the PAEA is wrong. It believes that there is no urgency towards shifting any institutional costs between Standard Regular and Standard Mail ECR because the PAEA allows the Postal Service to make such intra-class shifts under the price cap regime. AAPS Reply Brief at 2.

¹³² MOAA makes this same point. MOAA Reply Brief at 2-8.

[5373] *Commission analysis.* In each case, the Commission must independently apply each of the factors of § 3622(b) to each subclass to determine the appropriate allocation of institutional cost between all the subclasses. Over time, there are changes in worksharing, postal operations, value of service, competition, and other potential factors that must be taken into consideration when setting the cost coverages for the various subclasses of mail. At the same time, it is difficult to justify very large shifts in institutional cost burden in one case, since that may correspondingly produce undesirable large swings in rates.

[5374] Witness O'Hara notes that it is important to maintain a reasonable contribution per piece in each Standard Mail subclass, and the Commission agrees. Nevertheless, the main issue is determining what is a reasonable per-piece contribution for each subclass. The major purpose of dividing the third-class Bulk Regular into Standard ECR and Standard Regular in Docket No. MC95-1 was to recognize the cost and demand differences between them, although because that particular reclassification case was "contribution neutral," those differences were not able to be fully realized at that time. In Docket Nos. R97-1 and R2000-1, after taking into account all of the factors of the Act, the Commission found that Standard ECR's institutional cost burden should be lowered relative to the other subclasses based on this and other information. The last two rate cases, Docket Nos. R2001-1 and R2005-1, did not give the Commission a full opportunity to consider the relative cost coverages between all the subclasses, and accordingly, the "base" relative institutional cost burdens in this case for the Standard Mail subclasses might not be exactly where the Commission would have set them if Docket Nos. R2001-1 and R2005-1 were fully litigated. Nonetheless, that is the Commission's starting point.

[5375] Given that backdrop, the Commission examines the Postal Service's proposed rates for ECR. The Postal Service proposal decreases Standard ECR's per-piece contribution from 9.98 cents in Docket No. R2005-1 to 9.74 cents in the instant docket. This implicitly agrees with witness Mitchell that the current institutional contribution for ECR is too high.

[5376] The Commission finds that based on the facts and circumstances of this case and applying all the factors of the Act, the Postal Service's proposal is justified, although it may not go quite far enough. The Commission is persuaded that in order for the separation of subclasses in Docket No. MC95-1 to have meaning, the current cost, demand and other differences between the subclasses, as well as changes in mailer preparation and postal operations must be recognized more than the Postal Service has proposed in this case.

[5377] The Commission agrees that changed circumstances since Docket No. MC95-1 should be taken into account when setting institutional cost burdens, but only to the extent that those changed circumstances relate to the factors of the Act. The participants have not pointed out any additional facts related to the criteria of the Act that the Commission has not yet considered. The relative volume trends, in and of themselves, between First-Class Mail and Standard Mail are not directly related to setting institutional cost burdens under the Act. As Valpak and MOAA note, the Commission has not used relative volumes to help set cost coverages in the past, although changes in volume based on price can be relevant in evaluating differences in demand.

[5378] The Commission also agrees that witness Sidak's rebuttal testimony does not give appropriate weight to the differences between the ECR and Regular subclasses. Indeed, these differences were found to be so important that the Commission recommended dividing commercial Standard Mail into separate subclasses in Docket No. MC95-1. In setting cost coverages on a subclass by subclass basis, the Commission must appropriately recognize these differences as part of applying the pricing factors of the Act.

[5379] Several participants address witness O'Hara's examination of relative per piece contributions between Standard Regular and Standard ECR. It is appropriate and indeed necessary for the Commission to consider relative unit contributions, total contributions, cost coverage, as well as any other relevant comparisons, to get a complete picture of the various ways that one subclass compares to another in terms of

each's institutional burden. In short, there is no goal to obtain equal per-piece contributions from the two subclasses, but observing whether or not such a situation occurs can be an important part of due diligence. The Commission finds it appropriate that at recommended rates the unit contribution of ECR is now below the unit contribution of Standard Regular.

[5380] The Postal Service criticizes witness Mitchell for not considering the effects of his cost coverage recommendations on other subclasses and the revenue requirements of the Postal Service as a whole. This criticism is unwarranted. First, placing such a burden on intervenors would unnecessarily discourage their helpful contributions to the record, since this would place a very large additional litigation cost on participants who are only concerned about the isolated portions of the postal system that they utilize. Second, the adversarial process allows any participants who foresee problems with other participants' proposals to point out those problems for the Commission's consideration. This helps the Commission make decisions on a full and complete record.

[5381] MOAA's observation that the actual cost coverages for ECR have been considerably higher than those projected is not helpful in the Commission's analysis. As the Postal Service notes, MOAA does not identify any sort of bias or other problems with the Postal Service's forecasting methodology. Without evidence pinpointing forecasting problems, and with no better forecasting methodology presented on the record, the Commission does not find any reason to adjust the Postal Service's current ECR forecasts in this case based upon higher than predicted past cost coverages. The Commission recommends rates that achieve a cost coverage of 206.3 percent for ECR mail with a unit contribution of 9.47 cents per piece.

b. Standard Regular Subclasses

[5382] *Postal Service's Standard Regular cost coverage proposal.* The Postal Service proposes rates with an average increase of 9.6 percent, resulting in a cost

coverage of 169.7 percent under accepted costing methodologies. It claims that this target cost coverage is reasonable and that its proposed rates are fair and equitable when all the factors of the Act are considered. USPS-T-31 at 27-28.

[5383] The characteristics of Standard Regular mail, according to Postal Service witness O'Hara, indicate that Regular mail possesses "a relatively low intrinsic value of service" because (1) Regular mail is deferrable; (2) the Postal Service uses ground (versus air) transportation for its delivery; and (3) Regular mail lacks access to the collection system. *Id.* Mailers with needs for specific delivery dates are required to coordinate with the Postal Service which will strive to meet these needs. *Id.* The mail within Standard Regular has substantial mailer preparation, but not as much as ECR.

[5384] Regular and Nonprofit Regular both have price elasticities of about -0.3, which is higher (in absolute value) than that of First-Class letters (approximately -0.2), but lower than all the subclasses in Package Services, which suggests, according to O'Hara, an "intermediate" economic value of service. Due to their use of demographic targeting, the Regular subclasses face less alternative delivery service competition than the ECR subclasses.

[5385] *Participants' Standard Regular cost coverage proposal.* As discussed above, Valpak witness Mitchell argues that the cost coverage for Standard ECR is too high and should be reduced. He argues that the loss in institutional contribution from ECR should be made up by raising the institutional burden on Standard Regular. To do so, he proposes a cost coverage for Standard Regular of 180.2 percent.¹³³ This would result in an average rate increase for Regular of 17.56 percent. He bases his Standard Regular subclass cost coverage recommendation on an analysis that explicitly addresses all relevant non-cost factors of § 3622(b), and concludes that there is very little reason for Standard Regular cost coverage to be much below the cost coverage for First-Class. VP-T-1 at 94-97.

¹³³ If, however, it appears that another rate case will be filed under the current procedures, he would recommend a cost coverage for Standard Regular of "at least 175 percent." VP-T-1 at 97.

[5386] On the other hand, The Flute Network argues that the value of service for Standard Regular and in particular, Standard Nonprofit Regular letter mail, is low since the Postal Service does not meet its published delivery performance standards. Witness Pritchard testifies regarding data that she collected about the quality of service for the delivery of the Flute Network's Standard Mail.¹³⁴ She argues that her data shows that "both senders and receivers are getting very poor service, and it has been deteriorating for at least two and a half years that I can document." Flute-T-1 at 19.

[5387] Postal Service service standards call for The Flute Network's mailings to be reaching addresses nationwide within 10 days, and locally in 1 or 2 days. However, her data show that actual experience has been much worse. Specifically, her research shows that for the bulk of those 228 subscribers reporting the date that the February 2006 issue was received, it took between 12 and 19 days to deliver. Further, the bulk of the 307 subscribers who reported when the March 2006 issue was received said that it took between 32 and 41 days to deliver.¹³⁵ She concludes that the Postal Service is not living up to its own standards with respect to Standard Mail, and "one must question the kind of value in the so-called 'value-added' service that would substantiate an increase in postal rates ... when services are not provided as promised, and when the value of a piece of mail is so degraded by late delivery that the service ends up being totally useless." Flute-T-1 at 48.¹³⁶

[5388] The Flute Network submits that consistent and reliable service is at the core of what is value of service. It acknowledges that there is probably no way to forestall increases in postal rates, but believes that the "dismal" service that Standard Mail customers (especially Standard Regular Nonprofit letter mail customers) have been

¹³⁴ She notes that "there is nothing unusual about The Flute Network which would allow one to imagine that the experiences we've had are a problem unique to us." Flute-T-1 at 48.

¹³⁵ Witness Pritchard also kept track of the delivery of The Flute Network's issues from January 2005 to the May/June 2006 issue to her personal residence. Her experience was that the delivery time from Waynesville, NC to San Bernardino, CA took between 7 and 46 days depending on the issue.

¹³⁶ She also includes first-hand experiences of peer companies and subscribers.

experiencing, as demonstrated by witness Pritchard's testimony, should not go unrecognized. It asks that the Commission take this information into account when setting rates. Furthermore, it asks the Commission to include a "strong recommendation" that there be a firm commitment on the part of the Postal Service to demonstrate substantial improvement in the delivery service performance for Standard Mail. Flute Brief at 30.

[5389] The Postal Service argues that The Flute Network's survey is not representative of Standard Mail and should be afforded no material evidentiary weight. It points out that the survey only concerned one publication, and there is no evidence to suggest that its mailing patterns are representative. It does concede that "the data may provide a basis for concluding that there are opportunities for improving some of the service provided to a single publication." Postal Service Brief at 146.

[5390] *Commission analysis.* The Postal Service proposal increases the institutional cost contribution per piece for Standard Regular from 7.18 cents in Docket No. R2005-1 to 9.49 cents in the instant docket. This implicitly conforms with witness Mitchell's argument that the current institutional cost burden for Standard Regular is too low. Again, the Commission finds that based on the facts and circumstances of this case and applying all the factors of the Act, the Postal Service's proposal does not go quite far enough in raising the institutional cost burden for Standard Regular.

[5391] Nevertheless, the Commission has to be careful in making sure that it does not go too far in reallocating institutional costs. In addition to potentially producing undesirable large swings in rates for the two subclasses (under § 3622(b)(4)), it could also give the mistaken impression that the value of service in Standard Regular is relatively high, which runs contrary to the testimony submitted by The Flute Network.¹³⁷

¹³⁷ Although The Flute Network's arguments are said to apply to "Standard Mail (especially Standard Non-profit [Regular] Letter Mail)," Flute Brief at 3, the data presented are for the Regular subclasses. Accordingly, in light of the differences between the ECR and Regular subclasses discussed above (especially with respect to degrees of worksharing and dropshipment), the Commission considers these arguments applicable only to the Regular subclasses.

[5392] A more thorough analysis of the actual delivery performance for Standard Regular has never been presented for the Commission's consideration. The Commission is grateful for the testimony and data provided by The Flute Network. Although the data collected can not be considered a random sample or even close to a scientific analysis, the data unquestionably shows that service provided to The Flute Network newsletter is severely lacking, and it raises serious questions as to the delivery performance for other Standard Regular origin-based national mailings. It can not be dismissed as pure coincidence, especially given that the Postal Service has never presented any data showing delivery performance of Standard Regular Mail, let alone any better, more statistically unbiased data than The Flute Network's. The Commission finds that The Flute Network's data is reason to refrain from increasing the Standard Regular institutional cost burden much more than proposed by the Postal Service. The Commission recommends a cost coverage for Standard Regular of 170.8 percent with a unit contribution of 9.54 cents per piece.

4. Classification Proposals

[5393] The Postal Service proposes classification changes seeking to recognize shape, and advances in mail processing technology. USPS-T-36 at 15. The Postal Service believes that establishing classifications to facilitate recognizing cost differences is important and complies with the requirements of 39 U.S.C. § 3623. With the exception of the proposal to eliminate the automation basic rate category in ECR, discussed below, intervenors do not oppose the Postal Service's proposed classification changes. However, several intervenors offer their own additional classification changes. Each proposal is discussed in turn.

a. Regular and Nonprofit (Regular) Subclasses Classification Proposals

[5394] The Postal Service believes that its classification changes will lead to rates that better reflect the costs of the mailstreams in which each piece is likely to be processed and delivered. This will also, according to the Postal Service, encourage mailers to adopt practices that are more efficient from mail processing and delivery perspectives and lead to lower overall costs for Standard Regular.

(1) Nomenclature Changes

[5395] The Postal Service proposes the following nomenclature changes to DMCS §§ 321-324 in this docket: (1) change the name of the Standard Nonprofit subclass to Standard Nonprofit Regular and (2) change the name of the rate categories currently known as “presorted” to “non-automation.” It believes that the former proposed change will remove potential confusion about whether the term “nonprofit” is used as a subclass name or otherwise. The Postal Service believes that the latter proposed change better describes the non-barcoded mail in these categories and will avoid potential confusion since all Standard Mail is required to be presorted. These unopposed changes to rename certain categories and subclasses will result in more clear DMCS language. The Commission incorporates these changes into its recommended decision.

(2) Shape-Based and Presort De-averaging Changes

[5396] The Postal Service proposes several rate design changes to continue the de-averaging of the nonletters rate category in both the Regular and Nonprofit Regular subclasses that was started with the residual shape surcharge in Docket No. R97-1. It also further de-averages rates by presort level. Witness Kiefer argues that these changes will better align pricing with the way that mailpieces are processed and delivered, as well as furthering the Postal Service’s goal of establishing a more shape-based mail processing and delivery system. USPS-T-36 at 9-10. The Postal

Service's proposals, as well as intervenor classification proposals are discussed below by shape.

(a) Letters

[5397] The rate structure for automation letters is not proposed to change. Witness Kiefer does propose to expand rate categories for non-automation letters into machinable and nonmachinable letters. Since the Postal Service barcodes machinable letters at the automated area distribution center (AADC) which causes finer levels of presorting have little or no value, witness Kiefer proposes that non-automation machinable letters have two presort rate options: mixed automated area distribution center (MAADC) and AADC. USPS-T-36 at 13. For nonmachinable letters which are sorted manually, he seeks to mirror those presort levels in existence for automation letters. The Postal Service believes that the cost of manual sortation varies significantly depending on how finely presorted the letters are when presented for processing.¹³⁸ Accordingly, the Postal Service is proposing a rate structure to de-average the least finely presorted manual letters from more highly presorted pieces to encourage mailers to make their letters machinable, or if not, to more finely presort them. *Id.* at 13-14.

[5398] *"Heavy Letters" proposal.* PostCom witnesses Robert Posch and Godfred Otuteye propose to increase the maximum weight for Standard Mail automation letters from 3.5 ounces to four ounces.¹³⁹ PostCom-T-3 and PostCom-T-8. Under the Postal Service's existing rates, automation letters that weigh more than 3.3 ounces but not more than 3.5 ounces, pay the flat piece and pound rates, but receive a discount of the difference between the letter and flat minimum piece rates. See DMCS Rate Schedules 321B, n.2 and 322, n.4. Such mailpieces are known as "heavy letters." Currently

¹³⁸ See USPS-LR-L-48, STANDARD.xls, worksheet NONAUTO NMACH SUM.

¹³⁹ On brief, PostCom recognizes that the record shows that the heaviest weight letter that appears to have been tested by the Postal Service is 3.7 ounces. Accordingly, PostCom states that if the Commission does not find a sufficient evidentiary basis for increasing the weight limit to four ounces, it should consider raising it to 3.7 ounces to comport with the evidence. PostCom Brief at 17.

automation-compatible letters weighing between 3.5 and four ounces pay applicable flats rates. PostCom witnesses Posch and Otuteye propose to increase the maximum weight of Standard Mail automation Regular and ECR letters from 3.5 ounces to 4.0 ounces. Their proposal would allow automation letters that weigh more than 3.3 ounces but not more than 4.0 ounces to pay the flat piece and pound rates, but receive a discount in the difference between the letter and flat minimum piece rates.

[5399] In support of this proposal, they make the following three arguments. First, PostCom argues that these “heavy letters” can generate business for the Postal Service through a multiplier effect – direct mailers would be allowed to use the additional weight to promote their own products or clubs through inserts in those heavier mailpieces. This could, in turn, lead to larger and new mailing lists, more list rentals, and corresponding growth in additional solicitation mailings, potentially providing the Postal Service with volume growth through additional business reply correspondence, package shipments, payment remittance, and other First-Class customer correspondence. PostCom-T-3 at 3.

[5400] Second, PostCom’s witnesses argue that the existing pricing structure discourages adding additional inserts and constrains the use of mail as a marketing medium. For example, if a solicitation including two 1/10 ounce inserts weighs 3.5 ounces, the large letter-flat differential makes adding an additional 1/10 ounce insert cost prohibitive. However, PostCom argues that extending the maximum weight to 4 ounces would permit mailers to include approximately five more inserts in the mailpiece at roughly the same incremental cost, keeping businesses from sending solicitation advertising dollars to print media, television, or electronic media.

[5401] Third, PostCom witnesses argue that it is unfair for the Postal Service to treat these pieces as flats for purposes of rates while treating them operationally as

letters, and such treatment is not reasonably related to costs.¹⁴⁰ PostCom-T-3 at 6 and PostCom-T-8 at 3,10; *see also* PostCom Brief at 12.

[5402] On rebuttal, Postal Service witnesses Laws and McCrery argue that the maximum weight for “heavy” letters should not be raised to 4.0 ounces. They point to a study done in 2001 which reported “excessive amounts of damage” to the Postal Service’s processing equipment when complete sets of letters weighing 3.7 ounces were run. Tr. 11/2843-46 and USPS-RT-16 at 13. Witness McCrery notes that since the study was completed, there have been no changes to the equipment fleet that would change the study’s conclusions.¹⁴¹ USPS-RT-14 at 6. Further, witness Laws claims that although witness Otuteye states that his pieces above 3.5 ounces are processing successfully on the automated letter sorting equipment, the Postal Service has experienced “countless” instances of “heavy letters” below the 3.5 ounce limit processing poorly. USPS-RT-16 at 13. He believes that the established weight limit should be retained with the goal of encouraging an automated letter mailstream that has a high probability of processing at an acceptable throughput and jam rate. *Id.*

[5403] On brief, PostCom makes an additional argument. It claims that the 2001 study was biased, as evidenced by its use of the word “preemptive,” and that this treatment of letters is discriminatory under section 403(c) of the Act. It further notes that the 2001 study showed that the 2 percent seeded decks of 3.7 ounce letters mail were “no cause for concern.” Tr. 11/2846. Accordingly, “running heavy letters on the automated equipment may require operations personnel to blend them in with other lighter pieces as they are fed into automation equipment.” PostCom Brief at 16. Additionally, PostCom believes that the evidence shows that “there is no evidence that it

¹⁴⁰ Witness Otuteye’s observations and personal experience with the Postal Service demonstrates that automation compatible mailpieces above the breakpoint, or heavier than 3.5 ounces, are processed on the Postal Service’s automation equipment. PostCom-T-8 at 7.

¹⁴¹ Witness McCrery does note that certain machines are being upgraded for “expanded capabilities,” however, even after that process is completed, only 617 out of approximately 5,200 machines will be able to process heavier mailpieces by the middle of 2007. USPS-RT-14 at 6-8. These expanded capabilities machines also have a much lower throughput than their non-upgraded counterparts. *Id.* at 7, n.4.

was the weight of the mailpieces, rather than some other characteristic” that caused equipment problems. *Id.* at 15.

[5404] *Commission analysis.* PostCom claims that it is not asking the Commission to dictate operational matters to the Postal Service, yet its proposed classification change may require operations personnel to process heavy letters by seeding them with lighter ones. Absent exceptional circumstances, it is not appropriate for the Commission to dictate how the Postal Service is to process its mail.

[5405] Even though the current 3.5 ounce weight limit may not be a perfect measurement for determining when unacceptable amounts of equipment damage will occur, it is an adequate proxy for the actual mail characteristics that are causing damage to the processing equipment. The Commission is sympathetic to mailers who send items that may be processed without problems on automation equipment, yet are not charged the lower automation rates. However, lines of demarcation between rate categories must be drawn. PostCom needs to work with the Postal Service to try to find mail preparation standards that will allow heavier pieces to be processed on automation equipment without excessive damage.

[5406] PostCom’s bias and discrimination claims are without merit. The use of the word preemptive does not mean that the Postal Service was predisposed to a particular outcome and is contrary to the 2 percent seeded results. Further, section 403(c) does not require that each mailer’s individual mailpiece be changed for the actual mail processing costs for that particular mailpiece. Many of the Postal Service’s costs are based on averages or proxies when better information is not available. Section 403(c) accommodates proxies until better data can be developed. Finally, PostCom’s arguments that heavy letters may have a multiplier effect that will foster indirect volume growth are entirely speculative and are entitled to little weight.

[5407] The Postal Service’s classification proposals for letters are unopposed and the Commission does not independently find any reason to refrain from adopting them. The Commission concludes that the expanded letter rate categories will allow costs to be more accurately reflected.

(b) Flats

[5408] The Postal Service proposes to replace the current, broad nonletters shape category with three new categories that it believes “better reflect how each type of mail is processed.” USPS-T-36 at 15. Most pieces that were previously nonletters will continue to be processed in the flats mailstream, according to the Postal Service, and therefore will be treated for ratemaking purposes as a separate flat shape category. The two other new shape-based categories that the Postal Service proposes to create are parcels and “Not Flat-Machinable” (NFM) pieces, discussed below.¹⁴²

[5409] Eligibility for flats rate treatment is proposed to be tightened under the Postal Service’s proposal. Certain rigid pieces or pieces (currently qualifying for automation nonletters rates) whose thickness exceeds 0.75 inch will not qualify as flats under the Postal Service’s proposal. USPS-T-36 at 15-16. Witness Kiefer argues that the separation of nonletters into flats and other shape-based categories will make it easier for the rate designs for pieces in different mailstreams to evolve toward more rational rate structures and relationships. His proposed flats rate design also de-averages the presort categories for automation and non-automation flats. This allows finer presort discount categories to have deeper discounts for the most highly workshared mail and, conversely, higher rates for the most costly, least workshared flats.

[5410] *Commission analysis.* The Postal Service’s classification proposals for flats are unopposed and the Commission does not independently find any reason not to adopt them. The Commission concludes that the tighter flats definition will more closely reflect operational realities and the enhanced de-averaging of rate categories will encourage efficient mailer behavior.

¹⁴² These NFM pieces are also sometimes referred to as “hybrids.” USPS-T-36 at 4, n.1.

(c) Parcels

[5411] Currently, parcels are simply charged nonletter rates with a surcharge, and parcels presort and dropship options are the same as those pertaining to flats. Witness Kiefer's proposal splits parcels away from flats for rate purposes. Specifically, he proposes the following parcel-related classification changes:

- Abolish the residual shape surcharge;
- De-average the rate design so it is independent of the flats rate design;
- Separate rate categories for machinable and nonmachinable parcels;
- Create a non-barcoded parcels surcharge; and
- Allow parcels access to DDU discounts.

Witness Kiefer argues that this set of classification changes are appropriate for the following reasons:

- It facilitates adjusting prices for Standard Mail parcels to increase their cost coverage and facilitates the Postal Service's goal of a long run merger of these parcels into a general parcel subclass;
- It permits rate distinctions reflecting and encouraging worksharing and machinability in ways that are not available in the current nonletters rate design;
- It allows offering of options, such as expanded dropship discounts, that are not currently available, or that may not make sense for the majority of the current nonletter category; and
- It gives more visibility for parcels in the Postal Service's cost and volume reporting systems and will therefore give the Postal Service and Commission better information on which to base pricing decisions for these parcels in the future.

This proposal for a separate classification for parcels is of great importance to the Postal Service and is a very high pricing and classification goal for nonletters in this docket.

Postal Service Brief at 278 (citing USPS-T-36 at 10; USPS-RT-11 at 6, 7).

[5412] *Ride-Along inserts*. PostCom witness Horowitz proposes to allow, at no additional charge, up to two ounces of advertising inserts with merchandise in Standard Mail parcels even if such Ride-Alongs breach the 16-ounce maximum weight limit. USPS-T-6 at 10-12. Witness Horowitz argues that his proposal is beneficial because it

will increase volume and revenue for both mailers and the Postal Service by generating additional fulfillment packages and payments via First-Class Mail. He also notes that Bulk Bound Printed Matter allows print materials to be included — whether or not they relate to the eligible product — without limitation.

[5413] On rebuttal, Postal Service witness Kiefer argues against this change. USPS-RT-11 at 3. He does not dispute the contention that allowing advertising inserts would have some value to mailers; however, he does not believe that the Commission has enough information to determine whether such benefits will be trivial or material. He also believes that witness Horowitz's proposal raises the following concerns that need to be addressed before it should be seriously considered for recommendation: (1) the proposal fails to address how the Postal Service is to determine that the additional weight is due to advertising inserts only, not increased merchandise weight; (2) the proposal fails to address the fairness of implementing this proposal in Standard Mail, but not in other classes where similar benefits could, arguably, ensue; (3) the proposal fails to address the rationale for limiting the proposal to parcels given that similar multiplier effect benefits could exist with flat-shaped pieces; and (4) the proposal fails to address the extra costs of allowing mailers to include this additional advertising material. *Id.* at 5.

[5414] *Commission analysis.* On this record, there is no evidence that there will be any positive multiplier effect that will increase net contribution to the Postal Service by increasing the weight limit of Standard Mail parcels for Ride-Alongs. All the record contains on this point are statements that a higher weight limit increases the ability to send third-party inserts which might generate additional mail volume. This type of testimony is insufficient to convince the Commission of the existence of an actual positive multiplier effect. It does not address whether potential parcel Ride-Along inserts may be mailed anyway as either their own mailpieces or as inserts in other pieces. Further, the concerns raised by the Postal Service relating to implementation of the details of the proposal, fairness, and the lack of data regarding cost considerations are serious and need to be adequately addressed before the Commission can recommend such a proposal.

[5415] The Postal Service's classification proposals for parcels are unopposed and the Commission finds that adopting them is in the best interest of the Postal Service. The changes will encourage worksharing, allow pricing Standard Mail parcels to better reflect costs, and will allow the Postal Service to better track these mailpieces in the appropriate data reporting systems, resulting in more accurate costs. This should result in future pricing decisions based on more accurate costs.

(d) Not Flat-Machinables

[5416] The Postal Service is concerned about pieces that are somewhat flat shaped, but rigid, or that are between .75 and 1.25 inches in thickness. USPS-T-36 at 10. Many of these pieces currently pay postage as automation flats under the USFM 1000 (formerly FSM 1000) exception. However, the Postal Service's operational experience has shown that these pieces are commonly processed, not in the automation flats mailstream, but either manually or in the parcel mail stream.¹⁴³ This means that these pieces may be counted as parcels for cost allocation purposes but counted as flats for volume purposes making it difficult to accurately estimate the unit cost of Standard Mail parcels.

[5417] However, while many of these pieces are processed as parcels, according to witness Kiefer, many of these pieces have characteristics that allow them to be merged into the flats mailstream at some point. Small rigid flat-shaped pieces that are thin enough can be cased by the carrier and do not have to be held out as parcels. Accordingly, the Postal Service proposed the following solution:

- Tighten the definition of what qualifies as a flat for rate purposes; pieces that are inflexible or too thick should no longer be afforded flats rate treatment and the current USFM 1000 exception should be eliminated.

¹⁴³ See Tr. 18A/5322-5341 and USPS-T-36 at 21-22.

- Create a separate rate design for not flat-machinables (NFMs) – the small, flat-shaped pieces that no longer qualify as flats due to their rigidity, but could still be cased along with flats for delivery purposes.
- Establish that pieces currently eligible to pay flat rates, but that would not ordinarily qualify as either flats or NFMs, be eligible for NFM rate treatment for rate migration purposes. The Postal Service proposes to mitigate the effect on pieces going from automation flats rates to parcel rates by allowing these pieces to qualify temporarily for NFM rates.

This proposal for a separate classification for NFMs is of great importance to the Postal Service and is a very high pricing and classification goal for nonletters in this docket. Postal Service Brief at 278, 80 (citing USPS-T-36 at 12; USPS-RT-11 at 6, 7).

[5418] The new proposed category for these types of pieces is called not flat-machinable and is proposed to have the following classification elements:

- A de-averaged rate design independent of the flats rate design;
- A non-barcoded NFM surcharge; and
- Eligibility for DDU discounts.

The NFM proposal will, according to the Postal Service, better align NFM mail with the way it is processed, allow rates to better reflect costs, and encourage mailers to adopt more efficient practices, worksharing, and machinability, which will in turn lower Postal Service costs. Witness Kiefer believes that the creation of the NFM category will allow these pieces to be better tracked in the Postal Service's cost and volume reporting systems resulting in better information for future pricing decisions. Creation of this category will also mitigate the rate impact on those UFSM automation flats that would not qualify as flats (and otherwise would become Standard Mail parcels).

[5419] *Commission analysis.* No participant opposes the Service's not flat-machinable classification changes. Nonetheless, the NFM category is troublesome, given that there are no cost data for these pieces or reliable volume estimates broken down by mail mix. The reliability of the NFM data is a serious issue for several participants, but is used as the basis for arguments to mitigate NFM rates; not as a rationale for opposing classification changes. Accordingly, the Commission's analysis of this data quality issue is discussed in section V.C.5.c. On balance, the Commission finds

it is more important to create the NFM category now, with less than perfect data, in the hope that such data will be developed to allow future rate design decisions for such mailpieces to be based on accurate costs.

[5420] The Commission finds that all these proposed changes are consistent with the requirements of 39 U.S.C. § 3623 and are fair and equitable. They will move the classification schedule more in the direction of recognizing shape-based costs caused by shape-based mail processing technology. They will also offer greater opportunities for worksharing and align the mail better with operations.

b. ECR and Nonprofit ECR Subclasses Proposals

[5421] There are several proposed classification changes to ECR and NECR subclasses in this case. The Postal Service's proposal and participants' proposals are discussed below, categorized by shape.

(1) Letters

[5422] Postal Service witness Kiefer proposes to eliminate the DDU discount for letters. Since the Postal Service intends to delivery point sequence (DPS) as many letters as possible by machine, and since DPS equipment is located mostly at plants, entering letters at the delivery unit no longer contributes to operational efficiency. The proposal does not prohibit entering ECR mail at delivery units; it only eliminates the discount for DDU entry.¹⁴⁴ However, witness Kiefer expects that given the extra cost to mailers of dropping mail at DDUs, few mailers will continue to do so.

[5423] *Automation Non-automation letter rate category.* Witness Kiefer's proposal also eliminates the automation basic rate category for letters. This rate is currently only available for mail sent to sites that do not receive DPSed letters from the plant.

¹⁴⁴ According to witnesses Kiefer and McCrery, removing the rate incentive to deposit letters at delivery units makes sense if those letters have to be transported back to plants at added cost.

However, the Postal Service intends to further centralize the sequencing operations in plants to the greatest extent possible and reduce the dependence on automated or manual sorting in delivery units. Accordingly, witness Kiefer believes that this rate is no longer warranted and assumes that ECR and NECR basic automation letters will migrate to the Regular subclasses and pay the automation 5-digit rates.

[5424] Valpak witness Mitchell contests the Postal Service's proposal to eliminate the automation basic letter rate arguing (1) that the automation basic ECR letter rate should remain in the DMCS and, (2) as a related issue, the rate for non-automation basic ECR letters should be de-linked from the 5-digit automation Regular letter rate.¹⁴⁵ Witness Mitchell notes that in PRC Op. R2005-1, ¶¶ 6074-75, the Commission stated that it "finds persuasive witness Mitchell's arguments for decoupling the ECR basic and Standard Regular 5-digit automation rates...."¹⁴⁶ He argues that the Postal Service's proposal to eliminate automation basic ECR effectively seeks to undo portions of Docket No. MC95-1 which sought to recognize the economic differences in the ECR and Regular subclasses. Moreover, since the automation basic letters are in accord with the definitions of ECR and the Postal Service's processing operations are "no different, no better, and no broader tha[n] its processing options for subject automation letters in ECR," VP-T-1 at 124, witness Mitchell argues that Witness Kiefer's rationale for eliminating the rate category in favor of 5-digit automation regular letter category is not persuasive. Similarly, witness Mitchell argues that ECR basic rates should not be "artificially elevated" by being linked to 5-digit automation Regular, and should instead be based on their costs.

[5425] On rebuttal, Postal Service witness McCrery testifies that continuing the preparation of automation letters in pure carrier route trays no longer conforms to

¹⁴⁵ Although the "decoupling" of basic ECR letters and 5-digit automation Regular letters may be a "rate" issue, as opposed to a "classification" issue, it is discussed here due to its relationship to the proposed elimination of the automation basic rate category.

¹⁴⁶ Witness Mitchell argues that this is appropriate since any non-cost based elevation in the rates for basic letters also elevates the rates for high-density and saturation letters as a result.

operational realities and increases costs. He notes that close to 90 percent of the delivery point sequencing of letters is performed on DBCS equipment and that unrestricted carrier route preparation of automation letters would only result in more finely presorted trays that would provide no additional value in postal processing since the older equipment – where the carrier route presort was valuable – is being completely phased out. USPS-RT-14 at 3-4. Also, witness Kiefer argues that it is important to set the ECR basic letter rate above that of the Regular 5-digit automation letter rate to promote the automation program and to avoid giving mailers a rate incentive to prepare relatively higher cost carrier route bundles or containers rather than lower cost full 5-digit letter trays. Tr. 5/920;¹⁴⁷ USPS-RT-14 at 3-6.

[5426] *Commission analysis.* The Postal Service is operationally shifting towards more DPSing at the plants and less delivery point sequencing in smaller offices. In fact, the Postal Service “is in the early stages of ... completely phasing out the CSBCS fleet.” Postal Service Brief at 288. Eliminating the automation basic rate will help streamline the Postal Service’s offerings and operations. It will also further the Postal Service’s goal of centralizing delivery point sequencing on DBCS machines in postal plants. Accordingly, the Commission recommends eliminating the automation basic ECR letter rate category.¹⁴⁸

[5427] With respect to the de-linking proposal, in Docket No. R2005-1, the Commission found witness Mitchell’s arguments for decoupling the ECR basic and

¹⁴⁷ This also affects the letter/flat rate differential, discussed below.

¹⁴⁸ In its brief, Valpak concludes that one potential solution has not yet been considered: putting automation requirements on all basic ECR letters and putting a surcharge on those that are not automation compatible. Valpak Reply Brief at IV-23. This idea might benefit all mailers and better align the ECR letters rate categories. Indeed, although the Postal Service states that making automation mandatory in basic ECR will “provide no additional value in postal processing,” USPS-RT-14 at 3-4, this statement rings hollow. Since the Postal Service’s rationale for keeping basic ECR letters and automation 5-digit letters linked is to encourage automation, having basic ECR with an automation requirement would also accomplish this same goal. It also would further the Postal Service’s goal of increasing the automatable mailstream. The Commission encourages the Postal Service to explore the feasibility, cost, and benefits of this approach, especially given that the high-density and saturation rate categories adopted an automation requirement recently.

Standard Regular 5-digit automation rates to be persuasive. The Postal Service has not provided any new information or arguments to rebut those persuasive arguments.¹⁴⁹ Accordingly, the Commission sets the rates for ECR basic letters and for Standard Regular 5-digit automation letters independently. Nevertheless, the Commission's rate design results in an ECR basic letter rate above the Standard Regular 5-digit automation letter rate.

[5428] The remainder of the Postal Service's classification changes with respect to ECR letters are unopposed. The Commission finds that they are supported by evidence in the record and recommends their adoption.

(2) Flats

[5429] Witness Kiefer proposes the same eligibility qualifications for flats rates in ECR as proposed in the Regular subclasses. Pieces that do not meet flats rate eligibility become parcels and pay parcel rates.¹⁵⁰ Witness Kiefer also proposes to change the rate design for ECR flats by making all mail that uses a detached address label (DAL) pay a surcharge to encourage on-piece addressing.

[5430] *Scope of DAL Surcharge.* As a preliminary matter, there is a dispute about which ECR flats rate categories should be subject to the DAL surcharge. In its rate request, the Postal Service proposed DMCS language that would apply the DAL surcharge to "saturation rate pieces." USPS Request, Attachment A at 21, n.7. Witness Kiefer confirms that the Postal Service does not currently allow high-density flats to use

¹⁴⁹ The Postal Service notes that ECR trays might be mistagged, resulting in higher costs. USPS-RT-14 at 5. However, as Valpak notes, these types of mistakes can happen in any mail subclass or rate category and are contrary to Postal Service protocol. Valpak Brief at IV-6. This is not a valid reason for getting rid of a discount; it is a reason to improve Postal Service mailing regulations or enforce the regulations so that mailers follow protocol.

¹⁵⁰ Because there is no UFSM 1000 exception in ECR/NCER today, witness Kiefer expects the number of pieces that will lose eligibility for flats rate treatment to be relatively small. Accordingly, he does not propose an NFM category for the ECR subclasses.

DALs. See Tr. 5/903.¹⁵¹ However, witness Kiefer also confirms that 7.7 percent of high-density mail that is dropshipped to DDUs use DALs. Tr. 18D/6666. This causes SMC-Advo Witness Crowder to argue that because the record shows that high-density flats also use DALs, the DAL surcharge should apply to those pieces as well; not just saturation flats with DALs. SMC-RT-1 at 9.

[5431] SMC-Advo contends it would be unfair for the DMCS to impose a DAL surcharge on saturation flat mailers (who are authorized to use DALs), while exempting high-density flat mailers that may (impermissibly) be using DALs, particularly if those high-density DAL mailers are competitors with saturation DAL users. SMC-Advo Brief at 18. Postal Service witness Kiefer agrees, stating “there is no need for the DMCS language to specifically refer to ‘Saturation Rate Pieces’ and could easily refer to ‘flat-shaped pieces.’” Tr. 5/903. NAA believes that this change is unnecessary since it reads postal regulations as forbidding the use of DALs in high-density mailings. NAA Reply Brief at 12, n.14.

[5432] *Commission analysis.* The participants seem to agree that high-density flat mailers should not be using DALs. Nonetheless, there is evidence in the record showing that DALs are used by some high-density flat mailers – even though current postal policy forbids it. If high-density mailers continue inappropriately using DALs, they should not be rewarded with a lower rate (or the absence of a surcharge) for their inappropriate behavior. Moreover, not broadening the proposed DMCS language could create unnecessary confusion and a lack of clarity as to whether, in fact, high-density flats with DALs should be subject to a DAL surcharge. Since the Commission is affirmatively considering the issue, the absence of Commission clarifying action could be misinterpreted to mean that the Commission does not believe that high-density flats with DALs should be subject to the DAL surcharge. Accordingly, the Commission is clarifying

¹⁵¹ Response to Advo/USPS-T-36-1 was properly designated, but inadvertently left out of the transcript.

DMCS § 324.6 to include “flat-shaped and parcel-shaped pieces” as those mailpieces subject to the DAL surcharge. See USPS-T-36 at 32, 34.

[5433] With respect to the Postal Service’s proposal to redefine the flats qualification requirements to the same as those proposed for the Regular subclasses, the Commission finds the proposal justified and supported under the Act for the same reasons the Commission is adopting these changes in the Regular subclasses.

(3) Parcels

[5434] All nonletter shaped pieces that do not meet the qualifications for flats rates eligibility are proposed to pay ECR parcel rates.¹⁵² The Postal Service believes that this proposed change in rate eligibility requirements will affect a relatively small number of residual shape nonletters, one reason being that ECR rates do not have the UFSM 1000 exception that currently permits significant numbers of pieces in the Regular subclasses to pay flats rates. Currently, only a small number of ECR pieces pay the residual shape surcharge and the number is declining, according to witness Kiefer.

[5435] *Commission analysis.* No participant opposes the Postal Service’s classification changes for the parcel rate categories. The Commission finds that all of these Postal Service’s proposed changes are consistent with the requirements of 39 U.S.C. § 3623 and are fair and equitable. They will move the classification schedule more in the direction of recognizing cost causing characteristics and align the mail better with operational technology. The Commission’s recommended decision includes these classification changes.

¹⁵² This also would eliminate the residual shape surcharge for the ECR subclasses.

5. Rate Proposals

[5436] Postal Service witness Kiefer (USPS-T-36) proposes rates for all four Standard Mail subclasses. Many participant witnesses contest numerous Postal Service proposed rates or suggest alternative rate designs of their own. The Commission first addresses the appropriate rate design methodology to use to design rates including benchmarks and the presort tree. Second, the Commission addresses arguments for increasing passthroughs to 100 percent of avoided costs. Third, the Commission discusses the Postal Service's proposals for the Regular subclasses followed by participants' criticisms of those proposals. Fourth, the Commission addresses the Postal Service's proposals for the ECR subclasses followed by participant concerns and alternative ECR rate designs. Finally, the Commission addresses issues related to the nonprofit subclasses.

a. General Rate Design Methodology

[5437] Prior to Docket No. R90-1, rate design for Standard Mail was based on an algebraic formula that used avoided costs¹⁵³ for presorting and barcoding to develop rate differences. This process was modified in Docket No. R90-1 to accommodate the introduction of shape-related rate differentials, additional barcode discounts, a discount for saturation mail, and dropship discounts. An essential feature of the Docket No. R90-1 approach was a device referred to as a "presort tree." This helped the rate designer detect and correct rate anomalies and allowed those evaluating rates to explicitly and systematically consider all shape-related, presort, and automation cost differences in reconciling rates with the policy and pricing factors of the Act. The rate designer selected passthrough percentages to apply to the avoided cost differences to

¹⁵³ As used in the context of this discussion, the term "avoided cost" is used generically and includes the Postal Service costs that are avoided as the mailer selects among different shapes within the subclass, as well as Postal Service costs avoided as a result of worksharing.

develop rate differentials. Each passthrough selection was evaluated for consistency with *all* the rate setting criteria of the Act. The Docket No. R90-1 approach used a single benchmark.

[5438] Prior to Docket No. R90-1, the Standard benchmark was the basic non-automation presort rate. This was the least workshared mail and accordingly, the most costly. From Docket No. R90-1 through Docket No. R2005-1, the benchmark was the basic non-automation nonletter with no dropshipping. Similarly, in those dockets, this was the most costly type of mail in Standard Regular.

[5439] In the current docket, witness Kiefer proposes a rate design methodology for Standard Regular that differs from what he calls “the ‘formula’ approach in use (with modifications) since Docket No. R90-1.” He believes his proposal achieves “the Postal Service’s goals of having more finely disaggregated and flexible rate structures for Standard Mail.” USPS-T-36 at 12-13. He appears to use the following eight benchmarks: (1) MAADC automated letter; (2) MAADC machinable letter; (3) MADC nonmachinable letter; (4) MAADC automated flat; (5) MADC non-automated flat; (6) MADC not flat-machinable; (7) MADC nonmachinable parcel; and (8) machinable parcel.¹⁵⁴ This new proposed methodology uses a multitude of free-standing rate categories, each with its own benchmark and presort tree. This method changes the established practice of calculating a base minimum piece rate and deducting or adding rate differentials to calculate other minimum piece rates. Instead the Postal Service calculates separate minimum per-piece rates for MADC or MAADC in each category. It does not explicitly compare costs, rates or other relationships between the various benchmarks. This calculation is discussed further in the sections describing the Postal Service’s proposed rates.

¹⁵⁴ In its response to Notice of Inquiry No. 2 (July 21, 2006) at 10, the Postal Service contends that “witness Kiefer actually uses five benchmarks.... Prices for the three additional items identified in Notice of Inquiry No. 2 (automation letters, automation flats, and nonmachinable parcels) are derived by applying proposed rate differentials to the non-automation machinable (benchmark) rates for letters and flats and to the machinable parcel (benchmark) rates for parcels.” The actual number of benchmarks used by witness Kiefer is not relevant to this discussion. It is sufficient to note that the Postal Service proposes multiple benchmarks.

[5440] The Commission has stated in the past that it is important for its application of the various statutory ratemaking criteria to be done in a transparent manner. Previous rate decisions have attempted to explain how specific rate levels within a subclass have been determined though a single presort tree starting with a single benchmark that allows each rate to be compared with all the other rates in the subclass in terms of the percent of avoided costs that the rate reflects. *See e.g.*, PRC Op. R90-1, ¶¶ 5945-58.

[5441] When passthroughs deviate from 100 percent, rate differences do not fully reflect cost differences. Without some analytical framework by which the relationship of proposed rate differences and cost differences can be evaluated, there can be no assurance that the rates within a subclass are cost based or that any departures are consistent with the other policies and criteria of the Act.

[5442] In response to Notice of Inquiry No. 2 and in response to questions on the record, the Postal Service argues that the value of a presort tree that links different shapes is questionable because those shapes are subject to different mail preparation requirements. However, the use of multiple benchmarks between shapes obscures the degree to which shape-related cost differences might be reflected in rates. Regardless of the appropriate way to make that comparison, that comparison can and must be made.¹⁵⁵ In Notice of Inquiry No. 2, the Commission sought the best analytical framework to make those necessary comparisons. No participant has presented testimony or argument in favor of a framework different from the presort tree. Instead, several participants¹⁵⁶ argue both for and against making those comparisons explicit and the use of multiple benchmarks.

¹⁵⁵ Even if multiple benchmarks are chosen, one can still implicitly compare the relationship of rate differences and cost differences between those multiple benchmarks. The Postal Service acknowledges that this comparison is appropriate and necessary under the criteria of the Act. USPS Response to Notice of Inquiry No. 2 (August 17, 2006) at 16 (“Cost and non-cost relationships between the separate trunks were given appropriate consideration as they always have, despite the evolution of the model from the traditional single-trunk to a multiple-trunk framework.”).

[5443] Accordingly, the question becomes whether all rate comparisons within a subclass should be explicit in one tree, or implicit in multiple trees with different benchmarks. The participants' arguments on these matters are addressed below.

[5444] Valpak supports the single presort tree with the single benchmark approach. Valpak witness Mitchell notes that “witness Kiefer appears to distinguish between the presort tree as a ‘visual aid’ and as a method for the mechanical calculation of rates. VP-T-1 at 107. Mitchell argues that “the tree does nothing more than make the relationships transparent” both for vertical and horizontal rate comparisons. *Id.* He notes that the presort tree allows the Commission “to recognize the costs explicitly and to make decisions on articulated bases,” while providing a visual and workable framework that focuses on relevant costs and relationships of rates to costs. *Id.* at 103, 105, 108.

[5445] With respect to choosing a benchmark, witness Mitchell identifies the fact that “the cost differences are what the cost differences are, and standing on one limb or another does not make them any different.” Additionally, with respect to the multiple benchmark approach to separate shapes and certain other mail characteristics advocated by witness Kiefer, witness Mitchell argues that “so long as these categories are in the same subclass, I see no better way to get a handle on them than to consider their relative costs, which is exactly the handle the presort tree provides.” Further, the relative costs should be explicitly considered since rate categories within the same subclass are linked as variants of one another. VP-T-1 at 109. Valpak also contends that “with multiple benchmarks, the Postal Service does not need to address in any way

¹⁵⁶ Comments of Time Warner Inc. in response to Notice of Inquiry No. 2 and No. 3 (August 17, 2006) (Time Warner Comments to Notice of Inquiry No. 2); Parcel Shippers Association Response to Notice of Inquiry No. 2 (July 26, 2006) (PSA Comments to Notice of Inquiry No. 2); Comments of Valpak in Response to Notice of Inquiry Nos. 2 and 3 (August 17, 2006) (Valpak Comments to Notice of Inquiry No. 2); Response of USPS to Notice of Inquiry No. 2 (August 17, 2006) (USPS Comments to Notice of Inquiry No. 2); *see also* Postal Service Brief at 305; Valpak Brief at IV-1; Valpak Reply Brief at IV-3; VP-T-1 at 107; Response of United Parcel Service to Notice of Inquiry Nos. 2 and 3 (August 17, 2006) (UPS Comments to Notice of Inquiry No. 2); SMC-Advo Brief at 32, n.7. SMC and Advo do not comment on the appropriateness of the presort tree, but they do point to what they refer to as a “hidden defect” – the fact that the presort tree compares minimum-per-piece rates by shape and density level to unit costs that include weight-related cost for pound-rated pieces – which can imply that a rate design is efficient when it actually is not.

the cost of letters or flats, and indeed [the Postal Service's] Standard Mail rate design witness..." does not explicitly do so. Valpak Brief at IV-4.

[5446] PSA supports the presort tree but argues that passthroughs between shapes should be calculated by comparing the entire shaped-based revenue with the entire shape-based cost differences. It believes this is appropriate for the following reasons: (1) it ensures that the shape-based passthroughs do not inadvertently link shape and weight, and (2) it provides flexibility to design shape-specific rates at a more detailed level. PSA Comments to Notice of Inquiry No. 2 at 2-5.

[5447] Time Warner contends that for the Commission to perform its function properly, the categories within subclasses must be defined in a way that makes comparison of cost and rate relationships between and among those categories possible and meaningful. To that end, it believes that one of the most fruitful methodological approaches for making comparisons in rate structures is the presort tree. Time Warner Comments on Notice of Inquiry No. 2 at 4, 7.

[5448] The Postal Service argues that a single comprehensive presort tree in this case would be so complex that it would introduce more confusion than clarity.¹⁵⁷ It believes that rate anomalies are discovered by examining rate charts and that "merely comparing passthroughs in a presort tree will never provide reasonable assurance that all rate anomalies were uncovered." USPS Comments on Notice of Inquiry No. 2 at 10. The Postal Service contends that the proper way to divide a subclass into appropriate small presort trees is through their distinct mail processing streams since mail rarely moves between processing streams. *Id.*

[5449] Witness Kiefer argues that in choosing benchmarks, it is appropriate to choose a high volume category since it is more likely to show up in the Postal Service's cost sampling system. This provides more statistical confidence in the starting point's cost estimates. A single tree with one benchmark, the Postal Service contends, would

¹⁵⁷ UPS seems to agree with the Postal Service that presort trees should have unique benchmarks for each shape, although it believes that fewer benchmarks are more simple to work with. UPS Comments to Notice of Inquiry No. 2 at 4.

compel an analyst to place rate categories adjacent to each other that have little in common, or complicate the tree by expanding it an additional dimension.¹⁵⁸ It notes that “[t]he essential difference between the Postal Service’s approach and witness Mitchell’s is that witness Mitchell presents his flats and letters benchmarks via a cost and passthrough framework, whereas the Postal Service does not.” Postal Service Brief at 308.

[5450] *Commission analysis.* Transparency is key in the ratemaking process and indeed, one of the main goals of the Act was to allow ratemaking to be a public process. By definition, all rates within a subclass are related and must be considered by the Commission. As Valpak notes, “[t]he presort tree is meant to be helpful in facing a situation where any ordinary mind likely would be taxed by the complexity, which grows with each case. It does not provide constraints or limitations on rate design. All rate and cost relationships normally shown in the tree exist, regardless of whether they are shown in a tree....” Valpak Comments on Notice of Inquiry No. 2 at 10. The Postal Service’s argument about the complexity of a single tree misses the mark. Anyone interested in rates of mail with particular characteristics can “zoom in” on a particular area (shape, automation requirement, etc.) of the tree to view those rates and rate relationships in isolation. A single tree can always be thought of as the sum of multiple, smaller trees. Valpak’s criticism that witness Kiefer did not explain how he gave consideration to passthroughs between shapes highlights the problems with the multiple tree approach. It is much more difficult to see and evaluate those significant relationships between shapes without an explicit passthrough and the justifications for deciding on that passthrough.

[5451] It may be that there will come a time when a single presort tree is not practical, but the Commission has not reached that point. Moreover, even if that time

¹⁵⁸ The Postal Service also notes that the presort tree does not address cross-subclass relationships such as the relationship between ECR basic letter and Regular automation 5-digit letter. That particular relationship was previously discussed at length.

comes, the relationships between trees should be explicitly recognized through a discussion of a “tree to tree” passthrough.

[5452] The Postal Service’s argument that choosing a benchmark should be based on a “typical” rate category has merit. Accordingly, the Commission chooses benchmarks for the Standard Mail subclasses that are from typical rate categories, i.e., those with significant volume. Here, as discussed in more detail below, the Commission uses the automation 5-digit letters rate category for the Standard Regular subclasses and the basic flat rate category for the Standard ECR subclasses.

[5453] PSA’s argument that shape passthroughs should be calculated by comparing the entire shape-based revenue with the entire shape-based cost differences is not persuasive. The shape differentials on the presort tree are effectively piece differentials. Aggregated costs and revenues include cost differentials that should be accounted for in the pound rate. Accordingly, the Commission does not adopt PSA’s proposal. PSA’s proposal does highlight, however, the fact that the accuracy of the pound rate is important. The accuracy of the pound rate is addressed in the part of this section dealing with ECR flat rates.

b. Arguments for 100 Percent passthroughs

[5454] For many of its proposed rates, the Postal Service does not propose 100 percent passthroughs of avoided costs. PostCom and PSA argue the Commission should increase those passthroughs to 100 percent. In particular, PostCom witness Pursley argues that the passthroughs for destination entry discounts should be increased to 100 percent of their avoided costs. PostCom-T-2 at 2.¹⁵⁹ She states that both the Commission and the Postal Service have previously indicated preferences for 100 percent passthroughs of costs avoided by destination entry, provided such passthroughs are consistent with other pricing goals. She notes, however, that the

¹⁵⁹ Witness Crowder agrees with witness Pursley on this point. SMC-RT-1 at 17.

Postal Service's proposed passthroughs for destination BMC, destination SCF, and destination DDU are 87 percent, 85 percent, and 85 percent respectively for Standard Regular letters, flats and NFMs.

[5455] She believes that 100 percent passthroughs are appropriate to provide mailers with the necessary incentives to prepare their mailing in a way that minimizes the combined mail processing and transportation costs to the postal sector. Increasing the destination entry discount, witness Pursley testifies, will likely increase the amount of Standard Mail flats that are dropshipped and palletized, which will in turn lower costs for both the mailers and the Postal Service. Increasing the presort discount, witness Pursley testifies, will provide mailers with the necessary incentives for co-mailing and 5-digit palletization, which will increase the efficiency of the Postal Service, especially given the installation of the Flat Sequencing System. PostCom-T-2 at 2.

[5456] The Postal Service contends that witness Kiefer proposes less than full passthroughs for piece-rated pieces for all shapes since discounts are given as if the pieces weighed 3.3 ounces regardless of their actual weight. USPS-T-36 at 14, n.6. Accordingly, the Postal Service argues, adjusting the passthroughs to 100 percent would amount to giving double credit for avoided costs. Tr. 5/912.

[5457] Additionally, the Postal Service is skeptical that increasing the discounts will encourage palletization since 87 percent of destination entered Standard Mail pounds are already entered on pallets.¹⁶⁰ It further contends that under its proposal, the DBMC discount for parcels would increase almost 33 percent.

[5458] On reply, PostCom notes that heterogeneity by weight is not an appropriate justification for less than 100 percent dropship passthroughs for the following reasons. First, calculating avoided costs using a weight other than the breakpoint weight could result in discontinuity at the breakpoint or rate anomalies. Tr. 28/9516. Second, the Commission has held that "factors other than (or in addition to) weight render a linear assumption below the breakpoint inappropriate...." PRC Op. R90-1, ¶ 6024. Third, the

¹⁶⁰ See PostCom-T-1 at 3, n.6 (citing USPS-LR-L-88, Appendix C, Table 6).

possibility that there may be some set of Standard Mail for which the discount exceeds the Postal Service's avoided cost exists even at the levels proposed by the Postal Service. Tr. 28/9515. Finally, the Postal Service ignores the other subsets of mail which exceed 3.3 ounces for which the discount is substantially less than the avoided cost to the Postal Service. PostCom Reply Brief at 5-7.

[5459] PostCom also argues that the Postal Service is "gambling" that there will be no loss of drop entry volume by basing its decision not to increase drop entry discounts on the fact that "desired mailer behavior" already largely occurs. This gamble is inappropriate since witness Pursley's testimony shows that the cost of palletizing and transporting mail has increased steeply in recent years and is likely to continue to do so. PostCom-T-2 at 5. It further contends that setting drop entry discounts at less than avoided costs produces a windfall for the Postal Service. PostCom Reply Brief at 5-7.

[5460] *Commission analysis.* Except as noted below, the Commission largely accepts PostCom's argument that the dropship and presort discounts should be increased to 100 percent passthroughs.¹⁶¹ Increasing dropship discounts is in line with ECP principles and could effectively encourage co-mailing and potentially increase palletization, although as the Postal Service argues, that is by no means certain. It should, however, at the very least help retain existing mailers who already palletize their mail. The Postal Service's argument for setting discounts as if the piece-rated pieces have the maximum piece-rated weight (the breakpoint weight) is unconvincing for the reasons stated by PostCom – the high probability for discontinuity at the breakpoint and the potential for rate anomalies.

¹⁶¹ The Commission also disaggregates the delivery costs for letters and flats to calculate the cost savings. See section V.C.5.d.(2) non-automation for a thorough discussion of the reasons for disaggregating delivery costs.

c. Proposals for the Standard Regular Subclass

[5461] The Postal Service's proposal produces an average per piece increase in Standard Regular revenue of 9.6 percent and Standard Nonprofit Regular of 8.9 percent. Combined, the overall increase for the Regular subclasses would be 9.8 percent, with a resulting cost coverage of 176.5 percent.¹⁶²

[5462] To estimate the revenue impact of witness Kiefer's rate proposal given the new proposed categorizations, the Postal Service uses the following mail studies from witness Loetscher (USPS-T-28): (1) the mail characteristics study (USPS-LR-L-92) which disaggregates volumes from composite presort categories into finer presort categories and disaggregates the presort volumes for automation and non-automation flats,¹⁶³ and (2) a Standard Mail nonletters mail characteristic study that shows how current nonletter categories would be recategorized into automation and non-automation flats, not flat-machinables and parcels. Each Postal Service and intervenor Standard Regular rate proposal is discussed below organized by shape. The Standard Nonprofit Regular rate proposals are discussed in section V.C.5.e. of the Opinion.

(1) Letters

[5463] *Postal Service's rate proposals.* Witness Kiefer developed the Postal Service's proposed rates for each grouping of letters (automation, machinable, and nonmachinable) by selecting rate elements for the least workshared piece and developing the other prices to reflect worksharing, point of entry and other relevant factors.¹⁶⁴ In the case of the machinable letters group (which includes automation letters) the benchmark is a MAADC non-automation letter entered at an origin facility. To

¹⁶² These financial results include the effects of the assumption that mail formerly paying piece-rated ECR automation basic rates migrate to the Regular and Nonprofit Regular subclasses and pay 5-digit automation letter rates.

¹⁶³ See USPS-LR-L-36, Reclassified Comm. Pcs. & Lbs. and Reclassified NP Pcs. & Lbs., and supporting worksheets, for the details of witness Kiefer's volume recategorizations.

develop the minimum-per-piece rate for non-automation MAADC letters, Kiefer selects a piece charge of \$0.14 and a pound charge (or pound rate) of \$0.739. This approach, which is based on rate elements for a pound-rated piece, appears to be an artificial construct designed to facilitate the calculation of the minimum-per-piece rate for non-automation MAADC letters since there are no pound-rated letters other than heavy automation letters. Nevertheless, Kiefer combines these pound rate elements to calculate a minimum-per-piece rate of \$0.292.¹⁶⁵ The proposal reduces this base rate to reflect worksharing (sorting to a finer level than MAADC), entry at the DBMC or DSCF, and automation (automation pieces are proposed to have an additional \$0.04 discount off of non-automation prices). For all letters, witness Kiefer proposes to pass through only a portion of the destination entry savings reported by witness Mayes (USPS-T-25, USPS-LR-L-88) and a portion of the presort savings estimates reported by witness Abdirahman (USPS-T-22, USPS-LR-L-48) to maintain reasonable rate relationships between the different rate categories.

[5464] Witness Kiefer developed his benchmark for nonmachinable letters similarly. He adjusted the nonmachinable letters benchmark rate for each presort level, reflecting witness Abdirahman's estimates of the additional costs of nonmachinability. However, witness Kiefer believes that recognizing the full additional cost of manually processing nonmachinable letters would lead to excessive rate increases. Accordingly, he "tempered" the passthroughs for some of these additional costs. He then adjusted his base rates for nonmachinable letters to reflect finer presorting and dropshipping.¹⁶⁶

[5465] Letter shaped pieces weighing over 3.3 ounces that are not machinable as letters (and so can not avail themselves of the automation heavy letter discount), will pay

¹⁶⁴ Beginning with the approximate rate increase required to achieve the cost coverage targets provided by witness O'Hara, witness Kiefer used an "iterative" process to achieve revenue targets while keeping other rate design goals such as appropriate rate relationships in mind.

¹⁶⁵ The minimum-per-piece rate is calculated as follows: $\$0.14 + \$0.739 / 16 \text{ ounces} \times 3.3 \text{ ounces} = \0.292 .

¹⁶⁶ The details of witness Kiefer's calculations and adjustments are found in the Proposed Rates worksheet of workbook WP-STDREG.XLS (USPS-LR-L-36).

the applicable pound-rated flats rate under the Postal Service's proposal, if such pieces meet the new eligibility criteria for flats. Pieces not machinable as flats will pay the rates for either NFM or parcel pieces, discussed below.

[5466] *Commission analysis.* Except for arguments seeking 100 percent passthroughs, discussed above, no participant directly opposes the Postal Service's proposed rates. The Commission's recommended rates employ Efficient Component Pricing principles. However, the Commission finds that it is appropriate for the machinability differential between the MADC automation letter and the MADC nonmachinable letter to be lower than 100 percent. This lower passthrough is appropriate for the following reasons. The current rate design does not have a separate structure for nonmachinability. The current rate design recognizes only two categories of non-automation letters – basic and 3/5-digit – and charges a nonmachinable surcharge of \$0.042 regardless of presortation. See DMCS Rate Schedule 321A, n.4. Because the Commission's recommended classification effectively disaggregates the surcharge into nonmachinable rate categories, the less presorted pieces will no longer receive the benefits of the work done by the more highly presorted pieces. Recognizing 100 percent of the disaggregated cost differences would result in excessively large rate increases for some mailpieces.

(2) Flats

[5467] *Postal Service's rate proposals.* Witness Kiefer developed the Postal Service's proposed rates for automation and non-automation flats by choosing the piece and pound charges for the benchmark pound-rate piece. As elsewhere, the presort benchmark is the MAADC level and the benchmark for flats is a non-automation piece. The proposed piece charge for a pound-rate flat is \$0.279 and the corresponding pound-rate is \$0.739, which is slightly lower than the current pound rate. Combining these rate elements, Kiefer develops a minimum-per-piece rate of \$0.431 for a

non-automation MAADC flat.¹⁶⁷ The minimum-per-piece rate and the rates for pound-rated flats are then discounted to calculate the other presort, barcode, and dropship rates.¹⁶⁸ His proposed pound rate of \$0.739 is slightly below the current pound rate. This, witness Kiefer points out, is meant in part, to reflect that Standard Mail nonletters currently include parcels and that the higher pound rate was designed to recover more revenue from heavier parcels.

[5468] In choosing the passthroughs for more finely workshared mail in his flats rate design, witness Kiefer sought to “mitigate” the effects of de-averaging. Accordingly, he adjusted his proposed MADC and 3-digit presort rates so they were not as high as they otherwise would have been. However, as a direct consequence of that mitigation, the ADC and the 5-digit presort levels receive higher increases under his proposal than if he had not mitigated the effects of de-averaging. Nonetheless, witness Kiefer notes that the ADC and 5-digit presort categories increase significantly less than comparable Mixed ADC or 3-digit pieces. His proposed rate design gives flats the same per-pound dropship discounts as letters.¹⁶⁹

[5469] *5-digit automation flats.* PostCom witness Pursley argues that the Commission should recommend increasing the 5-digit presort discount for automation flat mail to 100 percent of avoided costs. PostCom-T-2 at 2.¹⁷⁰ Witness Kiefer testifies that he mitigated the effects of de-averaging the 3/5-digit presort rate category intentionally since the Postal Service did not think it was appropriate for the 5-digit rate category to receive a rate decrease when the overall average increase is above 10 percent. See USPS-T-36 at 16-17; see also USPS-LR-L-36, WP-STDREG-26-27.

¹⁶⁷ The minimum-per-piece rate is calculated as follows: $\$0.279 + \$0.739 / 16 \text{ ounces} \times 3.3 \text{ ounces} = \0.431 .

¹⁶⁸ See USPS-T-25; USPS-LR-L-88 (destination entry savings); USPS-T-20; USPS-LR-L-43 (presorting and automation savings).

¹⁶⁹ Details of these calculations and adjustments, including passthrough adjustments, are in the Proposed Rates worksheet of witness Kiefer’s workbook WP-STDREG.XLS (USPS-LR-L-36).

¹⁷⁰ Witness Pursley notes that the Postal Service has proposed to pass through only half of the cost savings associated with automation mail entered at the 5-digit level.

[5470] *Commission analysis.* Within flats, except for participant arguments seeking 100 percent passthroughs discussed above, no participant directly opposes the Postal Service's proposed rates. The Commission's recommended rates for flats reflect Efficient Component Pricing. Not using ECP encourages inefficient mailer behavior and potentially encourages Negotiated Service Agreements that would otherwise be unnecessary. *E.g.*, Docket No. MC2005-3; *see also* Valpak Brief at I-17, n.8. Mailers should be able to convert lightweight pieces to more efficient, less costly letters if they feel that these cost-based rates are no longer the most cost effective way to send their mailings. Accordingly, the Commission concludes that it is appropriate to recommend ECP rates for flats with the following exception.

[5471] The Commission finds it appropriate for the differential between the non-automation flat and the automation flat to be greater than 100 percent. The Commission concludes that a higher than 100 percent passthrough is justified on the following grounds. The Commission's recommended classification proposal disaggregates the current "basic" rate category into a Mixed ADC rate category and an ADC rate category. Lowering the discount from the current 4.7 cents to the 1.8 cents suggested by application of 100 percent passthrough could cause rate shock.

(3) Parcels

[5472] *Preliminary Elasticity Issue.* As a preliminary matter, PostCom witness Angelides argues that the price elasticity of Standard parcels is different from that of Standard Mail letters and flats in terms of elasticity. He contends that Thress's estimate for the elasticity of "destination entry Parcel Post" is a more appropriate proxy for Standard parcels than that of the entire Standard Regular subclass used by the Postal Service. He believes that Standard Mail parcels more closely resemble "destination entry Parcel Post" in terms of mail characteristics, use by mailers, and the availability of alternatives than Standard Mail letters and flats. Further, he highlights the fact that the large volume of Standard Mail letters and flats compared with Standard parcels obscures

the elasticity of parcels when taking the volume-weighted average elasticity of the three shapes.

[5473] The Commission is not convinced by witness Angelides argument for using a different elasticity for Standard parcels. The Commission has significant concerns that Angelides elasticity claim is overbroad and its validity has not been shown on this record. The Postal Service concedes that witness Angelides' claim of differing elasticities may be true, since subclasses contain a broad range of mailpieces. However, Parcel Select has active competitors with closely priced substitute products. Angelides does not present any evidence indicating that private carriers offer prices comparable to Standard Regular parcels. As the Postal Service points out, witness Angelides does not explore the consequences of adopting his claim or propose alternative volumes.¹⁷¹ If parcels have a higher elasticity than anticipated, this would require their rates to be priced even higher to achieve the same target contribution.

[5474] *Postal Service's Rate Proposals.* The Postal Service's proposal recognizes two types of parcels, machinable and nonmachinable. For parcels that are machinable on the BMC parcel sorting machines, witness Kiefer uses the least workshared piece (a Mixed BMC parcel) as the benchmark for choosing the piece and pound rate using cost information from witnesses Kelly and Miller.¹⁷² Witness Kiefer uses these costs as

¹⁷¹ PostCom contends that this argument boils down to "a fundamentally unlawful attempt to place the burden of proof upon PostCom." PostCom Reply Brief at 14. It argues that the burden of proof is on the Postal Service to justify the cost and revenue forecasts upon which the Postal Service relies. PostCom's argument is not persuasive. The Postal Service's proposal is supported by its direct case. The burden of going forward then shifted to PostCom as an opponent of the proposal. PostCom responded with the testimony of witness Angelides. In considering this record, the Commission concludes that the Postal Service has satisfied its burden. Its arguments on brief related to witness Angelides testimony are meant to undermine his testimony, not shift the burden of proof or persuasion.

¹⁷² USPS-T-30; USPS-LR-L-67; USPS-T-21; USPS-LR-L-45. Witness Miller provides cost estimates using the Parcel Post model for a pieces having the average size of a Standard Mail parcel that was sorted through both an originating and designating BMC (i.e., two BMC sorts). He also provided a cost estimate for a piece receiving only one BMC sort. Witness Kiefer used the former to arrive at estimates of the mail processing cost of a Mixed BMC machinable piece (i.e. receiving two machine sorts) and the latter for a BMC presorted machinable piece (i.e. receiving one machine sort). Witness Kiefer also used witness Miller's modeled costs for mail processing operations for a piece sorted to 5 digits to arrive at an estimate for the costs of a 5-digit presorted parcel.

guides in selecting what he feels are “appropriate” prices rather than as precise estimates of cost differences for setting presort discounts. He also designed these rate elements to limit the impact of rate increases on parcels.

[5475] Accordingly, he increases his proposed discounts for dropshipping parcels above what is being offered to letters and flats, and proposes that parcels entered at the DDU be eligible for an additional discount that is not available to flats to encourage cost-saving behavior. This results in entry discounts that recognize the fact that parcels generally are more costly to transport and move due to their larger size.

[5476] Witness Kiefer’s rate design proposes significant presort discounts for workshared parcels – significantly higher than the discounts for presorting machinable letters and flats – due to the higher costs of parcel sorting. However, since Witness Kiefer’s rate design “strongly mitigated” his benchmark rate, he reduces the passthroughs for the presort savings suggested by witness Miller’s cost estimates. As a result, the proposed rate design offers what he refers to as “reasonable” incentives for additional presorting while recovering what he believes is “reasonable” revenue from more highly workshared pieces. USPS-T-36 at 19. He intends to provide mailers with a strong incentive to provide lower-cost workshared parcels to the Postal Service for processing while offering mailers a way to significantly offset a large portion of the proposed rate increases.

[5477] Witness Kiefer’s rate design for nonmachinable parcels is similar to the machinable parcels design, with the following distinctions: (1) there are rates for piece-rated parcels;¹⁷³ and (2) the presort categories differ to reflect the different mail processing paths for machinable and nonmachinable parcels. He uses witnesses Kelly’s and Miller’s cost data in determining his rate design for nonmachinable parcels.¹⁷⁴ He believes the cost data suggests a high mail processing cost for pieces requiring manual processing. However, since his proposal already gives non-workshared machinable

¹⁷³ Currently, piece-rated parcels must weigh less than 3.3 ounces. Witness Kiefer points out that since a parcel must weigh at least six ounces to be considered machinable on the PSM, no piece-rated parcel can currently qualify for machinable parcel rates.

parcels a significant increase, he argues that “strongly mitigating” the rates suggested by witnesses Kelly’s and Miller’s cost information is appropriate.¹⁷⁵ He uses the same pound rate for nonmachinable parcels as for machinable parcels imposing a “modest” nonmachinability differential.¹⁷⁶ This differential effectively passes through only a small fraction of the cost differential between machinable and nonmachinable parcels yet, according to witness Kiefer, provides some incentive for mailers to make their pieces machinable where possible.

[5478] The Postal Service’s proposal makes nonmachinable parcels eligible for the same enhanced destination entry discounts as machinable parcels and gives significant presort incentives. Witness Kiefer notes that nonmachinable parcels presorted to 5-digit ZIP Codes should follow approximately the same mail processing path as machinable parcels presorted to 5-digit ZIP Codes. Accordingly, he proposes the same rates for nonmachinable 5-digit presorted parcels and machinable 5-digit presorted parcels.

[5479] The Postal Service believes that there is significant operational value to having a barcode on as many parcels as possible. Accordingly, Witness Kiefer proposes that eligibility for machinable and nonmachinable parcel rates require the piece to bear a

¹⁷⁴ He uses witness Miller’s estimates of the costs of an Irregular Piece and Parcel (IPP) manually processed through two BMCs to estimate the costs of the mail processing for a Mixed ADC-sorted nonmachinable parcel (i.e. two manual sorts before 3 digits). He also uses witness Miller’s modeled costs of manually processing an IPP after the piece had been sorted to 3 digits to estimate the costs of a 3-digit presorted parcel. He estimates the cost of an ADC-presorted parcel as the mean between the Mixed ADC and 3-digit presorted parcels costs. Witness Kiefer makes the assumption that 5-digit presorted nonmachinable pieces would have the same unit mail processing costs as 5-digit presorted machinable pieces. The Commission recognizes that these pieces are processed in separate mailstreams when developing rates.

¹⁷⁵ In his rebuttal testimony, however, witness Kiefer points out that a rate anomaly exists with respect to nonmachinable parcels that have been presorted to 3-digit ZIP Codes, specifically, in that those pieces would receive a lower rate than a comparable machinable parcel sorted to the BMC. USPS-RT-11 at 8; Tr. 33/11147-49. The Postal Service suggests that the Commission change this rate relationship to encourage machinability. *Id.*; see also Tr. 18D/6663 and 5/959. PostCom pointed out this rate anomaly in cross-examination. Tr. 33/11147-50. The Commission agrees that this is sound rate-making practice and incorporates this suggestion into its recommended rate design.

¹⁷⁶ Witness Kiefer’s proposed pound rate for parcels and NFMs (\$1.001) is higher than his proposed flats pound rate (\$0.739). USPS Request, Attachment A at 12.

Postal Service approved barcode or require mailers to pay a surcharge of \$0.05 per piece for pieces without a barcode.¹⁷⁷

[5480] Witness Kiefer believes that his parcel rate design offers mailers significant opportunities to offset much of the proposed rate increases if they can presort their pieces and bring them to destination facilities.

[5481] *Impact of Rate Increases.* The average rate increase proposed for Standard Regular parcels is nearly 50 percent with some parcels increasing more than an 80 percent. Tr. 5/949; USPS-LR-L-36, WP-STDREG-27. PostCom witness Horowitz testifies that postage costs for Cosmetique’s parcel continuity shipments will increase by around 47 percent, and as a result, the cancellation rate for its members will increase by up to 25 percent. PostCom-T-6 at 6-7. Witness Horowitz believes that the proposed parcel rate increases will accelerate his company’s exploration of alternative marketing and product delivery channels. *Id.* at 7-8. He also argues that the Postal Service inappropriately fails to take into consideration the fact that, on average, Standard parcels are considerably heavier than the average flat, and therefore, the unit revenues the Postal Service derives from these parcels is greater than the unit revenues from flats. He asks that the Commission “address these problems by adjusting the rates and the discounts in the manner set forth in witness Glick’s testimony.” *Id.* at 10.

[5482] On rebuttal, witness Kiefer notes that “the Postal Service’s principal goal in this docket is to establish separate classifications with meaningful price differentials that lead to efficiencies.” USPS-RT-11 at 6. He acknowledges that the rate increases he proposes are large and they may have a major impact on some mailers, but urges the Commission to take into consideration that the Postal Service and its customers have long been aware that Standard Mail parcels have not been covering their costs.¹⁷⁸

¹⁷⁷ This surcharge does not apply to unabridged parcels sorted to 5-digit ZIP Codes.

¹⁷⁸ Although, the Postal Service does note that the proposed rates are still below the rates charged by alternative delivery systems and are below the shipping price that Cosmetique charges its customers. Tr. 24/8697-98, 8704-5, 8710-11.

Further, he notes that his proposed rates do include “significant mitigation” as well as “attractive” presort and dropship options. USPS-RT-11 at 3-10.

[5483] With respect to witness Horowitz’s weight argument, the Postal Service contends that witness Horowitz provides no justification for his assertion that increasing rates for heavier pieces is unfair and that following that reasoning, the Commission should totally abolish the pound rate for flats and letters and make the difference between flats and parcels a fixed charge. Additionally, it argues that there is nothing in the record to support anything but a linear pound rate. Postal Service Brief at 319.

[5484] *Data Quality*. PSA/PostCom witness Glick suggests that when the Postal Service proposes very large rate increases compared to the system-wide average, the Commission should require much more reliable supporting data. PSA/PostCom-T-1 at 5. He argues that with respect to Standard Mail parcels, the Postal Service’s proposal does not meet that higher burden. *Id.* at 5,11. He proposes less than full passthroughs because the data are unreliable. *Id.* at 2.

[5485] Glick cites the fact that the test year attributable mail processing costs for parcels are admittedly anomalous for at least some subclasses – with unit costs for First-Class presort parcels at \$3 and for some Standard parcels at more than \$24. USPS-T-14 at Attachment 14; *see also* Tr. 14/4245. Further, he notes that the Postal Service has not conducted a formal review of the reliability of CRA costs by shape, and that mailpieces that have the physical characteristics of parcels, can under certain circumstances be mailed as flats. When this happens, their costs may be counted as parcel costs by IOCS, and their volumes may be counted as flats volume by RPW. Tr. 5/956. Given that parcels are a small subcategory of Standard Mail, “a very small error in classification from a major shape (flat) to minor shapes (parcels) would be magnified.” Tr. 13/3631. Witness Glick argues that witness Smith’s “fix” for this inconsistency should be “used with caution,” and that other ways to perform an adjustment might be more appropriate. He believes that shifting IOCS costs for Standard Regular parcels with Postnet barcodes from parcel costs to flat costs – which would result in a 43 percent downward adjustment – may be more appropriate. *See* Tr. 14/4284.

[5486] For these reasons and due to the rate impact arguments discussed above,¹⁷⁹ witness Glick argues that the average rate increase for Standard Mail parcels should be limited to 30 percent. He argues that Postal Service witness Kiefer limited his proposed rate increases for Parcel Post to 30 percent, and he believes that this limitation should also apply to Standard Mail parcels to avoid “unexpectedly large rate increases.” PSA/PostCom-T-1 at 9 (quoting witness Kiefer, USPS-T-37 at 17). He notes that this maximum will yield an average Standard Mail parcel revenue per piece of approximately \$1, and he posits that this will produce a more appropriate rate relationship between flats and parcels.

[5487] On rebuttal, Postal Service witness Kiefer argues that borrowing a rate design approach from another subclass is ill-advised. He contends that the 30 percent limit for Parcel Post should not apply to Standard Mail because in Standard Mail, the Postal Service is proposing a reclassification of pieces that are not presently covering their costs.¹⁸⁰ Further, he believes that when items are being reclassified, broader price changes should be expected than when price changes are being proposed for essentially unchanged rate categories.

[5488] The Postal Service argues that a higher cap is appropriate for Standard Mail parcels because the base to which the increase applies results in actual dollar amount increases that are smaller than Parcel Post. Postal Service Brief at 313-14.

[5489] On brief, PSA contends the Postal Service’s rationale for not applying a 30 percent cap limit is disingenuous. PSA argues that borrowing the Parcel Post cap is appropriate here because the point at which a mailer experiences rate shock does not

¹⁷⁹ In its reply brief, the Alliance for Nonprofit Mailers (ANM) notes that it agrees with PostCom’s and PSA’s arguments that the proposed rate increases for Standard Mail NFMs and parcels exceed levels justifiable by cost data and would cause undue rate shock to mailers. ANM notes that this is a particular concern to ANM members that include boxes of greeting cards and other front-end premiums in fundraising solicitations. ANM Reply Brief at 1-2. DMA Nonprofit Federation also argues “rate shock” for Standard Mail NFMs and parcels and urges the Commission to consider the rate impact on nonprofits of all rates increases. DMANF Brief at 9-10.

¹⁸⁰ The Postal Service also notes that the 30 percent cap is not rigid in Parcel Post; there are some rate cells that have increases exceeding 50 percent. USPS-RT-11 at 7, n.2.

depend on the characteristics of a subclass. PSA notes that since intra-BMC Parcel Post as a whole barely covers its costs and because the Postal Service's proposed Parcel Post cap applies to *all* rate categories, many Parcel Post rate cells may not cover their costs. Furthermore, PSA notes that it is contrary to established practice to look at the actual increase from the base rather than the relative percentage increases.

[5490] With respect to the PostCom and PSA arguments about the reliability of parcel data, the Postal Service contends that virtually all complex data contain some level of uncertainty and margin of error, but the data it uses in this case are not unreliable. See Tr. 5/1092-4, 1102-3, 1123. Furthermore, the Postal Service criticizes witness Glick's conclusion that any potential errors in their data means that parcel costs are too high – "they could just as well be too low." Postal Service Brief at 312, 314.

[5491] *Mitigation Techniques Concerns*. PostCom argues that the Postal Service ignores the "perverse" effects that its top-down approach to rate mitigation for the Standard parcel categories will have on affected mailers. Witness Kiefer mitigated those categories by reducing the rate paid by the least efficient mailer. PostCom believes that this proposal goes against the Postal Service's objective of encouraging more efficient preparation of mail through worksharing since it provides for greater increases on more finely sorted mail than on the less finely sorted mail. PostCom Reply Brief at 14-15. This puts a significantly higher rate burden on those companies committed to worksharing and creates disincentives for mailers to rely on consolidators in order to achieve more efficient mail preparation.

[5492] *DBMC Discount*. PSA recommends that the Commission increase the DBMC discount to bring it in line with those proposed by the Postal Service for DSCF and DDU entry for Standard Mail parcels. Witness Glick believes this is appropriate for the following reasons: (1) currently about half of Regular parcels are origin entered and these parcels are much more likely in the short term to be able to offset some of the rate increases by converting to DBMC entry, (2) parcel shippers will likely incur more costs entering parcels at the DBMC due to Docket No. N2006-1, "Evolutionary Network Development" (END). PSA/PostCom-T-1 at 9-10; PSA-T-1 at 2-4.

[5493] The Postal Service argues that PostCom and PSA arguments premised on the impact of END is misplaced. It believes that (1) dropship discounts are not based on mailers costs, they are based on avoided Postal Service costs; and (2) the impact of END in the test year is unknown – there may be more DBMCs just as there may be fewer DSCFs. See Tr. 18D/6616-23. It further notes that in the last three omnibus rate cases, the Commission has recommended dropship discounts that never exceeded 85 percent of avoided costs. See Postal Service Reply Brief at 213.

[5494] *Commission analysis.* The Commission largely accepts PostCom’s and PSA’s arguments that the Postal Service’s proposed rates for parcels are “too high” given the demonstrated uncertainty in the data quality and the potential for rate shock. While the current data are imperfect, implementation of more meaningful rate distinctions will help the Postal Service gather more accurate cost information and ultimately better align rates and costs. Without a meaningful flat/parcel rate differential, the Postal Service will not be able to do so to the detriment of the postal system. The Commission therefore uses the existing data but mitigates most parcel rates somewhat more than initially proposed by the Postal Service.

[5495] The Commission does not accept PSA’s proposal to limit the increase on Standard parcels to 30 percent. It must be remembered that previously, all such pieces were only paying a uniform residual shape surcharge and were not covering their costs. In fact, parcel shaped pieces had not been covering their costs for quite some time. It is unfair for mailers who are covering their costs to effectively subsidize parcel mailers who are not covering the costs they impose on the system. While the Commission prefers to avoid large increases, it concludes that it is more important for parcels to move toward the point at which they cover the costs they impose on the system.

[5496] The Commission largely accepts PostCom’s parcel mitigation technique argument that, where possible, more highly workshared mail should receive lower rate increases than their less workshared counterparts. Adopting this approach will encourage more efficient mail preparation and co-mailing. This results in parcel rates

that are slightly higher than the Postal Service proposes at the least workshared level, and lower rates at the more highly workshared levels.

[5497] The Commission does not accept the Postal Service's proposal to recommend different pound rates for parcels¹⁸¹ than for flats and letters. The Postal Service does not provide an adequate justification for doing so. Similarly, the Commission does not accept PSA's proposal to take into account the average weight of pieces when setting rates. The pound rate reflects weight-related costs above the breakpoint. Whether or not parcels are typically heavier than flats is immaterial. Weight-related costs are reflected in the pound rate while shape related cost differences between flats and parcels are reflected in the flat/parcel shape differential. In other words, there is no evidence on the record to support the Postal Service's presumption that a 14 ounce parcel is more expensive to process than a 14 ounce flat due solely to their weights. If the Postal Service has evidence of this nature, it should share that data with the Commission. In past cases, the Commission has asked the Postal Service to undertake a comprehensive study to support the pound rate. *See e.g.*, PRC Op. R2000-1, ¶ 5494. This analysis underscores the importance and necessity of that undertaking. Accordingly, the Commission's recommended rate design uses a uniform pound rate for letters, flats, NFMs, and parcels, and the Commission again urges the Postal Service to undertake an updated, comprehensive study of weight-related costs by shape.

[5498] The Commission also does not accept the Postal Service's proposal to give "enhanced" dropship discounts to parcels. The Postal Service's rationale for proposing a higher dropship discount for parcels is to recognize the larger cost savings for avoiding more costly parcel transportation costs. This rationale relies on the unproven assumption that parcels are more costly to transport than other mailpieces and avoiding these operations would result in higher cost savings. While this assumption may be

¹⁸¹ The Postal Service also proposes a different pound rate for NFMs. The same analysis discussed herein applies to the Postal Service's proposal to have a different pound rate for NFM mailpieces.

correct, there is no cost evidence on this record to support this conclusion. Accordingly, the Commission recommends the same dropship discounts for parcels as for letters and flats.¹⁸²

[5499] Similarly, PSA's argument for increasing the DBMC discounts for parcels due to the impact of Docket No. N2006-1 is unpersuasive. The Commission's recommended rates give an appropriate DBMC dropship discount for parcels. As the Postal Service points out, the impact of the END initiative on the test year is unknown.

(4) Non Flat-Machinables

[5500] *Postal Service's Rate Proposals.* Witness Kiefer bases the Postal Service's proposed NFM rate design on the understanding that NFM pieces are typically small and they have similar cost characteristics to parcels that are too small to be processed on the parcel sorting machines at BMCs. Since the Postal Service has no specific cost models for NFMs, he believes it is appropriate to use the same cost data developed for nonmachinable parcels and strongly mitigate the rate impacts arising from using these cost data. He bases his NFMs rate design on a piece rate below the rate for machinable parcels and the pound rate for parcels.¹⁸³ These rate elements represent what he believes are "heavy mitigation" of the costs of processing NFMs manually or in the parcel mail stream. Witness Kiefer also proposes generally higher discounts for NFMs than for

¹⁸² PSA advocates offering the same "enhanced" dropship discounts that the Postal Service proposed for parcel dropshipping to NFM dropshipments because, like parcels, NFMs are more costly to transport and move about due to their larger size than letters or flats. PSA Brief at 30. For the same reasons that the Commission is not recommending enhanced dropship discounts for parcels, it is not recommending enhanced dropship discounts for NFMs.

¹⁸³ On cross examination of witnesses Kiefer and McCrery, PostCom highlighted the fact that the rate schedule as proposed does not explicitly mention a "BMC" rate even though it is expected that certain NFMs will be required to be sorted to the BMC. The Postal Service stated that it believed that their proposed rate schedule should be clarified to make sure that those pieces sorted to the BMC should pay the same rates as those pieces sorted to the ADC. Tr. 33/11152 and 34/11505-06. The Commission's recommended decision incorporates this suggested clarification.

parcels so as to lower the piece rates further, although his proposed destination entry discounts are the same as the ones he proposes for letters and flats.

[5501] The net impact of the Postal Service's proposal would be a "significant" rate increase for NFM pieces, particularly for those pieces with little or no worksharing. At the same time, the proposed rates would offer mailers opportunities for worksharing to mitigate the impact of the rate increase and give the mailers a price incentive to reconfigure NFM pieces to meet the new flats definition.

[5502] *Impact of Rate Increases.* The Postal Service's proposed rate increases for NFMs range from approximately 60 percent to more than 200 percent. USPS-LR-L-36, WP-STDREG-27. PostCom witness Knight and MBI witness Wilbur present testimony on the ways that the NFM category will negatively affect their businesses. Witness Knight testifies that these rate changes "will make it impossible for my company to remain in the business of selling music and video products by mail." PostCom-T-7 at 2. He notes that the average increase in postage costs for the delivery of 34 percent of BMG Columbia House's CDs and DVDs will increase approximately 97 percent. This, along with increases in Media Mail and Standard Mail parcels will, he testifies, cause BMG Columbia House to lose more than 800,000 club members every year.¹⁸⁴ Witness Knight testifies that this will also have an effect on the profitability of marketing lists and force them to reduce their marketing efforts by 13 percent per year. Witness Knight also believes that the Postal Service has not taken into account these effects which could cause the Postal Service to fall short of its expected revenue estimate by \$19.9 million in the subclasses used by his company, and, in the long run, put in jeopardy the whole \$100 million that it spends on postage per year. He believes that a "wiser choice of the Postal Service would be to adapt its operations to fit the existing and traditional specifications of its customers products, or, at the very least, to give some consideration to what has worked up until the present time." PostCom-T-7 at 2. Direct Marketing

¹⁸⁴ Witness Knight estimates that for 46 percent of BMG Columbia House's music and video shipments in the parcel rate categories will increase by 61 percent. PostCom-T-7 at 7-8.

Association Nonprofit Federation (DMANF) makes a similar suggestion. DMANF Brief at 10.

[5503] MBI witness Wilbur similarly testifies that the NFM rates as proposed will result in an estimated increase of 88 percent, or an increase of \$200,000 a month for its collectables business; “the largest we have ever encountered,” and thus not reasonably anticipated. He believes that the suddenness and severity of the rate hike is “unduly onerous” and “bordering on punitive.” Accordingly, he urges the Commission to apply this rate hike in stages to allow mailers time to modify packaging or incorporate increased costs into their pricing. MBI-T-1 at 1-2. Additionally, changes in mail preparation rules could end up causing many NFMs to presort less and pay even higher rates than estimated by the Postal Service. PSA/PostCom-T-1 at 12-13.

[5504] Postal Service witness McCrery contends that rigid, boxed mailpieces currently classified as automation flats do not get processed as automation flats. He claims that they have not been processed as automation flats since 1998 and that the Postal Service has repeatedly communicated this problem and its intention to fix this problem publicly and to individual mailers through rate case proceedings, a formal “Product Redesign” effort, and other means. As a result, he does not believe mailers should be surprised by these developments. He argues that a modified definition of flat-shaped mail more in line with processing operations and delivery is “vitaly important” so that this volume can be processed properly and tracked in the Postal Service’s data systems. He also believes that such a change in connection with the creation of the NFM categories will provide customers with necessary incentives to modify their mailpieces to become more compatible with postal processing and delivery – resulting in removing costs from the system to the benefit of all mailers. USPS-RT-14 at 8-13.

[5505] In response to MBI’s arguments about gradual implementation of rate increases, the Postal Service argues that setting the implementation date for rates is a matter reserved to the Governors, not the Commission. It therefore urges the Commission to reject MBI’s arguments about implementing this rate change over a more gradual time frame. Postal Service Brief at 319-20.

[5506] *Data Quality*. As with Standard Mail parcels, PSA/PostCom witness Glick suggests that “the data quality ‘bar’ should be set much higher when the Postal Service seeks huge rate increases than for those that are in line with the overage average increase.” PSA/PostCom-T-1 at 5.¹⁸⁵ He argues that with respect to NFMs, the Postal Service’s proposal does not meet that burden. PSA/PostCom-T-1 at 5,11.¹⁸⁶ He proposes less than full passthroughs for NFMs due to unreliable data. *Id.* at 2.

[5507] Witness Glick notes the following problems with the Postal Service’s NFM data: (1) the Postal Service has no CRA costs for these pieces, (2) these pieces are often counted as parcels by IOCS and flats by RPW, (3) the modeled mail processing costs are questionable given that the mail flows for these pieces have not yet been mapped out, (4) the Postal Service uses inaccurate proxies for how the pieces will be presorted or entered into the system,¹⁸⁷ and (5) the Postal Service does not have robust volume estimates due to inadequacies in Loetscher’s Non-ECR Non-Letter Redefinition Study. PSA/PostCom-T-1 at 11-12; *see* USPS-T-36 at 22; Tr. 11/3009.

[5508] In particular, PostCom contends that the NFM definitions and tests used in the Redefinition Study are different than the proposed DMM implementation definitions. Since the deflection and rigidity tests are different, the measurement points are inconsistent, the cutoff points are different, and caseability requirements have changed, PostCom believes that the Redefinition Study bears little or no relation to the pieces that will actually be categorized as NFMs under the proposed Implementing Rules. The

¹⁸⁵ *See also* PostCom-T-6 at 9 (Horowitz) (“We ask the Commission to recognize that the Postal Service must support its rate proposals with evidence”).

¹⁸⁶ For NFM pieces weighing 3.3 ounces or less, the proposed rate increase ranges from 77.8 to 215.6 percent. *See* PSA/PostCom-T-1 at 13 for other examples of large proposed increases for NFMs.

¹⁸⁷ For revenue estimation purposes, the Postal Service assumed that the distribution of NFMs by presort level would be similar to the current distribution for UFSM 1000 flats and that the distribution entry would be similar to parcels. Tr. 7/1496. Witness Glick believes these assumptions are problematic since the preparation requirements are likely to be similar to those for parcels, and unlike those for UFSM 1000 flats. For example, higher presort minimums could result in some NFMs being entered at lower presort levels and paying higher rates than those estimated by the Postal Service.

study should therefore be accorded no evidentiary weight by the Commission.¹⁸⁸

Further, it argues that the Redefinition Study utilizes an extremely limited sample – one unrepresentative day of sampling in January 2005 of only 50 routes/box sections measuring only 1,743 Standard Mail nonletter pieces. This makes “the confidence intervals around the NFM volume estimates ... large.” PSA/PostCom-T-1 at 12.

[5509] PostCom also complains that the Redefinition Study does not identify the mailpieces, processing methods, or mailpiece distributions by presort or point of entry. Tr. 7/1548-49, 1550-61. The Postal Service merely assumed that the destination entry discount distribution would be the same as those for Standard parcels rather than UFSM 1000 flats even though the Postal Service does not “know much about how the pieces that will be hybrid [NFM] will shake out and how large the mailings are, [and] what type of entry that they will” be. *Id.* at 1569. For these reasons and due to the rate shock arguments discussed above, PostCom believes that it would be more reasonable for NFMs to pay the non-automated flat rates, rather than the proposed NFM rates.

[5510] The Postal Service contests PostCom’s argument about setting the NFM rates near those of non-automated flats since

the reason the non-automated flats rates are 40% lower than the proposed rates for NFMs is because a non-automation flat is a flat that is not bar-coded, but can still be processed in large part on the AFSM-100 flats sorting equipment and be delivered in flats bundles within delivery. An NFM (non flat-machinable) cannot or will not be processed on flats sorting equipment (hence the name) and is seldom delivered as a flat.

Postal Service Reply Brief at 202. (Footnote omitted.)

[5511] The Postal Service argues that the PostCom and PSA criticisms of witness Loetscher’s Redefinition Study are not persuasive. The differences between the Redefinition Study and the proposed Implementation Rules are not significant. The

¹⁸⁸ PostCom also notes that the Postal Service introduced a new distinction in their proposed Implementation Rules – pieces weighing more or less than 6 ounces. This distinction is not considered by the Redefinition Study and the Postal Service does not provide any discussion regarding costs and revenues related to this new distinction. PostCom Brief at 27 (citing 71 Fed. Reg. 56608).

original caseability distinction is irrelevant since it is an internal distinction between NFM pieces, not one that distinguishes NFMs from flats or parcels. Additionally, the Postal Service notes that the study did not take place over just one delivery day; it instead took place from January 7-January 31, 2005. It admits that the study's methodology does not measure the presort or dropship characteristics of the sampled pieces, but believes that the data provide the best possible estimates of the presort and dropship characteristics of NFM mail. The Postal Service also urges the Commission to look at the practical implications of finding the study non-credible because the implementing regulations "slightly" change the study's parameters – it would chill the ability of mailers to have input into designing implementing regulations.

[5512] The Postal Service argues that virtually all complex data contain some level of uncertainty, but the data used to support its NFM rate proposals are not unreliable. See Tr. 5/1092-4, 1102-3, 1123.¹⁸⁹ Those that previously benefited from the misclassified NFMs should not be able to use the mismatches in the data system to further support unwarranted rate benefits. Additionally, the Postal Service notes that any alleged error could also mean that the true NFM costs are understated, not necessarily overstated. Postal Service Brief at 312, 314.

[5513] *NFM Mitigation Techniques Concerns*. Similar to its argument with respect to parcels, PostCom contends that the Postal Service inappropriately mitigates rates. It notes that witness Kiefer mitigated NFM rate categories by reducing the rate paid by the least efficient mailer. Instead, PostCom argues, a more efficient methodology is to follow the Postal Service's policy objectives enunciated with manual letters – significant increases for the "least finely presorted manual letters and more moderate increases for

¹⁸⁹ The Postal Service believes that PostCom's and PSA's arguments relating to NFM cost and volume estimates miss the point. The Postal Service did not use witness Miller's cost study to independently derive cost information. To arrive at NFM rates, it used the mail processing cost estimates from non-machinable parcels in USPS-LR-L-45, WP-STDREG-0621, marked up those costs, and then mitigated the proposed rates. USPS-T-36 at 23. Because of this, "there is not a direct link between the [Loetscher's Redefinition] study's results for NFM volumes and witness Kiefer's rate design." Postal Service Brief at 207-08. Even if the volume estimates are inaccurate, those imprecise volume estimates would support higher rate increases to make up for any potential overstatement in volume.

highly presorted pieces.” PostCom-MFSA Reply Brief at 14 (quoting USPS-T-36 at 13-14). (Italics omitted.) This will ensure that mailers who commit to and invest in worksharing are properly incentivized. *Id.* at 15.

[5514] Postal Service Witness Kiefer acknowledges that “mitigation was done at the highest level of the rates, and then subsequent price differences due to worksharing were perhaps shrunk a little bit because the cost differences could not then be fully passed through; otherwise we would have ended up with negative prices....” Tr. 33/11146.

[5515] *Commission analysis.* The Commission recognizes the merits of PostCom, MBI, and PSA suggestions that the proposed rate increases for NFM rates are too large due to rate impact concerns and a high degree of uncertainty surrounding the accuracy of the data used to set NFM rates. However, while the current data are far from perfect, the Commission finds that recommending meaningful rate distinctions between flats, NFM rates, and parcels will help the Postal Service gather more accurate cost information with which to base future ratemaking decisions. Without a meaningful flat/NFM rate differential, the Postal Service will not be able to gather accurate cost information. The Commission therefore uses the existing data to develop its recommended NFM rates but mitigates most of those NFM rates somewhat more than initially proposed by the Postal Service.

[5516] The Commission does not accept PostCom’s argument that NFM pieces should pay non-automation rates. As the Postal Service points out, NFM rates are not merely non-barcoded pieces that can be processed on the Postal Service’s flat sorting equipment; NFM rates can not be processed on the flat sorting equipment at all. Accordingly, pricing NFM rates at the level of non-automation flats would not be appropriate. The Commission also finds convincing the fact that mailers have been on notice – both publicly through testimony presented in several previous rate cases and through more informal means – that NFM rates were causing problems with the Postal Service’s flat sorting equipment and changes would need to be made.

[5517] Similar to parcels, the Commission largely accepts PostCom’s argument that, where possible, more highly workshared NFM rates should receive smaller rate

increases than less workshared NFM mailpieces. This rate design will encourage greater overall efficiency in the postal sector. Applying this technique results in rates that are slightly higher than the Postal Service at the least workshared level and lower for more finely workshared NFMs.

(5) Customized Marketing Mail

[5518] The Postal Service proposes to change the reference point for the Standard Regular customized market mail (CMM) mail. Currently, it is priced as a piece-rated origin-entered non-automation basic nonletter, plus the residual shape surcharge. With the proposed elimination of the surcharge, a new reference point for CMM is necessary. The Postal Service proposes to use the rate for an origin-entered 5-digit presorted NFM as the reference rate. USPS-T-36 at 25-27. That proposed rate is \$0.489 per piece. The Postal Service believes that this change in the reference rate appropriately reflects CMM's presort level, nonstandard shape, and rate relationships with non-automation flats. *Id.* at 26.

[5519] *Commission analysis.* No participant opposes the Postal Service's proposal to set the CMM rate equal to that of an origin-entered 5-digit presorted NFM. The Commission finds that tying the CMM mailpiece to the origin-entered 5-digit presorted NFM is appropriate. It will reflect CMM's nonstandard shape, amount of worksharing, and maintain a reasonable rate relationship with non-automation flats.

d. ECR Rate Proposals

[5520] Witness Kiefer's proposed rates result in average revenue per piece increase of 8.1 percent for Standard Mail ECR and 8.2 percent for Standard Nonprofit ECR. Combined the two subclasses are proposed to have an average rate increase of 7.9 percent, with a resulting cost coverage of 214.2 percent.¹⁹⁰ The details of the Postal

¹⁹⁰ ECR and NECR financial results exclude former automation basic letters that the Postal Service assumes migrate to the Regular subclasses.

Service's ECR rate proposals and intervenor counterproposals are discussed below organized by shape. The NECR rate proposals are discussed in the next section of the opinion.

(1) Letters

[5521] *Postal Service's Rate Proposals.* Witness Kiefer selects the basic density level as the benchmark. He sets the basic minimum-per-piece letter rate equal to the basic minimum-per-piece flat rate as these rates are equal currently. To develop the minimum piece rate for a high-density letter, Kiefer selects a piece charge of \$0.098 and a pound charge (or pound rate) of \$0.613. The selected rate elements are based on unit mail processing and delivery costs from witnesses Talmo and Kelly, respectively. This approach, which is based on rate elements for a pound-rated piece, appears to be an artificial construct designed to facilitate the calculation of the minimum-per-piece rate for high-density letters since there are no pound-rated letters other than heavy automation letters. Nevertheless, Kiefer combines these pound rate elements less the proposed high-density letter discount to calculate a minimum-per-piece rate of \$0.19.¹⁹¹ The minimum-per-piece for saturation letters equals the proposed high-density letter rate less the proposed saturation letter discount. He then adjusts his rates based on cost differences due to density from witness Talmo and entry point from witness Mayes maintaining the same rate differentials for dropshipping in both Standard Regular and ECR.

(2) Flats

[5522] *Postal Service's Rate Proposals.* Witness Kiefer proposes having all mail that uses DALs pay a surcharge of \$0.015 per piece. He believes that this rate incentive

¹⁹¹ The minimum-per-piece rate is calculated as follows: $(\$0.098 + \$0.613 / 16 \text{ ounces} \times 3.3 \text{ ounces}) - \$0.034 = \$0.19$.

strongly encourages mailers to put addresses directly on their mailpieces.¹⁹² This change is being proposed because the Postal Service has determined that it wants to encourage on-piece addressing for all mail to improve efficiency.¹⁹³

[5523] To develop the minimum-per-piece rate for a basic flat, Kiefer uses the piece and pound charges for pound-rated flats combined as shown in previous formulas. He selects these charges based on unit mail processing and delivery costs from witnesses Talmo and Kelly, respectively. He then adjusted the rates based on cost differences due to density from witness Talmo and entry point cost differences from Witness Mayes maintaining the same rate differentials for dropshipping in both Standard Regular and ECR. Witness Kiefer also continues the “past practice” of setting the basic flat rates equal to the basic letter rates.

[5524] *DAL Surcharge*. Several participants comment on the Postal Service’s DAL surcharge proposal. Witness Gorman notes that over the last five years or so, changes in postal operations, including letter automation and casing methods have eroded the benefits of DALs, and that the Postal Service has been looking for ways to mitigate DAL costs – even considering the potential elimination of DALs as an addressing option. On behalf of the Saturation Mailers Coalition (SMC), Witness Gorman testifies that the industry sought a proactive solution with the Postal Service to get ahead of the curve and give mailers an incentive to convert to less costly procedures. The industry’s proposed two-part solution is as follows: (1) a rate incentive for DAL mailers to convert to lower-cost addressing procedures, and (2) an on-piece addressing alternative to DALs on city delivery routes – “simplified but certified”¹⁹⁴ – for DAL mailers who can not convert to on-piece “city-style” addressing. SMC-T-1 at 6-7.

[5525] Gorman points out that in order for DAL mailers to qualify for the proposed on-piece addressed flat rate, they must incur additional investment and operating

¹⁹² However, because Witness Kiefer seeks consistency with the rollforward cost projections, for net revenue calculation purposes, he assumes that all current DAL mail will pay the surcharge.

¹⁹³ See USPS-T-44, section 3.1.

expenses coupled with revenue dilution that could be several times greater than the DAL surcharge. He believes that for many, conversion to the city-style on piece addressing is not cost-effective or workable. That is the main reason why SMC proposes the simplified but certified alternative.¹⁹⁵

[5526] Witness Gorman also urges the Commission not to alter the 1.5 cent DAL surcharge proposed by the Postal Service. He contends that any reduction in the proposed surcharge would cause “severe harm and chaos within the industry due to the high cost, difficulty, and lead time involved in converting to on-piece addressing.” SMC-T-1 at 13. Given this long lead-time required for conversion, he testifies that any mailer who wants to convert to avoid the surcharge must do its cost/benefit analysis on the conversion and spend the money to completely re-tool its operations before the Commission issues its recommended decision, and any changes to the 1.5 cent proposed surcharge will cause anxiety and frustrate this analysis.

[5527] He believes that “certainly more than 70% of total DAL volume” will convert. Tr. 28/9542-43. Indeed witness Crowder testified Advo and Harte-Hanks alone – two mailers that have already committed to converting – account for 87 percent of total DAL volume. Tr. 35/11842. This contrasts sharply with the Postal Service’s assumption that no DALs will convert.

¹⁹⁴ Currently on city delivery routes, the only “on piece” addressing format that the Postal Service permits for commercial mailings is “city-style” addressing, such as 123 Elm Street. On rural routes, by contrast, simplified addressing to “Postal Patron” or similar has been permitted for well over half a century. SMC’s proposal would allow the same simplified addressing on city routes. This is the “simplified” part. “Certified” means that the mailer is required to certify to the Postal Service that it has an up-to-date mailing list. Tr. 28/9530. This simplified but certified proposal is limited to saturation mailers who mail on a regular basis, at least twelve times per year and who maintain a certified mailing list as prescribed by the Postal Service. Tr. 28/9530. This proposed limitation is to keep simplified addressing as a narrow remedy to this DAL issue and should not lead to a “undesirable flood” of new mail volumes. SMC-T-1 at 14-15.

¹⁹⁵ Witness Gorman notes that “[w]e recognize that a decision to extend simplified addressing from rural to city delivery routes is a Postal Service operational determination outside the Commission’s control.” SMC-T-1 at 13. Nevertheless, no estimate as to the impact on the Postal Service or competitors was presented. Due to this, the Commission concludes that there is not enough evidence on the record for it to formulate an opinion on the simplified but certified proposal.

[5528] Witness Crowder makes the conservative assumption that 50 percent of Saturation DAL flats will convert to on piece addressing which results in cost reductions of approximately 100 million that have not been taken into account by the Postal Service. SMC-RT-1 at 5-19. This could justify substantially lower ECR rates than have been proposed. *Id.* at 19; MOAA Brief at 20-21.

[5529] NAA Witness Sidak believes that the Postal Service has not supported its proposed DAL surcharge with an analysis that specifically calculates the incremental costs of the DALs.¹⁹⁶ Instead, according to witness Sidak, the Postal Service set the surcharge at a level that it hopes will create a sufficient incentive to encourage mailers to shift to on-piece addressing. Due to the lack of data, he proposes that the Commission consider the DAL surcharge proposal as a premium charge for an optional service or an optional rate element available to ECR saturation mailers, rather than as a cost based charge.¹⁹⁷ Witness Sidak notes that by viewing the proposed DAL surcharge as a premium charge for an optional service that the Postal Service would prefer not to provide (handling and delivering the DAL), it would be consistent with rate elements for other optional services (such as Certified Mail) that are priced to reflect additional costs that they cause relative to other mail. In the case of a DAL, the combined cost of the saturation rate plus the DAL surcharge could exceed the rate for high-density flats. He believes that this result is not anomalous and may be appropriate since DALs offer benefits to the mailer that are not available to high-density mailers that are ineligible to

¹⁹⁶ He does acknowledge that the Postal Service does provide some data concerning DAL costs, but claims that no Postal Service witness offered testimony that clearly quantified the marginal costs of DALs on a per-unit basis or the net incremental cost effect of some large portion of the approximately 4 billion DALs converting to on-piece addressing. NAA-T-1 at 12, 15. Furthermore, witness Sidak notes that witness Kiefer did not cite any cost analysis of DALs when proposing his DAL surcharge.

¹⁹⁷ As a result, the surcharge would not have to be cost-based in order to achieve the Postal Service's objective. Witness Sidak does not, strictly speaking, consider the DAL surcharge to be an instance of value added pricing; however, due to the Postal Service's lack of marginal cost analysis on the issue. He considers it akin to the pricing accepted in the Repositionable Notes case. He does note that the Commission has yet not accepted value pricing in the absence of costs except in the experimental case of Repositionable Notes. See Docket No. MC2004-5, PRC Op. at 18-19.

use DALs. He defers to witness Ingraham's specific proposals for the proper amount of the DAL surcharge.

[5530] *Disaggregated Delivery Costs.* NAA witness Ingraham argues that the Postal Service inappropriately violates the ECP rule by passing through more than 100 percent of cost differences between basic and high-density flats and also between high-density and saturation flats. NAA-T-2 at 16.¹⁹⁸ Witness Ingraham hypothesizes that this occurs because the Postal Service incorrectly relied on aggregated basic/high-density unit delivery costs, which, in turn, may have led Postal Service witness Kiefer to use excessive passthroughs to obtain his proposed rate design. Witness Ingraham submits that a better approach is to use the disaggregated delivery costs for basic and high-density flats and pass through 100 percent of those cost differences between density tiers.¹⁹⁹

[5531] The Postal Service and SMC-Advo criticize witness Ingraham for disaggregating delivery costs but using aggregated high-density/saturation mail processing costs. They argue that this aggregation of mail processing costs is a basis for less than 100 percent passthrough. On the other hand, NAA contends that it should use the most reliable available data; and the Postal Service effectively admitted that it did not have any reliable evidence of any mail processing cost differences between high-density and saturation. NAA further points out that the Postal Service used the same aggregate costs in its calculations.

[5532] *High Density/Saturation Flat Rate Differential.* NAA's witness Ingraham evaluates the Postal Service's proposed rate differential between ECR high-density and saturation flats. He concludes that the proposed difference could give saturation mailers

¹⁹⁸ Witness Kiefer proposes to passthrough 120 percent between high-density and saturation rates (based on disaggregated delivery costs) because it was "comparable to what we've had in the past between saturation and high-density flats." Tr. 5/1072.

¹⁹⁹ Witness Ingraham's alternative proposed rate designs use de-averaged delivery costs and 100 percent passthroughs. See NAA-LR-T-2 at 1-3.

a competitive advantage over newspapers' Total Market Coverage programs.²⁰⁰ According to witness Ingraham, the Postal Service's proposal "dilutes the negative incentive of the DAL surcharge while distorting significantly the relative price of high-density ECR flats to saturation ECR flats." NAA-T-2 at 11. He believes that although the Postal Service's rationale for the surcharge is sound, the proposed DAL surcharge when combined with the proposed saturation ECR flat rates does not produce an appropriate rate differential between high-density and saturation flats.

[5533] In essence, witness Ingraham argues that the Postal Service is inappropriately "mitigating" the rate increase for saturation flats in order to offset the higher costs of DAL mailers converting to on-piece addressing by increasing the saturation/high-density rate differential.²⁰¹ He believes that it is inappropriate to do so for the following reasons: (1) the optional DAL surcharge would have no offset for the majority of saturation flat mailers since DALs are only used by a minority of saturation mailers;²⁰² (2) Kiefer's proposal unrealistically assumes that no DAL mailings would shift to on-piece addressing;²⁰³ (3) there is no evidence quantifying the potential costs for mailers to convert to on-piece addressing; (4) every mailer in all other subclasses of mail must use on-piece addressing and the Postal Service does not offer that fact as a rationale for rate mitigation; and (5) conversion costs can be amortized over time as an offset. NAA-T-2 at 13-14; NAA Reply Brief at 11-12.

²⁰⁰ Total Market Coverage programs rely on high-density ECR flats to deliver advertising materials to households that do not receive newspapers containing those same advertisements.

²⁰¹ NAA-T-2 at 13; *see also* Tr. 5/921-22. If the DAL surcharge is counted as part of the saturation flat rate, the rate differential would only be 0.7 cents, compared to the current 0.9 cents. Tr. 5/921. If not, the rate differential is 2.2 cents.

²⁰² 56.3 percent of saturation ECR flat mail do not use DALs. *See* NAA-T-2 at 13 n.15 (citing USPS-T-30 at 13 and USPS-LR-L-36, WP-STDECR, "Comm Piece-Pound Dist – BY," cell M15).

²⁰³ Witness Ingraham contends that witness Kiefer's implied assumption that the demand for optional DALs is perfectly price-inelastic is inappropriate since a major DAL user, Advo, has already declared its intention to convert to on-piece addressing. NAA-T-2 at 13.

[5534] Witness Crowder contests witness Ingraham's analysis of the appropriate high-density/saturation rate differential. In particular, she argues that he should have based the rate for on-piece addressed saturation flats on costs excluding the costs for DALs that they do not use. SMC-RT-1 at 10. Witness Crowder believes this is consistent with ECP because it should ensure that (1) mailers make correct decisions concerning postal usage, (2) mailers are properly rewarded for switching to on-piece addressing, and (3) competitive relationships are not harmed.²⁰⁴

[5535] SMC-Advo states that while in theory NAA seems to agree with it that "the amount of the DAL surcharge should not influence the 'base' saturation rate paid by all saturation mailers," it incorrectly uses the saturation flats costs including DAL costs. SMC-Advo Reply Brief at 26 (quoting NAA Brief at 7). Witness Ingraham's rate differential calculations ignore the fact that on-piece saturation mailers currently are paying a rate that is too high because the current rate averages-in the cost of DALs they do not use.

[5536] *Letter/Flat Differential and the Pound Rate*. Postal Service witness Kiefer "continued the practice of setting the basic letter rates equal to the corresponding flats rates." USPS-T-36 at 31. Valpak Witness Mitchell argues that the letter/flat differential should be recognized for the following reasons: (1) the initial proposal in Docket No. R90-1 was to recognize 50 percent of the letter/flat differential with the understanding that it would increase in subsequent cases; (2) there is no compelling policy reason for preferring flats over letters; (3) not recognizing the differential discourages mailers from sending less costly letters; (4) letters and flats are separate products with separate mail processing streams and those differences should be recognized; and (5) the Commission previously stated that it "finds persuasive witness Mitchell's arguments for ... expanding the letter/flat differential at the basic level to better reflect cost differences."

²⁰⁴ ECR competes with private delivery alternatives (including newspapers Total Market Coverage programs), and within ECR there is competition between mailers of saturation flats, saturation letters, and high-density flats. Tr. 28/9531-32.

PRC Op. R2005-1, ¶¶ 6074-75. Accordingly, witness Mitchell proposes a passthrough of 100 percent of the letter/flat differential at the basic level in ECR.²⁰⁵

[5537] On rebuttal, Postal Service witness Kiefer states that he is “sympathetic” to the view expressed by witness Mitchell that flats should bear a greater share of the Standard Mail institutional cost burdens, yet he believes that “changes in relative letter-flat prices should be evolutionary” and “adjusted gradually” due to the effects that rapid changes will have on mailer’s businesses.

[5538] On behalf of MOAA, witness Prescott evaluates the impact of witness Mitchell’s proposal to incorporate passthroughs of 100 percent of the letter/flat differential at the basic level in ECR. He finds that (1) adopting witness Mitchell’s proposed letter/flat rate differential would disrupt the relationship between the Commercial ECR basic letter rate and the 5-digit automation letter rates in Standard Regular frustrating the Postal Service’s goal of increasing automation mail; (2) Mitchell’s calculated cost difference between letters and flats only includes mail processing and delivery costs, it should be based on total cost, including weight-related costs; (3) ECR letters and flats both make a substantial contribution to institutional costs, contrary to the limited Docket No. MC2005-3 study relied upon by witness Mitchell; and (4) witness Mitchell’s rate design is flawed because he fails to recognize that part of the cost

²⁰⁵ Although witness Mitchell chooses to use passthroughs of 100 percent in his proposed alternative rate design for his passthroughs from basic letters to basic flats, he argues that it is appropriate to apply separate institutional cost markups for letters and flats even though they are in the same subclass because flats and letters are different “products” with different cost and demand characteristics. VP-T-1 at 118. Accordingly, he believes that ideally, the passthrough between letters and flats at the basic level should equal the subclass cost coverage. *Id.* at 178. MOAA and SMC-Advo Witness Crowder contest this proposition arguing that (1) this would not improve economic efficiency because it would send incorrect price signals to mailers and competitors; (2) it does not take into account available market and demand information on ECR mail as a whole; (3) it does not take into account relevant cost and demand differences between high-density and saturation flats; and (4) there is no evidence in the record showing that letters and flats are different products. SMC-RT-1 at 32; MOAA Brief at 12. Witness Crowder analyzes the full extent of witness Mitchell’s ideal basic letter to basic flat passthrough – that equal to the subclass cost coverage. Her analysis shows greater coverage and unit contribution from the flats products and less contribution and coverage from the letter products than compared with witness Mitchell’s actual proposal. The Commission need not address this product pricing issue since no participant is actually advocating adoption of a passthrough equal to the subclass cost coverage in this proceeding.

difference between letters and flats is due to the average weight differences which needs to be reflected in the pound rate.

[5539] SMC-Advo witness Crowder criticizes Mitchell and Ingraham for focusing on only the piece rates and ignoring the interrelated pound rate. The problem, according to witness Crowder, is that the letter-flat cost differences do not reflect solely piece/shape-related differences. They instead include both piece/shape-related and weight-related cost differences. Accordingly, she argues that to the extent that the weight of pound-rated flats cause costs in the mail processing and delivery streams, those weight-related costs are accounted for in the letter-flat cost differential. SMC-RT-1 at 14. She contends that because the letter-flat cost differential includes weight-related costs, the passthrough must be less than 100 percent to avoid double charging for those weight-related costs. The major cause of this problem, according to witness Crowder, is that the pound rate is too high. For example, when she makes the extreme assumption that the entirety of ECR costs are solely weight-related (with no piece or shape-related costs), then the resulting cost would only be 45.7 cents per pound rather than the 64.1 cents proposed by the Postal Service. *Id.* at 16. Therefore, she argues that the pound rates should be lowered.

[5540] NAA argues against lowering the pound rate. It believes that such a change is “unsupported on the record and unfair when other mailers are facing large rate increases.” NAA Brief at 20. SMC-Advo identifies data on the record showing unit costs by ounce for flats are less than 20 cents all the way to the last ounce increment. See Tr. 18C/6295.²⁰⁶ NAA points out that these data include qualifications that it “may be subject to substantial sampling variability, particular higher ounce increments for letters and flats, and for parcels generally.” *Id.* SMC-Advo does not believe this qualification is material. The pattern established by the data does not exhibit any “wild” or “random gyrations” that one might associate with sampling variation.

²⁰⁶ The data also show that there is a large increase in the 15-16 ounce increment for flats (49.4 cents).

[5541] Association of Alternate Postal Systems (AAPS) urges the Commission to take into account the effect that lowering the pound rate will have on competitive alternate delivery services. It argues that the proposed reduction in the pound rate for ECR mail will produce actual reductions at those weights where competition with private carriers is greatest. It cites testimony from other dockets to support its position and asks the Commission to consider the “obvious impact” on competition.²⁰⁷ It also criticizes the Postal Service for not doing enough analysis on competition and for not updating its SAI alternative delivery study since 2000.²⁰⁸ AAPS complains that the Postal Service only considered the effects of the pound charge on the alternative delivery industry by comparing the average proposed increase for pound rated ECR mail to the subclass average increase.²⁰⁹

[5542] SMC-Advo believes that essentially AAPS is arguing that any reduction in any rate element will adversely affect competition by tipping the market balance in some unknown and unproven way. It contends that § 3222(b)(4) does not demand such an absurd result, especially since such a theory does not factor costs into the equation. It further argues that the purpose of § 3222(b)(4) is not to protect private delivery companies from competition but rather to consider the effects on both mail users and competitors.

²⁰⁷ AAPS Brief at 6; *see also* NAA Brief at 21. SMC-Advo and MOAA argue that AAPS is improperly submitting testimony through its brief and the Commission should either give it no weight or use the “adverse inference” rule. SMC-Advo Reply Brief at 32-33; MOAA Reply Brief at 13-15. The citations to other dockets that have not been properly designated for use in this docket will not be considered by the Commission. *See* 39 C.F.R. §3001.31(e). The Commission can and will consider obvious impacts, but only to the extent they are supported by a factual foundation based on record evidence. Based upon the current state of the record, there is no obvious impact on competition, one way or another.

²⁰⁸ The SAI study examined “the structure, rates, and/or the services of the segment of the alternative delivery industry...that is, companies engaged primarily in the door to door delivery of advertising material, product samples, and usually free newspapers.” Tr. 18B/5436.

²⁰⁹ The Postal Service notes that witness O’Hara in his institutional cost allocation and subclass cost coverage decisions also took into account the effects of competition by setting the cost coverage for ECR higher than any other subclass except First-Class Mail Letters and Sealed Parcels. Postal Service Reply Brief at 146.

[5543] The Postal Service points out that under its reduced pound rate proposal, and taking into account both the piece and the pound rate, pound-rated pieces would actually experience a net postage increase of at least 1.2 cents (and an even greater increase from the rates that were paid prior to January 2006).

[5544] *Ingraham's alternative rate designs.* Witness Ingraham proposes two alternative rate designs for ECR. The first uses de-averaged delivery costs for basic and high-density flats, 100 percent passthroughs, and treats the DAL surcharge as an optional rate element.²¹⁰ This rate design includes the Postal Service's proposed DAL surcharge of 1.5 cents and is based on the Postal Service's assumption that no DALs will convert to on-piece addressing in the Test Year. NAA-T-2 at 4. This produces revenues from commercial ECR that exceed the revenues forecasted under witness Kiefer's proposal by \$3.2 million.

[5545] His other proposed rate design makes the same assumptions as the first, but "rejects the Postal Service's unrealistic assumption that no DALs will convert" to on-piece addressing.²¹¹ Witness Ingraham's proposed DAL surcharge in this alternative is 1.4 cents, slightly less than the Postal Service's proposal. He also increases the Postal Service's proposed per piece rate for pound rated flats from \$0.101 to \$0.103 and increases the per piece letter rate by one-tenth of a cent over the Postal Service's proposed rate design (from \$0.098 to \$0.099).²¹² This produces revenues from commercial ECR that exceed the revenues forecasted under witness Kiefer's proposal by \$2.6 million.

²¹⁰ He uses the disaggregated delivery cost information provided by witness Kelly. Tr. 12/3404. He also uses the current pound charge of 64.3. NAA-T-2 at 18.

²¹¹ NAA-T-2 at 17. His assumption is 75 percent of DAL mailers convert to on-piece addresses resulting in the Postal Service capturing 80 percent of DAL city and rural delivery costs. He also assumes there would be no savings in DAL mail processing or city carrier in-office costs.

²¹² Under this proposal, piece rated saturation DAL mailers pay no more than one-tenth of a cent more than under witness Kiefer's proposal. The saturation flats entered at the DDU would pay no more than under the Postal Service's proposed rate design.

[5546] The Postal Service believes that witness Ingraham misinterprets Kiefer reasons for assuming that no DALs will convert. Kiefer made that assumption for the purposes of estimating net revenue so that the cost and revenue assumptions for DALs would be consistent. Witness Kiefer's rate design does not depend on the level of DAL usage. Even assuming that there will be mailers switching from DALs, that switch would, in parallel, reduce costs. Tr. 5/1008. The Postal Service also notes that Ingraham's proposals would lead to a rate relationship in which the rates for saturation flats using DALs will be higher than the rates for high-density flats. It views such a relationship as "odd" and something that would be "preferable to avoid." Postal Service Brief at 324.

[5547] SMC-Advo argues that Ingraham's rate design is inappropriate because (1) he incorrectly underestimates the unit incremental cost of a DAL; (2) he understates the extent to which the DAL costs will be saved, and passed those additional costs to on-piece addressed saturation flats mailers; and (3) he makes no attempt to adjust the unit cost of on-piece addressed high-density flats to reflect their known DAL usage.

[5548] *Mitchell's alternative rate designs.* After selecting what he believes are the appropriate cost coverages,²¹³ using cost avoidance that reflects both mail processing and delivery costs, he designs rates for each rate category using the presort tree. In setting rates, he discusses each cost, each passthrough and each important rate relationship, along with the history and previous Commission opinions on each rate.²¹⁴ In designing his specific rates, witness Mitchell advocates passthroughs of 100 percent unless the other factors of the Act justify deviating from that result for a particular rate category.

²¹³ Flowing from his choice of cost coverages for the Standard Mail subclasses, witness Mitchell proposes rates for all the rate categories within the four standard mail subclasses.

²¹⁴ As a preliminary matter, Valpak is now arguing that portions of SMC-Advo's cross-examination of witness Mitchell's rebuttal testimony (VP-RT-1) dealing with Advo-EX-1-5 was improper cross-examination since it was directed at witness Mitchell direct testimony (VP-T-1), not his rebuttal testimony. Valpak's concerns are not timely. An appropriate course of action would have been for Valpak to object to this line of questioning during the hearing.

[5549] On rebuttal, Postal Service witness Kiefer takes issue with witness Mitchell's rate design calling it "too doctrinaire," "too incomplete," and "focused on just one pricing factor out of many." USPS-RT-11 at 20, 26. He believes that Mitchell's approach does not adequately take into account current rate relationships or the impact on mailers. Similarly, Postal Service witness Robinson criticizes witness Mitchell's proposal as being an overly narrow focus on economic efficiency at the expense of the other factors of the Act, which she believes are relevant below the subclass level. She further points out that witness Mitchell does not consider the effects of his recommendations on other subclasses and the revenue requirements of the Postal Service as a whole. USPS-RT-10 at 21.

[5550] NAA criticizes Witness Mitchell's treatment of the high-density discount for flats. Specifically, Mitchell expressed doubt as to the disaggregated carrier delivery costs provided by witness Kelly and transferred 1.4 cents from the high-density discount to the saturation discount. NAA believes that this adjustment is arbitrary and unsupported by any data.

[5551] Valpak argues on reply that witness Mitchell's proposal in this regard is justified. Witness Mitchell found that the cost savings for high-density flats in this docket (relative to basic flats) to be anomalous compared with earlier dockets. He explained that the savings for high-density mail is understood to relate to more rapid casing which has not changed since previous dockets. Accordingly, he did not see any reason for the substantial cost increase in this case. Given the small volume and the historical passthrough range of 39-79 percent, he recommends a 68 percent passthrough. Valpak believes it was incumbent upon NAA to justify the unusual change in costs.

[5552] *Witness Crowder's Rebuttal.* SMC-Advo witness Crowder argues that both the Mitchell and Ingraham rate designs are flawed because (1) the unit costs they use to develop the saturation on-piece-addressed flat rate are incorrect and excessive since they fail to exclude DAL costs from on-piece addressed flats that will not use a DAL; (2) the unit costs they use to develop all piece-rate differentials incorrectly include weight-related costs for pieces over the breakpoint; (3) their proposed pound rates are

too high; and (4) they do not adjust attributable costs to reflect the cost savings that will result from saturation DALs leaving the system as a result of the surcharge.

[5553] Witness Crowder develops an alternative set of rates.²¹⁵ She suggests: (1) the on-piece addressed saturation flat piece rate should be lower than the level proposed by the Postal Service; (2) the piece-rate differential between saturation letters and flats should be less than proposed by the Postal Service, not greater as proposed by witness Mitchell; (3) the piece-rate differential between saturation and high-density flats should be about the same as the Postal Service proposes and greater than that advocated by witness Ingraham; and (4) the ECR pound rate should be lower than proposed by witness Ingraham. SMC-RT-1 at 2, 5. She believes that her rates are more appropriate than those of witnesses Mitchell and Ingraham because her rates comport with ECP principles and foster competition both with private delivery and between the various rate categories within ECR. She believes these rates have less bias and improve economic efficiency by providing better price signals to ECR mailers.

[5554] SMC-Advo argues that Crowder's unit delivery cost for saturation flats is appropriate because (1) it is the average unit cost for all flats that will be charged the on-piece-addressed saturation flat piece rate, (2) for saturation flats that convert from DALs to on-piece addressing, the method and cost of handling the flat itself will remain unchanged, SMC-RT-1 at 9-12; USPS-T-44 at 13, and (3) mail processing and in-office costs associated with DALs should be taken into account.²¹⁶

²¹⁵ Witness Crowder notes that SMC and Advo support the ECR rates proposed by the Postal Service. However, she believes that "to the extent the Commission considers departures from the USPS proposed ECR rates, it should avoid the severe rate distortions proposed" by other witnesses and should make any changes from the Postal Service's proposal in the direction shown in her analysis. SMC-RT-1 at 3. Valpak and NAA argue that witness Crowder's alternative rates should have been filed as intervenor direct testimony, but since they were filed as rebuttal testimony, they came too late for meaningful record evaluation. Valpak Brief at IV-7, n.8; NAA Reply Brief at 13. This argument is not timely. An appropriate course of action would have been to file a timely motion to strike or file for an extension of time to explore witness Crowder's alternative rates before cross-examination at the hearing.

²¹⁶ Even if this were added to witness Ingraham's estimate of delivery costs, the result would be an incremental DAL cost of approximately 1.28 cents, still below the proposed DAL surcharge. NAA Reply Brief at 10-11.

[5555] SMC-Advo further contends that the cost reductions from DAL conversion will be much larger than calculated by the Postal Service and assumes that the unit cost of DALs exceed the proposed surcharge. SMC-Advo asserts that cost savings from DAL conversion will be so large that ECR will make a larger contribution to institutional costs than proposed by the Postal Service – and it argues that the savings should be used to mitigate ECR rates. MOAA makes a similar argument. *See also* MOAA Brief at 20. The Postal Service’s witnesses make the assumption that no DAL conversion occurs in the test year and therefore do not reach the cost issue.

[5556] NAA disputes witness Crowder’s calculation of the on-piece addressed saturation flat cost and argues that Dr. Ingraham’s calculation is more appropriate. To arrive at the unit costs, witness Crowder divides the estimated Test Year costs associated with DALs by the estimated number of DALs put in the mailstream, arriving at a cost per DAL above 3 cents. NAA believes this approach is incorrect for purposes of estimating DAL costs for the following reasons (1) the cost savings of a partial conversion might not be linear, (2) the post-converted saturation flats will have the same delivery cost as an addressed flat, not the delivery costs of today’s unaddressed flats,²¹⁷ (3) because DAL costs have not previously had rate implications, the quality of DAL costs estimated by the postal accounting system has never undergone close scrutiny, and (4) the cost data associated with this approach do not take into account the cost effects of bulk and weight of the accompanying flats.

[5557] Valpak questions witness Crowder’s assumption that 50 percent of DALs will convert whereby the surcharge will only cover a third of the DAL cost. This would result in “\$67 million of unrecouped costs from DALs,” which will need to be made up by all other ECR mailers. *See* Tr. 35/11791; Valpak Brief at 7-9. Valpak argues that it would

²¹⁷ *See* SMC-LR-1, AC-UDCmodel.xls at 2, Summary TY, Row ECR, Cell P84. Witness Crowder’s estimated cost of the Test Year saturation flats is a weighted average of the costs of ECR saturation addressed flats and saturation flats with DAL host pieces, all divided by the total volume of saturation flats. In other words, she implicitly assumed that the converted flats will be handled as they are today when they are unaddressed even though they will have an on-piece address in the future – and addressed flats have higher costs – according to NAA. NAA Brief at 17, n.16; *see also* Tr. 35/11786.

be unfair for those costs to be recouped by the ECR subclass as a whole since DALs have never benefited ECR letters. Instead, it suggests that such costs be borne by ECR flat mailers or ECR saturation flat mailers.

[5558] On brief, SMC-Advo argues that witness Crowder's 50 percent conversion assumption is conservative. The actual conversion will be at least 87 percent, see Tr. 35/11842-43, so the issue of unrecouped DAL costs does not arise. SMC-Advo Brief at 16. Further, even if it does arise, it is appropriate for all ECR mailers to make up that unrecouped DAL costs since other unrecouped costs are normally borne by the entire subclass. As an example, SMC-Advo points to the current, below cost treatment of Standard parcels and NFMs. *Id.* at 17.

[5559] With respect to assumptions regarding DAL conversion to on-piece addressing, the Postal Service contends that both witnesses Ingraham and Crowder have made conflicting assumptions "none of which seem entirely implausible," which make satisfactory resolution difficult. Postal Service Reply Brief at 225. It believes that the conflicting state of the record underscores the difficulty of achieving anything approaching a precise quantification of net savings from potential DAL conversions, where there is no firm estimate of what the conversion volume will be, or exactly what operational procedures will be used on city and rural routes to handle formerly DAL host pieces that are now on-piece addressed flats. Accordingly, the Postal Service believes that these circumstances favor the retention of the cost analysis and rate design associated with the "neutral" assumption of no conversion. Once data are collected, it will be easier to address these matters in the future.

[5560] *Commission analysis.* The Commission recommends the Postal Service's proposed DAL surcharge of 1.5 cents. The Commission finds witness Gorman's testimony persuasive that a change to the surcharge would cause "severe harm and chaos" in the saturation mailing industry due to the cost of conversion and long lead time necessary to retrofit operations.

[5561] The record contains no definitive information on what operational procedures will be used on city and rural routes to handle former DAL host pieces. The

percentage that will be cased, flat sort sequenced, or taken directly to the street is unknown at this time. Consequently, the cost savings can not be reliably estimated. For this reason the Commission accepts, for cost calculation purposes, the Postal Service assumption that no conversion will be completed by the Test Year. Once the Postal Service begins making operational decisions on how it will handle this former DAL host mail, cost data should be reliable enough to change this conversion assumption.

[5562] The Commission accepts NAA's argument to disaggregate the delivery costs between the basic and high-density tiers. The Commission uses the most reliable available data unless overarching concerns dictate otherwise. Here, no persuasive reasons for using aggregated delivery cost data have been given. Further, the Postal Service itself used disaggregated data in its R2005-1 request. The Commission does not disaggregate the mail processing costs between high-density and saturation flats because the Postal Service effectively admitted that it did not have reliable evidence of any mail processing cost differences between the two tiers.

[5563] With respect to the high-density/saturation rate differential, the Commission passes through 100 percent of the cost differences. The Commission calculates the unit cost of a saturation flat by adding the total cost of ECR saturation attached label flats to the total cost of the unaddressed saturation flat pieces and then dividing by the total volume of saturation flats.

[5564] The Commission finds SMC witness Crowder's methodology for calculating ECR saturation flats more representative of operational realities. NAA witness Ingraham argues that the Crowder saturation flat calculation methodology relies on a disaggregation of unaddressed saturation flats. The Commission is not persuaded by this argument.

[5565] The Commission agrees with NAA that it is not appropriate to factor into the rate differential the potential cost of DALs. The DAL surcharge is a separate charge designed to recapture additional cost caused by the DALs. It should have no influence or relationship to the rates for saturation flats. They should be set independently of the surcharge. Nonetheless, the Commission does not believe that a 0.9 cent rate

differential is appropriate between high-density and saturation flats. The cost difference is 1.82 cents which would make the passthrough only 49 percent. No rationale for only passing through 49 percent at this level has been provided.

[5566] The Commission also agrees with SMC-Advo that the DAL costs, to the extent that any exist that are not recouped by the DAL surcharge, should not be paid by saturation flat mailers. The appropriate way to deal with this situation is for the entire subclass to make up any potential shortfall. This conclusion is buttressed by the fact that DALs currently are being used with high-density mailings.

[5567] As a related issue, the Commission does not accept the Postal Service's argument that the saturation flat rate combined with the DAL surcharge should not be greater than the high-density flat rate. The DAL surcharge has no relationship to high-density pieces in operations or otherwise. Accordingly, it makes no sense for the Commission to link those two rates.

[5568] The Commission recommends rates that reflect Valpak's suggestion to pass through 100 percent of the cost difference between letters and flats at the basic level. Additionally, the Commission lowers the ECR pound rate more than proposed by the Postal Service. In the past, the Commission had accepted proposals to not recognize the letter/flat differential at the basic level to encourage basic letter mailers to barcode their mail and enter it as ECR basic automation or Regular 5-digit automation. See R97-1, ¶ 5560; PRC Op. R2000-1, ¶¶ 5445-5452. However, with the Postal Service's proposal to eliminate the ECR basic automation rate category (which has been accepted by the Commission), and the Commission's recommendation to decouple the ECR basic rate from the Regular 5-digit automation rate category, the rationale for not recognizing the letter/flat differential at the basic ECR level no longer applies. The Commission also finds that recognizing the differential will encourage mailers to send less costly mailpieces, consistent with its Docket No. R2005-1 support for expanding the letter/flat differential at the basic level to reflect cost differences. The Commission does not believe that it should "gradually" recognize the differential as proposed by the Postal Service. Adopting a long-term timeline for completely recognizing the letter/flat

differential artificially keeps letter rates unfairly elevated to the benefit of flat mailers without justification. The Commission does not believe that is in the interest of either the Postal Service or the mailing community. Accordingly, the Commission recommends a full 100 percent passthrough at the basic level.

[5569] With respect to the ECR pound rate, the Postal Service proposes to lower the rate from \$0.643 to \$0.641. The Commission finds Crowder's analysis probative that under the extreme assumption that all costs are weight related, this would still produce just a 45.7 per pound cost. Consequently, the Commission recommends a pound rate of \$0.621. This is \$0.0220 lower than the current pound rate. A further reduction of the ECR pound rate may be justified. Given the lack of the anticipated comprehensive study on the pound rate, see PRC Op. R2000-1, ¶¶ 5459-5463, 5494, on this record, the Commission is hesitant to recommend a further lowering of the ECR pound rate.

[5570] The Commission finds no persuasive evidence on this record that the Commission's limited reduction in the pound rate will unduly interfere with competition as alleged by AAPS and NAA. These arguments amount to nothing more than allegations that any lowering of the pound rate will harm competition. Section 3622(b)(4) does not require the Commission to artificially keep the postal rates high to encourage competition. Rather, it requires the Commission to consider, based on the record, the impact of rate proposals on competition as well as the impact on mailers. The Commission has done so.

(3) Parcels

[5571] *Postal Service's Rate Proposals.* Witness Kiefer developed the rate design for ECR parcels based on the assumption that, in the future, ECR parcel categories will largely reflect pieces migrating from flats rates rather than pieces currently paying the residual shape surcharge. Accordingly, he selected piece and pound rates for ECR parcels that represent a fixed increment over the prices these pieces would have paid had they remained in the proposed flats rate categories. This approach, witness Kiefer

argues, will help mitigate the impact of moving from flats-rate treatment to parcels-rate treatment.²¹⁸ The proposed rate differential, \$0.20 per piece, is slightly less than the current ECR residual shape surcharge. Witness Kiefer's proposals have the same parcel-flats rate differential for both commercial and nonprofit ECR pieces. Further, as with flats, he proposes that saturation parcels that use DALs pay a \$0.015 per piece surcharge.²¹⁹

[5572] *Commission analysis.* The Commission's recommended parcel rate design reflects significantly less than 100 percent passthroughs in the flat/parcel shape differential. The Commission finds that without lowering the passthroughs, ECR parcel mailers would experience undue rate shock. This is due largely to the de-averaging classification changes proposed and recommended by the Commission in this case whereas previously, parcel mailers paid a fixed residual shape surcharge regardless of density level.

e. Proposals for the Nonprofit Subclasses

[5573] First, the Commission summarizes the Postal Service's proposed rates for the Standard Nonprofit Regular and Standard NECR subclasses. Then, the Commission examines the participants' arguments for deviating from the Postal Service's proposed Nonprofit rates.

[5574] *Standard Nonprofit Regular Subclass.* Postal Service witness Kiefer's proposed rate design for Standard Nonprofit Regular is the same structure as he proposes for its commercial counterpart. By law, the average revenue per piece for nonprofit pieces must be 60 percent of the average revenue for commercial pieces. Witness Kiefer follows the practice of R2005-1 and sets the destination entry discounts

²¹⁸ Witness Kiefer believes that many ECR mailers will reconfigure their non-eligible pieces to meet the new flats definition and thereby avoid being pushed into the parcels category. His proposed rate differential is designed in part to encourage such reconfiguration.

²¹⁹ For net revenue purposes, witness Kiefer assumes that all saturation parcels currently using DALs will continue to do so in the test year.

and non-barcode surcharge the same for both commercial and nonprofit pieces. For the other rate relationships, witness Kiefer adjusted the commercial per-piece and per-pound rate elements and automation/machinability differentials to develop corresponding nonprofit piece and pound rate elements.

[5575] *Standard Nonprofit ECR Subclass.* Postal Service witness Kiefer bases his NECR letters, flats, and parcel rate proposal on the corresponding commercial ECR piece and pound rates as well as the density differentials to achieve the required 60 percent ratio between the average NECR rate and the average ECR rate.

[5576] *Worksharing Discounts.* Witness Mitchell raises an issue with the calculation of Standard Nonprofit Regular and Nonprofit ECR discounts. He argues that the rate differential for the Nonprofit subclasses should be the same as their commercial counterparts. The following reasons underlie his argument: (1) the intent of Pub. L. 106-384 is to move the Nonprofit rates closer to the actual costs of their commercial counterparts and fully recognizing costs through accurate discounts will help reach that goal; (2) setting different discounts for performing the same worksharing function would be a form of unjustified discrimination; (3) having different discounts would make decisions for mail preparation firms (who work for both nonprofit and for-profit entities) more difficult and less efficient;²²⁰ (4) although this will cause certain rates to increase or decrease substantially, this is acceptable since mailers whose rates should be decreased have a greater right to have their costs properly recognized; and (5) if mailers are informed through rates of the true cost consequences of alternatives they have, they may change their mailing patterns and avoid sharp rate increases. See VP-T-1 at 110-113; 114 n.43.

[5577] MOAA points out that witness Mitchell's rate proposal would create a rate structure for ECR nonprofit mail that results in a negative piece rate element for high-density and saturation mail weighing more than 3.3 ounces. MOAA views such a

²²⁰ As an example of a situation where the Commission found this rationale persuasive, he cites to Docket No. R90-1 where he argues that the Commission held dropship discounts for the nonprofit and commercial categories should be the same.

relationship as an “anomaly.” Tr. 32/10969. On cross examination, however, Valpak pointed out that a negative piece rate element occurs in at least a few other circumstances under current rates for Standard Nonprofit Mail and therefore, has been found acceptable. *Id.* at 10970-72.

[5578] DMANF asks the Commission to consider the impact that the proposed rates will have on Nonprofit Standard Mail volume. In particular, it argues that society has grown increasingly reliant upon nonprofit organizations for social safety net services, education, and arts. The proposed rates will have a negative impact on their ability to raise funds through mail solicitation. It also argues that the rates will have a negative impact on First-Class mail volumes since fewer solicitations will produce fewer donations mailed at First-Class rates. DMANF questions the Postal Service’s proposed rate increases as counterintuitive. For example, proposed increases for automation mail are much greater than the overall average increase in this proceeding yet automation mail is usually thought of as cheaper to process. It also notes that traditionally, Nonprofit Standard letters have been characterized as “relatively low-cost to process.” DMANF Brief at 6.

[5579] The Postal Service argues that nonprofit costs are, by law, irrelevant to the rate level for the nonprofit subclasses. Instead, it notes that nonprofit rates are set to yield per-piece revenues that are 60 percent of commercial revenues. Postal Service Reply Brief at 200 n.4 (citing 39 U.S.C. § 3626(a)(6)).

[5580] *Commission analysis.* Public Law 106-384 requires nonprofit rates to be set in relation to their commercial counterparts regardless of nonprofits’ independent costs. The Commission can not ignore that law and depress rates simply to facilitate fundraising as DMANF seems to suggest. Also the Commission agrees with witness Mitchell that, in line with 39 U.S.C. § 3626(a)(6), absent exceptional circumstances, the discounts for nonprofit subclasses should be the same as their commercial counterparts. This avoids any potential discrimination assuring that cost savings and worksharing initiatives by nonprofit mailers are recognized to the same extent as commercial mailers. The Commission recognizes that this results in substantial rate increases for some

nonprofit mailers of flats, but those mailers may change their mailing behavior patterns (e.g., sending letters instead of flats) to avoid these significant rate increases. The Commission deviates from using the same discounts as commercial in two instances. First, the passthrough between nonmachinable letters and non-automation flats in Nonprofit Regular is increased substantially in order to mitigate the rate increases for non-automation flats.²²¹ Second, the rate differential between non-automation MADC and automation MADC flats is set at 3.50 cents in Nonprofit Regular rather than the 3.75 cent differential set for commercial Regular. The Commission finds that absent this additional mitigation, these nonprofit mailers would face an excessive increase.

6. Sequenced Mail Costs and Capacity Constraints

[5581] Witnesses Haldi and Mitchell assert that fairness should be taken into account in carrier costing. See VP-T-2 at 58-59, 67-68 and VP-T-3 at 11. Witness Mitchell poses the following hypothetical example. Suppose that the Postal Service is planning its operations and sees that the current carrier system can carry 50 million extra bundles to the street. It looks at its current situation and finds that it has 49 million bundles of saturation flats and 49 billion bundles of saturation letters. As a matter of operating policy, the Postal Service has two options: (1) take the saturation flats to the street as “extra bundles” and Delivery Point Sequence (DPS) the saturation letters, or (2) take the saturation letters to the street as extra bundles and Flat Sort Sequence (FSS) or manually case the saturation flats. Since the costing system shows that it is cheaper to DPS letters rather than FSS flats, it is cheaper if the Postal Service chooses the first option.²²² The presence of the ECR saturation flats, which are then accorded treatment as an extra bundle cause the costs and rates of saturation letters to be higher than they would be if saturation flats were not present. Witness Mitchell believes that the

²²¹ This results in a seemingly anomalous rate relationship where non-automation flats are less expensive than nonmachinable letters. However, these rates are consistent with the unit costs. The Postal Service proposed rates with this anomaly in Standard Regular.

Commission should consider this a fairness issue and seek the comments of the community of pricing and costing experts to provide help on dealing with it.²²³ Valpak asks the Commission to “take special note in this docket to guard against any undue elevation in the rates for saturation letters based on overstated saturation letter costs and understated saturation flat cost.” Valpak Brief at III-10.

[5582] SMC-Advo Witness Crowder contests the Haldi and Mitchell suggestions that Saturation letters are subsidizing Saturation flats, and that the costs of Saturation ECR letter mail has increased due to the presence of Saturation ECR flat mail. SMC-RT-1 at 33. Witness Crowder argues that it is not the Saturation flats that are causing the Postal Service to DPS the Saturation letters. Rather, saturation letters generally do not have appropriate characteristics for extra bundle treatment on certain carrier routes due to their relatively small dimensions and light weight. Therefore, she believes, DPSing Saturation letters will actually reduce overall Saturation letter delivery costs since it is the lowest-cost option on many city delivery sections and on all rural routes. In fact, witness Crowder provides data showing that relative to its current unit cost, 100 percent DPSing of would result in a cost savings of approximately 28 percent of the current total letter saturation cost.

[5583] Valpak, however, believes that witness Crowder’s hypothetical 100 percent DPSing analysis is improper since it compares manual casing costs with DPS costs – not the lower costs of taking saturation letters directly to the street. Valpak also argues that witness Crowder’s hypothesis that saturation letters do not have appropriate physical

²²² However, saturation letters taken directly to the street would incur the lowest cost method of handling (for those letters) with a lower unit cost than any other alternative treatment (including DPSing). See *Id.* at 40 n.81. Yet, only 10 percent of all saturation letters on city routes are afforded this lower cost treatment and 34 percent of saturation letters on city carrier routes are being cased. *Id.* at 40 n.80. Accordingly, only a small portion of saturation letters are receiving the lowest cost treatment. Valpak Reply Brief at III-3.

²²³ Witness Mitchell states: “My purpose is not to answer these questions, but only to pose them.” He also offers two potential solutions. First, he suggests that both saturation flats and saturation letters be treated for costing purposes as though neither were carried as an extra bundle (and let any benefits from extra bundles accrue to saturation pieces as a group). Alternatively, he suggests that both be treated for costing purposes as though both were carried as an extra bundle. VP-T-3 at 12.

characteristics for sequenced bundle treatment is erroneous, given that billions of letters and letter shaped DALs have been and continue to be taken directly to the street. Further, no Postal Service witness has made the claim that there are problems taking saturation letters directly to the street.

[5584] Witness Crowder disputes the Mitchell contention that this situation presents a form of “cross-subsidy.” To counter this argument, Witness Crowder compares the proposed saturation flat revenues to the costs under the extreme assumption that all saturation letter mail processing and delivery costs are “caused” by the presence of saturation flats. This analysis shows that the proposed revenues from saturation flats more than cover the incremental cost of both saturation letter and flat mail processing and delivery. It also shows that if all saturation flats were eliminated from the system, rates for the other mail categories (including saturation letters) would need to be increased to absorb the contribution loss. Accordingly, she argues, saturation letter mailers can not claim they are subsidizing saturation flat rates or being treated unfairly. Valpak believes that witness Crowder’s arguments on cross-subsidy are irrelevant because “witness Mitchell ... does not use it to draw conclusions relating to cross-subsidies.” Valpak Reply Brief at III-11.

[5585] The Postal Service and SMC-Advo note that in PRC Op. R2005-1, the Commission rejected Valpak’s argument that marginal city carrier costs for Saturation ECR should be changed, instead finding that the established cost methodology measures costs in relation to current operating procedures. SMC-Advo Brief at 49; Postal Service Brief at 124. They also note that witness Coombs testified that, based on her experience, the conflicts suggested by Valpak are “highly unlikely,” “not common,” and “rare,” especially since ECR mail can be deferred. Tr. 13/3710, 3717-18, 3721. This means that the situation Valpak is highlighting is not frequent enough to justify concern. Postal Service Reply Brief at 126.

[5586] Valpak claims that this case is different due to “new and different record information” that came to light. This allegedly new information is that (1) there are capacity constraints on motorized routes due to physical space limitations on the

standard delivery vehicle; (2) ECR volumes are not uniformly distributed over all ZIP Codes; and (3) the Postal Service is effectively beginning to “permanently bump” saturation letters to DPS processing. Valpak Brief at III-5-9. Witness Haldi argues that when capacity constraints are present, the Postal Service’s costing system identifies higher costs for product which is the most flexible and can be handled at the lowest cost (saturation letters), while indicating that one of the least flexible and most difficult flat product to handle (saturation flats) has a lower cost.

[5587] *Commission analysis.* If saturation flats are not the cause of the higher DPS costs for saturation letters, then the fairness concerns raised by witness Mitchell do not arise. Tr. 22/8078. Therefore, the initial question is whether saturation letters are not afforded “extra-bundle” treatment due to saturation flats, or for some other reason. On this record, it appears that saturation letters are being DPSed due to a Postal Service operational decision that, currently, DPSing saturation letters is the most cost-efficient way to deal with those letters – from the perspective of the postal system as a whole. Support for this operational decision is found in witness Coomb’s testimony on operations.

[5588] The Commission finds, as it did in R2005-1, that the current cost system is designed to reflect current operating practices. Valpak fails to show current practices are inefficient or not cost-minimizing. The Commission finds that operations practices that are efficient and cost-minimizing for the system as a whole are fair.

7. Commission’s Recommended Rate Design for Standard Regular

[5589] The Commission’s recommendation produces an average increase in Standard Regular revenue per piece of 9.5 percent and Standard Nonprofit Regular of 6.7 percent. This results in an overall increase for the Regular subclasses of 9.3 percent, with a resulting cost coverage of 170.8 percent using Commission accepted costing methodology.

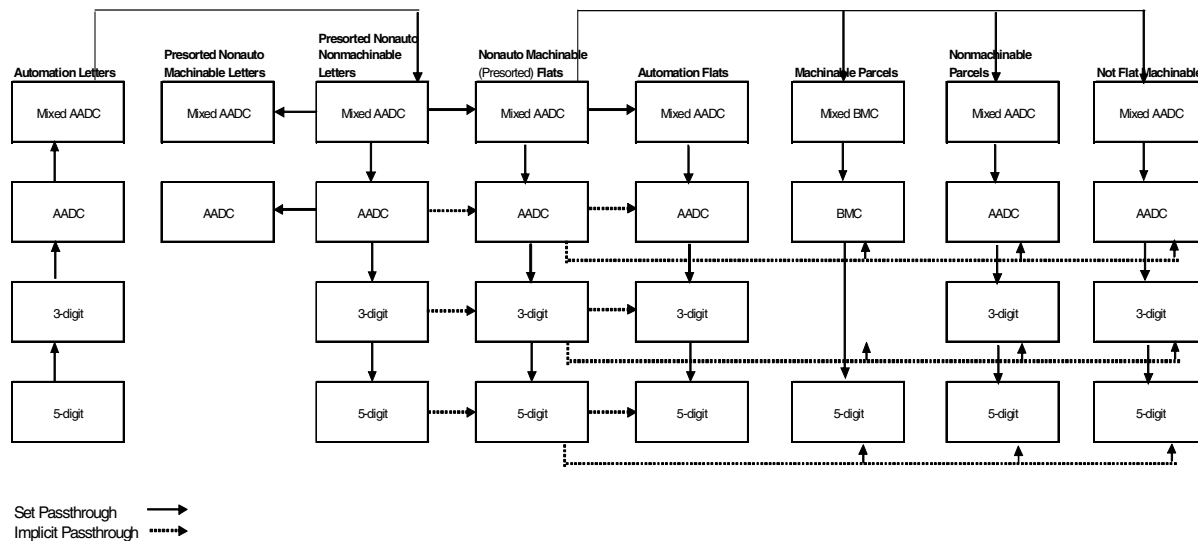
[5590] As discussed in section V.B.1.e., the Commission uses both mail processing and delivery costs in calculating avoided costs for determining appropriate discounts. As is done in First-Class, the Commission accepts the use of a single CRA cost estimate that combines the costs of non-automation and automation presort letters. In developing the CRA mail processing unit cost for Standard letters, the Commission assigns costs as either worksharing, fixed, or piggybacked in the same manner as First-Class presort letters.²²⁴ The Commission follows the same methodology for flats costs with the exception of non-MODS allied costs which are treated as fixed. This is done to avoid possible double counting of dropship savings since these costs likely vary with the level of dropship and are reflected in the calculation of dropship related savings. However, the Commission encourages further exploration of these costs and how they vary with both dropship and presort.

[5591] The delivery costs are disaggregated to the extent possible given the data on the record. For automation letters, a separate delivery cost is calculated for each presort level. For non-automation letters, a separate delivery cost is developed for machinable MADC/ADC and 3/5 Digit. One delivery cost is used for all nonmachinable, non-automation letters. Likewise, there is one delivery cost for all flats and one delivery cost for all parcels. The development of the delivery costs used in Standard Mail Regular rate design is shown in PRC-LR-L-11.

[5592] As it has since Docket No. R90-1, the Commission employs the use of the presort tree to help guide its rate design for Standard Mail. As discussed above, the Commission accepted the Postal Service's argument to use a typical mailpiece as the Standard Regular benchmark. Accordingly, the Commission begins its rate design analysis at the Automation 5-digit letters rate category. In general, the Commission uses the presort tree proposed by witness Mitchell. Figure V-1, depicts the presort tree used by the Commission.

²²⁴ See Section V.B. for further discussion of cost assignment.

Figure V-1



[5593] In line with Efficient Component Pricing principles, the Commission’s rate design recognizes 100 percent of the cost differences throughout the rate structure with several exceptions that are discussed in more detail below. First, the Commission’s rate design only passes through 30 percent of the shape differential between flats and parcels and 25 percent of the shape differential between flats and NFMs.²²⁵ This is done, for the most part, in order to mitigate the large rate increases that mailers of these pieces would otherwise experience. For example, the cost difference between a non-automation flat and a nonmachinable parcel is \$2.06. Passing through 100 percent of this difference would result in a rate increase of over 800 percent. In addition, the disaggregated parcel rates and the NFM rates are for new categories. In the past the Commission has mitigated passthroughs for new categories in recognition of untested cost differences and mailer behavior. To avoid rate anomalies — such as negative 5-digit rates — the Commission limits the presort passthroughs for these categories to 30 percent or less.

²²⁵ The 30 percent passthrough between flats and parcels also reflects the desire to correct the admitted rate anomaly with respect to nonmachinable 3-digit parcels and a comparable machinable parcel sorted to the BMC. See USPS-RT-11 at 8; Tr. 33/11147-49; see also Tr. 18D/6663 and 5/959; Tr. 33/11147-50.

[5594] Second, with respect to the automation differential between the non-automation flat and the automation flat, the Commission's rate design passes through 213 percent. The Commission believes that such a high pass through is justified for two reasons. One, the Commission's recommended classification proposal disaggregates the current "basic" rate category at this level into a Mixed ADC rate category and an ADC rate category. Consequently, although the current rate differential is 4.7 cents at the basic level, the current cost savings is only 1.8 cents due, in part, to this de-averaging. Dropping this discount to 1.8 cents in line with ECP could cause rate shock for those pieces mailing at the MADC level. Accordingly, the Commission's recommended rate design adopts passthroughs greater than 100 percent for the automation/non-automation flat differentials and 100 percent for the presort levels within the automation flat category. This rate design results in a rate differential of 3.75 cents for automation flats at the MADC level, 3.61 cents at the ADC level, 3.39 cents at the 3-digit level, and 2.67 cents at the 5-digit level.

[5595] Third, with respect to the differential between the Mixed ADC Automation letter and the MADC nonmachinable letter, the Commission's rate design passes through only 95 percent of the cost difference. This passthrough level is appropriate for the following reasons. The current rate design recognizes only two categories of non-automation letters, basic and 3/5-digit, and charges a nonmachinable surcharge of \$0.042 regardless of the amount of presorting done by the mailer. See DMCS Schedule 321A, n.4. The Commission's recommended classification proposal effectively disaggregates the surcharge into both machinable and nonmachinable rate categories. Recognizing 100 percent of the disaggregated cost differences would result in excessively large rate increases for some mailpieces. To maintain an appropriate relationship between non-automation machinable and automation machinable letters, the non-automation machinable letter rate was set at \$.003 above the automation rate. This results in a passthrough of 93%. Accordingly, the Commission's recommended rate design adopts a passthrough of less than 100 percent for the machinability differentials. A comparison of the passthroughs recommended by the Commission with implicit

passthroughs calculated for the Postal Service's proposed rates is provided in Table V-4 below.

[5596] The Commission's rate design also recognizes 100 percent passthroughs of the cost savings due to dropshipping for all mail shapes. The Postal Service proposed higher dropship savings for parcels in recognition of the untested assumption that parcels are more costly to transport, and avoiding these operations would result in higher cost savings. While this assumption may be true, no cost evidence was presented to bolster the claim. Accordingly, the Commission recommends the same dropship discounts for parcels as for letters and flats. Similarly, the Commission recommends the same pound rate for all shapes of mail.

8. Commission's Recommended Rate Design for Standard ECR

[5597] The Commission's recommendation produces an average increase in ECR revenue per piece of 6.9 percent and Nonprofit ECR of 8.8 percent. This results in an overall increase for the ECR subclasses of 6.9 percent, with a resulting cost coverage of 206.3 percent using Commission accepted costing methodology.

[5598] The Commission uses both mail processing and delivery costs in determining the cost avoidance for ECR mail. The mail processing costs are only disaggregated between basic and high-density/Saturation because the Postal Service has stated that it can not further disaggregate these costs. The Commission believes that mail processing cost differences exist between high-density and saturation and urges the Postal Service to further explore disaggregating these costs. For basic parcels the Commission uses the unit cost developed in Response to POIR 10, question 2.

[5599] The delivery costs are disaggregated for letter and flats by presort level. The average delivery costs for Standard Regular parcels are used as a proxy for ECR parcels for the reasons given in witness Kiefer's testimony.

[5600] As with Standard Regular, the Commission uses the presort tree to guide its rate design for ECR. Consistent with previous decisions, the benchmark rate remains

Table V-4

Tree Reference	Category	PRC Recommended Passthrough	Implicit USPS Passthrough
Automation Letters			
Vertical	MAADC and AADC	100%	74%
Vertical	AADC and 3-Digit	100%	132%
Vertical	3-Digit and 5-Digit	100%	104%
Horizontal	Automation MAADC Letters and Nonautomation Nonmachinable AADC Letters	95%	69%
Nonautomation Nonmachinable Letters			
Vertical	MADC and ADC	100%	56%
Vertical	ADC and 3-Digit	100%	28%
Vertical	3-Digit and 5-Digit	100%	42%
Horizontal	Nonautomation Nonmachinable MADC Letters and Nonautomation MADC Flats	100%	340%
Horizontal	Nonautomation Nonmachinable MADC Letters and Nonautomation Machinable MADC Letters	93%	55%
Horizontal	Nonautomation Nonmachinable ADC Letters and Nonautomation Machinable ADC Letters	95%	57%
Nonautomation Flats			
Vertical	MADC and ADC	100%	56%
Vertical	ADC and 3-Digit	100%	67%
Vertical	3-Digit and 5-Digit	100%	55%
Horizontal	Nonautomation MADC Flats and Automation MADC Flats	213%	227%
Horizontal	Nonautomation MADC Flats and Nonmachinable MADC Parcels	30%	30%
Horizontal	Nonautomation MADC Flats and Machinable MBMC Parcels	75%	72%
Horizontal	Nonautomation MADC Flats and NFM MADC	25%	23%
Automation Flats			
Vertical	MAADC and ADC	100%	70%
Vertical	ADC and 3-Digit	100%	81%
Vertical	3-Digit and 5-Digit	100%	49%
Nonmachinable Parcels			
Vertical	MAADC and ADC	25%	17%
Vertical	ADC and 3-Digit	30%	17%
Vertical	3-Digit and 5-Digit	30%	87%
Machinable Parcels			
Vertical	MBMC and BMC	100%	61%
Vertical	BMC and 5-Digit	100%	58%
NFM			
Vertical	MADC and ADC	30%	19%
Vertical	ADC and 3-Digit	30%	19%
Vertical	3-Digit and 5-Digit	30%	86%

the basic flat rate. The Commission uses a passthrough of 100 percent for all shape, presort, and dropship cost differentials, with the following exception. To mitigate rate increases and avoid rate shock the Commission uses a 50 percent passthrough for the flat/parcel differentials. The Commission recommends a pound rate of \$0.621; and a DAL surcharge of \$0.015.

D. Periodicals

1. Introduction and Summary

a. Overview

[5601] *Distinguishing features.* The Periodicals class is typically used by publishers of newspapers, magazines, journals and newsletters. Periodicals mailers must obtain an annual permit and meet several eligibility criteria, including a requirement that the publication contain a minimum amount of editorial content. USPS-T-7 at 211 (Thress). It is the presence of editorial content which gives rise to preferential rate and service treatment for mail in the Periodicals class.

[5602] Periodicals is comprised of two subclasses: Outside County and Within County. The Outside County subclass consists of three categories for ratemaking purposes: Regular (including Science of Agriculture publications), Nonprofit, and Classroom. Science of Agriculture publications, by statute, receive preferential rate treatment for the advertising portion of their Zones 1 and 2 mailings. Publishers of Nonprofit and Classroom Periodicals mail receive a 5 percent discount from Regular rate postage, except for advertising pounds.

[5603] Eligibility for the Within County subclass is limited to publishers who meet the general requirements for Periodicals and either of two conditions: the total paid circulation of the issue of the Periodicals publication is less than 10,000 copies or the number of paid copies of such issue distributed within the county of publication is more than 50 percent of the total paid circulation of such issue. DMM 707.11.3. Copies of Within County publications sent beyond the county line generally must be mailed at Outside County rates.

[5604] *Important considerations.* Several considerations influence Periodicals rate and classification decisions. These include the extremely low cost coverage for this class in recent dockets; the clear dominance, in terms of volume, of the Regular rate

category in the Outside County, and a profile which shows that most of the permit holders in the Outside County subclass generate a relatively small percentage of the volume. Most mailpieces in this class are considered flats (also “nonletters” for some purposes), but there are some letters as well (such as bulletins and newsletters) and some pieces identified as parcels.

b. Summary of the Postal Service’s Proposal for the Periodicals Class

[5605] *Outside County.* The Service proposes cost coverage of 106.4 percent for Outside County Periodicals, which corresponds to an average rate increase of 11.7 percent. USPS-T-35 at 2. Both percentages are calculated after applying the 5 percent discount (from Regular rates), except for advertising pounds, for Nonprofit and Classroom mailings. USPS-T-31 at 24. The proposed Outside County increase is based on the Service’s cost attribution methods, mail processing cost model, and cost coverage. It assumes adoption of the Service’s proposed structural reforms.

[5606] *Within County.* The Service’s cost coverage for the Within County subclass is 103.6 percent. USPS-T-35 at 2 (Tang). This is calculated before the 5 percent Nonprofit and Classroom discount is applied, using half of the “approximately” 107 percent coverage for Regular. This corresponds to an average 24.2 percent increase. *Id.* O’Hara acknowledges that this is “quite high,” but asserts that the mark-up formula leaves no room for mitigation. He notes, however, that in Docket No. R2005-1 the same mark-up formula resulted in a rate *decrease* of 2.3 percent for Within County Periodicals, and a rate increase of 5.4 percent for other mailers. USPS-T-31 at 26. The Service does not propose any structural changes for the Within County subclass. USPS-T-35 at 14.

c. Summary of Commission Recommendations

[5607] *Outside County.* The record on Outside County reveals virtually unanimous support for structural reform; unchallenged cost studies showing that bundles, sacks and

pallets impose costs on the system, independent of those associated with pieces and pounds; the expectation that many lightly-filled sacks will have been eliminated by the test year, given a recent rule change; and more potential for co-mailing and co-palletizing. The Commission recommends adoption of the framework underlying the Time Warner Inc. (Time Warner) proposal in this case and its related costing support, but with significant moderation of passthroughs.

[5608] The proposal in this case differs in significant respects from the proposal Time Warner sponsored, along with others, in Docket No. C2004-1. These differences, especially the elimination of a fully-zoned editorial pound rate, result in substantial moderation of the rate impacts associated with the previous proposal. The Commission recommendation further moderates the Time Warner proposal in this case. Time Warner, while maintaining full support for its proposal as filed, acknowledges that the Commission might find some moderation (or tempering) in order. U.S. News & World Report, Inc. affirmatively suggests that the Commission pursue that approach. U.S. News Brief at 13.

[5609] *Within County*. The record on Within County has been dominated by the sheer size of the Service's proposed 24.2 percent increase, driven largely by much higher reported attributable costs and lower reported volumes. This higher-than-average increase follows a case in which the Service reported *lower* costs for this subclass, and a rate *decrease*. Concern over delivery service, often directed mostly at copies sent to distant subscribers, extends in this case to the service accorded copies sent to subscribers in adjoining or nearby counties. Disagreement over how a statutory markup formula should be interpreted, which surfaced in the last case, is also an issue.

[5610] The record shows that the Postal Service and the National Newspaper Association (NNA) expended considerable effort, prior to the filing of this case, to address the cost and volume reporting issues that plague this small subclass. Regrettably, no fully satisfactory solution appears to be in the offing, as this case reveals continuing instability.

[5611] The Commission concludes, based on careful review of the record, that an imperfect solution is still the best solution in this case. It therefore accepts NNA's proposed four-year volume averaging technique, which is an approach the Commission used in Docket Nos. R97-1 and R2000-1. It does not recommend adoption of NNA witness Siwek's cost pooling technique, nor does it accept the alternative rate schedule he proposes. Use of the volume averaging technique, with Commission costing methods, results in an average rate increase of 18.3 percent with a cost coverage of 100.1 for the Within County subclass.

[5612] NNA's concerns about the Service's container charge are addressed in the Commission's extended discussion of Outside County issues.

2. The Outside County Subclass

a. Background

[5613] The record on Outside County Periodicals in this case has been dominated by a debate over structural reform. The discussion has been marked by the notable absence of support for the rate structure in its existing state and the emergence of three proposals for alternative structures. Suggestions for variations on these proposals also have been offered.

[5614] The proponents of the three main alternatives are the Postal Service, Time Warner and, acting jointly, the Magazine Publishers of America and the Alliance of Nonprofit Mailers (MPA-ANM). Their proposals differ in direction and degree, but reflect agreement that a more cost-based structure is needed. Other participants voicing opinions on substantive aspects of structural reform concur.

[5615] This consensus is the welcome result of the close scrutiny the Outside County Periodicals structure received in the recent Complaint of Time Warner Inc., et al. and in the ensuing Commission Order. Docket No. C2004-1, Order No. 1446. Indeed, each proponent characterizes its proposal as a response to the Commission's call for

measured, but meaningful reform. Other participants addressing the proposals also do so in that context. At the same time, the Commission is pleased that participants have not restricted discussion to the state of Periodicals as of the issuance of Order No. 1446 in October 2005, but have evaluated developments since then and offered considered assessments of the future.

[5616] *Main focus of the proposals.* The proposals address two separate but related reform issues. One is the continued viability of the fundamental structure. This is a core distinction between the general path suggested by the Postal Service and Time Warner, on the one hand, and MPA-ANM on the other. The Service and Time Warner seek to achieve the objectives of reform, in the first instance, by expanding the existing structure — in different ways — to include explicit recognition of certain new cost drivers. MPA-ANM contend that the same objectives can be met, at least on an interim basis, by unleashing the full potential of pallet discounts without expanding the basic structure.

[5617] The other reform issue is whether standing criticisms of the structure (which were raised in the Complaint, but predate it) have sufficient merit to warrant revisions along the lines proponents suggest. This is the heart of the debate over other features in the proposals, such as adding a set of discounts for destination entry of editorial pounds (dropshipping) and a surcharge for nonmachinable pieces.

[5618] Methodology concerns are subsumed within both issues.

b. Context of the Proposals

[5619] *Affected mailers.* The proposals at issue pertain exclusively to the Outside County subclass structure; neither the Service nor any other participant proposes any structural changes for the Within County subclass. However, copies of Within County publications mailed to subscribers outside the county of publication usually travel at Outside County rates. In addition, proponents address the rate for Ride-Along advertising pieces, and these pieces may be included in both Outside County and Within

County mailings. Thus, the proposed changes affect Within County mailers in these two respects.

[5620] *Existing structure.* The existing structure, which the proponents use as a frame of reference for their proposals, is often referred to as a piece-pound structure. This generally means that the main “building blocks” of postage rates are the number of pieces in a mailing and its total weight. This structure was established in 1971 as a result of favorable action on the Postal Service’s proposal, in the first rate case following passage of the Postal Reorganization Act of 1970, to move away from relying primarily on weight.²²⁶ Adoption of the structure included retention of a pre-existing zone system for computing postage. This system is comprised of eight numbered zones and a local zone.

[5621] Pieces and pounds have been the two basic rate elements ever since, but several discounts have been added.²²⁷ One discount, applied on a piece basis, recognizes the amount of editorial content in a publication (on a percentage basis, relative to advertising content). This is sometimes referred to as the “editorial benefit” in the Periodicals structure. The other discounts, considered worksharing in nature, recognize presorting, barcoding, presenting presorted mail on pallets, and co-palletizing.

[5622] The most recent significant attempt at fundamental structural reform, apart from the Periodicals Complaint in 2004 and the instant docket, was a proposal the Postal Service presented as part of the Docket No. MC95-1 omnibus reclassification case. That effort became mired in criticisms that it unduly favored large Periodicals mailers, and no substantive changes were recommended or implemented. However, the Service

²²⁶ There was a minimum-per-piece component at the time, but this operated primarily as a stop-loss mechanism for extremely lightweight pieces.

²²⁷ Outside County pound rates, which are based on the weight of the pieces in the mailing, have two components. One component is based on the weight of the advertising portion of the mail sent to each postal zone (the zoned advertising pound charge). The other component is based on the weight of the editorial (nonadvertising) portion *without* regard to zone (the “flat” editorial pound charge). Piece charges apply to each addressed piece in the mailing based on the level of sortation. See DMM 707.2.1.2—2.2.7.

indicated at the time that it intended to pursue structural improvements for Periodicals in a Headquarters project referred to as Product Redesign.

[5623] *Developments influencing proponents' submission of proposals for alternative structures.* Commission Order No. 1446, which forms the backdrop for the instant proposals, was issued at the conclusion of a Complaint case highlighting the relationship of Periodicals costs and rates. Complainants²²⁸ pointed, among other things, to

- a pattern of seemingly disproportionate cost increases, despite more mailer worksharing and greater attention to cost control;
- widespread use of lightly-filled mail sacks (“skin sacks”), sometimes on the assumption that this would foster better service; and
- a sense that the Service’s long-anticipated Product Redesign for Periodicals was languishing.

[5624] Complainants asserted that at least some of the problems Periodicals mailers were facing could be traced to an outmoded and inefficient piece-pound structure. They attributed the state of the structure to extensive changes over the years in postal operations, mailers’ practices, printers’ capabilities and to continued reliance on what they had come to view as overly-simplistic views of cost causation.

[5625] They contended that new studies and insights showed that the bundles in which most Periodicals pieces are presented (generally secured by ties, string or strapping); the containers in which these bundles are placed (usually a sack *or* a pallet), and the related presort level and point of entry into the postal system (“key linkages”) have emerged as important cost drivers in today’s mailing environment.²²⁹ They also noted that these costs were influenced by the number and weight of pieces in a bundle; how well the bundle is tied or otherwise secured (“bundle integrity”); the presort level

²²⁸ Time Warner Inc.; Condè Nast Publications, a Division of Advance Magazine Publishers Inc.; Newsweek, Inc.; The Reader’s Digest Association, Inc.; and TV Guide Magazine Group, Inc.

²²⁹ Sack and pallet usage is determined, in large part, by postal regulations imposing a maximum weight limit of 70 pounds for sacks, and a minimum weight limit for pallets. Pallet usage is generally optional at 250 pounds and mandatory at 500 pounds. Some exceptions are allowed.

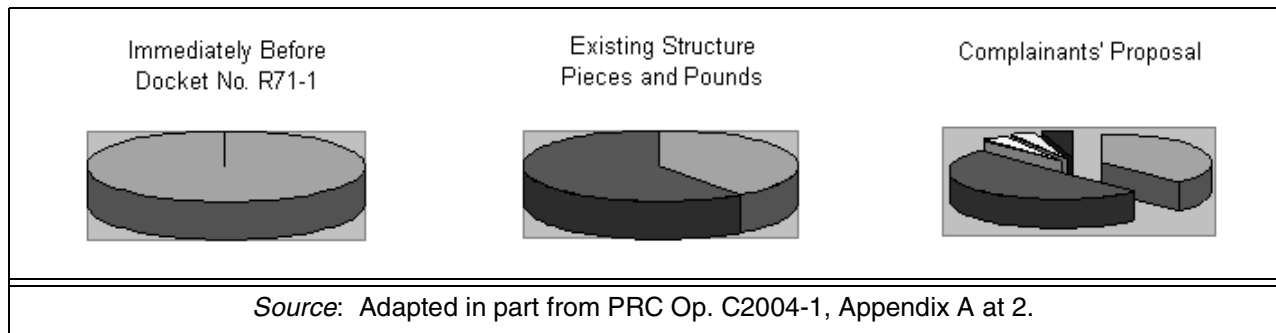
(“makeup”) of the bundle; the number of bundles placed in a sack or on a pallet; and the treatment accorded bundles once they are in the postal system, such as manual or automated processing. They claimed that their analysis showed, for example, that bundles presented in sacks are more likely to break than bundles on a pallet and that lightly-filled skin sacks (six or fewer pieces) are costly for the Service to handle, but that the rate structure does not reflect these considerations.

[5626] Complainants asserted, in essence, that although bundles and containers are inextricably related to the pounds and number of pieces in a mailing, they are also *independent* of those elements in an important cost sense. They further demonstrated that the costs associated with bundles and containers are not really “new” costs; instead, they are costs that have been present as long as bundles, sacks, and pallets have been used for Periodicals mail, but have been masked because pieces and pounds serve as proxies for all costs. They contended that this hidden quality impedes mailers’ ability to make informed decisions about mail preparation. They also claimed that if these costs were recognized in a more straightforward way in the rate structure, many mailers would respond to these more appropriate signals, bring down costs, and thereby improve the situation not only for themselves, but for *all* Periodicals mailers.

[5627] The Complainants proposed adoption of a structure which retained pieces and pounds as basic — and still quite important — elements, but minimized their role by adding bundles, sacks, and pallets as basic structural elements. This effectively “de-averaged” the traditional piece and pound elements. They proposed linking each container type to familiar worksharing-related components: presort level and point of entry. This eliminated pallet discounts as discrete elements in the structure, but continued to recognize pallet usage through direct linkage of containers to their entry point. They also proposed “zoning” the editorial pound charge in full and imposing distinctions between machinable and nonmachinable pieces. These changes addressed criticisms that the flat editorial pound charge hinders dropshipping and that the rates Periodicals mailers pay do not recognize the costs that nonmachinable pieces impose on the system.

[5628] The following table presents a graphic depiction of the major elements in several types of basic Periodicals structures. The left chart shows that weight (pounds) bore responsibility for revenue generation immediately before Docket No. R71-1. The middle chart reflects revenue-generating responsibility under the existing structure, apportioned 60 percent to pieces and 40 percent to pounds. This is close to where the division has hovered in recent years. The chart on the right shows that the Complainants' approach shifts some of the responsibility away from pieces and pounds and onto bundles, sacks, and pallets. Under the Complainants' costing approach, pieces contribute 49.2 percent, pounds contribute 30 percent, and sacks, pallets and bundles, on a combined basis, contribute 20.8 percent. Docket No. C2004-1, Tr. 1/54-56.

Table V-5



[5629] *Order No. 1446.* In its final Order addressing the Complaint, the Commission found considerable merit in Complainants' theories and analyses. However, it did not recommend adoption of their proposed rate structure, given several concerns. One was the impact on mailers, especially those with small- and medium-size circulation that might not be able to make more efficient use of sacks, to "move out of sacks" onto pallets on their own, or to take advantage of co-mailing and co-palletizing. Another concern was that some of these mailers might be among those that could be harmed by full zoning of the editorial pound rate. A more general, subclass-wide

concern, was that sack usage was extensive, given mailers' practices at the time, meaning that imposition of a new charge would necessarily have a large impact.

[5630] At the same time, the Commission indicated that the Complainants had demonstrated that the existing structure had many significant inefficiencies, and concluded that progress toward a more cost-based rate structure was both "possible and necessary." Order No. 1446 at 6.

[5631] The Commission urged the Postal Service to update cost studies; to implement cost control measures, such as new sacking regulations minimizing the use of skin sacks; and to pursue structural improvements that could form the basis of a prompt filing. The Commission also urged the Service to caution mailers that machinability was likely to be recognized in any future rate structure. In short, the charge was to develop a structure which encourages more efficient mailing practices without unduly harming mailers, especially those not well-situated to engage in impact-mitigating techniques, such as co-mailing, co-palletizing and dropshipping, and without unduly interfering with policy-based interests, such as maintaining a flat editorial pound charge.

c. Key Features of the Postal Service's Proposal

[5632] *Structural elements.* Witness Tang presents the Service's proposed alternative to the existing rate structure. The revised structure retains pieces and pounds as basic elements, but adds

- containers (collectively) as a third element, at a flat charge of 85¢ per container, and
- a set of editorial pound dropship rates for mailings entered at destination area distribution centers, destination sectional center facilities and destination delivery units.²³⁰

USPS-T-35 at 4, 7.

²³⁰ Subsequent references use the following abbreviations for these facilities: ADCs, DDUUs and SCFs.

[5633] The proposed container charge is the keystone in a package of changes the Service presents as part of its effort to improve the Periodicals rate structure. Tang believes uniform application of this charge across all types of containers, in conjunction with certain other proposed changes, will foster more efficient mailing practices, despite known differences in the costs of handling sacks and pallets.

[5634] Development of the charge reflects Tang's assumption that there will be a 65 percent reduction in small (lightly filled) sacks in the test year due to a May 2006 rule change requiring a minimum of 24 pieces per sack. Tr. 7/1616.

[5635] The record indicates that the Service anticipates applying the container charge to all Outside County mailings, not solely to those entered in sacks or on pallets. Ostensibly, mailings the Service permits to be presented in "flats" tubs and mailings it permits to be presented without being containerized will be subject to the charge.²³¹ *Id.* at 1615-18 (Response of United States Postal Service to Presiding Officer's Ruling No. 30). The stated rationale is that the container charge is "an integral part" of the Service's proposal. Tang also notes that the revenue associated with the charge helps hold down all Outside County Periodicals rates. *Id.* at 1648-49, 1656, 1664. She estimates this revenue at about \$43.3 million (or 1.75 percent of subclass revenue) on test year container volume of nearly 50.97 million sacks. USPS-T-35 at 5.

[5636] The new editorial pound discounts are another important part of the Service's package of changes because of the expectation that they will boost dropshipping. However, extension of these discounts to Periodicals mail dropshipped to local facilities necessarily curtails the traditional reach of the flat editorial pound across all zones and offices. This poses a potential policy conflict, as the Commission holds the view that the flat or "unzoned" nature of the editorial policy rate encourages wide dissemination of editorial material. At the same time, curtailment is limited because Tang proposes retaining a flat editorial pound rate for Outside County Mail in Zones 1 &

²³¹ Postal Service regulations appear to modify the original intent in certain limited respects, especially in connection with mailings containing mixed classes of mail. See 71 FR 56588 (September 27, 2006) and 72 FR 2090 (January 17, 2007).

2 through 8 (except for Science of Agriculture publications).²³² *Id.* at 7 and 9. The flat editorial pound rate increases by 14.3 percent under her proposal.

[5637] Tang offers the proposed change as a balanced approach which recognizes both the importance of encouraging dissemination of editorial content throughout the country and the importance of allowing editorial content to share in the efficiency associated with deposit of mail closer to the point of delivery. *Id.* at 8. She notes that the Commission observed, in Order No. 1446, that witness Taufique's similar proposal in Docket No. R2001-1 was "something between" the current flat editorial rate and full zoning. *Id.* at 7-8, citing Order No. 1446 at 42.

[5638] The proposed structure also

- retains, and increases, the editorial piece discount from 7.8 cents per piece to 8.9 cents per piece (applied to the percentage of editorial content);
- retains, and increases, another set of discounts for *pieces* dropshipped to destinating facilities ADCs, SCFs and DDU's; and
- eliminates all existing pallet discounts.

[5639] Tang justifies the elimination of the pallet discounts on grounds that the container charge, the new editorial dropship discounts and the increased dropship piece discounts, in combination, offer mailers a compensatory package of incentives. She asserts that this package will result in similar, or better, rates for many mailers. She also says that it addresses technical criticisms directed at the pallet discount design (per-piece application of pound-oriented savings). *Id.* at 7, 9, 11-12.

[5640] Finally, the Service's proposed structure

- maintains existing presort tiers on the piece side;
- continues to recognize automation, but does not add a surcharge for nonmachinable pieces; and

²³² Tang says that the flat editorial pound rate for Science of Agriculture would apply to Zones 3 through 8. *Id.* at 7.

- retains, and increases (from 13.1¢ to 15.5¢), the Ride-Along rate, which applies to certain Standard Mail (advertising pieces) attached to or enclosed in a Periodicals mailpiece.

Id. at 9-17.

[5641] The 5-digit automation flat and carrier route basic discounts are maintained at their current levels, with passthroughs increased to 800 percent and 148 percent, respectively. Tang says this approach reflects the Service's belief that sortation to these levels will continue to have value in the future mail processing and delivery environments. She asserts that "providing significant incentives also serves the purpose of mitigating the rate increase and retaining the hard-won presortation and barcoding by mailers." *Id.* at 12.

[5642] Tang develops the Ride-Along rate, which reflects an 18.32 percent increase, based on the methodology the Service used when this rate was proposed. However, Tang uses the volume forecast for the overall Periodicals class in lieu of a separate forecast for these pieces. *Id.* at 12-14.

[5643] *Consistency with Order No. 1446.* Witnesses Tang characterizes the proposed container charge as a response to Order No. 1446's interest in progress toward a more cost-based rate structure. She maintains that this rate will send an appropriate price signal to encourage better mail preparation, benefiting the entire Periodicals community. She also says that more efficient mail preparation, together with more worksharing, will contain Periodicals processing costs and keep rapid rate increases at bay. She associates the new editorial dropship discounts with these objectives as well. *Id.* at 4-5, 9.

[5644] Witness Taufique associates the Service's proposal with Order No. 1446's identification of a gradual approach to structural reform. He describes several Postal Service efforts in recent years to introduce beneficial changes, and says the Service's proposal in this case as a logical continuation of the philosophy of moving consistently and gradually in the direction of lower-cost preparation, especially by providing incentives for reducing the number of containers and for destination entry. USPS-RT-12

at 1-2. He asserts that witness Tang chose to continue with the “balanced approach” the Service has been pursuing. *Id.* at 3. However, he further states:

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

Id. at 3-4.

[5645] Taufique says the Service believes the proposed container rate sends “a consistent and clear signal” to the Periodicals community and continues to provide adequate incentives to encourage more mail preparation and worksharing. *Id.* at 4.

[5646] *Related matters.* Witness Tang relies on several other Postal Service witnesses and Postal Service documents for support.²³³ Postal Service witness O’Hara addresses the consistency of the proposed rates with the statutory criteria in 39 U.S.C. § 3622. USPS-T-31 at 24-26. Witness Tang addresses the proposed changes in terms of the statutory classification in 39 U.S.C. § 3623(c), and finds them consistent. USPS-T-35 at 16-17.

[5647] The piece/pound split under Tang’s proposal results in pieces generating approximately 63 percent of the required revenue and pounds generating the remaining approximately 37 percent. (Container revenue is added to the piece revenues.) Tang asserts that this split better reflects actual cost incurrence. *Id.* at 6-7.

[5648] Tang provides a detailed description of the development of her proposed rates in her prepared testimony, responses to interrogatories, and responses during cross-examination. This indicates that in many instances, she follows conventional

²³³ Tang relies on witness Thress (USPS-T-7) and on USPS-LR-L-66 for test year before rates volumes; on witness Waterbury (USPS-T-10) for roll forward costs; on witness Miller (USPS-T-20) for flats mail processing costs; on witness Mayes (USPS-T-25) for Periodicals dropshipping costs; on witness Talmo (USPS-T-27) for mail processing costs; and on witness Loetscher (USPS-T-28) for the Periodicals Mail Characteristics Study (USPS-LR-L-91). *Id.*

Periodicals rate design practices; in others, she makes adjustments to further certain objectives that are part of the Service's proposed approach to structural reform, such as encouraging more dropshipping, while mitigating impact on mailers that can not dropship. One example is the development of the flat editorial pound rate; another is the development of Science of Agriculture rates. *Id.* at 7-9.

[5649] *Service's assessment of rate impact.* The Service's proposed cost coverage for the Outside County subclass is 106.4 percent (after removing revenue for the preferred discounts). Tang characterizes this coverage as moderate. The proposed increase for the Outside County subclass is 11.7 percent, slightly below the proposed coverage of 11.9 percent for the Periodicals class as a whole. *Id.* at 2.

[5650] Witness Taufique suggests that in addition to considering impact in terms of the average percentage rate increase and in terms of impact on publications in the updated database, the Service's proposal (and the two others) should be evaluated in terms of what he considers a "key statistic" — standard deviation from the mean. USPS-RT-12 at 5. In support of this approach, he presents a table showing mean rate increases among the sampled publications of 13.20 percent for the Postal Service's proposal, 15.87 for the Time Warner proposal, and 13.43 for the MPA-ANM proposal. He notes that the Service's proposal has the lowest standard deviation overall (for "All Mailers"). He says this reflects the Service's effort to limit the impact of its proposal on various mailers to as narrow a range as possible. *Id.*

[5651] *Summary of other participants' positions.* American Business Media (ABM), Dow Jones & Company (Dow Jones), and The McGraw-Hill Companies, Inc. (McGraw-Hill) support the Service's proposal, but each qualifies its support in certain (mostly limited) respects. ABM suggests that the Commission recommend the Service's proposal or a hybrid version incorporating the MPA-ANM proposal, "tweaked to preclude excessive increases." ABM Brief at 26. Dow Jones states that the Service's proposed rate structure would be an improvement over the existing structure and asserts, without elaboration, that it avoids some of the problems identified by other parties with the existing rate structure. Dow Jones Reply Brief at 1. It opposes application of the

container charge to mail that is not put into containers or that need not be put into containers. *Id.* at 1-2.

[5652] McGraw-Hill qualifies its support of the Service's proposal in two respects. One relates to Tang's development of the flat editorial pound rate; the other to the application of the container charge. McGraw-Hill does not oppose the proposed editorial pound dropship discounts, but objects to the level of the flat editorial rate. It asks that the Commission reduce it to (or close to) 75 percent of the level of the Zone 1 & 2 pound charge, which would reflect its traditional level. McGraw-Hill Brief at 14-17. McGraw-Hill opposes application of the container charge to very small volumes of Periodicals mail. It suggests, among other things, that the Commission include in the Domestic Mail Classification Schedule a provision foreclosing the Service from applying this charge to small volumes of uncontainerized Periodicals mailings. *Id.* at 15-16.

[5653] The National Newspaper Association (NNA) and the Newspaper Association of America (NAA) address only the Service's proposed application of the container rate to certain mailings presented in flats tubs and to certain uncontainerized mailings. They oppose this aspect of the Service's proposal. NNA Brief at 22-25, NAA Brief at 47-48.

[5654] MPA-ANM, Time Warner and U.S. News oppose the Service's proposal. Both MPA-ANM and Time Warner sponsor alternative proposals and address the Service's proposal on brief. U.S. News witness White testifies that the Postal Service proposal would cause increases ranging from 14.6 to 19.2 percent for *U.S. News and World Report*, a publication that already uses efficient mailing practices. U.S. News also addresses the Service's proposal on brief.

d. Key Features of the MPA-ANM Proposal

[5655] *Structural elements.* Witnesses Cohen (MPA/ANM-T-1) and Glick (MPA/ANM-T-2) present the policy and cost support for MPA-ANM's joint proposal. Glick's assumptions and analyses pose alternatives to several key aspects of the costing analysis underlying the Service's proposed rate structure. These include, among others,

certain benchmarks and certain changes to the Service's mail flow cost model. This affects certain features of MPA-ANM's proposed rate structure and related rates and discounts. MPA/ANM-T-2 at 14, 16, 30.

[5656] MPA-ANM's proposed structure, in terms of basic elements, continues to rely exclusively on pieces and pounds. And, in contrast to the Service's proposed elimination of the pallet discounts, it incorporates a set of expanded and enhanced pallet discounts. This includes a per-piece pallet discount of 2.7 cents (which Glick describes as deeper than the Service's container charge) and a per-piece 5-digit pallet discount of 1.5 cents. *Id.* at 5, 24-29. These discounts (based on Glick's alternative benchmark) assertedly provide stronger worksharing incentives and reflect better alignment with avoided costs. *Id.* at 30. However, MPA-ANM proposes that the pallet discounts continue to be applied on a per-piece basis. Tr. 30/10306.

[5657] The MPA-ANM structure includes the new set of pallet discounts, instead of a container charge, but otherwise generally mirrors all other elements in the Service's structure, although rates and discounts differ. For example, the MPA-ANM structure, like the Service's, introduces a set of editorial pound dropship ("destination entry") discounts. MPA/ANM-T-2 at 4. This modifies the existing editorial pound rate element in the same (limited) way as the Service's proposal, and therefore poses the same potential for a policy conflict. However, MPA-ANM's proposed discounts are larger than those proposed by the Service, in line with its interest in stronger incentives for worksharing. *Id.* Use of Glick's alternative benchmark also has the effect of increasing these discounts, relative to the Service's approach. *Id.* at 32.

[5658] The MPA-ANM structure, like the Service's, also retains a discount for editorial content, but changes the conventional approach. Ordinarily, the entire discount operates as a reduction solely from the piece rate (thus, the traditional reference to the "per piece editorial discount"). Glick proposes maintaining the aggregate amount of discount the Service has proposed, but shifts some of it from the piece side to the pound side. This provides a smaller per-piece editorial discount, relative to the Postal Service's

(8.6 versus 8.9 cents), but allows the increase in the flat editorial pound rate to be limited. *Id.* at 34-35.

[5659] In support of his approach, Glick observes that limiting the increase in the flat editorial pound rate is a consideration because introduction of the new editorial dropship discounts means that this element, as a matter of arithmetic, is subject to a “push up effect.” He notes that Postal Service witness Tang addressed this concern by adjusting (reducing) the flat editorial pound rate in the Service’s proposal by 1.3 cents. *Id.* at 34, citing USPS-T-35 at 9. He addresses the impact, which is somewhat greater because of the larger proposed discounts MPA-ANM proposes, by making a similar, but somewhat, larger adjustment of 2 cents. *Id.* This reflects a difference of 0.3 cent between his editorial pound rate adjustment and Tang’s. *See* Tr. 30/10253.

[5660] In terms of presort and automation piece rates, MPA-ANM’s interest in limiting impact on very small non-local mailers that can not co-mail or co-palletize includes a proposed reduction in the 3-digit presort discount, relative to that proposed by the Service. MPA/ANM-T-2 at 12. (Glick’s proposed reduction is 1.5 cents). The MPA-ANM proposal forgoes introducing a nonmachinability surcharge; however, it retains — but reduces — automation discounts by 0.5 cents per piece. *Id.*

[5661] The reduction in the automation discounts allows the differential between automation rates and the carrier route rate to be expanded, and Cohen considers this differential as critical to encouraging more co-mailing. MPA/ANM-T-1 at 19. It also lowers the very large (greater-than-100 percent passthroughs) that underlie the existing discounts. MPA/ANM-T-2 at 13.

[5662] Glick indicates that exclusion of a rate distinction between machinable and nonmachinable pieces reflects his acceptance of many aspects of the Postal Service’s proposal. Due to time and resource constraints, he limited his review to containerization, dropshipping and commingling. Tr. 30/10310. Cohen acknowledges a cost difference between machinable and nonmachinable pieces, but suggests that it might be advisable to postpone the introduction of such distinction until there is an opportunity to consider

machinability standards developed in connection with deployment of the Flats Sequencing System (FSS). *Id.* at 10175-76.

[5663] The MPA-ANM proposal includes a Ride-Along rate of 14.6 cents, which is higher than the existing 13.1 cent rate, but lower than the Service's proposed 15.5 cents. MPA/ANM-T-2 at 35.

[5664] *Consistency with Order 1446*. Cohen asserts that the Joint Proposal is a response to concern the Commission expressed in Order No. 1446 about mitigating the impact of structural changes on small mailers. MPA/ANM-T-1 at 6. She makes clear that the proposed pallet discounts reflect MPA-ANM's considered assessment that the goal the Service's container charge seeks to achieve — more efficient containerization, especially more pallet usage — can be achieved more effectively, on an interim basis, by creating stronger incentives for publishers to engage in dropshipping, palletizing and presorting, while avoiding very large rate increases for small publications. *Id.* at 6.

[5665] At the same time, Cohen emphasizes that MPA-ANM's decision not to support the Service's proposed container charge "by no means signifies a belief that containers are unimportant as a cost-causing element of Periodicals Mail." Instead, she says container handling "is a significant component of periodicals processing and needs to be appropriately reflected in cost-based rates." On behalf of MPA-ANM, she urges the Service to propose in the next case a more sophisticated and economically efficient set of container charges, "in a manner that properly reflects the cost differences between container types, and to consider the effect of presort and entry point on those costs." *Id.* at 23-24.

[5666] *Related matters*. Cohen asserts that the MPA-ANM proposal generates virtually the same cost coverage (106.3 percent versus 106.4 percent) and total revenue (\$2.392 billion versus \$2.394 billion) as the Service's proposal. *Id.* at 21. The MPA-ANM testimonies provide the proposed rate schedule and a comparison of their proposed rates to the Service's. *Id.* at 5 (Table 1), MPA/ANM-T-2 at 8 (Table 1). Glick's supporting analyses are provided in several library references. *See, for example*, MPA/ANM-LR-1, and MPA/ANM-LR-6 (Glick's version of the Service's Outside County

Periodicals rate design spreadsheet) and MPA/ANM-LR-2 (revised version of the Service's flats presort cost avoidance model).

[5667] Development of the MPA-ANM proposed rate schedule reflects correction of certain errors in the Service's filing. MPA/ANM-T-2 at 4-5.

[5668] *MPA/ANM's impact assessment.* Both Cohen and Glick assert that the MPA-ANM proposal avoids very large rate increases for small publications, even if they do not respond to the rate changes by engaging in more co-mailing and co-palletizing. MPA-T-1 at 20; MPA-T-2 at 3. Glick also contends that the proposal avoids the anomalous results associated with the Service's, where increases for commingled titles of publications would be similar to, or higher than, the increases without commingling and dropshipping. *Id.* at 9. Glick also asserts that the MPA-ANM proposal results in rates that are dramatically less than the increases the Commission was concerned about in the Complaint case. *Id.* at 10. He maintains that the proposal would produce an average rate increase approximately 5 percent above the subclass average for the sample of small publications in the Complaint case database, and that none of these publications would receive increases of more than 10.5 percent above the average. *Id.* at 11, citing Table 4.

[5669] *Summary of other participants' positions.* Apart from the Postal Service and Time Warner, two participants address the MPA proposal on the merits: ABM and McGraw-Hill. ABM cites two main reasons for opposing MPA-ANM's proposal. One is the evidence presented by ABM witnesses Cavnar and McGarvy, indicating that notwithstanding the emergence of more co-mailing and co-palletizing opportunities, many mailers will still not be able to take advantage of the increased incentives in the MPA-ANM proposal. ABM Brief at 6. The other is the contention, by witness Bradfield, that the impact of the MPA/ANM proposal is greater, in certain respects, than that of the Postal Service's. *Id.* at 8. Notwithstanding these arguments, ABM suggests — without further elaboration — that the Commission might consider a hybrid version of the Postal Service's proposal and the MPA-ANM proposal. *Id.* at 26.

[5670] McGraw-Hill characterizes the MPA-ANM proposal as a “status quo” approach. McGraw-Hill Brief at 3. One reason for its opposition is the rate impact of the MPA-ANM proposal, which it contends is more severe on certain mailers than the Service’s. Another reason is the proposal to split the editorial discount between the piece and pound rates. *Id.* at 5.

[5671] NNA does not address the overall merits of the MPA-ANM proposal, but urges the Commission’s consideration of a 5-digit pallet discount on grounds that for some larger newspapers, an incentive to create 5-digit pallets would provide additional reason to abandon sacks. NNA Reply Brief at 11.

e. Key Features of the Time Warner Proposal

[5672] *Structural elements.* Witnesses Mitchell (TW-T-1) and Stralberg (TW-T-2) present the policy and cost support for Time Warner’s proposed structure. Stralberg’s cost model is a comprehensive alternative to the Service’s model.²³⁴ The proposed Time Warner structure

- continues to rely on pieces and pounds as basic elements;
- introduces bundles, sacks and pallets as new elements and links them to presort level and point of entry;
- introduces a distinction between machinable and nonmachinable pieces; and
- de-averages the Basic Rate piece category into ADC and Mixed ADC categories and retains other recognition for presorting and pre-bardoding.

TW-T-1 at 11-12.

[5673] The new structural elements are applied as separate charges, on essentially the same basis as pieces and pounds in the existing rate structure. This is consistent with Time Warner’s theory that bundles, sacks and pallets are separate,

²³⁴ Stralberg’s alternative includes many aspects of the Service’s model, but certain key assumptions, such as automation coverage factors, differ. TW-T-2 at 35-36.

recently-recognized cost drivers. This differs sharply from Tang's proposal, which combines sacks and pallets into one "blended" container rate element and provides no separate recognition for bundles.

[5674] Mitchell proposes reflecting 60 percent of the costs of the new elements in the associated charges. *Id.* at 23. He expects the resulting incentives to be muted, but still adequate, at this level. He suggests passthroughs could be increased as mailers adjust their container practices and points to consistency of lower passthroughs with the "partial recognition" approach the Commission referred to in Order No. 1446. Mitchell averages container costs associated with entry at origin SCFs, ADCs and BMCs over three categories. This treatment evidences itself in his rate schedule, where all three entry points have the same rate. The rationale for this approach is that mailers using an origin SCF may tend to be small mailers or may not be well-positioned to shift to a higher-level (closer-to-destination) facility. Mitchell believes, however, that separate rates should be considered in the future. *Id.*

[5675] Mitchell's approach to piece handling costs is different. He states: "They are recognized fully for machinable and nonmachinable pieces, and for their automation variants, including de-averaging the basic category into mixed ADC and ADC categories, as has been done in other subclasses." *Id.* at 24. Mitchell supports full recognition on grounds that the costs and cost differences of machinable flats and automation flats have been recognized for some time, and that reducing this recognition would be a step backward and unfair to mailers who have invested in equipment and software to achieve various degrees of presortation. He also says "[t]he time has come to recognize the additional costs of being non-machinable." In support of this position, he asserts that many mailers have already made adjustments to achieve machinable status and many others have opportunities to do so. He believes appropriate signals should be sent. Mitchell also notes that many mailers have been investing in co-mailing opportunities, which he characterizes as "inherently efficient," and claims that it would be wrong to reduce the associated recognition in rates. *Id.*

[5676] Mitchell also proposes a separate rate for firm bundles, which he notes require individual handling. He asserts that since these types of bundles pay only one charge for multiple copies, they should be well-positioned to accommodate a charge that recognizes the costs caused. *Id.*

[5677] The proposed Time Warner rate structure, like the Service's,

- introduces editorial dropship discounts, with the same structural impact on the editorial pound rate as Postal Service's proposal, setting them at 83.2 percent of the corresponding advertising rate, approximately equal to the relationship in the Service's proposal;
- retains the flat editorial pound rate, setting it at 83.2 percent of the Zones 1 and 2 pound rate for advertising matter, equivalent to the Postal Service's proposal;
- retains the editorial per-piece discount and increases it to 8.9 cents, which is the same amount proposed by the Postal Service, and higher than the amount in the MPA-ANM proposal; and
- retains, and increases, the Ride-Along rate to 15.5 cents.

Id. at 12, Exhibit TW-1-A.

[5678] Mitchell develops Science of Agriculture advertising pound rates for Zones 1 and 2 and closer by setting them at 75 percent of the corresponding rate for the advertising pounds of publications that do not claim Science of Agriculture rates, consistent with a statutory preference. He does not extend this preference to editorial pounds, noting that this differs from witness Tang's approach. He considers her proposed treatment inconsistent with the introduction of the editorial dropship discounts. *Id.* at 12, n.10.

[5679] *Consistency with Order No. 1446 directives.* Mitchell asserts that Time Warner's proposal in this case responds to Order No. 1446 by incorporating recognition of bundle and container costs, but moderating the impact on mailers in several ways, such as using a reduced passthrough for bundle, sack and pallet charges and averaging certain container costs. He maintains that it responds to policy and impact concerns by eliminating full-scale zoning of the editorial pound rate. *Id.* at 11. He also asserts that the Commission paid particular attention to recognition of non-machinability in Order No.

1446, noting therein, among other things, that Periodicals is the only traditional class in which machinability is not explicitly recognized in the current rate schedule. *Id.* at 24-25. He indicates that the Time Warner proposal is therefore consistent with this aspect of the Order. He points out that revenue received from nonmachinable pieces helps hold down the rates for other mailers and supports the Service's automation program. *Id.* at 25.

[5680] *Related matters.* The rates associated with the Time Warner proposal were developed on a test year basis, using Commission costs (as provided in USPS-LR-L-95), modified by the exclusion of air transportation costs. *Id.* at 13, n.11. Cost coverage is 100.2 percent. The rate schedule appears in an exhibit to Mitchell's testimony. *Id.*, Exhibit TW-1-A. The Time Warner proposal obtains approximately 35 percent of the revenue from pound rates *Id.* at 12, n.8. Mitchell notes he does not have sufficient data to create a complete set of billing determinants for Nonprofit and Classroom rates and, among other things, recommends a method for estimating their revenue. He maintains that his approach provides an estimate that is at least as close as any that could be developed from other assumptions about these billing determinants. *Id.* at 13, n.11.

[5681] *Time Warner's impact assessment.* Mitchell asserts that the Time Warner proposal moderates rate impact on mailers in several ways, relative to the proposal it co-sponsored in the Complaint case. He notes that it does not include full zoning of the editorial pound rate, which the Commission observed accounted for a considerable amount of the rate impact identified in the Complaint case. He also notes that the new bundle, sack and pallet charges are proposed to be passed through at 60 percent, rather than the full (100 percent) proposed in the Complaint case, and that container costs (at origin facilities) are averaged across three categories. Mitchell also notes that mailers have many opportunities to avoid rate increases under the Time Warner proposal by changing their behavior, often in ways that do not entail significant effort. Moreover, he maintains that the new 24-piece sack rule will eliminate many sacks, meaning that the Commission's concern over the effects on mailers due to these sacks no longer exists. *Id.* at 11.

[5682] Time Warner, on brief, contends that the impact of its proposal is neither extreme nor unfair against the spectrum of publications in the subclass. Time Warner Brief at 48. It points out some publications that would experience a higher-than-average increases now pay below-cost rates. Time Warner singles out non-machinability as perhaps the most common reason why some publications would pay sharply higher postage under its proposal, and notes that Stralberg indicates that a change in format or use of automation-compatible polywrap are ways to avoid higher rates. It also reviews several other causes for the variation in percentage impact, such as the lingering presence of skin sacks, entry far from the destination, use of firm bundles, and the impact of eliminating the excessive automation passthroughs in current rates. Time Warner also notes that medium-sized publications may be able to avoid increased rates by co-mailing or co-palletizing. *Id.* at 52-54.

[5683] *Other participants' positions.* U.S. News, through the testimony of witness White and on brief, supports Time Warner's proposal. *See generally* USNews-T-1 and US News Initial and Reply Briefs. In addition, it suggests that the Commission consider adopting a variation on the proposal which retains the framework, but further moderates certain elements. US News Brief at 5-6.

[5684] The Postal Service and MPA-ANM, by virtue of their alternative proposals, do not support the Time Warner structure. ABM and McGraw-Hill sponsor the testimony of witnesses in opposition to both the Time Warner and MPA-ANM proposals.²³⁵ McGraw-Hill's opposition includes the contention that Time Warner's proposal is at odds with Order No. 1446. McGraw-Hill Brief at 21. It also contends that Mitchell's development of the flat editorial pound rate defeats the policy-related purpose of this element. *Id.* at 23-24.

²³⁵ By Presiding Officer's Ruling R2006-1/75, portions of the testimony of witnesses Bradfield, Cavnar and McGarvy from Docket No. C2004-1 were designated into the record of this proceeding. As clarified by subsequent ruling, R2006-1/91, portions of McGraw-Hill witness Schaefer's Docket No. C2004-1 testimony were also designated into the record of this proceeding.

f. Commission analysis

(1) Preliminary Comments

[5685] The Commission prefaces the remaining discussion with comments on five topics. They are:

- the validity of considering bundles, sacks and pallets as new cost drivers;
- certain cost and volume data;
- sack usage and alternatives to sacks;
- recognition of editorial content; and
- rate impact analysis.

[5686] *New cost drivers.* Review of the record indicates that no participant questions the validity of witness Stralberg's key findings, first presented in the Complaint case, that bundles, sacks, and pallets have emerged as important cost drivers in today's mailing environment, and that container presort level and point of entry into the system are key linkages.²³⁶ McGraw-Hill, for example, observes: "There appears to be an emerging consensus ... that the costs to the Postal Service of handling containers such as sacks and pallets are *not* incurred on a per-piece basis, but rather on a per-container basis." McGraw-Hill Reply Brief at 4.

[5687] Pertinent excerpts from the Complaint case record have been designated into the record of this proceeding. Discussion of the updated and expanded costing support Stralberg provides for the Time Warner proposal in this case appears later in this section.

[5688] *Data.* The Service's development of cost and volume data for Periodicals, although improved in many respects relative to the Complaint case, remains a concern. For example, the mail processing cost model that underlies the Service's presort and

²³⁶ The Postal Service Brief at 358-360 takes issue with certain aspects of Stralberg's development of an alternative cost model. In addition, Stralberg and MPA-ANM witness Glick reach different conclusions on how certain deficiencies they see in the Service's costing model should be resolved.

automation cost avoidance estimates fails to address Outside County cost drivers in important respects. In addition, contrary to the Commission's explicit request in Order No. 1446, the Service has not updated certain studies or undertaken any new ones. The Commission reiterates that the Service is in a unique position relative to all others in terms of data collection and studies. It bears a special responsibility in this area.

[5689] *Sack usage.* In Docket No. C2004-1, the record showed that many mailers engaged in the practice of mailing lightly-filled sacks. One practical consequence, in terms of the Complainants' proposal, was that introduction of a sack charge would have had significant negative impact on a considerable number of mailers. A recent rule change means that mailers must now comply with a 24-piece minimum requirement. Pursuant to this rule, low-volume sacks are expected to be reduced by at least 65 percent in the test year. That estimate may be conservative: it was developed in connection with the Service's proposed container charge and, in line with the conventional approach, does not reflect any change in behavior associated with imposition of the charge.

[5690] The Commission understands that the new sacking rules have not come without many years of effort or without some additional expense for mailers. It compliments the Postal Service and industry leaders on their work in bringing about this administrative improvement. In terms of curbing costs, this change should benefit the entire subclass. In terms of the issues on this record, it means that a concern that influenced the Commission's conclusions in the Complaint case has been mitigated in certain respects.

[5691] *Alternatives to sacks.* Order No. 1446 expressed the Commission's concern about the apparent absence of viable alternatives to sacks, and urged the Service to explore potential options. The record shows that the Service has not met with any success in finding a container that improves on sacks in any way that would have broad application for mailers in this subclass. However, the record does confirm that since 2004, the Service has been offering a formal program allowing certain mailers of very small volumes (generally the Outside County copies of Within County publications) to

forego sacks. They may either present their mail without using any sort of container or use a tub.

[5692] The existence of this program is relevant to the Service's announced intention to apply a container charge to mail submitted under this program.²³⁷ The Service's plan has met with widespread opposition from participants. *See, for example*, Dow Jones Reply Brief at 1-2, McGraw-Hill Reply Brief at 18; NAA Brief at 46, and NNA Brief at 26-27. The Commission rejects it.

[5693] Imposition of the container charge defies logic. Some of the mailings that are the target of this charge are not presented to the Postal Service in sacks because, pursuant to authorization, they are using a more efficient and more appropriate practice. An exchange between Postal Service witness McCrery and NNA counsel Rush drives this point home. In response to counsel Rush's inquiry about the existence of a program allowing certain small-volume mailings to be presented without being sacked, witness McCrery confirms that the Service began such a program in 2004. Tr. 11/3275. Then, in response to counsel's request for an explanation of the benefit to the Service of presenting mailings this way, as opposed to bringing the same amount of mail into the delivery office in a sack, McCrery states:

I'll first describe the differences and that may lead into benefit over-all. Either you have those carrier bundles and carrier route sacks in multiple bundles where those sacks are then moved and then the pieces or the bundles [are] then prepped for the carriers, the bundles would then be able to be dropped individually at the delivery unit by the customer. Similar to if it was a pallet without ... actually having the pallet. Then those bundles would be able to be moved into the delivery unit for the distribution to the carriers to be cased up and delivered.

²³⁷ The Service initially intended to assess the container charge on certain mixed-class mailings and certain mixed-subclass mailings, but commentary in a recent *Federal Register* notice indicates that it has modified its position.

The sack itself doesn't provide tremendous additional value in that regard where you may have one or two carrier route bundles. They may end up doing more damage than good

So to provide the flexibility for a customer not to deal with the sacks and in recognition of the limited value that they really have, we wanted to provide that option, in large part for newspapers, to give them flexibility to enter without that sack

Id. at 3271-72. Counsel then asked the witness whether it is it fair to say that in those situations "the sack doesn't help and it may hurt?" McCrery answered: "That's a safe assumption." *Id.* at 3272-73.

[5694] In response to an inquiry about the volume of mail involved in this option, McCrery states that he does not have a sense from any analysis or field visits, but has obtained an indication elsewhere: "I do know from conversations with folks within NNA and customers that they are availing themselves of that option, so I know it's being used by people that we intended it to be used for on some level." *Id.* at 3273. Significantly, he confirms that this mail accounts for only a small portion of volume

... when you know that destination delivery unit entry volumes are small to start with in comparison to the grand scheme of periodicals, the portion that then would be entered unsacked is of course also going to be a small portion of the mail in the grand scheme of things.

Id.

[5695] McCrery also confirms that this program has growth potential:

Q As the Postal Service moves into its FSS sortations,... would you anticipate that some of these new options will continue to remain available for periodicals?

A The ones we've spoken of I see no reason why they would not still be a potential option ...

Q So if you were trying to urge the industry to make that shift it would be a shift that you would foresee having some lasting value?

A I would.

Q And you think there's still room for growth in that area?

A Yes, I certainly don't believe everybody's availing themselves to it, though I know certainly some are. So I would say it's fair to say there is growth certainly with both the tub option and the unsacked option.

Id. at 3279-80.

[5696] The evidence seems clear that application of the Service's container charge to the mailings in question is inappropriate. It would incent mailers to combine mail for multiple destinations into a single container, making processing slower and more expensive.

[5697] *Rate impact analysis.* A typical way of assessing a rate or classification proposal is to consider it in terms of the average rate increase. The extensive de-averaging in the Complaint case proposal produced widely-varying percentage increases, so discussing impact in terms of the average subclass increase was of limited utility. The Postal Service developed a database of 251 publications, divided into small, medium and large categories (with density distinctions) that helped focus the discussion. In this case, the Service has updated that database, including an adjustment to reflect anticipated container usage under the new rule. Witness Stralberg also identifies a fourth category — a further breakdown of the small category — consisting of "very small publications." TW-T-2 at 30, n.29. ABM witness Cavnar and Postal Service witness Taufique suggest other approaches to assessing rate impact on this record. Cavnar testifies that cents-per-copy is an important perspective. ABM-T-1 at 6. Taufique states that he considers standard deviation from the mean a key statistic. USPS-RT-12 at 5.

[5698] The database is not a completely representative sample and could be improved in some respects, but the Commission finds it satisfactory for purposes of this

record. It acknowledges that other approaches may also warrant consideration, but emphasizes that the Act does not prescribe the use of a specific analytical tool or technique in assessing effect on mailers. In fact, reducing the requisite consideration of impact on mailers to a single statistical technique would not appear to be consistent with the statute. The Commission also notes that cents-per-copy comparisons may be of interest, but have some inherent limitations. An elementary one is that many elements affect the postage any publication is assessed, so one-to-one comparisons are quite difficult.

[5699] Participants and witnesses have presented considerable testimony on rate impact of the alternative proposals. In certain instances, the Commission's assessment of the overall merits of the proposed alternative structures means that the proffered impact analysis does not have as much bearing as it otherwise might.

[5700] *Balancing policies involving editorial content and efficiency.* In Order 1446, the Commission expressed two concerns about the Complainants' proposal to fully zone the editorial pound rate. One was its impact on a policy consideration (widespread dissemination and diversity of editorial matter in the Periodicals mailstream); the other was its impact on rates for mailers with small (low) circulation. In this case, Time Warner has not revived the "full zoning" proposal; however, like the Service and MPA-ANM, it proposes adoption of a set of editorial dropship discounts (destination entry discounts).²³⁸

[5701] The Commission recognizes that there are several ways that editorial content can be recognized in the rate structure. Given the limited nature of the change the proponents seek, record evidence that the private sector dropshipping capability has expanded since the Complaint was filed (meaning more mailers may be able to take advantage of destination entry discounts) and the universal support for this change on the part of all those addressing the proposal on the merits, the Commission does not oppose their introduction. It finds that this relatively limited change does not pose any

²³⁸ Development of these discounts differs in some respects in the various proposals.

undue diminution in the policy sought to be advanced and fosters other policies, such as recognition of mailers' worksharing efforts.

(2) Assessment of the Postal Service's Proposal

[5702] The Postal Service presents its proposal as a means of gradually introducing better cost signals and argues that it reflects a balanced approach. Supporters generally view the Service's proposal in broad terms; consider its relatively modest nature as a virtue; and believe the rate impacts are limited, relative to the other proposals. Opponents, on the other hand, criticize the proposal mainly on the grounds that the structure's key elements produce rates and incentives that seriously contradict the Service's stated objective of providing better cost signals.

[5703] The Commission gives the Service's position on rate and classification proposals deference, as it bears the responsibility for implementing and administering the ensuing changes. It also recognizes that the Service has attempted to respond to Order No. 1446's call for fundamental structural improvements. However, it became clear as the record developed that certain conceptual and practical aspects of the Service's approach had not been thoroughly considered prior to filing. Four aspects have been shown to be especially problematic: development of the container charge; development of the "replacement package" for pallet discounts; the combined effect of these features on the professed goal of providing better price signals; and the application of the container charge.

[5704] The Commission's reluctant conclusion is that the Service's goal of introducing price signals that foster more efficient containerization simply can not be achieved through the approach it advocates. The source of the contradiction between the proposal's objective and its results lies initially with the decision to propose a uniform container charge, rather than separate bundle, sack and pallet charges. This decision has two ramifications in terms of price signals. First, it means that bundle costs continue to be hidden. This might be an acceptable result, given the Service's interest in gradual

changes, had the approach to container costs been executed differently. However, the record supports a finding that uniform application of a single charge to all containers blurs confirmed cost differences between sacks and pallets and ignores presort level and entry point. The consequence is that a poor — even inaccurate — signal is given.

[5705] MPA/ANM witness Cohen assesses the development of the new charge this way: “Witness Tang, in an apparent desire for simplicity, has proposed a single uniform container charge, regardless of container type, presort level or entry point.”

MPA-ANM-T-1 at 19. She points out that this can lead to counter-productive results for several reasons, but especially because the 85-cent charge does not nearly reflect the cost difference between pallets and sacks. She asserts that the proposed charge would therefore send incorrect price signals on the value of palletization to the Postal Service.

Id. Time Warner further illuminates the scope of the problem that averaging sack and pallets presents in terms of cost recognition through the following queries:

- Is a sack charge of 85 cents reasonable when some sacks cost \$4.75 to handle, and others \$1.60?
- Is a pallet charge of 85¢ reasonable when some pallets cost \$66.70 to handle, and others \$1.60?
- When bundles cost from 10 cents to 44 cents to handle, and there are large numbers of bundles, is it reasonable to neglect these costs and somehow average them in with the piece rate?
- When adjustments in the number of pieces in sacks cause associated adjustments in the costs of bundle handling, should the costs of bundles be ignored?
- When handling a 5-digit sack costs \$5.60 if it is origin-entered and \$2.30 if it is destination-entered, should the rates simply disregard these cost differences?

Time Warner Reply Brief at 2.

[5706] The Service has not challenged the foregoing assertions regarding the proposed container charge; instead, it appears to defend it as part of a “balanced” approach to improving the rate structure.

[5707] The problem posed by the nature and amount of the container charge is magnified by the decision to include the container charge in a “replacement package” of

elements which, among other things, eliminates the pallet discounts. There is general agreement, even among those who do not support the Postal Service's proposal, that the new package does increase some incentives for presorting and dropshipping; however, both supporters and opponents alike regard these incentives as modest, and critics claim they are often outweighed by the elimination of the pallet discounts.

[5708] Tang maintains that her approach provides similar — or better — incentives. The Commission finds that there is considerable record evidence indicating that the replacement package is not as salutary as she believes. Witness Cohen maintains that the overall percentage rate increases for many mailers who already engage in efficient practices (such as co-mailing and co-palletization) would be similar to or higher than they would experience if they did not engage in such practices. She attributes this to two shortcomings in the design. One is that the elimination of the pallet discounts largely offsets the increased incentives that the new editorial pound destination entry discounts provide for palletizing and dropshipping. The other is that the cost avoidances in the destination entry discounts are understated, in part because a large share of nontransportation (bulk transfer) cost avoidances have been ignored. Cohen also directs a targeted criticism at Tang's proposal to increase the rate difference between the 5-digit automation and carrier route basic rates — a difference she considers critical to the encouragement of co-mailing — by only 4.5 percent over current levels. MPA/ANM-T-1 at 18-20.

[5709] Cohen supports her contention that the package the Service has proposed is not well-suited to furthering the Service's asserted objectives by referencing MPA-ANM witness Glick's analysis of the effect of the Postal Service rates on a group of small and mid-size publishers who are currently engaged in co-mailing. She notes:

They range in size from Ogden Publications' Mother Earth News, at about 217,000 pieces per issue, to Ogden's Gas Engine, at 15,000 pieces per issue. Table 2 in Witness Glick's testimony (MPA/ANM-T-2) shows how the seven magazines, which are currently co-mailed, would fare with and without co-mailing under witness Tang's rate design.

As shown by witness Glick, only one of the magazines, *Interweave knits*, would face a substantially reduced rate increase when co-mailed and dropshipped compared to mailing alone. The other small and mid-size magazines studied would face increases similar or larger when engaged in worksharing.

Id. at 20.

[5710] The Commission further finds the record clearly indicates that the effects Cohen has discovered are not limited to the publishers in Glick's study. U.S. News witness White comes to a similar conclusion about the poor — even contradictory — signals in the Service's proposed rate structure for a large, highly efficient mailer. He testifies that he modeled the impact of the Postal Service's proposal on five issues of *U.S. News & World Report* and found the rate increase to be 16 percent, with the amount per issue ranging from 14.6 percent to 19.2 percent. He attributes the variations to advertising percentage, copy weight, and the number of copies qualifying for the experimental co-palletization discounts. USNews-T-1 at 4.

[5711] Witness White notes that his company has a long history of responding to the Postal Service's pricing signals by changing the way it mails, but his conclusion is: "The rates proposed in Docket No. R2006-1, however, provide no obvious new opportunities to make our mail more efficient for the Postal Service and may in fact result in mail that is less efficient for the Postal Service to handle." *Id.* His testimony provides additional extensive discussion of the impact of the Service's proposal on company operations. *Id.* at 6-15. The Service has not refuted witness White's conclusions.

[5712] The Commission finds itself faced with credible, consistent and cumulative testimony that both the container charge and the entire Postal Service package do not send the intended signals to major segments of the class. The Service has not been able to show that the examples provided on this record are isolated or unique instances. Regrettably, the key features of the Service's proposal provide incentives that are so modest that they are, in many instances, outweighed by the elimination of the pallet discounts. In other cases, they are so contradictory that mailers that already engage in efficient practices would not receive appropriate recognition for their efforts. This is

clearly contrary to the Service's stated objective of not only incenting new, more efficient behavior, but also recognizing — and continuing to encourage — other mailers' ongoing efficient practices. The Commission concludes that these features of the proposed structure impair the stated objective of providing better price signals and preclude a favorable recommendation.

[5713] Given the conclusion that there are fundamental problems with execution of the Service's objective, the impact arguments ABM and McGraw-Hill offer lose much of their currency. The comparisons flow from a faulty premise; namely, that the structure, in general, is oriented toward providing better price signals. In addition, the Commission finds that it need not reach a decision on the merits of other matters, such as the proposed increase in the editorial benefit, McGraw-Hill's request that witness Tang's development of the flat editorial pound rate be revised, or ABM's suggestion (without elaboration) that the Commission consider a hybrid Postal Service/MPA-ANM structure. The Service's Ride-Along proposal is addressed in the discussion of the MPA-ANM proposal.

[5714] Although the Commission concludes that it can not recommend the Postal Service's proposal, it nevertheless commends the Postal Service for its continuing commitment to making the Periodicals mailstream more efficient. It appreciates the interest postal management has demonstrated in Periodicals reform, its pursuit of an innovative, ambitious approach to Periodicals rate design, and its responses to the Commission's data requests.

(3) Assessment of the MPA-ANM Proposal

[5715] The hallmark of the MPA-ANM proposal is its use of a set of expanded and enhanced pallet discounts in lieu of a container charge. MPA-ANM emphasizes that this is not a rejection of Order No. 1446's call for better cost recognition and better price signals, but an interim approach which accomplishes the same goals. The main criticisms of the MPA-ANM proposal nevertheless focus on its failure to introduce any

explicit recognition of new cost drivers; its much stronger reliance on per-piece pallet discounts; and its corresponding dependence on enhanced co-mailing, co-palletizing and dropshipping.

[5716] McGraw-Hill, criticizing the strong reliance on the existing structure, characterizes the MPA-ANM structure as a status quo approach that perpetuates *non-cost* based ratemaking. McGraw-Hill Brief at 19, Reply Brief at 4 (emphasis in original). Time Warner states: “The proposal ... does not even pretend to move in the direction of recognizing the cost drivers that the Commission has said should be recognized. Its goal is to retain and enlarge a per-piece pallet discount, even though pallet costs are not piece-related.” Time Warner Brief at 14.

[5717] The Commission agrees that the MPA-ANM proposal is at odds with the conclusions reached in Order No. 1446 about the need for structural reform. Only one element can be considered fundamentally new, and this is the set of editorial dropship discounts common to all of the proposals. These have a limited role in improving price signals.

[5718] The set of pallet discounts MPA-ANM proposes are more cost-based than the existing ones due to certain costing changes developed by witness Glick, so provide better signals in that respect. However, they retain the long-criticized feature of being applied on a per-piece basis, which perpetuates illogical aspects of the existing structure.

[5719] ABM, on brief and through its witnesses, takes issue with two aspects of the proposal’s reliance on worksharing incentives. One is the assumption that the private sector is ready, willing and able to meet the demands for co-mailing, co-palletizing and dropshipping that the enhanced incentives might generate. The other is that some mailers may choose not to avail themselves of those opportunities, even if made available, for business reasons and therefore would still need to rely on sacks.

[5720] Developments since passage of the Postal Reorganization Act of 1970 have significantly altered not only the way the Service processes Periodicals, but the Service’s role in the entire mailing process. The private sector now not only provides printing services, but also offers co-mailing, co-palletizing, consolidating, dropshipping and other

mailing-related services. Most of these practices are tied to presort discount and “zone-skipping” (dropshipping) opportunities in the Periodicals rate structure, although improved service is also a consideration.

[5721] In Order No. 1446, the Commission concluded that there was a mixed record on co-mailing and related worksharing opportunities. It was clear that many larger mailers had been availing themselves of these services for some time, but it was less clear that others, especially those in the small volume category, could participate, given the state of the industry. Order No. 1446 at 6.

[5722] In this case, the record again includes a considerable amount of testimony on this topic. MPA-ANM witness Cohen’s testimony indicates that there have been many favorable developments since issuance of Order No. 1446. MPA-T-1 at 11-16. This supports, in many respects, her contention that the industry is poised for further growth, and that enhanced incentives would trigger developments that would benefit mailers and suppliers alike.

[5723] In addition, U.S. News witness White provides an update of testimony US News submitted in the Complaint case addressing a real-world example of a mailing program involving two weeklies. It appears that advances in the printing industry have allowed US News and its mailing partner to move from co-mailing to co-binding.²³⁹ White says this was done, in part, because his company thought it positioned them well for truly cost-based rates.

[5724] It seems equally true, as ABM witness McGarvy observes, that co-mailing of weeklies still relies to a large extent on at least one partner having considerable volume, and that some services are either not yet available for certain formats, such as tabloids, or are just beginning to be made available. Moreover, the record makes clear that some

²³⁹ Witness White describes co-binding as a process that uses selective-binding to combine the assembling and mailing of two or more publications on the same binding line. He states that the effect on postage is identical to co-mailing, with copies of the publications being mixed together in the same bundles as well as in the same containers. USNews-T-1 at 3.

mailers may choose not to avail themselves of these services — even if widely available — for business reasons, such as maintaining editorial freshness. ABM-RT-2 at 3-6.

[5725] The Commission assessment is that the record in this case indicates that there is no reason that the state of the mailing services industry should stand as an automatic bar to adoption of proposals tied directly or indirectly to such services, assuming all applicable statutory considerations are met. Instead, theory and reality should converge in the rate structure, thereby sending price signals that provide the Postal Service, mailers and others with the information they need to achieve lowest combined cost. In this sense, the MPA-ANM proposal demonstrates two strengths. One is the recognition that the “practical reality” of the mailing environment, present and future, calls for many senders of Periodicals mail to focus on joint cost-reducing opportunities. The other is that publishers, printers and others involved in mailing decisions respond to the price signals conveyed in postage rates, even imperfect ones. MPA-T-1 at 7-8.

[5726] However, the MPA-ANM proposal poses the prospect of even further investment and entrenchment in the current structure. Thus, its limited structural changes, offered in the interest of mitigating the impact of the Service’s container charge, unduly constrain progress in a vital area. The Commission concludes that the more appropriate course is to begin now to recognize the actual cost drivers identified in Docket No. C2004-1.

[5727] Given this conclusion, the Commission does need to reach a decision on MPA-ANM’s 5-digit pallet discount.

[5728] *The Ride-Along rate.* MPA-ANM propose a Ride-Along rate of 14.6 cents, rather than 15.5 cents, as the Service has proposed. They consider the Service’s proposal, which reflects an 18 percent increase, excessive, and contend that an increase in line with the subclass average would be more appropriate. MPA-ANM Reply Brief at 44. The Service, on the other hand, defends the development of the rate on grounds that it follows the original method, applies to an advertising piece that otherwise would not be allowed to be included in the host publication; that no costs associated with the

weight of these pieces are added to the subclass advertising pound totals; and that the revenue adds to the subclass's contribution.

[5729] The Commission appreciates MPA-ANM's concern that Ride-Along pieces not be saddled with a disproportionate increase. This might decrease its appeal to advertisers, and the revenue-enhancing benefits witness Taufique emphasizes could be lost. At the same time, the rate does not reflect any departure in methodology. Moreover, these are separate marketing-oriented pieces that would not otherwise be carried at Periodicals rates. The Commission does not accept the MPA-ANM proposal. It recommends a 15.5-cent rate, which is the level proposed by the Postal Service and adopted by Time Warner.

(4) Assessment of the Time Warner Proposal

(a) Witness Stralberg's cost support

[5730] The Commission finds that the Stralberg model is a comprehensive and well-constructed simulation based on currently available information. It adopts this model and its results for purposes of the Periodicals recommendation made on this record.

[5731] The model Time Warner witness Stralberg uses to describe the mail processing cost behavior of Outside County pieces is a modified version of the model he presented in Docket No. C2004-1. That model builds upon the Postal Service Periodicals flats model described by witness Miller in USPS-T-20 and provided in USPS-LR-L-43 (USPS version) and in USPS-LR-L-102 (PRC version). Witness Stralberg makes several modifications to the Miller model to more accurately reflect the current operational environment for Outside County Periodicals mail. The changes he incorporates highlight the differences in costs for machinable and nonmachinable Outside County flats.

[5732] The key elements of Stralberg's modifications are refinements to the model he developed for Docket No. C2004-1. Changes were made both to update previous costs and to introduce methodological enhancements.

[5733] *Manual incoming secondary.* Witness Stralberg reintroduces incoming secondary flats coverage factors. TW-T-2 at 11-14. Such factors had been removed from witness Miller's model, even though witness McCrery testifies that 44.7 percent of flats in incoming secondary operations are finalized manually. Tr. 11/2853. Stralberg's modifications to Miller's Periodicals flats model received very little criticism.

[5734] Witness Miller testifies that the figure cited by witness McCrery was used by management to assess performance, so it should not be used for modeling costs. Tr. 33/10994. Miller further asserts that no one knows the true percentage of flats finalized in incoming secondary operations. *Id.* at 10995. It is clear from the record of this and previous proceedings, however, that manual sortation continues to be a factor in the costs of processing Outside County subclass mail. Ignoring the impact of manual operations appears likely to distort the cost differences they give rise to. Witness Stralberg's modification reflects the probability that 29.9 percent of nonmachinable flats flowing to an incoming secondary operation will be finalized manually. He has further made a reasoned assumption that the manual processing of flats will diminish by the test year. Flats routed to an incoming secondary operation are given an 85 percent chance of being machine sorted. The remaining 15 percent are assumed to be manually sorted. TW-T-2 at 13-14.

[5735] The Commission noted the need for updated information on manual flats processing in Docket No. C2004-1. In Order No. 1446, it observed the following about the changing environment for Periodicals flats processing:

Base year MODS data provided in Docket No. R2001-1 show that 59 percent of Periodicals Outside County Regular Rate processing costs are generated by manual sorting operations. The mail processing environment for Periodicals is changing, however. The AFSM-100 inventory was expected to increase from 355 to 534 between fiscal years 2001 and 2002.

These and other changes in the operating environment subsequent to Docket No. R2001-1 should be reflected in any rate design for Periodicals.

Order No. 1446, ¶ 4009 (footnote omitted).

[5736] Witness Stralberg has responded to the Commission's Order by submitting a model with updated and expanded information, taking into account the need to assess the future Periodicals processing environment as well as the current environment. This represents a significant improvement in the modeling process. The resulting cost estimates reflect this improvement. Notwithstanding witness Miller's assertions, the inclusion of these factors by witness Stralberg is an appropriately conservative method for reflecting a more realistic representation of Periodicals flats sorting operations. The Commission encourages the Postal Service to obtain more precise estimates of the manual sortation of flats.

[5737] *Flats preparation.* Witness Stralberg also distributes the flats preparation cost pool (MODS 035) to rate categories in proportion to how much each rate category uses the pool. TW-T-2 at 9-11. Miller treats this cost pool as fixed. There is merit in Stralberg's argument that these Outside County Periodicals costs arise because flats are being loaded onto machines to be sorted: were all flats sorted manually, such an operation would not exist.

[5738] Stralberg notes that the Miller model fails to distinguish between machinable and nonmachinable flats on the UFSM 1000 machines. Because Stralberg is isolating the costs of machinable and nonmachinable flats, this distinction is essential. Miller did not need to distinguish between these two types of flats, given the Postal Service's proposal. Consequently, witness Stralberg's description of what he terms a distortion in Miller's model necessarily implies a higher percentage of mechanized flats sortation than actually exists. *Id.* at 11-14. Stralberg's assumptions are reasonable and seem to better reflect operational realities. Analysis of this issue has evolved over time and should continue to evolve as flats operations change. The Commission recognizes that different processing mailflows exist for different subclasses. Consequently this cost is treated

somewhat differently for First-Class and Standard flats. Further analysis in this area should be undertaken.

[5739] *Bundle breakage.* Witness Miller's flats model reroutes pieces from broken bundles to a manual incoming primary followed by a manual incoming secondary. USPS-LR-L-45, tab "Bundle Sort". His bundle breakage assumption is that 10 percent of bundles from sacks and pallets are broken. USPS-LR-L-45, tab "Bundle Data". Witness Stralberg assumes "that when a bundle is broken in a manual sort from a pallet or wheeled container, the bundle will already have made it to the next sort level and therefore requires less additional piece sorting." TW-T-2 at 21-22. The omission of bundle recovery in Miller's model seems to limit its ability to fully identify costs. Stralberg's adjustments for bundle recovery are warranted. The Commission urges the Postal Service to study bundle recovery rates to more accurately assess the costs of bundle breakage.

[5740] *Other adjustments.* Witness Stralberg makes other adjustments to the Miller flats model, expanding the CRA adjustment used by Miller because he believes the mail processing costs he models are incurred in more cost pools than the ones Miller included. *Id.* at 23. Stralberg reasons that cost pools such as "NonMODS allied" that include some container handling and some bundle sorting be fully proportional or fully fixed. Based on witness Van-Ty-Smith's estimate, he treats these costs as 37 percent proportional. Tr. 10/2474-75. He includes Outside County nonletter costs recorded at all piece sorting operations, including letter operations. His rationale is that some flats appear in the letter operations because workers are handling flats while logged into a letter operation.

[5741] *Commission adjustment.* As discussed in Chapter III, the Commission adjusts wage rates and piggyback factors used in the Stralberg analysis to reflect events subsequent to the Postal Service's filing in this docket. These adjustments also are reflected in other mail classes.

[5742] As in his Docket No. C2004-1 container cost analysis, witness Stralberg relies on the Postal Service's Mail Characteristics Study (USPS-LR-L-91). In addition,

he uses information obtained from Postal Service witness Loetscher's responses to Time Warner interrogatories to further refine his container costs.²⁴⁰ Stralberg testifies that his calculated container costs are substantially higher than those he developed in Docket No. C2004-1. He points out that the test year after rates wage rate is 23 percent higher than the 2003 rate used in the Complaint proceeding. In addition, newly available mail flow data show that some containers incur more intermediate handlings, and thus more costs, than he previously assumed. *Id.* at 36.

[5743] *Methodological changes.* Witness Stralberg relies on the Postal Service's "web-based survey" to refine his container mail flows. The survey data, unavailable for use in Stralberg's previous version of his model, provides more detailed information on the flows of 5-digit containers, mixed ADC sacks, and unit bundle costs. *Id.* at 37-44.

[5744] The changes witness Stralberg makes in his application of the Periodicals flats cost model and his calculation of container costs represent improvements in the ascertainment of cost behavior for this mail. He has responded to specific criticisms and suggestions in Order No. 1446. By its nature, the modeling process is one of evolution as more is learned about the behavior of costs. As the automation of flats progresses, more specific cost information will emerge concerning the characteristics of machinable and nonmachinable Outside County flats. The Commission expects that refinements will continue to be made over time as the processing environment for Periodicals Outside County mail changes.

(b) Witness Mitchell's Rate Design

[5745] The Time Warner proposal uses essentially the same rate design framework as the Complaint case proposal, but incorporates several adjustments intended to moderate impact. This leads most participants to address the proposal in terms of whether those adjustments, considered in light of this evidentiary record, sufficiently

²⁴⁰ See, for example, Tr. 7/1505-29.

mitigate concerns the Commission raised in the Complaint case, including the rate impact on mailers.²⁴¹ US News, a supporter of the Time Warner proposal, contends that they do. It asserts:

The Commission's only criticism of the original Mitchell model in C2004-1 is that it would lead to inordinately high rate increases for some small mailers. Mitchell's current proposal incorporates those concerns, following the same logic as before but softening the impact on certain mailers (and necessarily balancing that by making worksharing incentives less than they were in the C2004-1 proposal. These efforts ... are reasonable

U.S. News Brief at 13.

[5746] Opponents generally counter with claims that the proposal is still too much, too soon and still has unacceptable rate impacts. *See, for example, ABM-RT-2 at 7.*

[5747] *Assessment in light of an updated record.* For all participants except McGraw-Hill, witness Mitchell's decision not to propose a fully zoned editorial pound rate appears to moot the two concerns the Commission expressed in the rate case (undue rate impact on certain small mailers and abridgement of public policy). The Commission has noted its approval of the inclusion of editorial pound rate dropship discounts in its preliminary comments, so that aspect of the Time Warner proposal does not pose a difficulty.²⁴² Mitchell also proposes an editorial discount that is equivalent to the Service's proposed rate and higher than both the existing rate and the rate proposed by MPA-ANM. Therefore, there is continued recognition of the presence of editorial content.

[5748] McGraw-Hill nevertheless contends that the Time Warner proposal undermines the unzoned editorial pound charge because

²⁴¹ McGraw-Hill asserts that the Time Warner proposal is at odds with the guidance in Order 1446. McGraw-Hill Brief at 21. The Commission finds this assertion unfounded.

²⁴² McGraw-Hill points out that Time Warner proposes increasing the flat editorial pound charge to a level that is 83 percent of Zones 1 and 2 advertising pound charge. It notes that the traditional level is 75 percent. McGraw-Hill Brief at 25, n.24.

... non-transportation costs that are nevertheless distance-related would be recovered from 100% editorial publications (as from all other publications) through container charges that (like the zoned advertising pound charges) increase with the distance that a container travels through the postal system.

McGraw-Hill Brief at 25-26.

[5749] It notes that origin-entered containers would pay much higher container charges than destination-entered containers under the Time Warner proposal, and concludes that a 100 percent editorial publication would pay substantially more than the unzoned editorial pound charge “for the privilege of making a greater use of Postal Service transportation.” *Id.* at 26. To that extent, McGraw-Hill finds that the purpose of the unzoned editorial pound charge is defeated. *Id.*, McGraw-Hill Reply Brief at 15-17.

[5750] The policy of promoting editorial diversity and widespread dissemination of editorial matter is one of many that must be weighed and balanced. Some of those considerations include recognizing costs and promoting worksharing. The Commission finds that cost-based container charge differentials reflecting dropshipping alternatives can not reasonably be said to defeat the public policy purpose underlying the flat editorial pound charge. It therefore rejects the suggestion that the Time Warner proposal should not be adopted on this ground.

[5751] *Sacks*. The sack charge in the Complaint proposal raised three main concerns: full passthrough; the considerable number of sacks that would be subject to it, given the extensive use of lightly-filled sacks; and the lack of practical options for avoiding the charge, given the state of private sector co-mailing programs. In this case, Mitchell reduces the passthrough of the sack charge, as well as the bundle and pallet charges, to 60 percent. He also averages a set of container charges over three categories.

[5752] Both of these steps moderate the impact of the proposal; in fact, Mitchell expresses some concern that this moderation will mute the effectiveness of the structure. However, even with this moderation, some participants claim that the sack charges still have an unacceptable impact on certain mailers who can not avoid using sacks. They

suggest that this means adoption of a more cost-based structure should be postponed. ABM-T-2 at 7.

[5753] The Commission noted earlier that the current state of the mailing services industry is not an automatic bar to recommendation of the Time Warner proposal. It has considered whether a closer look reveals any reasons why the state of the industry would foreclose the Time Warner proposal. It concludes that the current record supports a finding, in a qualitative sense, that there has been an expansion of opportunities for co-mailing and related services since the Complaint case was filed. This appears to be due to some degree to incentives in current rates, advances in technology, growing familiarity with the programs, and the expectation that the Postal Service would file a request seeking approval of a more cost-based rate structure in this case.

[5754] The Commission observes that the incentives in the MPA-ANM proposal, in general, appear to be more directly tied to co-mailing than those in the Time Warner proposal. The Time Warner structure ties elements, in the first instance, to postal costs and operations. It fosters worksharing by identifying these costs much more directly than before, thereby allowing choices to be made with a clearer idea of the consequences, but the elements themselves are not dependent on co-mailing.

[5755] Supporters of postponement cite two main reasons: (1) mailers with very small volume are unlikely to ever be able to move out of sacks because co-mailing is unlikely ever to be universally available; and (2) mailers with unique business models or corporate philosophies will never find certain aspects of co-mailing acceptable, such as the potential for delays occasioned by others in the pool or the need to maintain established advertising deadlines.

[5756] Postponing adoption of a more cost-based structure for mailers in the first set appears to make little sense because they apparently will never be able to take advantage of co-mailing service. Furthermore, the changes Time Warner has made relative to the Complaint proposal should mitigate the impact of the sack charge. Thus, adoption of the Time Warner structure relative to them could not be considered unfair, in an overall sense. Mailers in the second set are differently situated. Their use of sacks

appears to be “required” primarily because they exercise their prerogative to have certain business considerations constrain their preparation options. Postponing adoption of co-mailing incentives for these mailers is not a reasonable approach to ratemaking in today’s environment either, as their needs also may never be met. Moreover, adoption of the proposed structure would not preclude them from deciding against co-mailing, but would more accurately reflect the cost of this choice. It also would allow other mailers who are willing to exercise more flexibility to mitigate rate increases through worksharing efforts. This would advance the overall fairness of the structure.

[5757] *Assessment of machinability and automation issues.* In Order No. 1446, the Commission clearly indicated that a rate distinction between machinable and nonmachinable pieces is a much-needed and long overdue improvement in the Periodicals structure. It is disappointing and perplexing that neither the Postal Service nor MPA-ANM proposals include this distinction. Witness Tang offers no direct explanation of this omission in her testimony, apparently excluding it on the basis of the Service’s institutional interest in gradual changes in the Periodicals structure. MPA-ANM witnesses Cohen and Glick acknowledge the cost consequences of non-machinability, but do not propose recognition. Glick indicates the reason is an allocation of resources in preparing for the rate case; witness Cohen says she would like to review the standards that will be developed for use with Flat Sequencing System (FSS) technology before including explicit recognition.²⁴³ Tr. 30/10176.

[5758] Review of the responses to Presiding Officer’s Information Request No. 19 and related material clearly indicates that the introduction of a machinability distinction will have a significant rate impact on mailers who do not sort to the carrier route. There are two reasons. One is that there is currently no recognition of these distinctions in the rate structure, so introducing such recognition has a de-averaging effect. Mailers who now present machinable mail benefit from the de-averaging through lower rates that

²⁴³ McGraw-Hill notes its approval of MPA-ANM’s exclusion of a rate element recognizing non-machinability. McGraw-Hill Brief at 22-23.

recognize their lower costs; those who present nonmachinable pieces will pay rates that reflect their higher costs. The other reason is that current automation discounts “over-reward” many mailers, and that passthroughs are far in excess of 100 percent. This means a move to full (100 percent) passthrough has an additional impact.

[5759] The Commission is concerned about this impact; however, it finds that the proposed introduction of a distinction between machinable and nonmachinable pieces is an appropriate step for several reasons. First, nonmachinable pieces impose more costs on the system than machinable pieces. Second, flats machining and flats automation are not novel postal processing methods. Third, machinability has been recognized for some time in other classes. Fourth, some mailers may be able to avoid a surcharge by making relatively minor adjustments. The record shows that for many pieces, compliance with machinability standards can often be achieved through the addition of a barcode or through other reasonable changes, such as switching to approved polywrap.

[5760] In addition, the Commission finds that the objections to introducing a non-machinability surcharge run mainly to adjustment and impact issues, not to disagreement over the existence of cost differences. Awaiting formal development of FSS-related standards is not a compelling reason for postponing this improvement in the rate structure. Mailers routinely adjust to new standards as the mail processing environment evolves. Moreover, there is no indication on the record that FSS deployment will pose challenges so daunting that they undermine the advisability of introducing a machinability distinction at this time.

[5761] Rate impact is a legitimate concern. In addition, much like the sack issue, some mailers with exceptionally heavyweight pieces are not likely to be able to avoid a surcharge. (Although again, the costs these pieces impose on the system would be more fairly recognized, and not averaged into the rates paid by other mailers.) This appears to be an area where suggestions that the Commission consider further moderation of the Time Warner proposal have a strong bearing.

[5762] *Special situations.* Under the Time Warner proposal, rates would reflect the higher costs associated with firm bundles and supplemental mailings. There has been

no strong opposition to this, but the Commission believes that the proposed treatment of firm bundles is another area where suggestions for further moderation pertain. While all mailers of firm bundles would benefit from moderation, mailers of Classroom publications would almost certainly benefit the most. The identification of firm bundles in the carrier route category facilitates this step.

[5763] *Commission conclusion.* The Commission acknowledges witness Mitchell's position that he has built sufficient moderation into the structure and rates, and that this moderation means that the effects (price signals) will be muted. At the same time, it finds that further moderation would better suit the needs of the subclass as a whole at this time. Time Warner does not advocate further moderation, but acknowledges that the Commission might see fit to make some in the interest of tempering impact. Thus, the Commission does not accept the Time Warner proposal as filed. It finds making reasoned adjustments within the framework is the most appropriate approach.

[5764] *Commission recommendation — modified Time Warner approach.* The Commission recommends the framework sponsored by Time Warner witness Mitchell. This framework closely mirrors postal operations in most respects, and recognizes the strengths of the private sector in providing co-mailing and related services. It follows logical patterns and development of rates is straightforward.

[5765] This approach allows measured efficiency signals to be introduced. Impacts are moderated for nearly all mailers. The introduction of several new elements and a new, better conceptual approach warrant moderation. Overall considerations of fairness and equity, in some instances, call for more targeted moderation, given certain circumstances. The following summarizes the adjustments and tempering the Commission recommends based on this record

- an increase in the editorial per piece discount, from 7.8 to 9.1 cents; this is higher than proposed on this record;
- the introduction of recognition of the costs of bundles, sacks and pallets at 40 percent passthrough, rather than the 60 percent proposed by Time Warner;

- further moderation, with respect to firm bundles and the mixed ADC sack charge, by passing through only 20 percent; and
- introduction of machinability distinctions, but with moderation of the impact by passing through 60 percent for nonmachinable pieces; 60 percent for 3-to 5-digit non-automation nonmachinable pieces; and 70 percent for 3 to 5-digit automation nonmachinable.

[5766] The Commission has made these adjustments pursuant to the method witness Mitchell described in response to ABM/TW-1-2 (Tr. 31/10464-65).

[5767] For machinability distinctions, witness Mitchell uses the Mixed ADC non-automation machinable piece as his key rate. The Commission also uses this as its key rate. The Commission-recommended “key rate” is 43.1 cents. As an illustration of the effect of recognizing nonmachinability, the Commission notes that the recommended rate for the Mixed ADC nonautomation nonmachinable piece is 53.4 cents. (The latter rate could be viewed as a surcharge of 10.3 cents. The rate schedule expresses the differential in terms of rates.)

(5) Consistency with Statutory Criteria

[5768] The Commission has reviewed its recommendation in terms of the policies of title 39 and applicable classification criteria (factors) in 39 U.S.C. § 3623.²⁴⁴ Three factors — fairness and equity, relative value, and desirability of special classifications — bear directly on the recommended restructuring.²⁴⁵

[5769] Consistency with fairness and equity (the first factor) stems from the fact that the structural changes are part of a comprehensive, rational framework. This framework

²⁴⁴ The six statutory classification criteria are: 39 U.S.C. § 3623(c)(1) — the establishment and maintenance of a fair and equitable classification system for all mail; 39 U.S.C. § 3623(c)(2) — the relative value to the people of the kinds of mail matter entered into the postal system and the desirability and justification for special classifications and services of mail; 39 U.S.C. § 3623(c)(3) — the importance of providing classifications with extremely high degrees of reliability and speed of delivery; 39 U.S.C. § 3623(c)(4) — the importance of providing classifications which do not require a high degree of reliability and speed of delivery; 39 U.S.C. § 3623(c)(5) — the desirability of special classifications from the point of view of both the user and the Postal Service; and 39 U.S.C. § 3623(c)(6) — such other factors as the Commission may deem appropriate.

improves recognition of cost drivers, which is inherently fair to mailers. At the same time, significant steps are taken to temper rate impact. This tempering means that costs are not recognized as fully as they might otherwise be, but that negative rate impacts are not as significant as they might be. Special consideration, in the form of additional tempering, is provided for firm bundles, which experience higher than average increases under the restructuring, and are often sent by many Classroom mailers.

[5770] Worksharing activities are recognized and rewarded more appropriately, and this contributes to the fairness and equity of the schedule as well. The recommended structure also begins to recognize the cost of nonmachinable pieces, and thereby relieves other mailers of some of these costs. Some mailers with mailpieces subject to the new surcharge have practical options for altering their pieces so that they meet machinability standards.

[5771] A set of new editorial dropship discounts resolves a problem that has arisen in connection with the flat editorial pound rate and the emergence of dropshipping services. The introduction of these discounts is fair and equitable in that it does not impair the public policy of widespread dissemination of editorial matter and diversity of editorial content, and allows more mailers to dropship if they so chose. A flat editorial pound rate applies in other respects. In addition, the Commission recommends increasing the editorial per-piece discount. This advances the fairness and equity of the schedule by giving greater recognition to the feature that distinguishes Periodicals from other classes of mail. This increased benefit is equally available to all mailers in the subclass, without regard to other characteristics, such as volume, machinability, or presort level, which often affect eligibility for discounts. This is an inherently fair approach.

²⁴⁵ The Commission finds that the third and fourth factors do not pertain to any discernible extent to its recommendations. However, it is conceivable that the recommended changes, as a whole, might improve the speed and reliability of delivery. The Commission finds that the sixth factor has no discernible bearing on its restructuring recommendation.

[5772] The Commission's reasoning with respect to its evaluation of the fairness and equity of the recommended restructuring applies in large part to the second factor, relative value. The restructuring includes a significant increase in the editorial per-piece benefit. This fosters consistency of the recommendation with the second factor by providing greater recognition of the relative value to the people of the kinds of mail matter (here, Periodicals mail) entered into the postal system. The desirability and justification for special classifications is a consideration subsumed within the second factor. The Commission concludes that the benefits of linking bundle, sack, and pallet charges to presort level and entry point justifies this special classification.

[5773] The recommended changes are desirable from the perspective of both the Postal Service and mailers, and thus consistent with the fifth factor, because they better reflect the way mail is presented, processed, and delivered in today's mailing environment. This allows mailers to better determine the cost of their mailings and to make informed decisions about their use of the Nation's postal system. This is desirable because it allows mailers to change their behavior in ways that allow them to mitigate rate increases, but does not require mailers to change their behavior.

[5774] *Consistency with statutory rate criteria.* The Commission also has reviewed its recommended decision on changes in Periodicals rates in terms of the policies of title 39 and the rate criteria in 39 U.S.C. § 3622, and finds it consistent with those that are applicable. The recommended rates are the result of necessary and appropriate structural improvements. The rates that flow from the recommended rate structure are also fair and equitable. They reflect costs to a greater extent than current rates, but are tempered to avoid undue rate impact.

[5775] The rates reflect the second factor — value of the mail service to mailers — in a much more effective way than existing rates. This is because the rates send better signals to mailers, and thereby allow them to determine how best to meet their needs for delivery.

[5776] The rates exceed attributable costs by a small margin, and thus are consistent with the requirement that rates cover costs.

[5777] The rates are consistent with the fourth factor — effect on mailers (in this instance, business mailers using the Periodicals class) — because they balance cost recognition with moderation of impact. The effect on mailers is not uniform, because the recommendation involves significant de-averaging. This is not an inappropriate or irrational result, however, because the varying percentage increases reflect both variations in cost incurrence and the impact of de-averaging. This is acceptable, as it reflects mailers' use of the postal system.

[5778] The fifth factor (available alternatives) has no bearing of any significance on the development of the recommended rates. Consistency with the sixth factor (degree of mail preparation) is the hallmark of the rates. The Commission adopts the reasoning underlying its finding of consistency with fairness and equity and effect on mailers. It emphasizes that the rates mirror the way mailers prepare and present their mailings.

[5779] The recommended rates are consistent with the seventh factor (simplicity of structure and identifiable relationships) in several important respects. First, although the revised rate structure has more rate elements than the existing schedule, it is understandable because it is based on the way Periodicals mail is prepared and presented in today's environment: in mailings with a certain number of pieces, weighing a certain number of pounds, presorted in bundles, and then entered (typically) on a sack or pallet. In addition, the charges associated with these fundamental elements are logically tied to container presort level and point of entry into the postal system. Mailers are familiar with the concepts of presorting to specified levels and entering their mail at established points, so linking new bundle, sack and pallet charges to these features is a logical and straightforward adaptation of existing rate schedule features elements. Similarly, mailers generally know whether pieces in their mailings meet the Service's machinability standards prior to presentation. Thus, a rate distinction between machinable and non-machinable pieces is a simple concept.

[5780] The rates reflect the eighth factor (ECSI) in several ways. The editorial per piece benefit is increased by a significant amount over the existing level (from 7.8 cents to 9.1 cents). This reflects the fact that the presence of editorial content is the defining

feature of the class that Periodicals mailers use for the delivery of their publications. It also allows mailers in the four volume groupings addressed on this record — very small, small, medium, and large — an opportunity to receive a rate benefit for carrying editorial content. Thus, the revised schedule does not focus exclusively on efficiency measures. A new set of editorial pound dropship discounts does not interfere with the flat rate’s role in fostering the wide dissemination of editorial matter and diversity of editorial content.

3. Within County Subclass

a. Background

[5781] Cost and volume issues dominate the Within County record, although delivery service issues also emerge as a concern. The cost issue centers on substantially higher reported attributable costs, relative to the last rate case. These drive a proposed average subclass increase of 24.2 percent. This is more than two times the class-wide increase and about three times system-wide average. Moreover, it follows a rate *reduction* in the last omnibus rate case, based on much lower reported costs.

[5782] The National Newspaper Association (NNA) urges the Commission to recommend no increase whatsoever for Within County mailers, given problems it claims undermine reliance on the estimates generated by the underlying In-Office Cost System (IOCS). In the alternative, NNA urges the Commission to recommend rates based on its proposed alternative rate structure. These rates reflect a lower overall percentage increase than the Service proposes.

b. Key Features of the Postal Service’s Proposal

[5783] The Service’s Outside County restructuring proposal does not extend to the Within County subclass.²⁴⁶ USPS-T-35 at 15. Witness Tang asserts that the Service’s proposed rate design “essentially has not changed from the previously established

practice of the Commission and the Postal Service.” *Id.* at 14. Within County discounts are generally based on Outside County cost avoidance, with passthroughs Tang deems “appropriate.” The proposed Ride-Along rate of 15.5 cents applies equally to Within County and Outside County.

[5784] *Summary of participants’ positions.* The National Newspaper Association opposes the Service’s proposal, and sponsors the testimony of witnesses Heath (NNA-T-1), Sosniecki (NNA-T-2) and Siwek (NNA-T-3) in opposition. The Newspaper Association of America (NAA) endorses NNA’s position on use of witness Siwek’s pooling procedure and his proposed rate structure. NAA Brief at 46-47.

c. Key Features of the NNA Proposal

[5785] NNA witness Siwek notes that the Service reports total volume variable costs for Within County increase from \$62.8 million in FY 2004 to \$77.9 million in FY 2005, or a 24.1 percent increase. NNA-T-3 at 2-3. A review of pertinent data leads him to observe, in connection with the reported increases, that the Service’s estimates of Mail Processing and City Carrier In-Office costs for the Within County subclass in base year 2005 are suspect. He finds that

- the Within County cost increases are heavily concentrated in just two cost segments;
- these two segments account for 63.3 percent of the overall cost increase; and,
- two major sub-segments of these segments, in turn, show increases of 40.4 percent and 44.0 percent.

Id. at 3.²⁴⁷

²⁴⁶ The concern over application of the Service’s proposed container charge to certain Within County mailings is addressed in the Outside County discussion. The Commission has not accepted the proposal that gives rise to that charge and explicitly rejects the Service’s proposed application of that charge to certain mailings that contain copies of Within County mailings that pay Outside County rates.

²⁴⁷ Cost segments 3 and 6 (Clerks and Mail Handlers and City Delivery Carriers-Office, respectively). The major sub-segments referred to are the Mail Processing sub-segment and the In-Office Direct Labor sub-segment.

[5786] On a per unit basis, Siwek considers the cost increase for the Within County subclass “even more outlandish.” *Id.* In support of this conclusion, he notes that Postal Service witness Bozzo states that Within County showed the largest percentage increase in mail processing unit costs — 65 percent — overall, and 56 percent above the general increase in mail processing volume variable cost. *Id.* at 3-4. (Percentages assume use of the Service’s method, before CRA adjustments).

[5787] Siwek finds it significant that the these reported increases coincide with the Service’s implementation of a substantial IOCS Redesign Project, and that the Service nevertheless proposes to rely on its redesigned data collection survey instrument in this case. He opposes this approach on grounds that the changes were implemented without the kind of subclass-specific testing that might have indicated how the redesigned system would affect the costs of the Within County subclass. He asserts that the redesigned IOCS project resulted, in essence, in an almost totally new IOCS data collection effort. No separate tests for Within County were conducted.

[5788] Siwek also finds related tally practices flawed. He asserts that the process the Service uses does not allow the actual rate that was paid by a publication that was tallied to be determined. He also questions the currency of certain directories the Service uses. Witness Heath, a newspaper publishing executive and experienced industry trainer, bolsters Siwek’s technical observations with practical insights about how errors could intrude upon the estimating process. NNA-T-1 at 7-10.

[5789] Based on these observations, Siwek proposes that the Commission use a sample pooling technique. Specifically, Siwek proposes pooling (combining) the FY 2005 and 2006 samples to increase the IOCS sample size on which cost estimates for Within County Periodicals could be based. He characterizes the pooling technique as an adaptation of a sequential sampling method. He asserts that the sequential sampling methodology can be used for the sampling of rare populations and argues further, that since Within County Periodicals represent a relatively low-volume subclass in the In-Office Cost System, the incidence of mail in this category can be viewed as a rare event. *See* NNA-T-3 at 17.

[5790] *Revenue estimates.* Witness Heath asserts that the Service's Revenue, Piece and Weight (RPW) system produces results that do not fit small newspaper trends. He attributes this to the fact that much of this mail is entered at rural post offices where automated systems are sparse, and to the belief that sampling error has undermined the accuracy of RPW estimates for many years. He notes that the Commission has provided some relief for the Within County subclass by averaging volumes over a multi-year period, and urges it to do so again. NNA-T-1 at 12-13. NNA renews this request on brief. NNA Brief at 17-18.

d. Commission analysis

(1) Reliance on Cost and Revenue Systems

[5791] *Siwek's pooling proposal.* Witness Siwek's proposal involves sequential sampling. In this type of sampling, an initial sample is selected to determine the prevalence of an event and to estimate the sample size required to obtain a desired number of such events in the sample or to achieve a desired level of precision for related estimates. A subsequent sample is then drawn and the intended estimation and analysis for the targeted population can be facilitated by combining data from the two samples. A sequential sampling scheme should in general be accounted for in the estimation process.

[5792] The problem the Commission discerns with Siwek's proposed technique is that while the illustrations he presents for the suggested sample design provide smaller estimates of cost increases with improved precision, his pooling procedure is a misapplication of the sequential sampling methodology. Survey conditions associated with the IOCS samples are not consistent with the primary assumption imposed by sequential sampling. Sequential sampling assumes that both the initial and subsequent samples are selected from the same population and that the survey reference periods are coincidental. The IOCS samples were selected from two different populations for which there were two separate reference periods. See, NNA-T-3 at 17, Appendix B.

[5793] Moreover, Siwek's primary focus is the validity of estimates of cost increases related to Within County Periodicals between 2004 and 2005. This is significant because another critical assumption implicit in the adaptation of the sequential sampling technique he invokes is that the values of the population parameters of interest would not change during the period between the initial and second samples. The acceptance of this assumption would imply that volume variable costs for the population would be constant over the two samples, which is an implausible result.

[5794] The Commission finds that witness Heath, who has extensive professional familiarity with Within County mailing practices, convincingly points out the potential for mistakes in the Service's tally practices. However, it does not find that this overcomes reliance on the new system in the aggregate. Witnesses Siwek and Heath offer insights into why measurement error and the low precision level of the IOCS Within County estimates may have occasioned very sizable mean square errors; however, the proposed sample pooling procedure is not statistically sound and be recommended as a viable solution to the insufficient Within County sample size and imprecise estimates.

(2) Rate Design

[5795] *Siwek's rate design changes.* Siwek's alternative structure is based largely on the contention that Tang's adoption of Outside County cost avoidance estimates and her piece-pound allocation are inappropriate. The Commission does not find Siwek's position persuasive on these points. The Commission notes that Tang's design reflects a concern for rate shock at the basic sortation level. Siwek's alternative does not appear to account for this. The Commission does not find that Siwek's piece/pound adjustment is warranted.

(3) Volume Averaging

[5796] The Commission does not readily turn to the proposed volume-averaging technique as a solution to the disproportionate Within County increase the Service has

proposed, but finds that NNA has made a convincing case that the attendant relief is warranted. This approach is not without precedent, as it was used in Dockets No. R97-1 and 2000-1. The Commission appreciates the Postal Service's preference for relying on the volume estimates generated by a system that has not been shown to have significant flaws on this record. The Commission uses four-year averaging in the interest of fairness and equity. The Commission urges a management review of the Within County sampling process, given the persistent problems that arise in this subclass.

[5797] The Commission adjusts the base year 2005 volume for the Within County Periodicals class to reflect volume over the four-year period represented by FY 2002 through 2005.

(4) Within County Markup

[5798] A question of statutory interpretation has arisen in connection with the methods the Commission and Postal Service use to determine the Within County markup. Section 3626(a)(3) of title 39, U.S. Code, requires that the markup for Within County be set at one half that of "the most closely corresponding regular rate category." It also specifies the use of attributable costs in the markup calculation.

[5799] In Docket No. R2005-1, the Commission and the Postal Service used different methodologies to determine the Within County markup. In Notice of Inquiry No.1 in this case, the Commission noted that it had observed, in its Docket No. R2005-1 Opinion, that it agreed with witness Robinson's basic approach to achieving consistency with 39 U.S.C. § 3626(a)(3) (the "cost floor" provision), but applied a different definition of revenue, a different definition of costs, and different attributable cost treatment rules. NOI No. 1 (issued June 16, 2006) at 1. It explained:

Specifically, the Commission uses a total Outside County revenue figure, while the Postal Service uses a revenue figure that does not reflect the 5 percent discount given to preferred rate mail. It also uses attributable costs instead of incremental costs and, using accepted cost attribution methodology, reaches a higher level of attribution than the Service. ...

When these alternatives are used in the markup exercise, they yield results that necessarily differ from the Postal Service's.

NOI No. 1 at 1, citing PRC OP, R2005-1, para. 6113.

[5800] The Governors approved the Commission's recommended Within County Periodicals rates, but characterized the Commission's approach to estimating revenue in the underlying markup calculation as a change from previous approaches. They urged the Service, in preparing the next omnibus rate case, to review how best to estimate revenue. *Id.* at 2.

[5801] The Service's response to the Notice of Inquiry expresses its position that that Congress intended the Within County markup to be based on Regular Rate and that the markup before discounts most closely approximates the markup of Regular Rate. NNA, based on reference to professional accounting standards, asserts that the use of undiscounted revenue in the markup calculation is an accounting error. It also argues that using gross revenue to calculate the markup essentially allows the Service to recoup some of the discount the statute intended for Within County by raising its markup.²⁴⁸

[5802] *Commission conclusion.* Resolution of this issue turns on interpretation of a point not clearly addressed in the statute. The Commission appreciates the Service's perspective. At the same time, in the absence of any clear legislative direction, NNA's response to NOI No. 1 provides additional support for using the approach the Commission employed in Docket No. R2005-1. The Commission concludes that use of total revenue before application of the 5 percent discount is a more appropriate approach to the determination of the Within County markup. In line with established practice, the Commission also uses attributable costs instead of incremental costs. The result is a slightly lower markup than would result from the use of the Postal Service's method. The cost coverage for the Outside County subclass is 100.2. The cost coverage for Within County is 100.1.

²⁴⁸ Response of United States Postal Service to Notice of Inquiry No. 1, June 16, 2006; Response of the National Newspaper Association to the Commission's Notice of Inquiry No. 1, June 16, 2006.

(5) Delivery Service

[5803] In recent cases, concern over the speed and reliability of service received by Within County publications has tended to focus on delayed delivery of newspapers sent to subscribers that live quite a distance from the county of publication. NNA witness Sosniecki provides a useful perspective on the much broader service concerns in this subclass. His testimony highlights the special service challenges that newspapers on or near a county line face. It also documents the considerable worksharing Within County publishers perform to obtain delivery service through the postal network. NNA-T-2 at 7-11.

[5804] The Commission acknowledges the efforts that Within County publishers undertake prior to presenting their mailings to the Postal Service. As Soskniecki indicates, this can now extend not only to traditional efforts, such as presorting, but to using CASS-certified software and making several runs to different post offices. The Service's intended Network Redesign may further complicate Within County mailers' interaction with the Postal Service. The Commission urges the Postal Service to encourage its managers in the field to find ways to prevent service delays and inconsistencies and to effectively assist publishers who bring persistent service problems to their attention. Generally, all subscribers to Periodicals publications desire speedy, reliable and consistent delivery. However, witness Sosniecki's testimony shows that subscribers to Within County publications have service needs that differ somewhat from those who subscribe to monthly or quarterly publications. The Commission urges the Service to bear these needs in mind as it proceeds with Network Redesign.

(6) Commission Recommendation

[5805] The Commission follows the Postal Service's rate design methodology for the Within County subclass with two exceptions. First, the volume forecast has been adjusted, in line with adoption of NNA's suggestion that four-year averaging be used to address cost and volume inconsistencies. The basis for the forecast volumes is an

average of the volumes from fiscal years 2002 through 2005. The following table summarizes these adjustments.

Table V-6
Within County Subclass
Volume Forecast Comparison

	USPS (000)	PRC
Test Year Before Rates	722,431	749,766
Test Year After Rates	700,140	731,966

[5806] The second adjustment corrects the Postal Service's cost attribution methodology process. These changes result in a somewhat lower overall increase than proposed by the Postal Service. The Service's proposal would result in an overall increase of 24.2 percent for Within County mail. The Commission-recommended rates result in an overall increase of 18.3 percent for the subclass.

[5807] *Consistency with statutory rate and classification criteria.* The Commission has reviewed the criteria applicable to its Within County recommendation. The recommended rates are fair and equitable, cover attributable costs, and provide the contribution to institutional cost required by the Act.

E. Package Services Mail

[5808] Package Services Mail contains four subclasses: Parcel Post, Bound Printed Matter, Media Mail, and Library Mail. These subclasses share common traits including: none is sealed against postal inspection; none receives preferential handling or transportation; and generally, each consists of parcels containing merchandise, although heavier catalogs and directories may also be mailed as Package Services mail.

1. Parcel Post

a. Introduction

[5809] Parcel Post mail consists of any mailable matter that is not required to be mailed or entered as First-Class Mail or Periodicals.²⁴⁹ Thus, any Package Services matter is eligible to be mailed at Parcel Post rates. Parcel Post, the only subclass available for mailing pieces measuring over 108 inches in length and girth combined, may not exceed 70 pounds or 130 inches in combined length and girth. Parcel Post in excess of 108 inches in length and girth combined are charged the oversized rate.

[5810] The current Parcel Post rate structure is based on weight, distance from origin to destination, mail preparation requirements, and machinability. It consists of the following rate categories:

- Intra-BMC and Inter-BMC, which the Postal Service refers to as retail rate categories. USPS-T-37 at 1.²⁵⁰ Intra-BMC rates are applicable to Parcel Post originating and destinating in: (1) the service area covered

²⁴⁹ Under certain circumstances, Periodicals may be mailed as Package Services mail. Sample copies of authorized publications may be attached to or enclosed with merchandise mailed at Parcel Post rates. In addition, nonsubscriber or nonrequester copies over the 10 percent annual limit of the total copies mailed to subscribers or requesters are subject to, among others things, the appropriate Package Services rate.

²⁵⁰ Notwithstanding the retail label, witness Kiefer notes that a non-trivial amount of commercial mail is mailed at Intra- and Inter-BMC rates. Tr. 8/2162-63.

by the same BMC or Associate Service Facility (ASF), (2) the same state of Alaska or Hawaii, and (3) the territory of Puerto Rico. Inter-BMC rates apply to Parcel Post originating in the service area of a BMC or ASF, in Alaska, Hawaii, or Puerto Rico and destinating outside the area, state, or territory.

- Three destination entry classifications, collectively labeled Parcel Select, as follows: Destination Bulk Mail Center (DBMC), Destination Sectional Center Facility (DSCF), and Destination Delivery Unit (DDU). These rate categories provide destination entry discounts for Parcel Post mailings of 50 or more pieces, prepared as specified by the Postal Service, and addressed for delivery within the applicable destination service area, *e.g.*, DBMC, DSCF, or DDU. *See* DMCS §§ 521.23–26.
- Two rate categories, collectively labeled Parcel Return Services (PRS), designed to facilitate the return of merchandise by a retail customer to a merchant. The two rate categories, Return Bulk Mail Center (RBMC) and Return Delivery Unit (RDU), provide workshare discounts to the merchant (or an agent) for retrieving returned parcels at a designated delivery unit or bulk mail center. *Id.* at §§ 521.27–28.

b. Postal Service Proposal

[5811] Witness Kiefer develops the Postal Service’s proposed Parcel Post rates relying on, among other things, the revenue targets and projection of fees provided by witness O’Hara (USPS-T-31), and cost estimates furnished by witnesses Miller (USPS-T-21) and Mayes (USPS-T-25). USPS-T-37 at 1. The proposed rates were expected to produce an average increase of 13.8 percent, with corresponding cost coverage of 115.2 percent. *Id.* at 3. Taking into account mail mix changes, growth in Parcel Return Service volumes, and the effects of migrating Priority Mail (due to dim-weighting), the proposed rates generate a per-piece Parcel Post revenue increase of 17.4 percent. *Id.* at 22. By rate category, the average rate increase is as follows: Intra-BMC 17.7 percent, Inter-BMC 13.1 percent, DBMC 15.9 percent, DSCF 16.3 percent, DDU 11.2 percent, Parcel Return RBMC 12.0 percent, and RDU 9.1 percent. *Id.* at 3. On an aggregate basis, Parcel Post retail rates, Intra-BMC and Inter-BMC, increase by 15.2 percent, Parcel Select rates increase by 12.0 percent, and PRS rates increase by 10.7 percent. *Id.*

[5812] Witness Kiefer proposes to maintain the method for computing the rate design, except for two relatively minor changes. First, he proposes to require all DBMC machinable parcels to be barcoded. Second, he proposes to increase the balloon rate from 15 to 20 pounds. Generally, consistent with previous rate cases, witness Kiefer develops rates independently for Inter-BMC, Intra-BMC, DBMC, DSCF, and DDU. Parcel Return Service rates (RDU and RBMC) are based on the benchmark rates (Intra-BMC) less a portion of the avoided cost savings per piece. *Id.* at 8-13.

[5813] Kiefer begins the rate design process by developing preliminary rates for each rate category using a per-piece component and a per-pound component varying by zone to recover volume-variable costs. He applies a uniform factor to all piece-related and weight-related charges to make a contribution to institutional costs. He also uses transportation costs developed by witness Mayes (USPS-T-25) and processing costs developed by witness Miller (USPS-T-21).

[5814] Upon review, Kiefer found that the preliminary rates produced, for some weight and zone combinations, excessive increases over current rates. Accordingly, following past practices, Kiefer then applies constraints to mitigate the impact of rate changes. *Id.* at 17. The constraints include maximum increase and decrease caps, intra-subclass and inter-class rate relationships, zoning factors, and rate adjustment factors. *Id.* at 17-18.

c. Proposed Classification Changes

(1) DBMC Barcode

[5815] Witness Kiefer proposes to require all DBMC machinable parcels to be barcoded, with the cost savings from barcoding reflected in the DBMC rates. Currently, mailers may barcode DBMC machinable mail and receive a per-piece barcode discount. Under the proposal, any DBMC machinable piece without the appropriate barcode would be charged the corresponding Intra-BMC rate. A barcode discount will remain available for Inter-BMC and Intra-BMC mail. *Id.* at 7.

[5816] *Commission analysis.* The proposed change simplifies the acceptance of DBMC parcels. The mail processing cost savings are reflected directly in the DBMC rate. No party opposes this proposed change. The Commission finds it to be reasonable and recommends it.

(2) Balloon Rate

[5817] The balloon rate applies to Parcel Post pieces weighing less than 15 pounds and measuring more than 84 inches, but less than 108 inches, in length and girth combined. Consistent with a similar Priority Mail classification change, witness Kiefer proposes to increase the weight for balloon rate pieces from 15 pounds to 20 pounds. *Id.* at 7, 13. Under the proposal, balloon-rated pieces would pay the applicable 20 pound Parcel Post rate. *Id.*

[5818] *Commission analysis.* The current Parcel Post balloon rate has not been changed since Docket No. R97-1. No party opposes the proposal. As discussed previously regarding a similar change in Priority Mail, increasing the balloon rate will bring the Postal Service more in-line with other carriers' oversized parcel rates. The Commission recommends the proposed classification change.

d. Rate Design

[5819] The Commission's consideration of Parcel Post rates is colored by two overarching issues. First, the Postal Accountability and Enhancement Act (PAEA), Pub. L. 109-435, changes the postal rate-setting landscape by, among other things, creating a competitive class of products that includes bulk parcel post. See 39 U.S.C. § 3631.

[5820] Second, Parcel Post rate categories have significantly different cost characteristics and price elasticities, with Intra- and Inter-BMC, the retail rate categories, at -0.37 and Parcel Select, the destination entry categories, at -1.4. To paraphrase witness Panzar (Tr. 26/9259), the question is why are these rate categories in the same

subclass. Plainly, retail and Parcel Select rate categories need to be separated into two subclasses, a result mandated under the PAEA.

[5821] Of more immediate concern, however, the lack of homogeneous elasticities precludes, for all practical purposes, using Efficient Component Pricing to design Parcel Post rates. Without a rational economic alternative to design rates, the Commission's options are somewhat limited. As the discussion below makes clear, the Postal Service's proposed Parcel Post rates are more a product of the rate analyst's judgments than application of any coherent economic theory. The rates are heavily constrained to mitigate the impact of excessive rate changes. Although this is not an inappropriate objective, it would be preferable if Parcel Post rates tracked costs more closely, a goal that may assume greater importance given the split of Parcel Post into competitive and market dominant products. The Commission sees no benefit in imposing different constraints, particularly when the result may roil the markets in unintended or unforeseen ways. Thus, the Commission concludes that it has little choice in this proceeding but to use the Postal Service's rate design, modifying it where appropriate to achieve efficiencies. Should the Postal Service file another rate request with the Commission, it should bifurcate Parcel Post into two subclasses with rates for each developed independently based on the relevant costs of service and demand characteristics. *See also* PSA Brief at 8.

(1) Markup of Transportation Costs

[5822] In developing proposed Parcel Post rates, witness Kiefer utilizes estimated transportation costs provided by witness Mayes for Intra-BMC, Inter-BMC, and Parcel Select rate categories. USPS-T-25 at 9-15. To develop the per-pound component of the rates for each rate category by rate cell, he proportionally marks up the sum of estimated transportation costs, weight-related non-transportation costs, and excess balloon costs.

[5823] UPS, through witness Luciani (UPS-T-2 at 3-6), criticizes this approach, contending that it improperly marks up estimated transportation cost avoidances used to

develop proposed worksharing rates. UPS Brief at 28.²⁵¹ The result, UPS contends, is inconsistent with Commission precedent, yields rate differentials in excess of avoided costs, and is inconsistent with Efficient Component Pricing. *Id.* UPS urges the Commission to reject the Postal Service's rate design and to reaffirm the approach adopted in Docket No. R97-1. *Id.* at 28-29.

[5824] The Postal Service and PSA submitted testimony in rebuttal to witness Luciani's proposal. Like witness Luciani, PSA witness Glick (PSA-RT-1) generally endorses Efficient Component Pricing. However, he contends that Parcel Post is unique, warranting a departure from the rule. PSA-RT-1 at 3. He notes that the own-price elasticity for non-destination entry Parcel Post, -0.374, is substantially different from that for Parcel Select, -1.399. In addition, he contends that the cross-price elasticity between non-destination entry Parcel Post (the retail rate categories) and Parcel Select is minimal, at best. Consequently, citing the differences in demand characteristics, he argues that the Postal Service's practice of marking up transportation cost differences is reasonable. *Id.* at 3-5.

[5825] Additionally, witness Glick cites witness Panzar's testimony (Tr. 26/9259-61) that, given the significant difference in elasticities, the inverse elasticity rule would apply in lieu of Efficient Component Pricing and that the markup on workshared mail would be less. PSA-RT-1 at 5-6. Lastly, witness Glick argues, based largely on the same data used by witness Luciani, that the implicit markup on Parcel Select substantially exceeds that on non-destination entry Parcel Post, 27 percent versus 12 percent. PSA-RT-1 at 5-6; *see also* PSA Brief at 5-9.

[5826] On behalf of the Postal Service, witness Kiefer contends that witness Luciani's proposal is based on a flawed understanding of the Postal Service's Parcel Post cost data. USPS-RT-11 at 11. He argues that witness Luciani errs in

²⁵¹ Luciani advocates that Parcel Select rates be developed by marking up Inter-BMC transportation costs and deducting the transportation cost differences corresponding to each rate category. He characterizes these transportation cost differences as avoided costs. UPS-T-2 at 3-6. Luciani's criticism appears to be limited to the transportation costs. However, as noted, Kiefer's development of the per-pound component includes more than just transportation costs.

characterizing transportation cost differences among Parcel Post rate categories as worksharing cost differences. Kiefer asserts that although the rate categories reflect different levels of worksharing, they are not pure worksharing categories for transportation purposes. Thus, while he defends the cost estimates, Kiefer argues that they do not control for differences in mail that use non-destination entry Parcel Post and Parcel Select rate categories. He states that the estimated rate category transportation costs developed by witness Mayes reflect different mail mixes, *i.e.*, differences in size, weight, and distance transported, that preclude treating transportation cost differences between categories as simply worksharing cost differences. He also contends that zone designations, at least for Inter-BMC, Intra-BMC, and DBMC, can not be directly compared due to differences in distance between origin facility and destination office. *Id.* at 11-13. Lastly, although recognizing that there may be some avoided costs in the transportation cost differences, Kiefer asserts that the avoided costs can not be reliably estimated. Therefore, he concludes the Postal Service methodology provides a reasonable way to address differences among Parcel Post rate categories. *Id.* at 14.

[5827] *Commission analysis.* At its core, witness Luciani's proposal is premised on applying ECP principles to develop Parcel Post rates. Witness Glick endorses ECP in concept, but argues that the disparate elasticities between retail and destination entry Parcel Post preclude applying it to this subclass. As discussed below, the Commission finds that the lack of homogeneous elasticities make full adherence to ECP in this instance inappropriate.

[5828] In considering the Postal Service's proposed rates, including those for Parcel Post, the Commission begins with the premise that rate differences should equal cost differences. Thus, the Commission applied ECP principles to develop preliminary Parcel Post rates. On review, these preliminary rates generated very substantial rate changes. The Commission also found that even with the application of certain constraints, the Parcel Post rates remained problematic in some respects. Nonetheless, the Commission may have opted to recommend constrained ECP rates, but for two overriding factors.

[5829] First, as noted, the PAEA identifies “bulk parcel post” as a competitive postal service. 39 U.S.C. § 3631. Given this impending change, the Commission is not persuaded that redesigning Parcel Post rates at this stage is appropriate or in the best interests of all stakeholders.

[5830] Second, and more importantly, the Commission is mindful of witness Panzar’s comment, as emphasized by PSA, that significant differences in price elasticity and the absence of cross-price elasticity between products (rate categories) militate against use of ECP and support greater reliance on demand characteristics in setting the markup. Tr. 26/9258-62; PSA Brief at 5-9. Because the subclass does not exhibit homogeneous elasticities, with retail categories at -0.37 and Parcel Select at -1.4, marking up Inter-BMC transportation costs, as witness Luciani proposes, would be inappropriate.²⁵²

[5831] Since these rate categories remain in the same subclass and with no record on which to recommend separate subclasses, the Commission’s recommended rates largely follow the Postal Service’s rate design, with workshare discounts generally based on passthroughs of 100 percent of the cost savings to better achieve productive efficiencies.²⁵³

²⁵² Given this conclusion, the Commission finds it unnecessary to address the merits of witness Kiefer’s arguments that the transportation cost differences between non-destination entry Parcel Post and Parcel Select can not simply be equated with worksharing cost avoidances.

²⁵³ As witness Luciani notes, in Docket No. R97-1 the Commission did not apply a markup to transportation cost differences. He acknowledges that in Docket No. R2000-1 the Commission employed the same methodology as used by the Postal Service in this proceeding, but discounts any precedential implications, arguing that the Commission did not address the issue and, moreover, its use of that method may have been inadvertent. *Id.* at 4-5. Although perhaps it should have been accomplished less obliquely than in workpapers, the Commission’s change in methodology in Docket No. R2000-1 was not inadvertent. As discussed above, under the circumstances in this proceeding, the Commission elects not to adopt Luciani’s proposal.

(2) Rate Categories

[5832] *Inter-BMC and Intra-BMC.* Witness Kiefer develops preliminary Inter-BMC rates by summing the Inter-BMC pound charges and the benchmark per-piece charge. Preliminary Intra-BMC rates are developed by summing the Intra-BMC per-pound charges and the benchmark per-piece charge minus the Intra-BMC/Inter-BMC per-piece cost differential.

[5833] To develop proposed rates, Kiefer employs several constraints applied to the preliminary rates. He applies a 30 percent maximum increase to both Inter-BMC and Intra-BMC rates; these rates are also subject to a maximum decrease constraint. In addition, Inter-BMC rates are subject to zoning factors and are set to be at least 10 cents below the corresponding Priority Mail rate.²⁵⁴ Intra-BMC rates are also developed subject to zoning factors and a 50 percent rate adjustment factor.²⁵⁵ In addition, Intra-BMC rates are set to be at least 5 cents below the corresponding Inter-BMC rate.

[5834] Witness Kiefer's proposed Inter-BMC rates also reflect a volume adjustment to account for the volume migrating from Priority Mail to avoid Priority Mail dim-weight pricing, a classification change proposed by witness Scherer in this docket. For test year purposes, witness Kiefer assumes that 877,033 pieces will migrate from Priority Mail to Inter-BMC due to this proposal. No party contests this estimate.²⁵⁶

[5835] Under the Postal Service's proposal, Intra-BMC rates increase on average by 17.7 percent. Proposed Inter-BMC rates increase on average by 13.1 percent.

²⁵⁴ The zoning factor is applied to the preliminary rate for each rate in that zone. For example, a zoning factor of 0.9 would decrease the preliminary rate of that zone to 90 percent of the preliminary rate value. In the case of Intra-BMC, Kiefer points out that not applying a zoning factor would result in rates that do not differentiate for each weight between Zones 1 & 2 and Zone 5, which would make it cheaper for mailers to use Intra-BMC as opposed to DBMC in some cases. The zoning factors and the rate adjustment factor mentioned above, are used to avoid anomalous rate increases in some rate cells, and also to retain reasonable rate relationships between rate cells while allowing for a more gradual transition in the direction suggested by the preliminary rates. See USPS-T-37 at 17-18.

²⁵⁵ The 50 percent rate adjustment factor reduces the preliminary rate increase by 50 percent in each rate cell.

²⁵⁶ Pursuant to the Commission's Priority Mail recommendation, this figure becomes 902,323.

[5836] *Commission analysis.* Recommended Intra-BMC rates increase on average by 24.1 percent. Recommended Inter-BMC rates increase on average by 13.3 percent. The recommended rates were developed using the Commission's costing methodology to calculate the worksharing cost avoidances. Witness Kiefer's proposed rates are based on cost avoidance figures from witness Miller that were corrected subsequent to the filing of Kiefer's testimony. Miller's original cost data, used by Kiefer, contained incorrect piggyback factors for certain parcel processing operations. See USPS-LR-L-46, Addendum. Kiefer did not modify his proposed rates to reflect the corrected data contending that the proposed rates continue to be reasonable. Tr. 8/2093.

[5837] *Parcel Select.* Kiefer develops preliminary Parcel Select rates by summing the respective pound charges (DBMC, DSCF, and DDU) and the benchmark per-piece charge (a non-discounted machinable Inter-BMC mailpiece) less the related cost differentials provided by witness Miller (USPS-T-21). Rejecting that outcome, Kiefer develops his proposed Parcel Select rates by constraining his preliminary rates, applying both a 20 percent maximum rate cap and differing rate adjustment factors, specifically 90 percent for DDU, 65 percent for DSCF, and 45 percent for DBMC.

[5838] At the Postal Service's proposed rates, DBMC rates increase on average by 15.9 percent; DSCF rates increase on average by 16.3 percent; and DDU rates increase on average by 11.2 percent.

[5839] *Commission analysis.* Based on the Commission's test year costs, the recommended Parcel Select rates increase on average as follows: DBMC 15.5 percent, DSCF 16.6 percent, and DDU 8.8 percent. The Commission's recommended Parcel Select rates vary from the Postal Service's proposed rates for the reasons noted above regarding Intra- and Inter-BMC rates.

[5840] PSA witness Finley argues that the Commission should, when considering the Postal Service's proposed DBMC rates, take into account increased mailer costs plus cost savings accruing to the Postal Service from the rollout of the Evolutionary Network Development (END) initiative in the test year. PSA-T-1 at 5-6; PSA Brief at

14-15. UPS witness Luciani appears to make a related claim, although he suggests that the END initiative is likely to result in reduced dropship worksharing cost avoidances. UPS-T-2 at 20.

[5841] On brief, the Postal Service asserts that the impact of END in the test year is unknown, stating that there is no evidence regarding END test year cost savings. Furthermore, it argues that neither this record nor that in Docket No. N2006-1 provides any guidance on the issue. Finally, it adds that mailers' costs are not relevant to the development of dropship discounts. Postal Service Brief at 330.

[5842] The Commission agrees that the test year effects of END are unknown. Thus, there is no basis on which the Commission could reasonably consider them for ratemaking purposes.

[5843] *Per-piece savings passthroughs.* Postal Service witness Miller (USPS-T-21) calculates mail processing cost avoidances for the Parcel Post rate categories. See USPS-LR-L-46. Witness Kiefer, based on Miller's cost avoidance estimates, develops preliminary Parcel Select rates which reflect a passthrough of 100 percent of the per-piece cost differences between rate categories. See USPS-LR-L-82.

[5844] UPS witness Luciani takes issue with several of witness Miller's cost estimates and, based on concerns about the accuracy of the underlying data, proposes to reduce the passthrough to 90 percent. UPS-T-2 at 7-15. He challenges the data underlying the cost model used to develop Parcel Post mail processing costs as suspect and of questionable validity. Among other things, Luciani cites Kiefer's use of data that are more than 20 years old used to estimate parcel sortation costs at the DDU, notwithstanding that no destination rate categories then existed. He also notes that BMC data from 1996 are used for cross-docking operations, unloading productivities, and arrival and dispatch profiles. *Id.* at 7-9; *see also* UPS Brief at 19-21.

[5845] Second, Luciani criticizes the use of a "CRA Proportional Adjustment Factor" to true up modeled costs with cost data from the Cost and Revenue Analysis (CRA), contending that the size of the adjustment (in percentage terms) and the frequency with

which it has been modified suggest fundamental flaws in the Parcel Post mail processing cost model. UPS-T-2 at 9-11; UPS Brief at 23-24.

[5846] Finally, Luciani argues that the prolific application of constraints to the Postal Service's preliminary Parcel Post rates is indicative that something must be wrong with the model. He argues that the constraints produce proposed rates that differ significantly from preliminary (unconstrained) rates, resulting in different per-piece contributions by rate category. UPS-T-2 at 12-13; UPS Brief at 24.

[5847] Given these concerns with the Postal Service's Parcel Post cost model, Luciani suggests that mail processing passthroughs be reduced to 90 percent of the worksharing cost avoidances.²⁵⁷ UPS-T-2 at 18-20; UPS Brief at 25-26. Luciani proposes that the 90 percent passthrough would be coupled with his proposal (discussed below) to change the CRA Proportional Adjustment Factor based on modifying the modeled DDU sortation costs from 10.7 cents to 24 cents. UPS-T-2 at 14.

[5848] Postal Service rebuttal witness Miller argues that Luciani's concerns about the modeled cost data are insufficient to justify lowering the mail processing passthroughs. USPS-RT-8 at 20-29. At the outset, witness Miller notes that witness Luciani did not conduct any studies which invalidate any of the cost model inputs. Moreover, he notes Luciani's agreement that the age of the study alone does not invalidate its results. *Id.* at 21. Witness Miller then examines the inputs criticized by witness Luciani, concluding that: (a) any changes in mail processing operations that may have occurred since the inputs were derived do not mean that reducing the passthroughs is appropriate, (b) the operations have not changed substantially, or (c) the change has not had a material effect on the cost model. See Postal Service Brief at 336-37. Witness Miller concludes that none of witness Luciani's concerns is well founded.

²⁵⁷ In the alternative, he suggests eliminating the CRA Proportional Adjustment Factor, i.e., using the modeled cost differences without grossing them up. UPS-T-2 at 18-19.

[5849] Witness Miller asserts that CRA adjustment factors can not necessarily be used to gauge cost model accuracy. USPS-RT-8 at 27. He responds to witness Luciani's claim that revisions to the adjustment factor are indicative of cost model instability by stating that updating studies to correct errors is a sometimes necessary and accepted practice to develop a more accurate record, not a sign of model instability. *Id.* at 28.

[5850] *Commission analysis.* As a solution for issues he raises concerning the Parcel Post mail processing cost model, witness Luciani proposes to limit mail processing cost avoidances to 90 percent. This figure is drawn from Docket No. R2000-1, in which the Commission applied that percentage to DSCF and DDU mail processing cost avoidances. UPS-T-2 at 18-19.

[5851] The Commission has a strong preference for passing through 100 percent of avoided costs. This sends appropriate price signals to mailers and promotes productive efficiencies. The Commission may adopt a lesser passthrough if warranted by the facts presented, *e.g.*, based on rate impact or to employ a conservative approach regarding a new rate category. In this instance, however, the Commission is not convinced that a departure from 100 percent passthroughs is appropriate.

[5852] Witness Luciani raises a number of concerns about the efficacy of the cost model. In rebuttal, witness Miller deflects these criticisms sufficiently to blunt them. On the one hand, the Commission is sympathetic to witness Luciani's responsibilities in this case. His review of the cost model is thorough and his suggestions that the Postal Service undertake further studies are reasonable. *See* Tr. 27/9466-67, 9479. On the other hand, his expertise about postal operations is necessarily somewhat more limited than witness Miller. *Id.* at 9469-70. This comment is not intended as a criticism of witness Luciani, but rather as an indication that Postal Service witnesses enjoy a "home field advantage," i.e., they have access to facilities, data, and operational personnel not available to others. In this instance, witness Luciani's more general observations about the cost model do not overcome witness Miller's more specific comments in defense of

the model. *See, e.g.*, USPS-RT-8 at 22-23 (regarding delivery unit parcel sorting productivities and BMC unloading productivities).

[5853] *DDU sortation costs.* Witness Miller estimates that the unit cost of manual sortation to carrier route at the DDU is 10.7 cents. This estimate relies, in part, on a productivity study done on Bound Printed Matter in 1982. *See* USPS-LR-L-46.

[5854] Witness Luciani criticizes the 10.7 cents estimate, citing both the vintage of the source data, a 1982 Bound Printed Matter study, and the CRA cost, 26 cents, for manual sortation to carrier route at non-MODS offices. UPS-T-2 at 13-15. He proposes that the Commission substitute 24 cents for the 10.7 cents in the cost model, the effect of which is to reduce the CRA Proportional Adjustment Factor from 1.194 to 1.038. *See* UPS Brief at 26-27.

[5855] PSA and the Postal Service filed rebuttal testimony. For PSA, witness Glick (PSA-RT-1) argues that the change would significantly overstate the cost of DDU parcels. He contends that using the 24 cents in lieu of 10.7 cents yields a unit CRA adjusted cost for DDU parcels of 53.1 cents, compared to the Postal Service's 41.9 cents. As a point of comparison, Glick examines In-Office Cost System (IOCS) data, concluding that the comparable unit cost at non-MODS offices is 37.5 cents. In addition, he asserts that the modeled costs, as used by both the Postal Service and Luciani, inappropriately include 15.59 cents of mail processing costs that DDU parcels avoid. PSA-RT-1 at 8-9. Accordingly, witness Glick urges the Commission to reject witness Luciani's proposal. Alternatively, he suggests that, if Luciani's proposal is accepted, the Commission should "distribute the vast majority of 'fixed' costs at postal plants only to non-DDU entered parcels." *Id.* at 9; *see also* PSA Brief at 9-11.

[5856] Witness Miller, on behalf of the Postal Service, offers a different theory for rejecting Luciani's proposed modification to the cost model. In addition to stating that parcel sorting methods have not changed since 1982, Miller contends that Luciani's selective adjustment to a single cost pool is inappropriate since, in theory, if the same adjustment were applied to all pools, some DDU cost avoidance would likely increase while others would decrease. Moreover, he suggests that a more complete approach

would require that certain cost pool values be set to reflect the fact that DDU parcels do not incur certain fixed mail processing costs included in the fixed cost model. If this were done, DDU cost avoidance would increase. USPS-RT-8 at 29-30; *see also* Postal Service Brief at 338-39.

[5857] *Commission analysis.* The Commission declines to adopt Luciani's proposed adjustment. Two factors weigh heavily in this decision. First, the age of the study, by itself, does not nullify the study results. Witness Luciani concedes this point. Tr. 27/9429. Miller testifies that parcel sortation methods have not changed since 1982 and updated costs are used to estimate test year processing costs. USPS-RT-8 at 29.

[5858] Second, and more significantly, making an isolated adjustment to the cost model is necessarily somewhat arbitrary and may lead to biased results. This is not to suggest that a selective adjustment may never be appropriate. For example, if the underlying data are demonstrably wrong, correcting that error would be warranted.²⁵⁸ That is not the case here. UPS raises questions about the DDU sortations, but has not shown the figure to be in error. Furthermore, the Postal Service argues, with some validity, that adjusting a single cost pool is inappropriate since, if all cost inputs were re-examined the result would likely vary from the current model, but whether the overall result would be to increase or decrease costs can not be stated definitively. Postal Service Brief at 338. In addition, witness Miller contends that a re-examination of all cost pools would show that there are tasks in several fixed cost pools that DDU parcels would avoid. USPS-RT-8 at 29. Witness Luciani appears to recognize this fact in principle. Tr. 27/9444. The point is that the cost avoidance estimates would likely change. But, again, without examining all cost pools, one can only speculate about how that exercise might produce results that deviate from Miller's cost model results.

[5859] The Commission's decision to rely on Miller's cost model is not taken lightly. The concerns raised by Luciani, including other suggested items, are not without merit.

²⁵⁸ In fact, as discussed below, the Commission employs this approach in updating the no-fee delivery confirmation cost to incorporate more accurate data.

The Postal Service is urged to re-examine the cost model inputs and modify them as necessary to erase any lingering or potential doubts about its continuing reliability.

[5860] *No-fee Delivery Confirmation.* In Docket No. R2001-1, the Postal Service proposed and the Commission recommended that Delivery Confirmation service be available to Parcel Select mailers without payment of an additional fee. The Parcel Select rates reflect the additional Delivery Confirmation costs. In this proceeding, witness Kiefer's proposed Parcel Select rates include the no-fee Delivery Confirmation costs of 10.7 cents per piece, assuming usage by 80 percent of Parcel Select volumes. USPS-LR-L-82, "WP-ParcelPost-REVISED.xls," sheet "Inputs." Witness Kiefer states that the assumption was developed by Postal Service pricing staff after consulting with Postal Service product management staff. In addition, he acknowledges that witness Page's estimate of the no-fee Delivery Confirmation costs was not used to design Parcel Select rates. Tr. 8/2094.

[5861] Witness Luciani argues that the costs have been understated. Based on USPS-LR-L-59, he contends that the no-fee Delivery Confirmation cost per piece should be 14.67 cents. In addition, based on RPW data, he argues that 85.9 percent of the Parcel Select volume will use the service. UPS-T-2 at 16; Tr. 8/2136-37 and 2152; *see also* UPS Brief at 26-27.

[5862] On behalf of PSA, witnesses Glick and Zwieg argue that the appropriate cost for no-fee Delivery Confirmation is 11.82 cents per piece. They both assert the 14.67 cents is overstated because it includes 2.85 cents for window costs, which Parcel Select does not incur. PSA-RT-1 at 11, PSA-RT-2 at 4, *see also* PSA Brief at 18-19.

[5863] *Commission analysis.* The assumptions used by witness Kiefer have been superseded by more reliable and better data. Accordingly, in developing its recommended Parcel Select rates, the Commission utilizes a no-fee Delivery Confirmation cost of 11.89 cents and a usage factor of 85.9 percent.

[5864] *Parcel Return Service savings passthrough.* Parcel Return Service (PRS) became a permanent service following the Commission's decision in Docket No. MC2006-1. PRC Op. MC2006-1, March 3, 2006. PRS permit holders or their agents

retrieve parcels in bulk from Postal Service facilities, either a BMC or a delivery unit. As noted above, the two rate PRS categories, which coincide with these options, are: Return Bulk Mailing Center (RBMC) and Return Delivery Unit (RDU). The permit holder guarantees payment of postage and retrieval of all PRS parcels mailed with a PRS label.

[5865] Witness Kiefer develops the Postal Service's proposed PRS rates using Parcel Post Intra-BMC rates as the benchmark. Due to differences in their mail processing and transportation costs, RBMC and RDU rates are developed separately. USPS-T-37 at 10-13. The proposed rates represent an average increase of 9.1 percent for RDU parcels and 12 percent for RBMC parcels. USPS-T-37 at 3.

[5866] Kiefer proposes to passthrough cost savings of 60.9 percent and 54.2 percent for RDU and RBMC, respectively. As a point of comparison, the passthroughs under the Commission costing methodology adopted in Docket No. MC2006-1, were 47.4 percent for RDU and 49 percent for RBMC. See Docket No. MC2006-1, PRC-LR-2.

[5867] PSA and PostCom take issue with the passthrough levels. Jointly, they sponsor the testimony of witness Glick (PSA/PostCom-T-1), who, citing the Commission's decision in Docket No. MC2006-1, advocates that proposed PRS rates be reduced by 20 cents to better comport with ECP principles. PSA/PostCom-T-1 at 13-14.

[5868] PSA also sponsored the testimony of John McAlpin who provides an overview of the parcel returns market, addressing market size, common return scenarios, trends, and competitive offerings. PSA-T-2 at 2-8. He argues that PRS rates are not competitive and urges the Commission, consistent with its decision in Docket No. MC2006-1, to passthrough a greater percentage of the cost savings. *Id.* at 9; *see also* PSA Brief at 21-23.

[5869] *Commission analysis.* In Docket No. MC2006-1, the Commission concurred with PSA's comment advocating an increase in PRS passthroughs in the next rate proceeding to better comport with ECP principles. PRC Op. MC2006-1 at 14. The issue is whether the proposed PRS rates make sufficient progress in that regard.

[5870] The Postal Service did not address this proposal on brief. In his testimony, however, witness Kiefer advances two reasons for exercising caution in selecting passthrough levels. First, he notes that Intra-BMC rates are heavily constrained. Second, he states that the average weight of PRS parcels is less than that for a typical Intra-BMC parcel. USPS-T-37 at 13.

[5871] Although neither Glick nor McAlpin directly addressed Kiefer's concerns, both urge the Commission to increase passthroughs based on ECP principles. Witness McAlpin provides testimony about the competitive returns market and argues that the Postal Service has some price flexibility because passthrough levels are set at only slightly above 50 percent. PSA-T-2 at 2. The Commission is not unmindful of witness Kiefer's cautionary concerns. *See* Tr. 8/2113-14. Nonetheless, if the benchmark is flawed (due to constraints) the Postal Service (and mailers) will be better served if the underlying benchmark problems are addressed directly, to yield cost savings better approximating cost differences.

[5872] PRS, which only became a permanent service offering in March 2006, is a relatively new worksharing discount. Under the circumstances, the Commission concludes that passing through 100 percent of the estimated cost savings is impractical. Rather, the Commission will adhere to its longstanding practice of increasing cost savings passthroughs in more measured steps. Accordingly, based on the record, including a review of witness Miller's cost model, the Commission finds it appropriate to increase the cost avoidance passthroughs to 61.8 percent for RDU and 57.3 percent for RBMC. These passthroughs advance the Commission's goal of having rates reflect cost differences. However, to expand the passthroughs further is unwarranted. Further expansion would likely require a decrease in rates which has not been shown to be

justified on the record.²⁵⁹ The Postal Service is urged to continue to improve the basis on which PRS rates are developed. See Postal Service Brief at 339, n.4.

(3) Discounts

[5873] *BMC presort discount.* This discount is available to Inter-BMC Parcel Post mailings of 50 or more pieces sorted to BMC destinations (for machinable parcels) or BMC/ASF destinations (for nonmachinable parcels) as specified by the Postal Service, and entered at a facility other than a BMC. DMCS § 521.41; USPS-T-37 at 15. Witness Kiefer proposes a discount of \$0.32 for these pieces, representing a 130 percent passthrough of the savings as calculated by witness Miller. Kiefer attributes the greater than 100 percent passthrough to a desire to avoid decreasing the discount from its current level. *Id.* at 15-16.

[5874] Under the Commission's cost methodology, BMC presort cost savings equal \$0.259 per piece. The Commission recommends rounding the discount to \$0.26, effectively passing through 100 percent of the savings. In Docket No. R2001-1, the BMC Presort discount was set at \$0.28, reflecting 100 percent passthrough of the cost savings. See Docket No. R2001-1, USPS-T-33 at 19. Pursuant to the settlement in Docket No. R2005-1, it was increased to \$0.30, intending to reflect 100 percent passthrough of the estimated cost savings.

[5875] The rationale offered by witness Kiefer to increase the passthrough to 130 percent is not persuasive. That the estimated cost savings have decreased is neither a valid reason to ignore the actual savings nor an adequate justification for passing through greater than 100 percent of the estimated savings. Accordingly, the

²⁵⁹ On brief, UPS suggests that acceptance costs should be included in the PRS final adjustment. See UPS Brief at 4. Witness Miller excludes any acceptance cost savings in calculating PRS costs because the Postal Service lacks detailed PRS distribution channel information. USPS-T-21 at 4. The Commission declines to adopt UPS's suggestion due to lack of information about PRS distribution channels. In the absence of that information, the Postal Service approach is acceptable.

Commission continues the practice of passing through 100 percent of the savings to establish the BMC presort discount.

[5876] *OBMC discount.* This discount is available to Inter-BMC Parcel Post mailings of 50 or more pieces presorted to BMC destinations (for machinable parcels) or BMC/ASF destinations (for nonmachinable parcels) as specified by the Postal Service and entered at a BMC other than the DBMC. DMCS § 521.42; USPS-T-37 at 16. Based on witness Miller's estimated cost savings of \$1.18, witness Kiefer proposes an OBMC discount of \$1.30, representing a passthrough of 111 percent. Kiefer defends the greater than 100 percent passthrough as a component of the overall mitigation process. *Id.*²⁶⁰

[5877] The current OBMC discount is \$1.23. Based on the Commission's costs, the OBMC per-piece cost savings are \$1.495. The Commission recommends the OBMC discount be set at \$1.50.

[5878] *Barcode discount.* The current barcode discount, \$0.03, is available for Intra-BMC, Inter-BMC, and DBMC machinable parcels that are part of mailings of at least 50 pieces and bear a correct, readable barcode for the destination ZIP Code as specified by the Postal Service. DMCS § 521.5. Based on witness Miller's estimated cost savings of \$0.032,²⁶¹ witness Kiefer proposes to maintain the barcode discount at \$0.03 for Intra- and Inter-BMC qualifying mailings. He indicates that his "proposed discount represents as close as possible to a 100 percent passthrough of the savings." *Id.*

[5879] Using Commission costing methods, the cost savings resulting from barcoding are \$0.029. The Commission recommends adoption of the proposed \$0.03 barcode discount.

²⁶⁰ Witness Kiefer bases his OBMC discount on the cost savings figure (\$1.18) from witness Miller's unrevised worksheets in USPS-LR-L-46, workbook "Parcel Post.xls." The revised version of the worksheets calculates the cost savings to be \$1.45. USPS-LR-L-46, "Parcel Post Rev 8-2-06.xls."

²⁶¹ Kiefer bases his proposed discount on Miller's 3.2 cents estimate. Subsequently, the Postal Service revised the estimate to 2.7 cents. *Id.*

(4) Parcel Specific Rates

[5880] *Nonmachinable surcharges.* Generally, a nonmachinable surcharge applies to Parcel Post parcels weighing less than 6 ounces or more than 35 pounds, or measuring more than 34 inches long, 17 inches wide, or 17 inches high. Other criteria as specified by the Postal Service may also apply, *e.g.*, to parcels below a minimum size and parcels containing liquids. See DMCS § 521.7; DMM § 401.2.3.2. Nonmachinable surcharges are intended to reflect the additional costs of handling parcels with characteristics that make them nonmachinable, *e.g.*, due to weight, odd size, contents, or packaging.

[5881] Nonmachinable surcharges are applicable to Parcel Post pieces mailed at Intra-BMC/ASF, Inter-BMC/ASF, DSCF, or DBMC rates not meeting machinability requirements. Kiefer uses witness Miller's estimates of the following additional costs of nonmachinability: Intra-BMC \$2.47, Inter-BMC \$3.62, DSCF (3-digit) \$1.01, and DBMC \$2.18.²⁶² Witness Kiefer proposes to passthrough 100 percent of the additional costs for Inter-BMC and DSCF nonmachinable parcels, yielding proposed nonmachinable surcharges of \$3.62 and \$1.01, respectively. He proposes the same nonmachinable surcharge, \$1.85, for the Intra-BMC and DBMC based on passing through less than 100 percent of the additional costs, specifically, 75 percent for Intra-BMC and 85 percent for DBMC nonmachinable parcels. *Id.* at 14-15.

[5882] In Docket No. R2000-1, the Commission recommended nonmachinable surcharges for Intra-BMC, Inter-BMC, and DBMC parcels reflecting passthroughs of 100 percent of the additional costs. PRC Op. R2000-1, *supra*, ¶ 5836. In Docket No. R2001-1, the Postal Service proposed to passthrough less than 100 percent. Docket No. R2001-1, USPS-T-33 at 18. The Postal Service's proposed surcharges became effective pursuant to the settlement in that proceeding. In Docket No. R2005-1, the proposed nonmachinable surcharges were developed, as were most proposed rates,

²⁶² Miller's addendum presents corrected figures which witness Kiefer does not use. USPS-LR-L-46, Addendum.

simply by marking up the then-current surcharges by the across-the-board increase. Thus, as witness Kiefer notes, the current nonmachinable surcharges are not based on the relative cost differences between machinable and nonmachinable parcels. USPS-T-37 at 14.

[5883] The economically sound practice of setting these surcharges based on passing through 100 percent of the additional handling costs, which began in Docket No. R2000-1, was not followed in the last two rate cases because of settlements. The Postal Service rectifies that with respect to its proposed surcharges for Inter-BMC and DSCF parcels. Under the Commission's methodology, the additional costs for Inter-BMC and DBMC nonmachinable parcels are \$3.89 and \$0.96, respectively. The Commission recommended surcharges are set at those levels.

[5884] Witness Kiefer defends passing through less than 100 percent of the additional costs for Intra-BMC and DBMC nonmachinable parcels as necessary to maintain DBMC rates at a discount to Intra-BMC rates. *Id.* at 15. As a consequence, Kiefer proposes that each of these surcharges be set at \$1.85. The current surcharges are not identical; for DBMC, it is \$1.53; and for Intra-BMC, it is \$1.42. The rationale for having identical surcharges is not apparent.

[5885] Under the Commission's costing methodology, the extra per-piece cost associated with handling nonmachinable Intra-BMC parcels is \$2.87. The Commission's recommended surcharge is \$2.87 based 100 percent passthrough. Although this results in a large increase, passing through a lesser amount unfairly shifts the cost burden to other mailers.

[5886] Using the Commission's methodology, the estimated additional handling costs associated with DBMC nonmachinable parcels are \$2.14. The Commission recommends the DBMC surcharge be set at \$2.14.

[5887] *Oversized Parcel Post.* Parcels measuring over 108 inches in length and girth combined but not exceeding 130 inches in length and girth combined are subject to the applicable oversized rate, *i.e.*, corresponding with the applicable Parcel Post rate category. Parcel Post is the only subclass available to mail oversized pieces.

[5888] Witness Kiefer develops the proposed oversized rates in a manner similar to that used to develop rates for regular-sized parcels. He allocates transportation and weight-related nontransportation costs based on cubic foot-weight relationships provided by witness Mayes. Witness Miller supplied piece-related cost differences between regular and oversized parcels. *Id.* at 13-14.

[5889] The recommended oversized rates are developed by applying the methodology used by witness Kiefer to the Commission costs.²⁶³

e. Cost Coverage

[5890] Two parties, the Postal Service and UPS, propose the same cost coverage, 115 percent for Parcel Post. *See* USPS-T-31 at 31 and UPS-T-3 at 22. Notwithstanding this similarity, the proposals produce different effects. The Postal Service's proposal corresponds to an average rate increase of 13.2 percent, whereas UPS's proposal results in an average rate increase of 15.1 percent. USPS-T-31 at 31; UPS-T-3 at 22. The difference in the two proposals is the underlying cost methodology, with UPS witness Geddes employing the Commission's methodology from Docket No. R2000-1, as he did with respect to his Priority Mail cost coverage proposal.

[5891] The Postal Service's proposed coverage is sponsored by witness O'Hara. In reviewing the non-cost factors of the Act, he notes Parcel Post's low intrinsic value of service, due, in large part, to its lower delivery priority and reliance on ground transportation. He also comments on the economic value of service, noting that, although the price elasticity for the subclass is relatively low at approximately -1.1 in the aggregate, its component parts exhibit substantially different elasticities. For Parcel Select, the price elasticity is -1.4, whereas for Inter- and Intra-BMC rate categories, it is -0.4. USPS-T-31 at 31.

²⁶³ Parcel Post is eligible for Pickup On-Demand service. The fees for Pickup On-Demand services are developed by witness Scherer and discussed in section B.6.

[5892] Witness O'Hara asserts that, although the 13.2 percent average rate increase will have some negative effect on mailers, the above-system average increase is justified by increasing Parcel Post costs. On the other hand, he contends that private delivery firms have been able to compete at current rates and, therefore, should not be competitively disadvantaged by the proposed above-average rate increase. *Id.* at 31-32.

[5893] In commenting on available alternatives, witness O'Hara distinguishes between business mailers and the general public. He notes that business mailers may have numerous alternatives, but that individuals may have more limited choices, notwithstanding UPS's and FedEx's expanded retail presence occasioned by their purchase of Mail Boxes Etc. and Kinkos, respectively. *Id.* at 32.

[5894] With estimated test year after-rate revenues of \$1,447 million and estimated incremental costs of \$1,273 million, witness O'Hara concludes that the proposed rates satisfy factor 3, and further that the proposed rate level is fair and equitable. *Id.*

[5895] On behalf of UPS, witness Geddes proposes a Parcel Post cost coverage of 115 percent which equates to an average rate increase of 15.1 percent. UPS-T-3 at 22. Witness Geddes contends that his proposed coverage is "presumptively reasonable" because it is essentially the same as recommended by the Commission in Docket No. R2000-1. *Id.*

[5896] In support of his proposed coverage, witness Geddes challenges the notion that Parcel Post is a lower value service. He contends that a number of relatively recent changes to Parcel Post service have increased its value and justify an improvement in cost coverage. The changes in service he cites include: the growth in Parcel Post volumes, particularly the Parcel Select rate categories; the availability of carrier pickup service, which enables customers to request that a package be picked up at the time of the next day's delivery; and the advent of a new rate category, Parcel Return Service, which enables recipients to return unwanted items to merchants using a pre-paid label. *Id.* at 22-24.

[5897] On brief, PSA opposes UPS's proposed Parcel Post cost coverage. It takes issue with UPS's contention that cost coverage should be increased based on the growth

of workshared volumes since the last litigated rate case, Docket No. R2000-1. PSA Reply Brief at 3-4. PSA argues, based on a comparison between test years in Docket No. R2000-1 and this proceeding, that non-destination entry volumes have grown, but that workshared volumes have remained essentially unchanged. *Id.*

[5898] *Commission analysis.* The Commission's cost coverage for Parcel Post is approximately 114 percent. This level is generally consistent with past Commission rate recommendations but represents a not insignificant increase in the unit contribution from Parcel Post volumes. In Docket No. R97-1, unit contribution equaled 25.3 cents, based on a cost coverage of 108 percent. In that docket, the Commission recommended the Postal Service's classification change to expand Parcel Select to DSCF and DDU volumes. That became effective in January 1999. In Docket No. R2000-1, unit contribution increased substantially to 40.9 cents, reflecting a coverage of 114.9 percent. At the Commission's cost coverage, 113.9 percent, unit contribution increases to 47.4 cents, an increase over Docket No. R2000-1 of 15.9 percent.

[5899] Parcel Post has a low value of service, reflecting its non-preferential handling, surface transportation, and lack of access to collection boxes. The disparate own-price elasticities of Parcel Select, -1.40, and retail Parcel Post, -0.37, complicate pricing Parcel Post.²⁶⁴ Because these rate categories remain for the time being in a single subclass, the non-cost factors of the Act often are at war with one another. Thus, for example, although impact on competitors (factor 4) and alternatives available (factor 5) may suggest an increase in coverage, in this instance they give way to countervailing considerations.

[5900] First, the implicit cost coverage for Parcel Select appears to be relatively high, particularly as compared to non-destination entry mail. Increasing coverage to

²⁶⁴ Witness Geddes argues that Parcel Select has increased Parcel Post's intrinsic value of service, noting that it accounts for approximately 70 percent of total Parcel Post volumes. UPS-T-3 at 22-23. While this latter observation is correct, it is less than complete in two respects. In considering value of service, he does not address the significantly different own-price elasticities of Parcel Select and retail Parcel Post. Furthermore, notwithstanding Parcel Select's percentage of total Parcel Post volumes, total volumes have remained relatively flat from the test year in Docket No. R2000-1 (367.6 million in TY 2001) to the test year in Docket No. R2006-1 (369.7 million in TY 2008).

address the latter could not be accomplished without necessarily increasing Parcel Select rates above the recommended levels, a result which, given the price elasticity of Parcel Select, would adversely affect mailers and the Postal Service.

[5901] Second, while alternatives are available to commercial mailers, retail Parcel Post mailers have fewer options even considering retail stores opened by UPS and FedEx. The record does not indicate that these options are equally available to potential retail customers, especially those in rural and more remote areas. In Docket No. R2000-1, the Commission concluded:

That alternatives exist does not require the Commission to recommend rates causing the Postal Service to cede markets to competitors. See *United Parcel Service, Inc. v. United States Postal Service*, 184 F.3d 827, 845 (D.C. Cir. 1999) (“[t]he Commission has consistently, and reasonably, held that [criterion 5] authorizes a reduction in rates to maintain the position of the Postal Service as a competitor in the mail delivery industry.”) Nor is it the Commission’s role to assure market share for the Postal Service. The Commission’s role is to protect competition, not competitors. *Direct Marketing Association, Inc. v. United States Postal Service*, 778 F.2d 96, 106 (2nd Cir. 1985).

PRC Op. R2000-1, ¶ 5788.

As in that proceeding, the recommended rates are designed with that goal in mind.

[5902] Third, considering possible rate levels, the Commission is mindful of the need to strike a balance between the needs of shippers and competitors. Shipper interests highlight the “fierce competition” between the Postal Service and private delivery companies, singling out UPS. PSA Brief at 5. PSA contends that unregulated carriers have pricing advantages over the Postal Service, including using the Postal Service’s published rates to their advantage. *Id.* As a competitor, UPS urges the Commission to apply costing methods and ratemaking principles to ensure that the Postal Service’s monopoly and competitive services are fairly priced. UPS Brief at 1. Notably, UPS does not contend that the Postal Service’s proposed rates are unfair or

anti-competitive. The Commission recommends rate increases which are above the systemwide average, and take these competing interests into account.

[5903] Parcel Select service offers mailers destination entry options with the degree of worksharing determining the mailer's optimum rate category. Notwithstanding any perceived advantages Parcel Select mailers may enjoy, *e.g.*, more reliable service, they can not be achieved without cost to the mailer. The recommended rates continue to reflect these worksharing efforts (factor 6) in an effort to promote productive efficiencies.

[5904] Finally, on this record, the recommended Parcel Post rates satisfy factor 3, the requirement that they cover attributable costs and make a reasonable contribution to overhead.

2. Bound Printed Matter

a. Introduction

[5905] The Bound Printed Matter (BPM) subclass is limited to advertising, promotional, directory, or editorial material in permanently bound printed volumes, excluding stationery, which does not have the nature of personal correspondence. See DMCS § 522.1. Examples include catalogs, books, directories, manuals, and similar permanently bound volumes. USPS-T-38 at 4.

[5906] BPM pieces may weigh up to 15 pounds. The BPM rate structure is based on weight, distance from origin to destination, and mail preparation requirements. In addition, it includes a flats/parcel rate differential and a barcode discount. It consists of the following rate categories:

- Single-piece — the single-piece BPM rate is charged per half-pound from 1 pound through 5 pounds and is charged per pound for the first pound and from over 5 pounds through 15 pounds.
- Non-automation Presort — the basic presort rate applies to BPM prepared in a mailing of at least 300 pieces as specified by the Postal Service.

- Carrier Route Presort — this rate category applies to BPM prepared in a mailing of at least 300 pieces as specified by the Postal Service. Mail sent under this rate category is not eligible for a barcode discount.
- Destination Entry BPM — applies to basic presort rate or carrier route presort BPM prepared as specified by the Postal Service and entered at a (1) destination bulk mail center (DBMC), (2) destination sectional center facility (DSCF), or (3) destination delivery unit (DDU).

[5907] A barcode discount applies to single-piece rate mailings of at least 50 pieces and basic presort rate mailings of machinable parcels and automatable flats prepared as specified by the Postal Service and deposited at designated facilities. The barcode discount is not available to BPM presort carrier route or DDU mailings, or BPM DSCF parcel mailings. The rate for flats is 8 cents less than the corresponding parcel rate.

b. Postal Service Proposal

[5908] Witness Yeh presents the Postal Service's proposed BPM rates with no fundamental rate design changes. *Id.* at 3, 7; *see also* Postal Service Brief at 339. Her proposed rates yield an average increase of 11.7 percent which equates with cost coverage of 124.9 percent. USPS-T-38 at 3. In developing her proposed rates, witness Yeh relies on estimated transportation costs provided by witness Mayes (USPS-T-25) and worksharing cost savings estimates provided by witness Miller (USPS-T-21).

c. Postal Service Classification Proposals

[5909] On behalf of the Postal Service, witness Yeh proposes to restrict the availability of individuals to mail single-piece BPM. She indicates that the Postal Service will no longer offer that mailing option at retail windows. Such pieces will only be accepted at retail windows (or by a carrier) if the customer has pre-applied postage.²⁶⁵

²⁶⁵ Initially, Yeh indicated that BPM would be required to be paid by either customer-generated postage meter or by permit imprint. Window clerks would not offer retail customers BPM as a mailing option. USPS-T-38 at 6 n.2.

Witness Yeh offers two justifications for the proposal — to reduce the complexity of retail transactions and to simplify window service operations. *Id.* As related to this change, Yeh proposes to rename the Single-Piece Rate Category as Nonpresort “to clarify the Postal Service’s parcel offerings.” USPS-T-38 at 6 (footnote omitted).

[5910] Two limited participators oppose the Postal Service’s proposal. Douglas F. Carlson submitted testimony arguing that the Postal Service’s proposal violates section 403(c) of the Act by unduly discriminating against certain mail users. DFC-T-1 at 32-36. He makes similar claims on brief. Carlson Brief at § II, at 7-9.²⁶⁶

[5911] Carlson argues that customers are entitled to use services listed in the DMCS without discrimination and that management can not bar access to an approved service by decree. DFC-T-1 at 32. He asserts that PVI (postage validation imprinter) labels are the Postal Service’s standard method of postage payment for window transactions and argues that customers are entitled to obtain a PVI label for all retail transactions. In response to the Postal Service’s proposed restriction on the availability of BPM, Carlson proposes to amend DMCS § 3040 to include postage validation imprinter as an acceptable means for prepaying mail. *Id.* at 35.

[5912] On brief, limited participator David Popkin also opposes the proposed restriction on BPM. Popkin Brief at 11-14.

[5913] The Postal Service argues that concerns expressed by Carlson and Popkin are unfounded. Postal Service Reply Brief at 270. It asserts “[n]o action that the Postal Service plans to take will treat different classes of customers differently. No customers will be denied access to services.” *Id.*

[5914] In addition, the Postal Service objects to Carlson’s proposed amendment to DMCS § 3040 as unnecessary because that section already provides that other prepayment methods may be specified by the Postal Service. *Id.* at 269. Further, it

²⁶⁶ In testimony and on brief, Carlson cites section 403(b) of the Act in support of his claim of undue discrimination. His claim falls under section 403(c).

argues that this section addresses prepayment options, not the particular technology that might be used. *Id.*

[5915] *Commission analysis.* Witness Yeh claims she is not proposing a classification change. Tr. 8/1969. For this reason, neither she, nor any other Postal Service witness, addresses the classification factors of the Act. See § 3623(c). The Commission finds this is a classification change and rejects it.

[5916] The proposal would essentially eliminate an existing, often less expensive, mailing option to the general public by requiring a degree of knowledge about postal rates inconsistent with the Postal Service's public service mandate and common carrier-type obligations. Carlson makes a reasonable case that the proposal unduly discriminates against individuals.²⁶⁷ The Postal Service apparently intends to refuse to tell retail mailers that a low cost option may be available. Such a policy is duplicitous and inconsistent with the basic obligations of a public entity. In essence, the proposal is a de facto classification change that can not be accomplished absent Commission action pursuant to section 3623 of the Act. In the absence of supporting evidence from the Postal Service, the Commission will not act *sua sponte* under section 3623, concluding that the record is insufficient to adopt the proposal.

[5917] To be clear, the Commission's conclusion is not a ruling on the merits of the proposal. As Carlson notes, the Postal Service may be able to "mount a convincing case for a change to the DMCS to achieve the goal of removing BPM as an option for retail customers." DFC-T-1 at 36. However, no evidence justifying such a change has been presented to the Commission. Since it is rejecting the Postal Service's de facto

²⁶⁷ The Postal Service contends that "[n]o action that the Postal Service plans to take will treat different classes of customers differently." Postal Service Rely Brief at 270. This comment does not address the discriminatory nature of its proposal. Currently, BPM is available to mailers electing single-piece and presort rate categories. Describing those currently eligible to use the subclass as "different classes of customers" mischaracterizes the eligible users. While it may be that the Postal Service does not intend to treat "different classes of customers differently," it is the putative distinction between the users, when there is none currently, which gives rise to the impermissible discriminatory treatment.

classification proposal, the Commission finds it unnecessary to adopt Carlson's proposed amendment to DMCS § 3040.

[5918] Finally, the Commission will not adopt the Postal Service's proposal to rename the Single-Piece rate category as Nonpresort. The only rationale Yeh offers is that the change will "clarify the Postal Service's parcel offerings." USPS-T-38 at 6 (footnote omitted). The rationale is not convincing. The Postal Service intends to "clarify" its service offerings by describing the Single-Piece Rate Category in terms of what it is not, i.e., nonpresort. Equally illogically, that objective could also have been pursued by describing the Presort Rate Category in terms of what it is not, i.e., non-single piece. Single-piece connotes no ambiguity requiring clarification, a point underscored by the limited application of the proposed change. See Tr. 8/1965 (no similar change proposed in other subclasses with analogous services). Furthermore, the proposed nomenclature change appears to be little more than a stratagem related to the proposal to curtail BPM availability.

d. Intervenor Classification Proposal

[5919] Amazon.com, Inc. (Amazon) proposes to expand the content requirement to allow books published in electronic format to be mailed at non-single-piece BPM rates. See Amazon Brief at 13.²⁶⁸ As part of this proposal, Amazon proposes that the Bound Printed Matter subclass be renamed as BPM. AMZ-T-1 at 22.

[5920] In support of its proposal, Amazon sponsors the testimony of witness Haldi, who presents a comprehensive effort to justify opening a classification devoted to permanently bound printed matter to its electronic counterparts. *Id.* at 22-23. He begins, for example, with a history of the subclass and modifications to it over time, including,

²⁶⁸ As originally formulated, Amazon proposed to allow books and closely related items, including movies, which are published in electronic format to be mailed at BPM rates. AMZ-T-1 at 7-8, 53. In an alternative proposal, witness Haldi suggests revised DMCS language that would leave implementing details to the Postal Service to specify whether all or only some sound and video recordings would be eligible to be mailed. Tr. 27/9402-03.

since 2001, the mailing of non-print attachments and enclosures with BPM mail. *Id.* at 9-16; *see also* Amazon Brief at 12-14. Witness Haldi contends that Amazon's proposal will not alter the nature of the BPM subclass because video and sound recordings will be mailed as small parcels and the proposal is consistent with expanding BPM eligibility to books. *Id.* at 14-16. Amazon contends that expanding BPM eligibility to electronic media will not negatively affect either BPM, because the change "is not expected to increase the cost of BPM parcels" (*id.* at 17) or Media Mail because the consequence of migrating pieces would be *de minimis*. *Id.* at 18.

[5921] Two parties oppose Amazon's proposal. The Postal Service submitted the rebuttal testimony of James Kiefer, who argues that the record contains no evidence quantifying the financial effects of the proposal on BPM or Media Mail. USPS-RT-11 at 27-32. To buttress this claim, witness Kiefer takes issue with Haldi's assertion that pieces migrating from Media Mail will increase Postal Service contribution. Kiefer argues that the processing and delivery costs to the Postal Service for similarly presorted and entered Media Mail and BPM would be the same regardless of the subclass. *Id.* at 27-29. Further, he asserts that the proposal would increase the number of parcels mailed as BPM thereby adversely affecting unit costs since flats are less costly to process and deliver than parcels. Finally, Kiefer argues that, since witness Yeh's rate design does not fully reflect processing and delivery cost differences between flats and parcels, expanding the classification to encourage more parcels is, at the very least, premature. *Id.* at 30-31. On brief, the Postal Service argues, based on Kiefer's rebuttal testimony, that Amazon's proposal is fatally flawed. Postal Service Brief at 340-41.

[5922] The Mail Order Association of America (MOAA) also urges the Commission to reject Amazon's proposal. On brief, MOAA asserts that Amazon has not adequately demonstrated that its proposal will not adversely affect BPM's costs. It argues that the most witness Haldi can offer is that he does not anticipate that the proposal will cause BPM costs to increase. MOAA Brief at 29, citing AMZ-T-1 at 13. MOAA also endorses Kiefer's rebuttal testimony as demonstrating the inadequacy of Amazon's proposal. *Id.*

at 30-31. Finally, MOAA argues that Amazon has not met its burden of proof that its proposal is reasonable. *Id.* at 31-33.

[5923] *Commission analysis.* If Amazon's proposal to expand BPM eligibility were simply part of an academic debate, it would get high marks for creativity and debating points. Ultimately, however, Amazon is unable to overcome, in the first instance, whether the premise for its proposal is legitimate and, secondly, its inability to adequately demonstrate the cost and revenue consequences of its proposal. Accordingly, the Commission rejects it.

[5924] Amazon's proposal to cobble together electronic media with bound printed matter on the theory that they represent the same thing in different format may be commendably creative, but it is not a sound basis for classification change, and, in particular, not on an ad hoc basis. The subclass, which has been in existence since 1939, consists of bound printed matter. Matter eligible to be mailed at BPM rates must, among other things, consist of advertising, promotional, directory, or editorial matter, be securely bound by permanent fastenings, and consist of sheets of which at least 90 percent are imprinted by any process other than handwriting or typewriting with, for example, words, letters, and images. DMCS § 522.1. That books and closely-related items published in electronic media may have similar content is too tenuous a rationale to justify expansion of the subclass. Moreover, as the Postal Service notes, policing the proposal would be problematic. Postal Service Reply Brief at 266-67.

[5925] The proposal also suffers a fundamental shortcoming, namely, the cost consequences of the proposal are unknown. Although Amazon endeavors to construct an argument that videos and sound recordings mailed as parcels will not adversely impact BPM costs, its efforts are unavailing. Its witness did not analyze the effects of the proposal on costs. Tr. 27/9401; *see also* Postal Service Reply Brief at 267-68, and MOAA Brief at 28-29, 31-33. Even aside from any question about their density, that video and sound recordings may be mailed as parcels is not dispositive that BPM costs will not change. At a minimum, the new volumes may cause mail mix to change, with parcels becoming a greater percent of total BPM volumes, thus causing unit costs to rise.

See USPS-RT-11 at 29. Amazon has not demonstrated this would not occur, nor, for that matter, has it shown the likely effects of its proposal on Postal Service revenues.

[5926] Although the Commission can not recommend this proposal, it commends two aspects of it for the Postal Service's consideration. First, one of the Postal Service's responsibilities, as enumerated in section 403(b)(2) of the Act, is "to provide types of mail service to meet the needs of different categories of mail and mail users." Thus, the (understandable) self-interest that prompts a mailer's classification proposal aside, it does signal a demand for service that may merit further examination. Second, Amazon's quest for a less costly alternative to Media Mail could also be couched in terms seeking a more cost-based rate structure. To that end, and generally consistent with various proposals put forth by the Postal Service in this proceeding, shape-based classification reform would appear to address mailers' concerns and the Postal Service's responsibilities under the Act.²⁶⁹ The Commission encourages the Postal Service to continue to evaluate these issues.

e. Cost Coverage

[5927] Three parties submitted testimony addressing BPM cost coverage levels. The Postal Service proposed BPM rates are based on witness O'Hara's target cost coverage of 125 percent, a level designed to produce an average rate increase of 11.9 percent. USPS-T-31 at 32. At the Postal Service's proposed BPM rates, revenue per piece increases on average by 11.7 percent, yielding a 124.9 percent cost coverage. Witness O'Hara addresses each of the pricing factors of the Act to arrive at his suggested cost coverage. *Id.* at 32-33.

[5928] On behalf of Amazon, witness Haldi contends that the proposed BPM cost coverage is too high and should be reduced. AMZ-T-1 at 27. He advocates a cost

²⁶⁹ To elaborate briefly, segregating parcels from flats would enable the Postal Service to design rates sending appropriate price signals to mailers based on the characteristics of the mail, including, for example, weight, origin and destination, and mail preparation. See, e.g., MOAA Brief at 29.

coverage for BPM of between 113 to 114 percent. He frames his recommendation based on the coverages proposed by the Postal Service for Parcel Post, 115 percent, and for Media Mail and Library Mail, 109 percent, asserting that, in the last fully litigated case, Docket No. R2000-1, BPM's cost coverage was below that for Parcel Post but greater than that for Media Mail. *Id.* at 27-29.

[5929] In support of his proposal, witness Haldi notes that BPM qualifies for some consideration for its Educational, Cultural, Scientific, or Informational (ECSI) value (factor 8) due to the presence of books in the subclass. Since Parcel Post qualifies for no ECSI consideration and 100 percent of the content of Media Mail and Library Mail does, he suggests that BPM's cost coverage must fall somewhere between the two. *Id.* 29-32. He also asserts, based on a comparison of own-price elasticities, that the higher BPM coverage can not be justified because BPM has a lower value of service compared to retail Parcel Post. *Id.* at 32. He also cites factor 4, effect of rate increases, arguing that there is no reason to increase the coverage above that established in Docket No. R2000-1. Lastly, he cites factor 1, concluding that his proposal is fair and equitable. *Id.* at 33; *see also* Amazon Brief at 6-12.

[5930] On behalf of PostCom and MFSA (PostCom), witness Angelides employs, in conjunction with proposed new BPM rate design, a cost coverage of 114.1 percent. PostCom-T-5 at 9-11. He criticizes Postal Service witness O'Hara's failure to consider adequately two issues that indicate a lower cost coverage for BPM. First, he argues that the variability of BPM's costs in the last several years suggests that the Postal Service's data collection system may not be accurately or consistently capturing BPM's attributable costs. He notes that the Commission commented on this issue in Docket No. R2000-1. *Id.* at 10, n.6. Second, he argues that historically the coverage has been below 124.9 percent, referencing the last three omnibus rate cases. He discounts the most recent two proceedings, Docket Nos. R2001-1 and R2005-1, because they were not fully litigated, observing that in R2000-1 the Commission's cost coverage was 114 percent. Witness Angelides, therefore, employs that coverage in his rate design. *Id.* at 11; *see also* PostCom Brief at 38-40.

[5931] On brief, MOAA and the Association of American Publishers (AAP) argue that the Postal Service's proposed coverage is too high. MOAA Brief at 33; AAP Brief 1-4. AAP endorses the cost coverage proposed by witness Angelides.

[5932] *Commission analysis.* The parties criticizing the Postal Service's proposed BPM cost coverage proceed from a common starting point, namely, the Commission's decision in Docket No. R2000-1, the last fully litigated rate case. That, in itself, is unobjectionable since the subsequent rate cases were decided by settlement, which, by their own terms, have no precedential value. They argue, based on considerations of ECSI value, that because BPM's coverage in Docket No. R2000-1 was bracketed between that for Parcel Post and Media/Library Mail, it should be so in this case as well. *See, e.g.*, Amazon Brief at 9-10 and AAP Brief at 3-4.²⁷⁰ The flaw in this approach is that the parties' conclusion simply assumes that the result in Docket No. R2000-1 continues to be appropriate without an analysis of the Commission's reasoning in that proceeding.

[5933] In Docket No. R2000-1, the Commission extensively addressed the history of the BPM subclass, including opening the subclass to books (without an advertising insert) in Docket No. R90-1 and the subsequent cost and cost coverage consequences of that classification change. PRC Op. R2000-1, ¶¶ 5878-88. In Docket No. R90-1, the Commission reduced the cost coverage for BPM to approximately 146 percent due to the migration of books to the subclass. PRC Op. R90-1, ¶ 6519. Nonetheless, the Commission concluded, and reiterated the point in Docket No. R94-1, that BPM and third-class regular rate should have a generally similar markup. *Id.* at ¶ 6520; PRC Op. R94-1, ¶¶ 5388-89. In Docket No. R94-1, the Commission's cost coverage for BPM was 136.6 percent. PRC Op. R94-1, Appendix G, Schedule 1. In Docket No. R97-1, the Commission's recommended rates were likewise based on a cost coverage of approximately 136 percent. PRC Op. R97-1, ¶ 5721. Against this background, the coverage recommended in Docket No. R2000-1 is atypical, and should have caused

²⁷⁰ PostCom does not explicitly rely on ECSI considerations, but it does rely on the outcome from Docket No. R2000-1. *See* PostCom-T-5 at 11. Moreover, witness Angelides appears to have adopted the result from Docket No. R2000-1 without any analysis of the pricing criteria of the Act. *Id.*

those opposing the Postal Service's proposal in this proceeding to examine the underlying reasons for the sharp decline.

[5934] As the Commission's discussion makes clear, the cost coverage recommended for BPM was shaped, in large part, by the more than 40 percent increase in BPM unit costs from the base year in Docket No. R97-1 to the base year in Docket No. R2000-1. PRC Op. R2000-1, ¶¶ 4034-35, 5887. Specifically, the Commission observed: "The BPM rates recommended in this case will significantly reduce the relative contribution to institutional costs by BPM as a means of ameliorating the impact of the rate increase. In fact, absent the size of the current increase, a larger relative contribution would seem warranted." *Id.* at 5887. In the current proceeding, no party has suggested that BPM unit costs have increased disproportionately so as to justify a reduced coverage.²⁷¹ Plainly, simple reliance on the Commission's cost coverage from Docket No. R2000-1 carries little weight regarding an appropriate cost coverage for BPM in this proceeding.

[5935] Two additional points are worth noting briefly. Each of the parties compares the Postal Service's proposed coverage in this case with the coverage adopted by the Commission, based on the Commission's costs, in Docket No. R2000-1. Since the Commission's attributable cost levels are higher than the Postal Service's, the result is, all things equal, a lower cost coverage. Furthermore, none of the parties, Amazon excepted, offered any analysis of the various pricing factors of the Act to support their recommended coverage. Witness Haldi reviews selected non-cost factors, including value of service. He compares the own-price elasticity of BPM (-0.491) to non-destination entry Parcel Post (-0.374), contending that BPM's lower value of service does not justify increasing BPM coverage to 125 percent. AMZ-T-1 at 32. This

²⁷¹ Witness Angelides discusses variations in BPM costs over the last several years, suggesting it may portend problems with Postal Service data collection systems. PostCom-T-5 at 10. PostCom has not attempted to demonstrate that costs in this proceeding are unreliable or that BPM costs have increased disproportionately. In testimony and on brief, PostCom notes that the Commission has expressed concern over BPM unit costs. As noted above, the Commission continues to encourage the Postal Service to develop a better understanding of the cost characteristics of all mail.

comparison is not valid. Only about five percent of BPM volumes is single-piece. Thus, the appropriate own-price elasticity comparison must also consider the elasticity of Parcel Select which is -1.40. USPS-T-31 at 11.

[5936] The Commission's recommended rates represent an average rate increase of 11.7 percent, corresponding with a cost coverage of 119.4 percent. The recommended rates satisfy the requirement that they recover attributable costs and make a reasonable contribution to institutional costs (factor 3).

[5937] Several non-cost factors bear significantly on BPM's cost coverage. First, BPM's intrinsic cost coverage is low since it does not receive preferential handling or transportation. On the other hand, its own-price elasticity (-0.49) is lower (in absolute value) than all other parcel subclasses, but higher than Standard Regular, suggesting a moderate economic value of service. On balance, these considerations suggest a somewhat higher coverage than for other Package Services.

[5938] Second, since Docket No. R87-1 the Commission has given BPM ECSI consideration (factor 8) in recognition that books comprise a sizable, if unquantified, portion of BPM volumes. In this proceeding, the Commission adheres to that practice, thus moderating BPM's coverage.

[5939] In considering the effect of the above-average rate increase on mailers and competitors (factor 4), the Commission notes that no mailer complains that the proposed rates are excessive or otherwise unfair; nor does any competitor raise any issue about the proposed rate level. On the other hand, although alternatives are available (factor 5), they appear to be limited and some are simply other subclasses. See USPS-T-31 at 33.

[5940] Based upon its review of the record, the Commission concludes that its recommended rates are fair and equitable. The Commission would caution, however, that its recommended rates are at the lower bounds of the zone of reasonableness. BPM has a moderate value of service; subclass volumes have grown steadily since FY 2003. Its unit contribution dropped sharply in Docket No. R2000-1 due to unexplained, significant attributable cost increases, which, as noted above, justified a substantially lower cost coverage. In Docket No. R2001-1, the Postal Service proposed

rates, approved as a result of a settlement, that restored the unit contribution to near-previous levels. Unit contribution has slipped somewhat since then and should be re-evaluated in conjunction with any future rate request.

f. Rate Design

(1) The Postal Service's Methodology

[5941] Witness Yeh indicates that her rate design utilizes the per-piece and per-pound zoned rate structure used in recent omnibus rate cases. USPS-T-38 at 7. She develops the pound component of the proposed rates based on witness Mayes' (USPS-T-25) estimated transportation costs per pound by zone plus an additional two cents per pound allowance, representing weight-related non-transportation costs. She then marks up these combined weight-related per-pound costs by a factor that reflects both the contingency and witness O'Hara's target cost coverage to generate BPM pound charges.²⁷² *Id.* at 8.

[5942] Yeh's markups, which are portrayed as cost coverages in her workpapers, vary substantially by rate category and zone. The markup used for single-piece varies by zone from 110 percent to 165 percent, whereas for basic presort it varies from 85 percent to 165 percent. Only in Zone 8 are the factors identical. For DBMC, the markup varies from 105 percent to 115 percent; for DSCF and DDU the markups are 130 percent and 155 percent, respectively. USPS-LR-L-41, sheet WP-BPM-13.

[5943] Witness Yeh indicates that she varied her markups from the target cost coverage, 125 percent, for three reasons: to generate sufficient revenues, produce acceptable rate increases, and maintain reasonable rate relationships. Tr. 8/1982.

²⁷² In her testimony, Yeh indicates that this exercise produced preliminary pound charges for Non-automation Presort, DBMC, DSCF, and DDU rates. However, as a review of her workpapers confirms, she developed the per-pound component for all proposed BPM rates in this fashion. Furthermore, although she characterizes this exercise as producing preliminary BPM rates, her workpapers only reflect her proposed rates.

While her workpapers only reflect her proposed rates, she indicates that, absent adjustments, rates for Zones 1, 2, and 3 would have been “unacceptably high.” *Id.* Thus, for single-piece, basic presort, and carrier route presort, she reduced the markup for these zones, but increased it for the remaining zones. She reduced the markup for DBMC for similar reasons, increasing it for DSCF and DDU to recover the DBMC revenue loss. *Id.* Finally, witness Yeh substituted non-dropship Zone 5 transportation costs as a proxy for “inexplicably high” DBMC Zone 5 transportation costs to avoid an anomalous result. USPS-T-38 at 8, n.4.

[5944] To develop the per-piece charges, Yeh subtracts the transportation and nontransportation weight-related costs from total attributable BPM costs. She apportions the non-weight-related costs between single-piece and presort categories, employing a 2-to-1 ratio, as used in recent cases, of single-piece to presort unit nontransportation costs. Adjusting the unit non-weight-related costs for revenue leakages, she marks up the result by O’Hara’s 125 percent target cost coverage to yield single-piece and presort per-piece charges. *Id.* at 8.

[5945] Per-piece charges for dropshipped rates are derived by passing through varying percentages of the worksharing cost savings, and subtracting those savings from the basic presort per-piece charge. The passthroughs associated with these rates are: DBMC 100 percent, DSCF 94 percent, and DDU 85.5 percent. Tr. 8/1977.²⁷³ She cites a need to mitigate unacceptable rate increases for presort mail and a desire to maintain reasonable rate relationships in support of passing through less than 100 percent of the per-piece cost savings for DSCF and DDU. USPS-T-38 at 11; *see also* Tr. 8/1982.

[5946] Witness Yeh’s proposed flat differential is based on witness Miller’s estimate of cost segment 7 delivery cost difference, 12.7 cents, between BPM flats and parcels. Yeh proposes to passthrough 123 percent of this cost difference to arrive at her proposed flat discount of 15.6 cents for presort and 16.0 cents for single-piece rate

²⁷³ As initially filed, witness Yeh’s proposed rates reflected a lower passthrough. Errors in certain underlying cost workpapers caused those percentages to increase to the implicit levels indicated.

categories. USPS-T-38 at 8-9 and Attachment A. She indicates that passing through more than 100 percent of the delivery cost differences is in recognition of mail processing cost differences between flats and parcels. Tr. 8/1983.

[5947] PostCom witness Angelides proposes a “new rate design” for BPM, which “results in a cost coverage reduced from that proposed by the Postal Service.” PostCom-T-5 at 9. He indicates that he adjusts witness Yeh’s proposed rates by changing the markup factors in Yeh’s rate design model, asserting that this modification “keeps her rate design largely intact[.]” *Id.* at 12. On brief, PostCom makes no mention of witness Angelides’ BPM rate design proposal.

[5948] Amazon and the Postal Service criticize the proposal as unsupported and ill-conceived. Amazon Reply Brief at 6-9; Postal Service Reply Brief at 269. Both note that Angelides’ proposed rate design is substantially different from witness Yeh’s, including, among other things, proposing to vary the per-piece charge by zone. See Amazon Reply Brief at 7-8.

[5949] *Commission analysis.* Yeh’s rate design is largely a product of judgment. She applies varying proportional markups to develop per-pound charges and less than 100 percent worksharing passthroughs for DSCF and DDU to produce proposed rates that do not reflect cost differences closely.²⁷⁴ She lacks cost data by rate category. *Id.* at 11-15. These observations are not meant to suggest that costs are ignored, for they are available at the subclass level. As witness Yeh acknowledges, her proposed rates are “not solely cost-based, but cost is an element I looked into[.]” *Id.* at 2017.

[5950] Witness Yeh’s development of the flat discount is also problematic. As noted, she relies on witness Miller’s estimated delivery cost difference between flats and parcels, 12.7 cents, which she marks up by 123 percent to account for potential mail processing cost differences between flats and parcels. She indicates that mail processing cost differences were not available to her when she developed her proposed

²⁷⁴ Witness Yeh obliquely states that her passthroughs for drop-ship rates “were exogenously chosen to produce rates that are consistent with all the rate design objectives.” Tr. 8/1975; see also *id.* at 2057.

BPM rates. *Id.* at 1983. Based on record evidence, it appears that the proposed flat discount does not reasonably reflect flat/parcel cost differences. Witness Kelley (USPS-T-30) analyzes cost segments 6, 7 and 10, and estimates BPM flat/parcel delivery cost differences to be approximately 29 cents per piece. Tr. 8/1988. In addition, witness Smith (USPS-T-13) develops mail processing costs by shape, including costs for BPM flats and parcels, estimating flat/parcel mail processing cost differences of 39 cents per piece. USPS-LR-L-53. Summing these figures yields delivery and processing cost differences of approximately 68 cents per piece, which, to understate the point, is significantly different from the basis Yeh uses to develop the flat discount. See Kiefer, USPS-RT-11 at 30 (“It is clear from witness Yeh’s testimony and workpapers that her proposed flat-parcel rate differential does not fully reflect all of the combined delivery and mail processing costs differences estimated by witnesses Kelley and Smith.”) In sum, witness Yeh’s rate design likely does not produce proposed rates that will promote productive efficiency.

[5951] PostCom did not address its BPM rate design proposal on brief, an omission the Commission interprets as an abandonment of the proposal. In any event, the Commission agrees with Amazon and the Postal Service that the proposal is unsupported, unjustified, and largely unexplained. Accordingly, the Commission rejects it.

[5952] No participant directly criticizes the Postal Service’s rate design, notwithstanding its departure from costs and reliance on varying markups. Because rates should, to the extent practicable, reflect cost differences, the Commission initially designed BPM rates based on Efficient Component Pricing principles, utilizing a uniform per-piece contribution. This exercise yielded preliminary rates for certain rate categories that, in the Commission’s view, would have been excessive. For example, rate increases for DBMC mail, which represents about 37 percent of all BPM volumes, would be nearly double those proposed by the Postal Service. This impact could, in theory, be mitigated by imposing rate caps on affected weight cells. That approach, while not optimum, would represent an improvement over the Postal Service’s rate design since it

would reflect costs more closely. A lack of data, however, precluded the Commission from exercising that option. First, the Postal Service lacks volume data by weight per piece. Thus, constraints could not be reasonably employed since their revenue consequences could not be determined.

[5953] Second, the Commission also found it impractical to establish the flat discount using a greater percentage of the flat/parcel cost differences than used by witness Yeh. Basing the flat discount only on Kelley's delivery costs differences, the Commission concluded that the resulting parcel rates were, in some categories, excessive. Again, the lack of data precluded attempting to mitigate the rate impact by employing constraints. In this instance, the missing data include volume by shape and weight per piece.

[5954] Ninety-five percent of the volume in this subclass is generated by commercial mailers. Their mail is deposited according to postage mailing statements which presumably set forth clearly the basis on which the rates are calculated, e.g., total pieces, the number qualifying as flats, weight per piece, and, if applicable, the zone.²⁷⁵ See DMM §§ 705.15 and 708. Hence, the data needed to design productively efficient BPM rates appear to be readily available and easily compiled. To the extent that the Postal Service does not already collect and compile these data, it should do so. Rate design should be less reliant on the judgment of its rate analysts and more dependent on the underlying costs of service, reflecting differences in shape, weight, mail preparation, and worksharing, including dropshipping. If the Postal Service submits another request for a recommended decision for changes in rates and fees, proposed rates should, to the extent practicable, reflect differences in the cost of service.

²⁷⁵ Moreover, other than single-piece, rates for BPM mail are based on the actual weight of the piece, not on postage pounds.

(2) Discounts

[5955] *Barcode discount.* A barcode discount applies to single-piece and basic presort flats and machinable parcels that are part of a mailing of at least 50 BPM pieces that bear a correct readable barcode and are prepared as specified by the Postal Service. USPS witness Yeh proposes this discount be set at \$0.03, representing a 100 percent passthrough of the cost savings adjusted for rounding to the nearest cent. Using Commission costing methodology, the barcode cost savings per piece is \$0.029. The Commission recommends the Postal Service's proposal to set the barcode discount equal to 3 cents.

3. Media Mail and Library Mail

a. Introduction

[5956] Media Mail and Library Mail are statutorily-derived, content-restricted subclasses. The rates for both subclasses are required to be uniform for mail of the same weight and may not vary with distance. See 39 U.S.C. § 3683. Library Mail is a reduced rate subclass, with rates set, as nearly as practicable, five percent lower than the corresponding Media Mail rates. 39 U.S.C. § 3626(a)(7).

[5957] Items mailable at Media Mail rates include: books, 16-millimeter or narrower width film, printed music and test materials, sound recordings, playscripts, and manuscripts. DMCS § 523.1; see also DMM § 373.2.2 and § 473.2.2.

[5958] Eligibility to mail at library rates is restricted to qualified users and by content. Certain materials, *e.g.*, books, printed matter, sound recordings, museum materials, and teaching aids, qualify as Library Mail if mailed between schools, colleges or universities, or other eligible institutions or organizations, such as public libraries, museums, and herbaria, and various nonprofit organizations or associations, or between such organizations and their members, readers, or borrowers. DMCS §§ 524.11a and

524.13; *see also* DMM §§ 383.2.2 - 2.3 and 483.2.2 - 2.3. In addition, certain matter, *e.g.*, 16-millimeter or narrower film, sound recordings, museum materials, and scientific and mathematical kits, qualify as Library Mail if mailed to or from certain institutions or organizations, *e.g.*, schools, colleges, universities, and public libraries and to or from various nonprofit organizations or associations. DMCS §§ 524.11b and 524.14; *see also* DMM §§ 383.2.4 and 483.2.4.

[5959] Media Mail and Library mailpieces may weigh up to 70 pounds. These subclasses have three common rate categories: single-piece, basic presort, and 5-digit presort. The latter two rate categories apply to Media Mail and Library Mail prepared in a mailing of at least 300 pieces as specified by the Postal Service.

[5960] They also share a common rate structure, consisting of three tiers: 1 pound, 2-7 pounds, and 8-70 pounds, respectively. Rates are based on weight per piece and presort level. A barcode discount applies to Media and Library Mail machinable parcels included in a mailing (of Media or Library Mail) of at least 50 pieces, except it is not available to pieces mailed at the 5-digit presort rate.

b. Postal Service Proposal

[5961] Witness Yeh presents the Postal Service's proposed Media Mail and Library Mail rates. USPS-T-38 at 15-18. She does not propose any classification changes.

[5962] Witness Yeh develops rates based on witness O'Hara's target cost coverage, 109 percent. At proposed rates Media Mail average revenue per piece increases by 17.9 percent. As noted, Library Mail rates are based on a five percent discount from the corresponding Media Mail rates. At proposed rates, Library Mail average revenue per piece increases by 18.2 percent. *See* USPS-T-38, Attachment D.

c. Cost Coverage

[5963] Two parties submitted testimony addressing Media/Library Mail cost coverage levels.²⁷⁶ The Postal Service's proposed rates are based on witness O'Hara's target cost coverage of 109 percent. USPS-T-31 at 34. O'Hara's target coverage is influenced principally by three factors: the need to recover attributable costs and contribute to institutional cost recovery (factor 3); low value of service (factor 2), and ECSI value (factor 8). USPS-T-31 at 34.

[5964] Witness Angelides, on behalf of PostCom, proposes a cost coverage, in tandem with his rate design, of 100.2 percent. PostCom-T-5 at 6. He criticizes witness O'Hara's development of his target coverage for failing to consider additional matters which, witness Angelides asserts, support a lower cost coverage for Media Mail. *Id.* at 4. These matters stem from the Commission's decision in Docket No. R2005-1, specifically, concerns expressed about Media Mail's cost variability and the cost coverage set by the Commission, 100.2 percent. He employs that level in developing his proposed rates. *Id.* at 4-5. Witness Angelides does not separately address the pricing factors of the Act.

[5965] *Commission analysis.* Witness Angelides' proposed cost coverage, 100.2 percent, appears simply to be pegged to the coverage employed by the Commission in Docket No. R2005-1 without any examination of the circumstances giving rise to that level or analysis of the pricing factors of the Act. Moreover, PostCom's proposed coverage yields a unit contribution to institutional costs of \$0.0043, a *de minimis* and unjustifiably low contribution.²⁷⁷ Hence, the Commission rejects PostCom's proposal.

²⁷⁶ Cost coverages for Media Mail and Library Mail can not be developed separately because cost data for these subclasses are reported on a consolidated basis. The phrase Media/Library Mail is used herein when discussing the subclasses on a combined basis.

²⁷⁷ PostCom's suggestion that the coverages from Docket No. R2005-1 should have some precedential support is misplaced. PostCom Brief at 39-40. By their terms, neither the settlement nor the Commission's Opinion and Recommended Decision has precedential value.

[5966] Witness O'Hara's proposed 109 percent cost coverage reflects consideration of the pricing factors of the Act. At the Postal Service's proposed rates and based on the Commission's costs, the unit contribution of Media/Library Mail is almost 9 cents. Although this represents an increase over Docket No. R2005-1, it can not reasonably be characterized as excessive, either in relative terms or when compared to results in prior dockets. In Docket Nos. R90-1 through R97-1, Media Mail's unit contribution ranged between 8 and 9 cents. It dropped in Docket No. R2000-1 to about 3 cents based on a cost coverage of about 102 percent necessitated by unusual circumstances presented in that case. As a point of interest, the unit contribution spiked to about 15 cents pursuant to the settlement in Docket No. R2001-1.

[5967] Circumstances, however, do not justify adopting the Postal Service's proposed coverage. Under the Commission's costing methodology, setting the cost coverage at 109 percent would generate an excessive rate increase not warranted either by cost increases or any of the non-cost factors of the Act.

[5968] The Commission's decision to moderate coverage to 103.7 percent for Media/Library Mail is influenced by several considerations. First and foremost, the recommended rates cover attributable costs and make a reasonable, if modest, contribution to institutional costs.²⁷⁸ On a unit basis, Media/Library Mail contribute approximately 9 cents per piece to institutional cost recovery. As noted, this level is consistent with prior Commission decisions.²⁷⁹

[5969] Second, the substantially below system average cost coverage is in harmony with the historical treatment of these subclasses. Media Mail and Library Mail are content-restricted subclasses available for mailing educational, scientific, and informational materials. The Commission's cost coverage is heavily influenced by

²⁷⁸ On brief, PostCom contends that the Postal Service's cost coverage is understated because it reflects a two-cent per-pound allowance for weight-related non-transportation costs, a rate design convention long-used to set Media Mail and Library Mail rates. *Id.* at 38-39. PostCom's conclusion is not well founded since it assumes, without foundation, that none of these weight-related costs would be reflected in Media/Library Mail rates. As is the case with the development of Parcel Post rates, the weight-related non-transportation costs would likely continue to be reflected in rates even assuming a change in distributing those costs. *See* PRC Op. R2000-1, ¶¶ 5793-97.

consideration of factor 8, the educational, scientific, cultural, and informational value to the recipient.

[5970] Third, both subclasses have low intrinsic and economic value of service, factor 2. Neither Media Mail nor Library Mail receives expedited processing or transportation. Furthermore, the price elasticity for this mail is -1.2, higher in absolute value than all Package Services other than Parcel Select.

[5971] Finally, the Commission's cost coverage takes into account both factor 4, effect on mailers, and factor 5, alternatives available. Although the above-average revenue increases for Media Mail and Library Mail, 17.9 and 17.4 percent respectively, will adversely affect mailers, they are a product of increased costs. Under the circumstances, increasing the Postal Service's proposed rate level by increasing coverage would produce excessively high rates not justified by any consideration of the non-cost factors of the Act.

[5972] In sum, the Commission finds that its Media/Library Mail cost coverage of 103.7 percent satisfies section 3622(b) of the Act.

d. Rate Design

(1) Postal Service's Rate Design

[5973] Witness Yeh develops proposed rates for Media Mail and Library Mail. She notes that, as a result of Pub. L. 106-384, the cost data for these two subclasses are reported on a consolidated basis. USPS-T-38 at 16. In developing rates, she apportions

²⁷⁹ Changes in coverage levels over time appear to be largely caused by cost fluctuations. See PRC Op. R2000-1, ¶¶ 5921-23; PRC Op. R2001-1, ¶ 3200. PostCom notes these variations and the Commission's call for the Postal Service to study the situation. PostCom Brief at 38-40. It argues that the Postal Service's inability or unwillingness to address the Commission's concerns justifies a coverage of 100.2 percent. *Id.* at 40. Although the Commission continues to urge the Postal Service to address the cause of sharp, yearly cost fluctuations in all applicable situations, in this proceeding witness O'Hara expressly noted that the above-average rate increases reflect cost increases. USPS-T-31 at 34. It does not appear that any party contested this statement or otherwise challenged the accuracy of the costs reported for these subclasses.

costs and develops rate elements jointly for Media Mail and Library Mail before splitting them into separate elements for the two subclasses.

[5974] Yeh derives the per-pound component by allocating all transportation costs plus an additional two cents per pound weight-related non-transportation costs to the total number of postage pounds. To calculate the per-pound charge, she divides these costs by the total postage pounds, marking them up by 11 percent to reflect the contingency and witness O'Hara's target cost coverage.

[5975] To develop the per-piece component, witness Yeh subtracts the transportation and weight-related non-transportation costs from the total attributable cost, dividing the result by total volume. She marks up this unit cost figure by 6.5 percent, again to reflect the contingency and O'Hara's target coverage. *Id.* at 16-17.

[5976] Witness Miller (USPS-T-21) supplies cost avoidance figures. To develop the one pound piece rate element for basic presort, witness Yeh passes through 134.8 percent of the estimated per-piece cost savings. To develop the piece rate for 5-digit presort, she passes through 180 percent of the per-piece cost savings.²⁸⁰

[5977] Witness Yeh's rate design differs from those employed by the Postal Service in recent cases in one respect. In previous dockets, Postal Service rate design witnesses routinely constrained rate increases on the first pound, compensating by increasing rates on heavier weight pieces, with pieces weighing between 2 and 7 pounds increasing more than pieces weighing between 8 and 70 pounds. Witness Yeh discontinues this practice, proposing the same per-pound charge for all pieces weighing more than one pound.

[5978] Witness Yeh suggests that her above-100 percent per-piece savings passthroughs for basic presort and 5-digit presort are needed to avoid unacceptably large increases in the first pound rate cells. *Id.* at 1908-09. To offset the revenue loss

²⁸⁰ Witness Yeh initially used passthroughs of 140 percent and 170 percent, respectively, to develop these per-piece rate elements. Errors were discovered in certain Media/Library Mail costs estimates. In lieu of revising her proposed rates, witness Yeh chose to substitute the implicit passthroughs noted above. Tr. 8/1978.

from the greater than 100 percent passthroughs and the lower markup on weight-related non-transportation costs, she employs a higher markup for weight-related costs. *Id.*

[5979] Finally, to propose separate Media Mail and Library Mail rates, witness Yeh multiplies the consolidated single-piece and presort rate elements by de-averaging factors, which are based on the relative number of Media Mail and Library Mail pounds in each rate category. Library Mail rates are derived by multiplying the Media Mail rate elements by 0.95, consistent with Pub. L. 106-384. USPS-T-38 at 18.

[5980] Witness Angelides, on behalf of PostCom and MFSA (PostCom), proposes a new rate design for Media Mail (and Library Mail), based on half-pound pricing increments for pieces weighing more than one pound but less than five pounds. PostCom-T-5 at 3. As noted above, his rate design is coupled with a proposed cost coverage of 100.2 percent. *Id.* at 5. He develops his proposed first pound and additional pound rates based on “First Pound Total” cost and “Additional Pounds Total Per Pound” costs from Yeh’s testimony. He contends that his approach “leaves witness Yeh’s model rate design largely intact, but at a reduced cost coverage.” *Id.* at 8.

[5981] The Postal Service opposes PostCom’s proposed rate design in testimony and on brief. *See, e.g.*, Postal Service Brief at 342. In rebuttal testimony, witness Kiefer argues that the premise for the proposal is unsound and unsupported by cost data. USPS-RT-11 at 33-35. The proposed half-pound rate increments are predicated on the perception that the current rate (one pound) structure “can result in dissimilar packages paying the same rate.” PostCom-T-5 at 6. Kiefer responds that averaged rates are common to all classes of mail, an accepted practice causing dissimilar pieces to pay the same rates. USPS-RT-11 at 33. Kiefer also argues that witness Angelides has not shown that variations in weight within the current one pound increments have a demonstrable effect on costs. *Id.* Finally, Kiefer contends that the proposal is internally inconsistent. *Id.* at 34-35.

[5982] *Commission analysis.* The Commission will not adopt witness Angelides’ proposed rate design. First, witness Angelides’ rate design differs in many respects, not just, as he claims, due to including one-half pound rates for certain weight increments

and reducing cost coverage. For example, his proposed per-piece and per-pound rate elements are not marked up, whereas witness Yeh does use markups, employing a greater markup for the per-pound than for per-piece rate elements. Second, the design of the half-pound rates is flawed. Witness Angelides fails to provide adequate support for factors and inputs used to develop the proposed rates. Accordingly, the Commission rejects PostCom's proposed Media Mail rate design.

[5983] Notwithstanding this result, the Commission is not unsympathetic to PostCom's attempt to redesign rates. Media Mail apparently is no longer an attractive alternative for many items that meet its statutory and content restrictions. To be sure, for certain eligible pieces such as video or sound recordings destined to a distant zone, Media Mail may be the least cost alternative. That advantage may not exist for either shorter hauls or mailings in bulk. PostCom's proposal may, in some respects, be viewed as a corollary to Amazon's proposal to expand BPM eligibility to additional items that may qualify as Media Mail. As PostCom notes, half-pound rates are available in single-piece BPM.

[5984] Witness Yeh's rate design represents an improvement over those used in previous cases. The Commission commends witness Yeh's decision to discontinue the practice of constraining the one pound rates to below cost levels and offsetting the revenue loss by increasing rates for heavier weight pieces. Compared to the system average, the proposed increase on the one pound rate may, at first blush, look excessive. That comparison, however, is flawed, first, because the one pound rate has long been constrained below cost and, second, because the proposed pound rate better aligns rates with costs.

[5985] In response to this change, however, witness Yeh employs a different constraint, applying considerably greater than 100 percent passthroughs to develop proposed per-piece charges for basic and 5-digit presort rate categories. She then attempts to offset the consequences of that by applying a higher markup (cost coverage) on the per-pound element. These efforts represent a departure from designing rates based on cost differences.

[5986] As it did with other subclasses, the Commission developed preliminary Media Mail and Library Mail rates based on Efficient Component Pricing. On review, the Commission found that certain rates increased substantially, particularly the 5-digit presort first pound rate. To mitigate this rate impact, the Commission imposed a rate cap equal to the maximum increase proposed by the Postal Service, 44.4 percent.

[5987] With this modification, the Commission developed ECP rates for Media Mail and Library Mail. The Media Mail rate elements were developed in a manner similar to witness Yeh's, but with passthroughs limited to 100 percent of the cost savings. In addition, the Commission employs an equal per-piece markup in lieu of the various proportional markups used by witness Yeh.

[5988] Under this process, only the one pound 5-digit presort rate exceeded the rate cap. The Commission finds that capping the rate is reasonable, notwithstanding that it results in a lesser contribution to institutional costs by 5-digit presort than from single-piece and basic presort. Absent the cap, the resulting rate would have been significantly greater. In addition, since 5-digit presort represents only about one percent of the total Media Mail volumes, the rate cap serves to mitigate the impact on those mailers, but does not require increasing the contribution per piece from other Media Mail rate categories. The recommended Library Mail rates are calculated using the Postal Service method of multiplying the Media Mail rate elements by 0.95. This design complies with the statutory requirement that such rates be set, as nearly as practicable, five percent lower than the corresponding Media Mail rate.

(2) Discounts

[5989] *Barcode discount.* A barcode discount is available to machinable pieces paying either the single-piece or basic presort Media or Library rate if they are part of a mailing of at least 50 pieces and are entered at designated facilities. Witness Yeh proposes a barcode discount of 3 cents, which represents a 100 percent passthrough of the per-piece cost savings as calculated by the Postal Service, rounded to the nearest

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cent. USPS-T-38 at 17. Using Commission methodology, the barcode per-piece cost savings equal 2.9 cents. Consistent with the Postal Service's proposal, the Commission recommends a 3-cent barcode discount.

F. Special Services

[5990] *Introduction.* The Postal Service proposes fee and classification changes to most special services. The classification changes include proposals to:

- establish a new Address Correction Service that will rely on the Postal Automation Redirection System (PARS) to make address corrections, and to modify the name of the current “Automated Address Correction Service” to “Electronic Address Correction Service,” as those labels are presently interchangeable in the DMCS;
- restructure the fees for Post Office Box and Caller Services;
- clarify that the customer’s post office determines whether to provide carrier delivery service or Group E post office box service;
- change the current language of “license” to “permit” for consistency in the Business Reply Mail sections of the DMCS;
- modify the current language for Merchandise Return service to indicate that the use of this service is not limited to the customers of permit holders, but includes the clientele of the permit holders’ customers, and to clarify that this service can be used to send, as well as return, parcels;
- remove On-Site Meter services from the DMCS;
- restructure the calculation of postage due for forwarding Standard Mail letters and flats for which the mailer requested Electronic or Automated Address Correction Services;
- obtain a delivery scan for all items insured for \$200 or less, including current “unnumbered” items, to remove the signature requirement for items insured from \$50.01 to \$200, and to revise the pricing structure for Express Mail Insurance;
- modify the DMCS language for Collect on Delivery service to indicate that nondelivery service requires the payment of a fee;
- establish a new fee structure for Confirm that is based on a flat subscription fee and a per-scan charge rather than three subscription levels of service; and
- change the term “accounting fee” to “account maintenance fee” to more accurately reflect the service the fee is collected for.

[5991] *Special Service combination lists.* In Presiding Officer’s Information Request No. 12, Question 8, the Commission requested that the Postal Service provide

valid reasons for not including complete lists of the special service combinations for each special service in the DMCS. The Postal Service responded that specifying the allowable special service combinations in the DMCS is contrary to customer and Postal Service interests because customers rely on the DMM rather than the DMCS for allowable combinations, and mail classification cases delay future combinations from being immediately available. The Postal Service concludes that "...the DMCS is in essence a legal document..." and that "...the appropriate place to provide this information is not where a lawyer would look, but where working professionals in the mailing industry...would look,...the DMM." Tr. 19/7027-30.

[5992] The DMCS is a legal document established pursuant to subchapter II of Chapter 36 of the PRA. As such, the DMCS must be comprehensive, including special service combinations, and the DMM can not supplement it where classification information is lacking. The Commission reminds the Postal Service that the DMCS is the governing legal rate and classification schedule until rates are established according to the regulations as yet to be issued pursuant to the PAEA. Each special service section, therefore, must contain a list of all the special service combinations available for that service.

[5993] The Postal Service further contends that the special service combination lists do not need to be included in the DMCS for the Commission to maintain control over the lists, and suggests that the Commission permit the Postal Service to make classification changes without requesting a recommended decision from the Commission as required by § 3623 of the Act. *Id.* at 7030-32. The Commission, disagreeing with the Postal Service's assessment and rejecting the Service's suggestion, expects the Postal Service to propose the appropriate changes to the special service combination lists in the DMCS during the next rate case, if there is one.

[5994] *Special Services Cost Coverages.* The DMCS category structure provides a convenient framework for review of the special services cost coverages. Services that have similar functions and that, theoretically, might have similar cost coverages are grouped within categories. Any specifics that cause an individual service to diverge from

the expected cost coverage for the category are discussed. For instance, several of the proposed rate increases have been tempered by the negative effect of a rate increase upon the general public (factor 4), resulting in lower than ideal cost coverage.

[5995] Addressing (910). Addressing services, which provide the correct address information, lower the Postal Service's mail processing costs by decreasing the Postal Service's preparation of mail for delivery. Improved address hygiene allows for an efficient mailstream and justifies a low markup (factor 6). The address change service for election boards and registration commissions aids these entities in carrying out their vital function in our democracy, which justifies a low cost coverage (factor 9).

[5996] Delivery Alternatives (920). The Post Office Box and Caller Services are high value premium services that can justify high cost coverages (factor 2). In this docket, the Postal Service proposes to continue the restructuring of the Post Office Box and Caller Services rates to more accurately reflect costs (factor 3). For Post Office Box service, the Postal Service limits the movement between fee groups as well as the proposed fee increases to avoid an excessive adverse impact on post office box users (factor 4).

[5997] Payment Alternatives (930). Payment services permit mailers to pay lower rates or enable customers of certain services to have postage and other fees deducted from a trust fund every time a transaction occurs rather than making on-site payments. By providing convenience and savings to mailers, the account maintenance fee and permit fee facilitate the use of other mail services, such as Bulk Parcel Return Service and Business Reply Mail, justifying a moderate to high cost coverage (factor 2).

[5998] Accountability and Receipts (940). Services in this category enhance the underlying host mailpiece's value to the mailer and are desired by mailers for their accountability and receipt products (factor 2). For example, Restricted Delivery controls or restricts the delivery of mail to the addressee, and Certified Mail provides evidence that an item was mailed. Therefore, a higher cost coverage for these services is reasonable.

[5999] Parcel Handling (950). Parcel Airlift provides service to certain military post offices on a space available basis. Because more expeditious alternatives for sending parcels exist, Parcel Airlift has a low value of service that validates a low cost coverage (factor 2). The limited means of military personnel using this service as opposed to a more expensive and faster service also justifies a low cost coverage (factor 4).

[6000] Stamped Paper (960). The Stamped Envelopes and Stamped Cards services enable customers to purchase mailing supplies while at the post office. A higher cost coverage for stamped envelopes and cards is reasonable because the services provide convenience for customers purchasing limited quantities and saves large volume customers the expense of applying stamps to envelopes (factor 2). The justifications for a high cost coverage must be balanced, however, against the effect of the rate increase on the general public and the Commission's philosophy of maintaining these services as a low cost method to send mail (factor 4). The balancing of these factors lowers the final cost coverage of Stamped Envelopes and Cards into the low to moderate range. Because the integer rounding constraint frequently restricts the Commission in its ability to set precisely appropriate cost coverages, the resulting coverages may be above or below the target coverage.

[6001] Postal Money Orders (970). Money Order service is of high value to customers because the Postal Service's money orders are recognizable, negotiable, and of higher quality than many of the alternative money order products available (factors 2, 5). The quality of the Service's product and the availability of alternatives, which justify a high cost coverage, must be balanced against the effect of a rate increase upon the general public however (factor 4). The Commission continues to view purchasers of domestic money orders as people of modest means with a more limited access to alternative financial vehicles. Therefore, although Money Order's value of service supports a high cost coverage, the Commission's goal is for a cost coverage somewhat below the systemwide average.

[6002] *Special Services Discussion:* A discussion of each special service follows. Separate discussions on the permit fee and account maintenance fee are included. The recommended fees for special services appear in Appendix One.

1. Address Correction Service (Fee Schedule 911)

[6003] Address Correction Service provides the mailer with an addressee's correct forwarding address, if known, or a reason why the Postal Service is unable to deliver a mailpiece as addressed. Manual, electronic, and automated services are available. Manual Address Correction Service provides the mailer with a photocopy of the mailpiece along with the correct address information on Form 3547 (for First-Class Mail, Standard Mail, or Package Services), or the cover sheet of a periodical²⁸¹ with the correct address information attached on Form 3579 (for Periodicals). For the Automated Address Correction Service, clerks in the Computerized Forwarding System unit make the address correction changes and electronically send this information to the mailer. The Postal Service is proposing to modify the name of the current Automated Address Correction Service to "Electronic Address Correction Service." USPS-T-40 (Mitchum) at 7, 10.

[6004] The Postal Service proposes to add a new Address Correction Service that is automated. It suggests that the name "Automated Address Correction Service" refer to this new option. Automated Address Correction Service relies on the Postal Automation Redirection System (PARS) to process address corrections automatically. Because PARS can process only letters, letters are the sole mailpiece eligible for Automated Address Correction Service. The Service emphasizes that the addition of the Automated Address Correction Service will enhance a mailer's ability to reduce its costs by increasing address hygiene. *Id.* at 8-12.

²⁸¹ Periodicals automatically receive Manual or Electronic Address Correction Service for 60 days in conjunction with forwarding and return service.

[6005] The price of Electronic Address Correction Service will continue to be lower than the price of the manual service because the cost of the electronic service is lower. In the same vein, the Postal Service proposes a lower price for the new automated option than for the electronic service. The costs for the automated service are lower due to the lack of human intervention to provide notice to the mailer. The Postal Service hopes the lower price of the automated option will encourage mailers to use the Address Correction Service and to improve the quality of their mailing lists, which will result in more effective mailings and less undeliverable-as-addressed mail. *Id.* at 8-9.

[6006] In the past the Postal Service charged mailers the manual or electronic fee according to the type of Address Correction Service performed on that mailpiece regardless of whether the mailer requested Electronic Address Correction Service. The Postal Service proposes to charge mailers electing Electronic Address Correction Service the electronic fee even for manual correction notices. *Id.* at 8-9.

[6007] Due to the classification changes proposed in its application, the Postal Service offers a new fee structure that distinguishes fees for the electronic and automated options by mail class, with First-Class Mail having lower fees. The Postal Service proposes higher fees for the electronic or automated address correction performed on other mail classes because the cost of First-Class Mail, which includes the forwarding and returning of mailpieces, reflects some of the cost of Electronic and Automated Address Correction Service. *Id.* at 8-10.

[6008] The Postal Service proposes to decrease the fees of manual correction notices from \$0.75 to \$0.50 and electronic notices for First-Class Mail from \$0.21 to \$0.06, while increasing the cost of electronic correction notices for classes other than First-Class from \$0.21 to \$0.25. The Postal Service also offers fees for automated notices based on the class of the mailpiece and the number of notices furnished per address. For First-Class Mail, the Postal Service proposes providing the first two automated notices for a specific address for free and charging \$0.05 for each additional notice. For Standard Mail, the first two notices for an address will cost \$0.02 with additional notices costing \$0.15. *Id.* at 6.

[6009] The Flute Network suggests discontinuing the Automated Correction Service marking “Temporarily Away” on returned mailpieces because the information is useless to mailers who pay a fee for the service. Flute-T-1 at 43.

[6010] The Commission recommends the new automated option, and applauds the Postal Service for employing technological advancements to increase the value of its services. The Commission adopts the structure and fees proposed by the Postal Service for Automated Address Correction Service and calculates an overall cost coverage of 139.3 percent. The Commission suggests that the Postal Service assess its utilization of the “Temporarily Away” marking.

2. Mailing List Services (Schedule 912)

a. ZIP Coding of Mailing Lists

[6011] The ZIP Coding of Mailing Lists service helps mailers use and sort by correct ZIP Code. For multiple 5-digit ZIP Code post offices, the Postal Service sorts the mailer’s address cards by 5-digit ZIP Code, bundling the cards for each ZIP Code. One fee is charged per mailing list or set of cards. USPS-T-40 at 37.

[6012] The test year cost is \$66.33 per thousand addresses. Applying a five dollar rounding constraint, the Service proposes increasing the current fee of \$105.00 per thousand addresses to \$110.00 per thousand addresses. *Id.* at 37-38.

[6013] The Commission recommends the fees proposed by the Postal Service. It estimates a 165.8 percent cost coverage, which provides a reasonable contribution for a service that potentially increases business due to less returned mail.

b. Correction of Mailing Lists

[6014] Eligible mailers submit a name and address list, or an occupant list (address only list) to the Postal Service for correction. The mailing list is submitted on cards or on

sheets of paper, and must be separated by post office or carrier route as required. Name and address list corrections include eliminating names to which mail can not be delivered or forwarded, providing forwarding information, and correcting the spelling of names and addresses, ZIP Codes, post office box numbers, and rural box numbers. Occupant list corrections include deleting invalid addresses, correcting the last lines of the address, placing directional signals to indicate carrier route information, and providing the number of units in multiple unit dwellings. *Id.* at 35-36.

[6015] The test year cost is \$0.318 per address contained on the mailing list. The Postal Service proposes increasing the current fee of \$0.30 to \$0.33 per address. The Postal Service further proposes to increase the minimum charge per corrected list containing 30 addresses from \$9.00 to \$9.90. *Id.*

[6016] The Commission recommends the Postal Service's proposed fees. The fees produce a 103.7 percent cost coverage, which is suitable for a service that reduces the Postal Service's costs by improving address hygiene.

c. Address Changes for Election Boards and Registration Commission

[6017] This service provides election boards and voter registration commissions with change-of-address information. Election boards and voter registration commissions also have the option of using a "Return Service Requested" endorsement or the National Change of Address Linkage System to gather similar address information. *Id.* at 30.

[6018] The cost for the Correction of Mailing Lists, projected to be \$0.318 per change of address in the test year, is a proxy for the cost of this service. The Service proposes increasing the \$0.28 fee for this service to \$0.32 per change of address. *Id.*

[6019] The Commission recommends the Postal Service's proposed fee for a cost coverage of 100.5 percent. This results in a minimal contribution to institutional costs consistent with the election boards' pivotal role in our democracy.

d. Carrier Sequencing of Address Cards

[6020] This service provides mailers with address cards sorted into delivery sequence. Three levels of service are offered: (1) basic carrier route walk sequencing of cards (delivery sequence sort), including the removal of cards with undeliverable or incorrect addresses; (2) the service described in (1) plus the insertion of blank cards indicating missing addresses; or (3) the service described in (1) plus the insertion of completed cards for the omitted addresses. The Postal Service does not charge for the delivery sequence sort or for inserting blank cards. A fee is applied to every card removed with an incorrect or undeliverable address, and to new completed cards inserted into the delivery sequence. New address cards are provided free of charge for rural route delivery addresses that have been converted to city delivery route addresses. *Id.* at 33.

[6021] The cost for the Correction of Mailing Lists, projected to be \$0.318 per address in the test year, is a proxy for the cost of this service. The Service proposes increasing the \$0.30 fee to \$0.33 per address. *Id.* at 32.

[6022] The Commission recommends the Postal Service's proposed fee for this service. This fee produces a cost coverage of 103.7 percent, which is reasonable for a service that lowers the Service's processing costs by enabling mailers to prepare cleaner mail.

3. Post Office Box and Caller Services (Fee Schedule 921)

[6023] *Post Office Box.* Post Office Box service is available to any customer requiring more than free carrier delivery or general delivery. The service allows a customer to obtain mail during the hours a post office box lobby is open or access is otherwise available. Semi-annual fees are charged for Post Office Box service, varying with the size of the box and the estimated cost of the space occupied by the box. Post Office Box service is provided for free to customers who are not eligible for carrier

delivery. The Postal Service proposes to clarify in the first footnote of Fee Schedule 921 that the customer's post office determines whether it will provide delivery service or the free Group E Post Office Box service. USPS-T-41 at 20-29.

[6024] The existing fee structure allocates costs among seven fee groups (not including no-fee Group E), which consist of five different size boxes. Postal Service witness Kaneer claims that the proposal continues progress toward cost homogeneity initiated in Docket No. R2000-1. The proposal significantly increases the number of post office boxes in Groups 4 and 5, and markedly decreases the amount of boxes in Group 6. The Postal Service anticipates that Group 4 will become the biggest group as locations shift fee groups in the future. *Id.* at 15-17.

[6025] The Postal Service maintains its transition to fair, cost based fees by using updated estimates of location costs, grouping post office boxes with similar costs together, and assigning the same fee to the post office boxes grouped together. By aligning the fees with costs, customers who use box service in higher cost locations pay a larger share of the revenue than customers who utilize box service in lower cost locations. To minimize fee impacts, the Postal Service proposes to limit facilities to shifting only one fee group up or down. ZIP Codes moving down a fee group will experience fee reductions, and Zip Codes moving up a fee group will experience the largest fee increases. The proposed changes to the post office box individual fee cells range from -27.8 percent to 48.6 percent. *Id.* at 15, 22, 25, 31.

[6026] The Postal Service develops the proposed fees by establishing relationships between location space cost and box size, and by apportioning space provision costs to occupied boxes for each fee group and box size based on box size capacity and the fee group's weighted average location space cost. The Postal Service first establishes three categories of costs – Space Provision, Space Support and All Other costs. Space Provision costs are allocated to post office boxes in proportion to their box-weighted average location cost for each combination of fee group and box size capacity. The Service distributes the Space Support costs, which include costs for custodial supplies and services, building supplies and services, and maintenance of plant and building

equipment, based on the cubic capacity of each box. The Postal Service allots the All Other costs, which did not vary by box size or location, proportionally to the number of boxes. Finally, it creates allocation factors for the above three categories – Space Provision cost per square foot, Space Support cost per square foot, and All Other costs per box in use – and average cost per square foot specifications for the seven fee groups. The Service uses the inputs in a model to apportion test year attributable costs to the fee group specifications and to calculate the total unit costs by box size for each fee group. Based on the costs for each of the seven fee groups, the Postal Service proposes the fees shown in Table V-7. *Id.* at 11-14, 21.

Table V-7

Proposed Semiannual Post Office Box Fees

Proposed Group	Size 1	Size 2	Size 3	Size 4	Size 5
1	\$42	\$64	\$118	\$242	\$390
2	\$35	\$54	\$94	\$184	\$326
3	\$28	\$46	\$84	\$150	\$250
4	\$20	\$34	\$52	\$102	\$196
5	\$18	\$26	\$48	\$88	\$148
6	\$13	\$20	\$35	\$62	\$110
7	\$10	\$16	\$28	\$48	\$86
E	\$0	\$0	\$0	\$0	\$0

[6027] *Post office box key duplication or replacement service:* The Postal Service provides the first two box keys to post office box customers at no charge upon payment of a refundable deposit. Customers may order duplicate, additional, or replacement keys for a fee. The test year cost for this service is \$4.26. The Postal Service proposes to increase the duplicate post office box key from \$4.65 to \$6.00. *Id.* at 23.

[6028] *Post office box lock replacement service:* The Postal Service will change the lock on a post office box upon the request of the post office box customer.

USPS-T-23 at 12. The test year cost for this service is \$9.18. The Postal Service proposes to increase the fee for this service from \$11.60 to \$14.00. USPS-T-41 at 24.

[6029] *Caller Service*: Caller Service is a premium service that allows business customers to pick up their box mail at a post office call window or loading dock during the time the office is open. Customers are able to pick up their mail early in the day to process orders and financial transactions. Caller Service also provides customers with a means to receive post office box type service when their volumes are too large for post office boxes or post office boxes are not available. USPS-T-23 at 2.

[6030] In Docket No. R97-1, a single caller service fee was established based on a study in which space costs played a limited role. USPS-T-41 at 24-25. However, nearly 30 percent of caller service costs are attributable to location space costs. *Id.* at 25; USPS-T-13 (Smith) at Attachment 12. The Postal Service proposes to align the caller service fees with space-related costs by utilizing the average cost per square foot for the planned post office box fee groups to derive the proposed caller service fees. USPS-T-41 at 25. As shown in Table V-8, these include both decreases and increases ranging from -14.7% to 45.2% to the current semiannual fee of \$434. *Id.* at 25-26. In addition to better reflecting the cost of service, the Postal Service claims that the proposed fees improve the price relationships between caller service and post office box fees by equalizing the disparate gaps between the two sets of fees. The unit costs for Caller Service range from \$219.02 for proposed fee Group 7 to \$385.08 for proposed fee Group 1.

[6031] *Reserve number service*: Reserved number service allows a customer to reserve a box number for future caller service use. Businesses could find the reservation of a caller service number useful if they are planning a promotion, campaign, or advertisement and would like to use a number that corresponds. The test year annual cost for this service is \$21.36. The Postal Service proposes to increase the calendar year fee for reserved number service from \$34.00 to \$38.00. *Id.* at 27.

[6032] *Commission analysis*. The Commission supports the Postal Service's continued efforts to adjust the post office box fees under its cost-based approach and its

Table V-8

Proposed Semiannual Caller Service Fees

Proposed Group	Proposed Fee	Proposed Percent Change
1	\$630	45.2%
2	\$550	26.7%
3	\$485	11.8%
4	\$475	9.4%
5	\$465	7.1%
6	\$415	-4.4%
7	\$370	-14.7%

decision to apply the same cost-based approach to Caller Service. The Commission concurs with the Postal Service's analyses of the statutory pricing and classification criteria as to Post Office Box and related services, and recommends the Service's proposed rates. Under Commission cost methodology, the cost coverage for this category is 156.6 percent overall, which is moderate. The Commission also agrees with the Service's analysis regarding its proposal to modify the footnote in Fee Schedule 921 concerning the no-fee Group E post office boxes.

[6033] The Commission recognizes that the caller service customers in fee Group 1 will experience a 45.2 percent increase, but concludes that the increase is necessary to align the caller service fees with the Size 5 post office box fees. The Commission finds that the 45.2 percent increase for fee Group 1 is warranted where 30 percent of the caller service costs are from Space Provision, which was not emphasized in past caller service cost studies, and customers in fee Group 1 are located in the higher cost areas of the country. *Id.* at 25. It notes that the increased fee will not have a large impact as fee Group 1 constitutes only 7 percent of the caller service volume.

[6034] Although some post office box sizes in certain fee groups experience a large percent increase, these increases are smaller than those experienced in Docket No.

R2000-1 when the new methodology was implemented. The Commission finds that these increases are appropriate during the continuing transition to align costs and fees.

4. Business Reply Mail

[6035] Business Reply Mail (BRM) is a special service that allows customers to distribute First-Class Mail and Priority Mail BRM cards, envelopes, self-mailers, cartons, and labels for eventual return to the customer. The customer agrees to pay postage and a per piece fee for each BRM mailpiece that is actually returned. Postage is paid at the applicable First-Class Mail or Priority Mail rates. USPS-T-39 at 16.

[6036] BRM service is available for purchase using the following five fee categories: (1) Qualified BRM (QBRM) with a quarterly fee (High Volume QBRM); (2) QBRM without a quarterly fee (Basic QBRM); (3) advance deposit account BRM; (4) nonadvance deposit account BRM; and (5) nonletter sized weight-averaged BRM. Each BRM fee category is subject to different Postal Service requirements, and could be preferable depending on a customer's level of return volume and type of mailpiece.

[6037] *Qualified BRM with quarterly fee.* A subset of BRM that the Postal Service approved for processing, QBRM mailpieces are cards and envelopes (up to two ounces) that are automation compatible, have a Facing Identification Mark (FIM) C, a unique ZIP+4 barcode, and meet other requirements specified by the Postal Service. The QBRM with quarterly fees, which charges a lower per piece fee, is designed for customers that receive a high volume of QBRM mailpieces.

[6038] The rate structure for High Volume QBRM consists of three elements: (1) a QBRM quarterly fee, which covers the rating and billing costs; (2) a per piece fee, which covers the cost of activities beyond those associated with First-Class Mail; and (3) a QBRM automation postage rate discount, which is included in the First-Class discussion in Chapter V, section B.2.i. The Postal Service proposes to decrease the QBRM quarterly fee from \$1,900 to \$1,800. Based on the results of a recent study, it proposes to increase the High Volume QBRM per piece fee from \$0.008 to \$0.009. *Id.* at 13.

[6039] *Qualified BRM without quarterly fee.* Customers receiving lower volumes of mailpieces meeting the QBRM requirements or electing not to pay the quarterly fee choose this fee category. The Basic QBRM rate structure consists of two elements: a QBRM automation postage rate discount, which is discussed in Chapter V, section B.2.i., and a higher per-piece fee. The test year estimated cost per piece is \$0.0244. The Postal Service proposes to decrease the current per piece fee of \$0.06 to \$0.05 for Basic QBRM. *Id.*

[6040] *Advanced deposit account BRM.* This fee category is for customers receiving a high volume of BRM mail, but whose mailpiece is not approved for BRM Accounting System processing or otherwise fails to qualify as a QBRM mailpiece. Customers pay a basic per piece fee that covers the costs for counting, rating and billing these mailpieces. The estimated test year cost for this service is \$0.0371. The Postal Service proposes to decrease the per piece fee from \$0.11 to \$0.08. *Id.*

[6041] *Non-advance deposit account BRM.* Customers receiving a low volume of BRM mail or electing not to pay the annual account maintenance fee choose this fee category. Because mailers receiving a relatively small number of BRM pieces find maintaining advance deposit accounts uneconomical, the Postal Service recovers maintenance costs for counting, rating, and collection on a per piece basis. The estimated test year cost for this service is \$0.404. The Postal Service proposes to increase the per piece fee from \$0.65 to \$0.70. *Id.*

[6042] *Nonletter-size weight-averaged BRM.* Customers receiving film and/or film canisters for processing prefer this fee structure, where weight averaging is used to count, rate, and bill the incoming BRM mailpieces based on a statistical projection from recent experience. The mailpieces must meet the basic BRM requirements established by the Postal Service, and can not exceed five pounds or be letter or card-shaped.

[6043] The nonletter-size weight-averaged BRM fee structure consists of two elements: a per piece fee and a monthly maintenance fee. The estimated test year cost per piece is \$0.0069. The Postal Service proposes to increase the per piece fee from

\$0.01 to \$0.011. The estimated test year cost for monthly maintenance is \$652.13. The Postal Service proposes to increase this fee from \$790 to \$900. *Id.* at 13, 20.

[6044] *Additional fees.* In addition to the per piece fees discussed above, each of the BRM fee categories requires the payment of an annual permit fee. The Postal Service proposes to increase this fee from \$160 to \$175, as discussed in section 26 below. Each category, except for nonadvance deposit account BRM, also pays an account maintenance fee. The Postal Service proposes to increase the fee from \$500 to \$550, as discussed in section 26 below. *Id.* at 14.

[6045] *Classification changes.* The Postal Service proposes to change the DMCS classification for this service by replacing the term “license” with “permit” for consistency in §§ 931.5 to 931.55 of the DMCS. Tr. 19/6710. The Postal Service also suggests changing “license to mail” to “permit to distribute” in DMCS § 931.54. *Id.*

[6046] *Intervenor comments.* The High Volume QBRM per-piece fee covers the cost of counting the mailpieces by hand, machine and weight for billing purposes. USPS-T-22 at 20. The Postal Service conducted a study in 2005 to document the practices used for processing and billing BRM, and found that 26.6 percent of High Volume QBRM are counted manually.²⁸² USPS-LR-L-34 at 5, 13. Postal Service witness Abdirahman incorporated the 26.6 percent figure into the R2005-1 cost methodology to obtain a unit cost of \$0.0046 for High Volume QBRM. *Id.* at 17, 20; USPS-LR-L-69. Postal Service witness Berkeley proposes marking up the unit cost of \$0.0046 by 95 percent, which will result in a per piece fee of \$0.009. USPS-T-39 at 19. This is an increase of 12.5 percent over the current fee of \$0.008. *Id.* at 13.

[6047] Major Mailers Association (MMA) challenges the Postal Service’s proposal to increase the High Volume QBRM fee asserting that the Postal Service’s 2005 BRM study is unsound and the resulting 26.6 percent figure regarding manual counting is

²⁸² In direct testimony Postal Service witness Loetscher stated that 26.6 percent of High Volume QBRM is manually counted. During MMA’s cross-examination of witness Loetscher regarding his rebuttal testimony, it came to light that the 26.6 figure was based on data that contained duplicate entries. The Postal Service removed the duplicates and indicated that the 26.6 figure was actually 27.1. USPS-LR-L-34 (Revised).

unreliable. MMA-T-1 (Bentley) at 28-9. MMA argues that the 2005 study design was flawed because the study's designer was not well-informed on the findings of the Postal Service's previous studies or the Commission's recommended decisions in past cases. MMA Brief²⁸³ at 11-12. It contends that the 2005 study is not representative of High Volume QBRM because all BRM was sampled, and that conducting the study hastily led to erroneous results in the data, including duplicate records and irrational entries. *Id.* at 13, 15, 17. MMA states that the study remained unsound even after the Postal Service removed the duplicate records, and lists other flaws in the study design, such as not collecting the volumes for individual accounts, not accounting for the use of more efficient counting methods when volume increases, and not accounting for seasonal variations in volume. *Id.* at 15-16, 19; MMA Reply Brief at 30, 33.

[6048] MMA contends that the 2005 BRM study's 26.6 percent finding regarding the amount of High Volume QBRM hand counted is unreliable. It argues that the Postal Service applied dubious weighting methods that increased the manual count from 7 percent of the sampled High Volume QBRM pieces to 26.6 percent of all High Volume QBRM pieces. MMA Brief at 21. MMA asserts that, based on the Commission's previous reliance on MMA's analysis that 11 percent of High Volume QBRM pieces were manually counted in Docket No. R2000-1, the 26.6 percent finding is unreasonable. MMA also contrasts the 26.6 percent finding to the Postal Service's testimony in Docket No. R2001-1 that only 0.4 percent of the High Volume QBRM was manually counted. MMA-T-1 at 29. It argues that the Postal Service's success in sorting 96.4 percent of letters on automation equipment undermines the Postal Service's finding that 26.6 percent of High Volume QBRM is manually counted. MMA Reply Brief at 35-36.

[6049] MMA claims that manually counting High Volume QBRM is at odds with the Postal Service's policy to utilize automated counting methods and with the national QBRM task force's study to develop the "best practices" to be used locally. *Id.* at 34,

²⁸³ All references to MMA Brief in Chapter V, section F, Special Services, refer to the Initial Brief of Major Mailers Association on Selected Special Service Issues, December 21, 2006.

36-37. It suggests that the Commission require the Postal Service to study why offices would hand count letters in amounts over 500 pieces. MMA Brief at 22. If the Postal Service is hand counting 26.6 percent of the High Volume QBRM, MMA proposes that the quarterly fee should be raised so that the breakeven or minimum qualifying volume is higher and efficient “best practice” counting methods can be used. MMA Reply Brief at 38.

[6050] MMA questions the Postal Service’s High Volume QBRM unit cost of \$0.0046 stating that 90 percent of that cost is tied to the erroneous assumption that 26.6 percent of these pieces are manually counted. It asserts that had the Postal Service assumed the same productivity for counting the pieces by weighing or counting machines, the unit cost would be \$0.00087. Based on its own analysis indicating that the unit cost is under \$0.001, MMA urges the Commission to consider eliminating the High Volume QBRM per piece fee or decreasing it to \$0.005. MMA Brief at 21-22.

[6051] In response, the Postal Service states that witness Abdirahman calculated the unit cost using the same methodology as employed in Docket No. R2005-1. Postal Service Brief at 374. It challenges MMA’s analysis and calculations, asserting that MMA developed its own calculation that combined various methods and assumptions from the past studies, which were flawed. *Id.* at 373-4, 376. The Postal Service contends that the studies in Docket Nos. R2000-1 and R2001-1 excluded accounts that received low volumes of QBRM and, thus, are unreliable due to selection bias that underestimated the amount of High Volume QBRM that is manually counted. *Id.* at 375; USPS-RT-9 at 4-7. It argues that the prior studies resulted in measurement bias that underestimated the amount of manually counted mailpieces because the studies did not consider that more than one accounting method was used per account. Postal Service Brief at 373-376, USPS-RT-9 at 7-8. The Postal Service emphasizes that even for high volume accounts, some pieces are counted manually, such as damaged pieces that are unable to be processed in automation, volumes received after the main processing window, and accounts with fluctuating daily volumes. USPS-RT-9 at 7-9.

[6052] The Postal Service contends that the new study was designed to avoid both selection and measurement bias. *Id.* at 10. It counters that the results of previous studies and the methodology employed in those studies have no bearing on how the new study was designed and conducted. Postal Service Reply Brief at 276. The Postal Service contends that the manual counting percentage of 26.6 is correct and is supported by the operational practice of hand counting low volumes because it takes fifteen to twenty minutes to set-up and sweep a machine. Postal Service Brief at 376; USPS-RT-15 at 4-5.

[6053] The Postal Service contends that MMA ignores the characteristics of High Volume QBRM. It notes that a minimum volume requirement does not exist for the High Volume QBRM category and explains that mailers choose this category and pay the quarterly fee based on their expected quarterly volume, not their expected daily volume. It explains that daily volume may be high only a few days per month, with most days having low volumes for that specific mailer. Postal Service Brief at 375.

[6054] The Postal Service contests the flaws in the study perceived by MMA. The Postal Service claims that information on individual account volume was not required to estimate the accounting and billing practices employed for all BRM pieces, which was the purpose of the 2005 study. It argues that the weighting method used was clearly explained and consistent with the sample design. The Service asserts that MMA provided no evidence that the statistically drawn stratum was not representative of High Volume QBRM because the sample was drawn to be representative of all BRM. It claims that MMA does not understand the difference between seasonality and day-to-day fluctuations in volume, and explains that the timing of the study is inconsequential because the aggregate volume of High Volume QBRM stays relatively constant throughout the year regardless of the seasonal fluctuations in an individual mailer's volumes. Postal Service Reply Brief at 273, 277-78.

[6055] *Commission analysis.* The Commission finds the Postal Service's conclusion that roughly 27 percent of High Volume QBRM mailpieces are manually-counted unreliable based on the fact that approximately 96 percent of letters

are sorted on machines. Tr. 10/2568, 2573. Because QBRM mailpieces are highly machine-compatible by definition, the Commission is hesitant to find that the percentage of High Volume QBRM manually counted is significantly above the mail sort percentage for letters. The Commission recognizes that the cost figures produced by MMA may be understated as the potential for small volume mailers to choose the High Volume QBRM category exists. However, the Postal Service provides no stratification of volumes received by High Volume QBRM users.

[6056] Finding the studies flawed, the Commission recommends decreasing the High Volume QBRM per piece fee from \$0.008 to \$0.005. Counting volumes by machine or by weight is both possible, and more efficient and cost effective than manual counting. The Commission finds that a reduction is also appropriate because the High Volume QBRM customers are already contributing to the institutional costs by paying postage in addition to the per piece fee.

[6057] Using the Postal Service's cost methodology associated with its 27 percent figure, a \$0.005 per piece fee results in a cost coverage of 95 percent. The Commission concludes that the 95 percent cost coverage is understated as it is based on the costs associated with the overstated 27 percent figure. The fact that the BRM services will collectively cover the overall costs, even if High Volume QBRM is slightly below covering its costs, permits the High Volume QBRM fee to be set at \$0.005.

[6058] The Commission recommends the remaining fees proposed by the Postal Service, and estimates a 172.5 percent cost coverage. It also adopts the Service's proposal to replace the term "license" with "permit" to achieve consistency throughout DMCS § 931.

5. Merchandise Return Service (Fee Schedule 932)

[6059] Merchandise Return service allows the permit holder to pay postage for parcels containing merchandise. It is similar to Business Reply Mail and is used for parcels mailed at First-Class Mail single-piece, Priority Mail and Package Service rates.

This service requires both a permit and an advance deposit account from which the return postage is drawn. A per piece fee is not associated with this service, because the cost for per piece Merchandise Return service is covered by the return postage. Mailers can purchase additional services such as Registered Mail, Insurance, Delivery Confirmation, Certificate of Mailing, Return Receipt, and Special Handling. USPS-T-39 at 38-39.

[6060] The Postal Service proposes to increase the permit fee from \$160 to \$175 and the account maintenance fee from \$500 to \$550, as discussed in section 26 below. The Postal Service also suggests modifying the current DMCS language for Merchandise Return service to indicate that the use of this service is not limited to the customers of permit holders, but includes the clientele of the permit holders' customers. The broader language proposed also clarifies that this service can be used to send, as well as return, parcels. *Id.* at 37, 40-41. The Commission adopts these classification changes as proposed by the Postal Service.

6. On-Site Meter Service

[6061] The Postal Service proposes to remove Fee Schedule 933 and DMCS § 933, which pertain to the fees and classifications regarding meter service, from the Domestic Mail Classification Schedule because On-Site Meter service was discontinued on February 28, 2005. *Id.* at 42. The Commission recommends the removal of these sections.

7. Bulk Parcel Return Service (Fee Schedule 935)

[6062] Bulk Parcel Return Service (BPRS) allows mailers of large quantities of Standard Mail machinable parcels that are either undeliverable-as-addressed or opened and remailed by addressees to be returned to designated postal facilities for pick-up by

the mailer or delivered in bulk by the Postal Service. This service is restricted to high-volume mailers that can demonstrate a high probability of receiving, or do in fact receive, 10,000 returned machinable Standard Mail parcels per year. Shipper-Paid Forwarding service is the only special service that may be purchased in conjunction with BPRS. *Id.* at 9-10.

[6063] Mailers using this service must pay an annual permit fee and an annual account maintenance fee. The Postal Service proposes to increase the permit fee from \$160 to \$175 and the account maintenance fee from \$500 to \$550, as discussed in section 26 below. *Id.* at 9.

[6064] Each returned parcel is levied a per piece fee, which is deducted from an advance deposit account. The estimated test-year BPRS unit cost is \$1.29. The Postal Service proposes to increase the per piece fee from \$1.90 to \$2.10. *Id.*

[6065] The Commission recommends the BPRS per piece fee proposed by the Service. This results in a cost coverage of 163.2 percent, which is reasonable for a competitive service.

8. Shipper-Paid Forwarding (Fee Schedule 936)

[6066] Shipper-Paid Forwarding is an Address Change Service that provides forwarding service for Standard Mail machinable parcels and most Package Services parcels for a period of one year from the date a recipient files a change of address form. Shippers must endorse the packages with "Address Service Requested." Bulk Parcel Return Service is the only special service that may be purchased in conjunction with Shipper-Paid Forwarding.

[6067] Postage for the forwarded pieces is assessed according to the service provided, including return service for parcels that can not be forwarded. An ACS participant code identifies the shipper, and the postage is deducted from the shipper's advance deposit account. The Postal Service proposes to increase the Account

maintenance fee for this service from \$500 to \$550, as discussed in section 26 below.
Id. at 5.

9. Premium Forwarding Service (Fee Schedule 937)

[6068] Premium Forwarding Service provides residential delivery customers and certain post office box customers the option of receiving their mail at a temporary address by means of a weekly Priority Mail shipment for a period of two weeks up to twelve months. The service applies to nearly all classes of mail sent to a primary address. It can not be used simultaneously with temporary or permanent forwarding orders, and is not available to customers whose primary address consists of a post office box of a certain size or a centralized delivery point. Premium Forwarding Service may not be combined with any services beyond those purchased by the original mailer.

[6069] Premium Forwarding Service is a two year experiment. The Decision of the Governors of the United States Postal Service on the Opinion and Recommended Decision of the Postal Rate Commission Approving Stipulation and Agreement on Experimental Premium Forwarding Service, Docket No. MC2005-1, issued May 10, 2005, approved the Commission's recommended fees and classifications for this special service. The Postal Service's filings in this case do not contain any requests for fees or classification changes for this service. The Commission does not recommend any fee or classification changes to the experimental Premium Forwarding Service.

10. Standard Mail Forwarding

[6070] The Postal Service offers forwarding service for Standard Mail letters and flats. Due to its inability in the past to count forwarded pieces for individual mailers, the Service charges for forwarded pieces by applying a formula, or weighted rate, to Standard Mail pieces returned to the mailer. USPS-T-40 at 47.

[6071] Automated and Electronic Address Correction Services improve this situation by allowing the Postal Service to record volumes of forwarded pieces by mailer. Postal Service witness Mitchum proposes charging mailers electing Automated or Electronic Address Correction Service on the basis of the number of pieces actually forwarded as opposed to the weighted charge. The Address Correction Service system will assign the Standard Mail Forwarding fee to the mailer identified by the data in the mailpiece's keyline or barcode. Returned pieces will be charged at the First-Class Mail rate rather than the weighted rate. Mailers that do not request Automated or Electronic Address Correction Service will continue to be assessed a weighted rate applied to the pieces returned to the mailer for forwarded Standard Mail. *Id.* at 47-48.

[6072] To incorporate these classification changes into the DMCS, the Postal Service proposes to amend DMCS § 353 and to add DMCS §§ 321.9, 322.9, 323.9, and 324.9. *Id.* at 48-9; USPS Request, Attachment B at 19-20; Tr. 19/6778. The Postal Service also suggests notes to Rate Schedules 321, 322, 323, and 324 for clarification. USPS-T-40 at 50.

[6073] The Postal Service proposes Standard Mail Forwarding per piece fees of \$0.35 for letters and \$1.05 for flats for mailers electing Automated or Electronic Address Correction Service. Postal Service witness Mitchum derives these fees by applying a cost coverage of 230 percent, which he considers similar to that charged for First-Class Mail, to the estimated test year costs of undeliverable-as-addressed letters and flats, which are \$0.153 and \$0.456 respectively. *Id.* at 48; USPS-T-26, Appendix A.

[6074] The Postal Service also proposes to decrease the Standard Mail Forwarding weighted rate applied to pieces returned to mailers who do not request Automated or Electronic Address Correction Service. Although the fee varies based on the weight of the returned mailpiece, the Service calculates average fees of \$1.36 for Regular Mail and \$1.13 for Nonprofit Regular mail. The Commission's average fees of \$1.34 and \$1.11 are slightly lower to reflect its recommended increase of 6.4 percent to the First-Class single-piece letter rate, which is lower than that proposed by the Postal Service.

[6075] The Commission adopts the proposed structure, which utilizes the Automated and Electronic Address Correction Services to more accurately assess costs of forwarding mail. The Commission recommends the proposed classification changes with some minor adjustments to reflect that two structures for Standard Mail Forwarding exist. The Commission adopts the Service's proposed fees for mailers electing the Address Correction Service option and the weighted rate for the remaining mailers.

11. Certified Mail (Fee Schedule 941)

[6076] Certified Mail provides a mailer with evidence of mailing of First-Class and Priority Mail, and guarantees that the Postal Service will obtain a signature upon delivery and retain a delivery record of the item mailed for a specified period. The mailer receives a mailing receipt if the mailpiece is deposited at a post office window or given to a rural carrier, and can check for the delivery date and time via the internet or a toll-free call center. Bulk mailers that provided an electronic manifest to the Postal Service can receive the delivery information by bulk electronic file transfer. Mailers can purchase Return Receipt or Restricted Delivery service in conjunction with Certified Mail. USPS-T-39 at 22-23.

[6077] The fee for Certified Mail is in addition to postage. The estimated test year per piece cost for Certified Mail is \$1.79. The Postal Service proposes to increase the fee from \$2.40 to \$2.65. *Id.* at 22.

[6078] *Intervenor comments.* Carlson urges the Commission to recommend that the Postal Service propose in the next rate case to provide the recipient's electronic signature as a basic feature of Certified Mail. Carlson argues that an overwhelming desire for a signature to be included with the service exists, because 91 percent of Certified Mail customers also purchased Return Receipt in FY 2005. The Postal Service will avoid, rather than incur, costs by providing an electronic signature as a feature of Certified Mail. Instead of processing two forms at the window and collecting the same information twice during delivery, these actions will be performed once. Carlson reasons

that the Service could increase the certified mail fee slightly to reflect the value of the added service. DFC-T-1 at 14-16.

[6079] The Postal Service responds that before deciding to pursue Carlson's proposal, it must consider whether its customers want such an enhancement, especially at a higher price. Postal Service Reply Brief at 308. The Postal Service states that in FY 2005 only 0.1 percent of Certified Mail customers chose the Electronic Return Receipt while 91 percent chose the Basic Return Receipt. *Id.*; Tr.15/4453-54; USPS-LR-L-123. The Postal Service states that the volume of Return Receipt is already declining, and including electronic receipt with Certified Mail may accelerate that decline resulting in a loss of contribution. Postal Service Reply Brief at 308; Tr. 15/4389.

[6080] *Commission analysis.* The Commission acknowledges intervenor Carlson's proposal to add Electronic Return Receipt as a feature of Certified Mail, but does not find sufficient evidence to justify asking the Postal Service to make such a proposal. Customers purchasing Certified Mail without Return Receipt exist. These customers may want the option of purchasing Certified Mail unencumbered by an additional signature feature that would increase the fee. The Commission urges the Service to continue evaluating how to make its services more valuable and responsive to its customers' needs. The Commission recommends the Postal Service's proposed fee of \$2.65, which generates a cost coverage of 147.9 percent.

12. Registered Mail (Fee Schedule 942)

[6081] Registered Mail provides added protection to mail and indemnity in case of loss or damage. A system of receipts is used to monitor and account for the flow of the mailpiece from acceptance to delivery. Registered Mail, therefore, is the most secure service offered by the Postal Service. As with Certified Mail, the mailer receives a mailing receipt, and can check for delivery date and time on the Internet. The Postal Service retains a delivery record of the item mailed. Registered Mail with Insurance can

be purchased on a graduated scale up to the actual value of the mailpiece (from \$0.01 through \$25,000). USPS-T-40 at 41-42.

[6082] The fee for Registered Mail is in addition to postage. The Postal Service proposes a 50 percent average increase in the fees for this service. The proposed fee for Registered Mail without Insurance is proposed to increase from \$7.90 to \$11.95. The fee for Registered Mail with the first step of Insurance, valued at \$0.01 to \$100, will increase from \$8.45 to \$12.70. The fee for Registered Mail with the second step of Insurance, covering \$100.01 to \$500, will increase from \$9.35 to \$14.00. Each successive step is charged an additional fee, which is proposed to increase from \$0.90 to \$1.35 per step. Registered Mail with Insurance over \$25,000 is charged a handling fee, which the Postal Service proposes to increase from \$0.90 per \$1,000 to \$1.35 per \$1,000. Because special arrangements must be made for items valued at over \$15,000,000, fees are assessed based on the special arrangements and the weight. *Id.* at 41-44.

[6083] The Postal Service claims that Registered Mail provides a very high value of service, but aims for a low cost coverage to alleviate the impact that a more substantial rate increase would have on customers of this service. *Id.* at 43. It contends that a 50 percent increase in the fees is necessary to cover costs and that this service has been priced below costs for the past few years. Postal Service Brief at 389. In the past, proposed increases to registered mail fees were based on an estimated allocation of costs the Postal Service calculated by applying a Revenue, Pieces and Weight (RPW) adjustment factor to remove the Service's penalty mail costs from the costs attributed to consumers. *Id.* at 390; Tr. 18D/6487-89. The Service asserts that an accurate allocation of costs is now available because it redesigned its data collection system, the In-Office Cost System (IOCS), to isolate the customer registered mail costs from the Postal Service registered mail costs. Postal Service Brief at 390; Tr. 18D/6487-88. The Postal Service explains that the registered mail cost assigned to customers increases from \$12,764 in Docket No. R2005-1 to \$54,377 in this proceeding because of the IOCS data

collection methodology and the Service’s treatment of overhead costs, such as “on break” and “clocking in and out.” Tr. 18D/6488-89.

[6084] *Commission analysis.* The Commission finds the Postal Service’s cost distribution unreliable. The R2006-1 MODS data for Registered Mail includes extremely questionable observations. Whether the MODS data reflects the redesigned IOCS data collection is unclear, and warrants further investigation. The Commission, therefore, uses the RPW adjustment factor applied in Docket No. R2005-1 to calculate its recommended fees, as shown in Table V-9. The fees represent a 20.7 percent increase and result in a 132.1 percent cost coverage, which maintains an adequate contribution from a high value service that provides an increased level of security.

Table V-9
Recommended Registered Mail Fees

Description	Current	PRC Recommended
No Insurance	\$7.90	\$9.50
\$0.01 to \$100	\$8.45	\$10.15
\$100.01 to \$500	\$9.35	\$11.25
\$500.01 to \$1,000	\$10.25	\$12.35
\$1,000.01 to \$25,000	\$10.25 + \$0.90 for each \$1,000 over \$1,000.00	\$12.35 + \$1.10 for each \$1,000 over \$1,000.00
\$25,000.01 to \$15,000,000	\$31.85 + \$0.90 for each \$1,000 over \$25,000.00	\$38.75 + \$1.10 for each \$1,000 over \$25,000.00
\$15,000,000+	\$13,509.35 + amount to be determined by Postal Service	\$16,511.25 + amount to be determined by Postal Service

[6085] The Commission urges the Postal Service to explore and implement the operational improvements that might reduce the costs of Registered Mail presented in the March 2006 Registered Mail Task Force Summary. USPS-LR-L-60.

13. Insurance (Fee Schedule 943)

[6086] Insurance provides up to \$5,000 in indemnity coverage for lost, rifled or damaged articles. This service is available for Express Mail and Package Services, and First-Class Mail (including Priority Mail) that contains items that could be sent as Standard Mail or as Package Services. Bulk Insurance (which takes the form of a per piece discount) is available for Standard Mail that is subject to the residual shape surcharge. Fees are charged based on the indemnity coverage chosen from \$0.01 to \$5,000. USPS-T-40 at 23.

[6087] The Postal Service proposes eliminating the signature requirement for items insured from \$50.01 to \$200 to reduce costs. In place of a signature, the Postal Service will obtain a delivery scan for all items insured for \$200 or less. For items insured over \$200, the Postal Service will continue to collect a signature. The Postal Service contends that acquiring delivery scans for items valued up to \$50 will enhance the value of this service by reducing package loss and fraudulent claims, as well as by allowing customers the opportunity to file insurance claims online. *Id.* at 22, 24.

[6088] The Postal Service proposes several classification changes based on its proposal to no longer collect signatures for items insured for less than \$200. USPS-T-40 at 24. The Service recommends that the language in DMCS § 943.251 be modified to reflect that Return Receipt and Restricted Delivery are available with insurance greater than \$200, not \$50. Tr. 19/6776.

[6089] The Postal Service proposes to increase the fee for items insured for \$50 or less from the current fee of \$1.35 to \$1.65 to account for the cost of obtaining the delivery scans. The fees for items insured from \$50.01 to \$100 will decrease from \$2.30 to \$2.05, due to replacing the acquisition of a signature with a delivery scan. Similarly, the fees for items insured between \$100.01 and \$200 will decrease from \$3.35 to \$2.45. The fee for items insured for a value of \$200.01 to \$300.00, the first level to maintain the signature requirement, will increase from \$4.40 to \$4.60. USPS-T-40 at 25-26.

[6090] The Postal Service charges a fee for each additional \$100 of insurance above \$300. The Postal Service proposes to reduce this fee from \$1.05 to \$0.90. The decrease in this fee, when coupled with the increase in the flat rate for items insured between \$200 and \$300, has the effect of increasing the fee from \$5.45 to \$5.50 for items insured for a value between \$300.01 and \$400 and of decreasing the fees for all items insured for more than \$400.01. *Id.*

[6091] A per piece discount is available for bulk mailers who send a minimum of 10,000 insured mailpieces annually. Currently, the Postal Service offers a discount of \$0.60 for items insured under \$50.01 and a discount of \$0.80 for items insured over \$50.00. *Id.* The Postal Service proposes to replace the two discounts with one Bulk Insurance discount of \$0.80 for all items to reflect the cost savings realized by the Postal Service. Postal Service Brief at 388; USPS-T-40 at 26.

[6092] Express Mail includes the first \$100 of indemnity coverage free-of-charge. Additional insurance for Express Mail is available for fees comparable to those charged for regular Insurance. Due to the low average indemnity costs for Express Mail Insurance, the Postal Service proposes to decrease the fee for the first additional \$100 of coverage from \$1.05 to \$0.75. The Postal Service also seeks to replace the current fee structure, which charges an extra \$1.05 per each \$100 after the first additional \$100, with a flat fee of \$2.10 for items valued between \$200.01 and \$500 and an additional \$1.35 for each \$500 increment above \$500. Finally, the Postal Service proposes a classification change that caps its regular Insurance liability for negotiable items, currency, and bullion at \$15 to match the current Express Mail Insurance limitation for those items. USPS-T-40 at 24-25.

[6093] *Intervenor comments.* The Office of the Consumer Advocate (OCA) recommends setting the cost coverage for Insurance close to zero due to the poor service provided by the Postal Service. OCA asserts that Insurance has a low value of service because the Postal Service fails to properly inform customers on how to pack an item to withstand damage, on the documents they must retain and submit with a claim, and on the rigors of submitting a claim. The clerks are not properly trained to answer

questions on the processing of insurance claims, and give a false sense that indemnification will be quick and easy to obtain. OCA explains that once the St. Louis Accounting Service Center receives a claim the average processing time is 48 days, not 10 working days as the Postal Service performance objective states. OCA argues that the Postal Service does not keep a log of submitted claims and that after window and carrier costs are covered little revenue is available for indemnification. OCA challenges witness Mitchum's assertion that indemnity costs have decreased because the Postal Service has experienced less loss and damage of insured items, countering that the Postal Service's mishandling of claims dissuades claimants from pursuing their indemnity payments. OCA Brief at 158-61.

[6094] OCA suggests that the Postal Service develop a fully trackable system in which all claims processing steps are logged, including the dates the post office received the complaint and sent it to the St. Louis Accounting Service Center. OCA wants the Postal Service to inform customers of the length of claims processing time; the reported incidence of damage and loss to packages, and the percentage of claims that are denied; and to give customers printed information that explains the documentation required to file a claim. Until the Postal Service accomplishes the above, OCA argues that the cost coverage should be set at one percent above costs. *Id.* at 161-162.

[6095] The Postal Service responds that only 0.4 percent of all items insured resulted in a claim, and that the remaining 99.6 percent of insured items were delivered safely. It explains that 15.7 percent of claims in FY 2005 were denied, and only 3.3 percent of claims, or 0.013 percent of all insured items, were open to inquiry. Postal Service Reply Brief at 301-02.

[6096] The Postal Service contends that while 48 days is the full time for resolution of all claims, including incomplete claims, the average time to resolve a claim is 15 days. It suggests that the imminent online claim filing system will speed up the claims processing, especially since the online system will not let customers file incomplete requests. The Service also states that the online system will digitally track all submitted claims. *Id.* at 303-04.

[6097] *Commission analysis.* The Commission adopts the proposed changes to the Insurance service, such as scanning all items insured for \$200 or less and capping its liability for negotiable items, currency, and bullion at \$15. It also recommends the fees for Insurance proposed by the Postal Service, which result in a cost coverage of 129.5 percent.

[6098] Regarding OCA's request that the cost coverage be set at 101 percent until service is improved, the Commission finds a price signal unnecessary and notes that most of the fees are being reduced. Although OCA raises valid concerns with the service, the percent of insured items resulting in a claim and the percent of claims rejected or open to inquiry are quite low. The Postal Service anticipates implementing operations that will further decrease these figures and that are in accordance with OCA's suggestions for advancing the service. The Commission believes that the Postal Service's plans to establish an online claim filing system and to scan all insured items upon delivery will improve the value of the Insurance service by reducing the average claim processing time.

14. Collect on Delivery (Fee Schedule 944)

[6099] Collect on Delivery (COD) allows mailers to send merchandise prior to the recipient paying for the item. Upon delivery, the recipient pays the Postal Service for the merchandise plus the applicable COD fee, and the Postal Service transmits the amount collected back to the mailer. If the recipient pays with cash, the Postal Service pays the mailer by a postal money order. If the recipient pays by check, the Postal Service sends that check to the mailer. COD mail is insured against loss, rifling, and damage to the item, as well as failure to receive the payment. USPS-T-39 at 27-28.

[6100] The fees are determined by the COD amount to be collected or insurance coverage desired for a particular item. The base COD fee is paid for collections up to \$50. A set increment is added to the base fee for different ranges of payments to be

collected on delivery. The amount to be collected from the recipient may not exceed \$1,000. *Id.* at 27-30.

[6101] The Postal Service proposes to reduce the size of the uniform incremental fee above the base fee. It explains that claims as a percentage of volume are highest for the collection of amounts up to \$50. As the amount to be collected increases, the percentage of volume with paid claims decreases. Therefore, the Postal Service proposes fees that reflect the lower claims cost per piece for higher collection amounts. *Id.* at 29-30.

[6102] As shown in Table V-10, the Postal Service proposes to increase the COD fees for amounts collected up to \$400. The current fee of \$10.00 for amounts between \$400 and \$500 will remain unchanged, and the COD fees for amounts from \$500 to \$1,000 will decrease.

Table V-10
Proposed COD Fees

Description	Current	USPS Proposed
Up to \$50	\$4.75	\$5.75
\$50.01 to \$100	\$5.80	\$6.60
\$100.01 to \$200	\$6.85	\$7.45
\$200.01 to \$300	\$7.90	\$8.30
\$300.01 to \$400	\$8.95	\$9.15
\$400.01 to \$500	\$10.00	\$10.00
\$500.01 to \$600	\$11.05	\$10.85
\$600.01 to \$700	\$12.10	\$11.70
\$700.01 to \$800	\$13.15	\$12.55
\$800.01 to \$900	\$14.20	\$13.40
\$900.01 to \$1000	\$15.25	\$14.25

See id. at 27.

[6103] The Postal Service also proposes the following increases: from \$4.20 to \$4.60 for registered COD; from \$3.15 to \$3.45 for a notice of nondelivery; from \$3.15 to

\$3.45 for an alteration of COD; and from \$3.70 to \$4.10 for Restricted Delivery. *Id.* at 26. In addition, it recommends changing the DMCS language to clarify that notice of nondelivery service requires the payment of a fee. Tr. 19/6711.

[6104] *Intervenor comments.* Growing Family, Inc. (Growing Family) argues that the Postal Service's proposed rates for COD are unfair and inequitable because the Postal Service changed its COD indemnification policy. Growing Family Brief at 2. Until May 2005, the Postal Service reimbursed Growing Family the full amount, consisting of the retail price of the item as well as the postage and COD fee, whenever it failed to return to Growing Family the amount to be collected or the item. GF-T-1 at 3. Upon receiving partial reimbursements for some of its indemnity claims in May 2005, Growing Family repeatedly asked the Postal Service for an explanation of the reduced indemnity payments. The Postal Service informed Growing Family in an August 16, 2005, letter that it would no longer pay the full amount claimed and explained that the past payments of the full retail value were not consistent with the standards set forth in the Domestic Mail Manual. After appealing this decision on October 6, 2005, Growing Family received a letter dated March 10, 2006, from the Postal Service identifying the four payment levels for indemnity claims. The letter explained that the Postal Service would pay the reproduction costs for items lost or destroyed before delivery, and the full retail value only when the Postal Service delivered the item and either failed to collect any money or lost a cash payment. *Id.* at 3-8.

[6105] Growing Family asserts that the Postal Service does not reimburse the full retail value regardless of the reason for the claim. *Id.* at 10-13. It provided evidence that for a majority of its claims the Postal Service paid the reproduction costs, which under the new policy indicates that the Postal Service lost the item before delivery. Growing Family also presented evidence that most of its claims were due to the carrier leaving the item without collecting the payment or the Postal Service's mishandling of the money, entitling it to reimbursement of the full retail value. Tr. 23/8236-37, 8242-46. Growing Family requests that the rates for COD be charged based on reproduction costs rather than the amount to be recovered from the recipient. Growing Family Brief at 17.

[6106] Growing Family also argues that the value of the COD service is low because the Postal Service lacks the ability to determine the basis for paying claims or to assess the reproduction costs of the item and, thus, underpays COD customers. *Id.* at 14. Growing Family witness Paul testifies that the amounts recently received on claims vary from \$15.05 to \$20.00 without any explanation of the basis for the reimbursement level, how the Postal Service assessed the reproduction costs, or why the postage and COD fees were not reimbursed. GF-T-1 at 11-13.

[6107] Growing Family asserts that the value of service is further diminished because the Postal Service no longer reimburses Growing Family for personal checks it collected but failed to return, instead instructing Growing Family to obtain a new check from the item recipient. Growing Family Brief at 15. Growing Family also provides evidence that the Postal Service denied claims stating that it had already tendered payment, but later presented Growing Family with money orders dated three years before, or supplied copies of money orders that were made out to entities and people other than Growing Family. Growing Family proposes a lower contribution to institutional costs to reflect this very low value of service. GF-T-1 at 12-16.

[6108] Growing Family contends that the forecast of COD indemnity payments for Test Year 2008, which is one input in COD's revenue requirement, is incorrect. Growing Family asserts that the Postal Service overstates the Fiscal Year 2008 revenue requirement by basing the Test Year 2008 forecast on the indemnity payments for Base Year 2005, the year in which its indemnity policy changed. Growing Family argues that under the new policy most claims in Test Year 2008 will be paid at the reduced rate, whereas in Base Year 2005, the year in which the Postal Service changed its policy, the Postal Service paid the full retail amounts for the first seven months before paying reduced amounts based on reproduction costs the remainder of the year. Growing Family states that making a "straight-line" forecast for Fiscal Year 2008 on the claims payment history of Base Year 2005 is inappropriate, and suggests that the revenue requirement and fee for COD be reduced to reflect the lower indemnity payments that will be made in Test Year 2008 under the new policy. Growing Family Brief at 8-9, 16.

[6109] Growing Family asserts that it did not develop a new revenue requirement because it did not have the human resources or the necessary data, and that the burden of proof shifted to the Postal Service once Growing Family established that under the new indemnification policy the Postal Service was reimbursing at much lower amounts than before. Growing Family Reply Brief at 2-3. Growing Family requests that the Commission recommend COD fees that provide a reasonable cost coverage based on a corrected indemnity forecast or that cover 101 percent of the excessive costs attributed to COD service by the Postal Service if an accurate measure of costs can not be identified. Growing Family Brief at 17.

[6110] OCA argues that the Postal Service's revisions to its payment policy for COD are arbitrary and unfair. OCA finds the Postal Service's application of its new policy months before it ever issued a decision that set forth the rationale for the policy disturbing. Because of the unilateral reduction in the value of service, OCA contends that the cost coverage of COD should be reduced to a level close to zero. OCA Brief at 162-63.

[6111] The Postal Service responds that witness Berkeley proposed a low cost coverage of 113 percent, reduced from the 129 percent that resulted from Docket No. R2005-1. It argues that Growing Family failed to counter Berkeley's testimony that COD has a high value of service because it enables sellers, including those that do not accept credit cards, and buyers, regardless of their financial situation, to engage in sales transactions. The Postal Service claims that calculating the COD fee based on the reproduction cost of the item will complicate the application of the fee schedule, because each mailer will have to calculate the replacement value in advance and instances exist where the mailer is reimbursed the full amount to be collected. Postal Service Brief at 377-78.

[6112] The Postal Service further asserts that Growing Family failed to submit any evidence that could be used to quantify the impact of the Postal Service's payment practice on the Postal Service's projected total COD claims payments in Test Year 2008. Postal Service Reply Brief at 280. The Postal Service argues that based on an

assumption that Growing Family represents 10 percent of indemnity costs paid to mailers and the fact that only 22 percent, or \$1,952,000, of the overall volume variable costs for COD in Base Year 2005 consisted of indemnities, Growing Family would account for 2 percent of COD total volume-variable costs. The Postal Service contends that reducing the cost coverage by 12 percent as suggested by Growing Family is inconsistent with a cost reduction that would be less than 2 percent of costs. *Id.* at 281-82.

[6113] *Commission analysis.* The Commission observes that while the Postal Service's policy clarification may well have been a classification change to COD, the issue was never fully litigated in that context. A rate case is not the proper proceeding to challenge whether the Postal Service changed or clarified a policy.

[6114] The Commission finds that a service performance problem exists with COD. The Postal Service is failing to be properly accountable for the item mailed or the payment collected from the recipient. The record contains substantial evidence that the Postal Service lacks the ability to determine whether items are lost during the delivery process, are delivered without payment being collected, or are mishandled while being returned to the mailer. The record also supports a finding that the Postal Service mishandles money orders and loses personal checks.

[6115] The Commission strongly urges management to exercise more control over COD service to assure that the Postal Service fulfills its COD responsibilities. The Postal Service should not offer a service, especially a service involving accountability for items mailed and payments collected, and then not properly provide the service the customer pays for.

[6116] The Postal Service's procedures are not achieving proper accountability for COD. COD items are not properly tracked, revenue is affected, and the service problem has escalated. Whether mailers knowingly file claims for funds the Postal Service already tendered, or the Postal Service denies claims when it has not provided the collected funds to the mailers, is not for the Commission to evaluate. Management may choose to utilize internal review and control systems such as the Inspector General in fully exploring the extent of this problem.

[6117] The Commission concludes that the 10.7 percent increase to the COD fees requested by the Postal Service is not warranted where the Service's performance is so severely lacking. It further observes that the Postal Service's proposal to eliminate the uniform incremental fee is punitive. Customers receiving the worst service, as evidenced by frequency of claims, would experience the greatest percentage increase.

[6118] The Commission recommends the fees shown in Table V-11. The base fee of \$5.10 is the result of increasing the \$4.75 fee for insurance coverage up to \$50 by 7.4 percent, which is below the rate case average increase of 7.6 percent. The remaining COD fees increased an average of approximately 8 percent and are the result of applying an incremental fee of \$1.15, which increases from \$1.05. The Commission also calculates new fees for registered COD, notice of nondelivery, and alteration of COD by applying an increase of 8.3 percent, 7.9 percent and 7.9 percent respectively to the Docket No. R2005-1 fees. The Commission adopts the Service's proposed fee of \$4.10 for Restricted Delivery with COD. The fees produce a cost coverage of 110.3 percent. The Commission finds the low cost coverage appropriate as the service is experiencing performance problems.

[6119] The Commission adopts the Postal Service's proposal to modify the language regarding the notice of nondelivery for clarification purposes.

15. Return Receipt (Fee Schedule 945)

[6120] Return Receipt service provides the mailer with proof that an item has been received. Mailers receive an original or copy of the recipient's signature, the date delivered and the address of delivery, if different from the address on the mailpiece. Four types of return service exist: Basic Return Receipt, Return Receipt for Merchandise, Return Receipt After Mailing, and Electronic Return Receipt. USPS-T-39 at 61. Electronic Return Receipt provides the same information as the Basic Return

Table V-11
Recommended Fees for COD

Description	Current	PRC Recommended
Up to \$50	\$4.75	\$5.10
Up to \$100	\$5.80	\$6.25
Up to \$200	\$6.85	\$7.40
Up to \$300	\$7.90	\$8.55
Up to \$400	\$8.95	\$9.70
Up to \$500	\$10.00	\$10.85
Up to \$600	\$11.05	\$12.00
Up to \$700	\$12.10	\$13.15
Up to \$800	\$13.15	\$14.30
Up to \$900	\$14.20	\$15.45
Up to \$1000	\$15.25	\$16.60
Registered COD	\$4.20	\$4.55
Notice of Non-Delivery	\$3.15	\$3.40
Alteration of COD	\$3.15	\$3.40
Restricted Delivery	\$3.15	\$4.10

Receipt, but in an electronic format via e-mail. Return Receipt After Mailing allows a customer to purchase the Return Receipt service after the item has been mailed.

[6121] Basic Return Receipt, Return Receipt After Mailing and Electronic Return Receipt are available for Express Mail, First-Class Mail and Priority Mail when purchased at the time of mailing with one of the following host special services: Certified Mail, COD, Registered Mail, and Insurance requiring a signature. Additional services available in conjunction with Return Receipt service are Delivery Confirmation, Parcel Airlift, Restricted Delivery, Signature Confirmation, and Special Handling. *Id.* at 61-62.

[6122] Return Receipt for Merchandise is available for Priority Mail, Standard Mail subject to the residual shape surcharge when Bulk Insurance is also purchased, and Package Services mail, but it does not require a customer to purchase any host special service. Delivery Confirmation, Insurance requiring a signature, Parcel Airlift and Special

Handling are additional services that a customer can purchase in conjunction with Return Receipt for Merchandise. *Id.*

[6123] The Postal Service proposes a classification change based on its proposal to no longer collect signatures for items insured for less than \$200. USPS-T-40 at 24. The Service recommends that the language in DMCS § 945.121 be modified to reflect that Return Receipt is available with Insurance greater than \$200, not \$50. Tr. 19/6776.

[6124] The Postal Service determines the fees for Return Receipt using the methodology relied on in Docket No. R2005-1. USPS-T-23 at 14. The Service proposes to increase the following fees: Basic Return Receipt from \$1.85 to \$2.15; Return Receipt for Merchandise from \$3.15 to \$3.50; and Return Receipt After Mailing from \$3.45 to \$3.80. USPS-T-39 at 60.

[6125] The Postal Service is proposing to decrease the Electronic Return Receipt fee from \$1.35 to \$0.85. *Id.* Postal Service witness Page explains that the decrease is due to a change in his assumptions from Docket No. R2005-1; he no longer assumes that sending the electronic return receipt via e-mail has a cost. USPS-T-23 at 15. Decreasing the fee to \$0.85 reduces the per-unit contribution for Electronic Return Receipt from \$0.46 to \$0.41, which is comparable to the Docket No. R2005-1 per-unit contribution of \$0.42 for Basic Return Receipt. USPS-RT-17 at 7. Witness Berkeley testifies that the higher cost coverage for Electronic Return Receipt as compared to Basic Return Receipt is justified because the faster availability of the signature provides a higher value of service. Tr. 15/4374.

[6126] As in Docket No. R2005-1, witness Page again uses the acceptance window transaction time for Basic Return Receipt to calculate the cost of the electronic version, because the window service field study did not collect data on window times for Electronic Return Receipt. In support of relying on the Basic Return Receipt window time of 25 seconds, witness Page asserts that for Electronic Return Receipt the window clerk must explain the procedure for obtaining the signature online, which takes time. USPS-T-23 at 14-15. Because the volume of Electronic Return Receipt is still low and the Postal Service is promoting greater usage, witness Berkeley explains that it is

probable that many transactions involve new customers who require more in-depth explanations. USPS-RT-17 at 3-4, 6-7. Anticipating more consumers of Electronic Return Receipt, the Postal Service is improving the service by distributing new scanners that capture the recipient's signature at delivery, making signatures available eight hours after the scanner is cradled. *Id.* at 5. The signature will no longer be sent to the Computerized Forwarding System to be scanned into the database. The Postal Service is also planning to modify the Automated Postal Center kiosks to allow the purchase of Electronic Return Receipt.

[6127] *Intervenor comments.* Carlson contends that Basic Return Receipt and Electronic Return Receipt transactions differ, and thus the 25 second acceptance window transaction time for Basic Return Receipt should not be used to calculate the cost of Electronic Return Receipt. He provides an example of an Electronic Return Receipt transaction, and indicates that a time of 10 to 15 seconds is more appropriate. DFC-T-1 at 6-7. Carlson faults the Postal Service for relying on a study that does not identify the number of post offices visited and does not indicate whether any Electronic Return Receipt transactions were observed. *Id.* at 7-8. He argues that the planned modification to the Automated Postal Center kiosks allowing customers to purchase electronic receipts without going to the retail window further emphasizes that the acceptance cost for Basic Return Receipt can not be used as a proxy for Electronic Return Receipt. Carlson concludes that the Postal Service has not provided adequate evidence to support an acceptance time of 25 seconds for Electronic Return Receipt. Carlson Brief at 20- 21; DFC-T-1 at 7-8.

[6128] Carlson also asserts that the Postal Service has failed to demonstrate that Electronic Return Receipt has a higher value of service than regular receipt or to justify a higher cost coverage of 194.5 percent compared to 145.8 percent. He contends that customers do not receive signatures faster with electronic receipt because the signatures must be scanned at the Computerized Forwarding System, and questions whether the new scanners will provide faster delivery of the signature. Carlson Brief at 21-22; DFC-T-1 at 8-9. He argues that the speed of receiving the signature is not

important to a majority of Electronic Return Receipt customers, and that the percent of electronic return receipts without signatures is too high for a service that customers pay extra for. The value of Electronic Return Receipt is further diminished because the service must be purchased at a retail window and customers seeking to register experience delays before the transaction appears in the Postal Service's tracking system. Based on the low value of service, Carlson proposes matching the cost coverage of Electronic Return Receipt to that of Basic Return Receipt at 145.8 percent, which results in a fee of \$0.65 (\$0.63 rounded to the nearest nickel). DFC-T-1 at 11-14.

[6129] The Postal Service responds that considerable risk exists that Carlson's proposal to set the fee at \$0.65, which reduces the proposed per-unit contribution from \$0.41 to \$0.22, will not cover costs for any transactions in which the customer has significant questions for the clerk. Also, the contribution from an Electronic Return Receipt fee of \$0.65 will be less than one-third of the proposed contribution from Basic Return Receipt. USPS-RT-17 at 7-8. The Postal Service speculates that a new cost study for Electronic Return Receipt will increase, rather than decrease, the cost estimate it provided. Postal Service Brief at 392. The Postal Service argues that slowly reducing the price of electronic receipt during its development is best, because keeping the price stable will limit the risk of a subsequent price increase due to a future analysis of electronic return receipt window service costs. Postal Service Reply Brief at 305-6.

[6130] *Commission analysis.* The Commission recommends the modifications to the DMCS language and the fees for Return Receipt proposed by the Postal Service. In an ideal world the Postal Service would have a separate acceptance window transaction time for Electronic Return Receipt. The Commission acknowledges, however, that the volume of Electronic Return Receipt is too low to justify the cost of conducting a study to determine a separate transaction time for Electronic Return Receipt.²⁸⁴ The Postal Service's arguments supporting its reliance on the Basic Return Receipt acceptance

²⁸⁴ As Carlson explained, an observer might not witness one Electronic Return Receipt transaction let alone a statistically significant number because on average each facility has fewer than seven transactions per year. DFC-T-1 at 8.

time for the electronic version are persuasive. The Commission recognizes that the Postal Service's plans to implement new scanners and to modify the Automated Postal Centers will increase the value of Electronic Return Receipt.

[6131] The fees recommended by the Commission produce a cost coverage of 142.1 percent. This is reasonable for a high value service that provides mailers with the recipient's signature.

16. Restricted Delivery (Fee Schedule 946)

[6132] Restricted Delivery allows a mailer to limit mail delivery to the addressee or the addressee's authorized agent. The addressee or agent must be an individual specified by name. The purchase of a host service, such as Certified Mail, COD, Insurance requiring a signature, or Registered Mail, is required for Restricted Delivery. Restricted Delivery is available both at the time of mailing and after mailing. If purchased after mailing, additional charges may be assessed to cover the cost of contacting the delivery post office. USPS-T-39 at 56-57.

[6133] The Postal Service proposes a classification change based on its proposal to no longer collect signatures for items insured for less than \$200. Tr. 19/6776; USPS-T-40 at 24. The Service recommends that the language in DMCS § 946.12 be modified to reflect that Restricted Delivery is available with Insurance greater than \$200, not \$50. Tr. 19/6776.

[6134] The fee for Restricted Delivery is charged in addition to postage and the applicable fee of the host special service. The estimated test year cost of Restricted Delivery is \$2.51. The Postal Service proposes to increase the current fee of \$3.70 to \$4.10. USPS-T-39 at 58.

[6135] The Commission recommends the classification change and fees proposed by the Postal Service. It finds the 163.6 percent cost coverage appropriate for a high value service that is desirable to mailers and recipients concerned with controlling or restricting the delivery of mail to the addressee or their agent.

17. Certificate of Mailing (Fee Schedule 947)

[6136] A certificate of mailing provides the mailer with evidence that an item was presented to the Postal Service for mailing. This service does not supply proof of delivery or insurance against damage or loss. Certificates of Mailing service is available for individual First-Class Mail, Priority Mail, or Package Services mailpieces, as well as bulk mailings. Lower fees are charged for certificates of mailing from a firm mailing book or customer manifest. A duplicate certificate of mailing is available for a fee at the time of the mailing or upon presentment of the original certificate. USPS-T-40 at 12-13.

[6137] The Postal Service proposes increases to the certificate of mailing fees. Table V-12 shows the current and proposed fees for this service.

Table V-12
Proposed Certificates of Mailing Fees

Service	Current Fee	Proposed Fee
Individual Pieces		
Original Certificate	\$0.95	\$1.05
Firm Mailing Book	\$0.30	\$0.35
Duplicate Copy	\$0.95	\$1.05
Bulk Pieces		
First 1,000 pieces	\$4.75	\$5.50
Each Additional 1,000 Pieces or Fraction	\$0.55	\$0.60
Duplicate Copy	\$0.95	\$1.05

Adapted from USPS-T-40 at 12, Table 2.

[6138] The Commission recommends the Postal Service’s proposed fees for Certificate of Mailing. The fees provide a cost coverage of 142.3 percent. This cost coverage is reasonable for a service that provides significant value to individuals requiring evidence of mailing.

18. Delivery Confirmation (Fee Schedule 948)

[6139] Delivery Confirmation provides a mailer with information about the date and time that an article was delivered or, if delivery was not successful, the date and time of attempted delivery. Delivery Confirmation can be purchased as a manual (retail) or electronic service. Retail and electronic mailers can access delivery information over the Internet. In addition, retail mailers can obtain delivery data via a toll-free call to the corporate call management system. The Postal Service maintains delivery information on file for both the retail and electronic services. USPS-T-39 at 33.

[6140] The Postal Service requires that mailers provide a mailing receipt if purchasing the retail service or an electronic manifest if using the electronic service. Mailers electing electronic Delivery Confirmation must also apply a barcode to the mailpiece and establish an electronic link with the Postal Service to exchange the electronic acceptance and delivery data. USPS-T-23 at 6.

[6141] Delivery Confirmation is currently available with First-Class Mail parcels, Priority Mail, Standard Mail parcels (electronic service only), Parcel Select parcels (electronic service only), and Package Service parcels. Mailers can purchase Delivery Confirmation in conjunction with Certificates of Mailing, COD, Insurance, Registered Mail, Return Receipts for Merchandise, and Special Handling. Restricted Delivery and Return Receipt are also available with Delivery Confirmation if purchased with either numbered Insurance, COD, or Registered Mail. USPS-T-39 at 33-34.

[6142] Postal Service witness Page modifies the methodology used in Docket No. R2005-1 to calculate the rates for Delivery Confirmation. Page distributes the window acceptance costs between the manual and electronic services because some electronic customers are submitting items with electronic labels at the window, thereby incurring window acceptance costs that were not included in past dockets. USPS-T-23 at 6. The Postal Service proposes 25 to 30 percent increases to all the Delivery Confirmation fees. Table V-13 lists the Postal Service's proposed fees for Delivery Confirmation. USPS-T-39 at 32-33.

Table V-13
Delivery Confirmation Fees

	Electronic		Retail	
	Current	USPS Proposed	Current	USPS Proposed
First-Class	\$0.14	\$0.18	\$0.60	\$0.75
Priority Mail	\$0.00	\$0.00	\$0.50	\$0.65
Standard	\$0.14	\$0.18	N/A	N/A
Parcel Select	\$0.00	\$0.00	N/A	N/A
Package Services	\$0.14	\$0.18	\$0.60	\$0.75

[6143] The Commission recommends the fees for Delivery Confirmation proposed by the Postal Service, resulting in a cost coverage of 116.3 percent. Although the 25 to 30 percent increases in fees are higher than the average increase for special services in this case, Delivery Confirmation is a relatively high value service and, as such, needs to maintain an adequate contribution to institutional costs.

19. Signature Confirmation (Fee Schedule 949)

[6144] Signature Confirmation provides a mailer access to Delivery Confirmation information and an image of the recipient's signature. It must be purchased at the time of mailing, and is available with First-Class Mail parcels, Priority Mail, and Package Service parcels. Signature Confirmation can be used in conjunction with Certificates of Mailing, Collect on Delivery, Insurance, Registered Mail, Restricted Delivery (if purchased with signature Insurance, COD, or Registered Mail) and Special Handling. USPS-T-39 at 67-68.

[6145] Signature Confirmation can be purchased as a manual (retail) or electronic service. With the retail service, mailers obtain delivery data via a toll-free call to the Corporate Call Management Program or over the Internet. Electronic Signature

Confirmation requires the mailer to establish an electronic link with the Postal Service to exchange acceptance and delivery data. *Id.* at 67-68.

[6146] Although the per-piece costs vary by class for this service, the Postal Service proposes set fees for electronic and retail Signature Confirmation regardless of the class of the mailpiece. The Postal Service suggests increases from \$1.35 to \$1.75 for electronic service and from \$1.90 to \$2.10 for retail service. *Id.* at 66.

[6147] The Commission recommends the fees for Signature Confirmation as proposed by the Postal Service. The fees produce a 139.7 percent cost coverage, which is suitable for a service that provides a signature and is the least expensive signature service.

20. Parcel Airlift (Fee Schedule 951)

[6148] Parcel Airlift provides air transportation of parcels to or from military post offices outside the contiguous 48 states. This service is provided on a space-available basis for Package Services mail that does not exceed 30 pounds in weight or 60 inches in length and girth combined. The parcel's weight determines the fee, which is in addition to postage. USPS-T- 40 at 40.

[6149] The Postal Service proposes several classification changes based on its proposal to no longer collect signatures for items insured for less than \$200. *Id.* at 24. The Service requests that the language in DMCS § 951.51 be modified to reflect that Parcel Airlift is available with Restricted Delivery and Return Receipt when purchased in conjunction with Insurance greater than \$200. Tr. 19/6776.

[6150] The Postal Service proposes to increase the fee for Parcel Airlift, but provides no costs for Parcel Airlift due to unit cost measurement difficulties. The fees will increase as follows: parcels up to 2 pounds from \$0.45 to \$0.50; parcels over 2 pounds but not more than 3 pounds from \$0.90 to \$1.00; parcels over 3 pounds but not more than 4 pounds from \$1.30 to \$1.45; and parcels over 4 pounds from \$1.80 to \$2.00.

USPS-T-40 at 39-41. The Commission recommends the classification change and proposed fees for Parcel Airlift.

21. Special Handling (Fee Schedule 952)

[6151] Special Handling provides preferential handling during processing and transportation, but does not provide preferential delivery. While a mailer may request this service with First-Class Mail, Priority Mail, and Package Services, Special Handling is required when shipping honeybees, crickets, or baby poultry using Package Services. Additional services available in conjunction with Special Handling are COD, Insurance, Parcel Airlift, and Return Receipt for Merchandise.

[6152] The Postal Service proposes a 10 percent total increase in the fees for this service. The item's weight determines the fee, which is in addition to postage. The Service proposes that the fee for items up to 10 pounds increase from \$6.25 to \$6.90, while the fee for items over 10 pounds increase from \$8.70 to \$9.60. USPS-T-40 at 45-46.

[6153] In the past four rate cases (Docket Nos. R97-1, R2000-1, R2001-1, and R2005-1) the Postal Service proposed fee increases based on unreliable cost estimates. In Docket Nos. R97-1 and R2000-1, the Commission found that it could not recommend an increase to special handling fees because the cost estimates were questionable and a sufficient record to justify any change did not exist. In the most recent two cases, Docket Nos. R2001-1 and R2005-1, the Commission felt constrained by the settlements to raise fees and urged the Postal Service to undertake the long anticipated cost study for Special Handling.

[6154] Due to the enactment of the PAEA, this proceeding will be the last omnibus rate case the Commission proceeds over unless the Postal Service files a request to modify the rates before December 20, 2007. The Commission acknowledges that the Postal Service will not be able to conduct a reliable study in the limited time frame for

filing a final case. It recommends the Special Handling fees proposed by the Postal Service.

22. Stamped Envelopes (Fee Schedule 961)

[6155] Stamped Envelopes, *i.e.*, envelopes with postage pre-attached, may be purchased from the Postal Service as individual envelopes, in household quantities of 50, or bulk quantities of 500. Envelope formats include regular, window, pre-cancelled regular, and pre-cancelled window. They may be purchased plain or with printed personalized information for a higher fee. Envelopes may be printed with different postage values, including pre-sort and non-profit rates. USPS-T-39 at 76-77.

[6156] The Stamped Envelopes volume has steadily declined with 2005 recording the lowest volume ever. The Postal Service proposes 9 to 13 percent increases in the fees.

Table V-14

Proposed Stamped Envelope Fees

Type	Current	USPS Proposed
Basic 6-3/4, each	\$0.08	\$0.09
Basic 6-3/4, 500	\$13.00	\$14.50
Plain over size 6-3/4, each	\$0.08	\$0.09
Plain over size 6-3/4, 500	\$15.00	\$16.50
Personalized 6-3/4, 50	\$3.75	\$4.25
Personalized 6-3/4, 500	\$18.00	\$20.00
Personalized over size 6-3/4, 50	\$3.75	\$4.25
Personalized over size 6-3/4, 500	\$21.00	\$23.00

Adapted from USPS-T-39 at 76, Table 15.

[6157] The Commission recommends the proposed rates for Stamped Envelopes and calculates a cost coverage of 104.1 percent. The Commission finds the cost

coverage justifiable because the service encourages the use of the mailstream and provides a low cost method for individuals to send mail.

23. Stamped Cards (Fee Schedule 962)

[6158] Stamped Cards are cards with postage pre-affixed. The Postal Service offers Stamped Cards for the price of First-Class postage and a fee for the card. Stamped Cards are available in single units, doubles (one for the sender and one for the return mailer), and in sheets of 40.

[6159] The Postal Service proposes to retain the current stamped cards fees of \$0.02 for the single card, \$0.04 for the double reply-paid cards, and \$0.80 for the sheet of 40 uncut cards. *Id.* at 71-72.

[6160] The Commission recommends the rates proposed by the Postal Service, producing a 135.2 percent cost coverage. Consistent with past decisions, the Commission supports a relatively low cost coverage in order to provide a low cost method for individuals to send mail. However, the whole cent rounding criteria constrains the Commission from setting a lower rate for this service, which has costs above one cent per card.

24. Money Orders (Fee Schedule 971)

[6161] The Postal Service offers a domestic money order, APO/FPO (military) money order, and an inquiry service. Traditionally, domestic money order usage has been thought to be weighted toward people with modest income levels, people without checking accounts, or people without credit cards. Postal money orders are popular in rural areas where access to alternative money order services is limited. APO/FPO money orders are generally sold to military personnel at military installations. Both domestic and APO/FPO money orders can be issued up to a maximum amount of

\$1,000. Inquiry service verifies whether a postal money order was cashed, and provides a copy of the paid money order. USPS-T-39 at 44-45.

[6162] The Postal Service proposes to increase the fees for this service, and contends that the proposed fees barely cover costs. The proposed fee increases are as follows: domestic money orders up to \$500 will increase from \$0.95 to \$1.10; domestic money orders between \$500.01 and \$1,000 will increase from \$1.30 to \$1.50; and APO/FPO money orders will increase from \$0.25 to \$0.30. *Id.* at 43, 48.

[6163] The Postal Service also proposes raising the inquiry fee from \$3.15 to \$5.00. To support the 58.8 percent fee increase, the Service provides a new cost methodology based on using the money order volume change between the base year and test year to calculate the inquiry inflation factor, as opposed to the past methodology of using the cost ratio. USPS-T-23 at 11. Additionally, form PS6401 can now be scanned, so the unit cost per form was updated to \$4.97. USPS-T-39 at 47.

[6164] *Commission analysis.* The Commission adopts the Postal Service's new methodology for calculating the unit cost per inquiry based on volume data. This cost methodology is more accurate than the previous methodology, which simply applied the cost increase ratio of the money order fee to compute the cost for the inquiry fee. The Commission recognizes that the new methodology results in a 58.8 percent increase to the inquiry fee, but finds that the increase is necessary to cover the costs of this service, which is labor intensive. The Commission concludes that the increase will not have a significant impact, as the volume of money order inquiries is minimal.

[6165] The Commission recommends the fees proposed by the Postal Service for money order inquiries, APO/FPO money orders, and domestic money orders valued between \$500.01 and \$1,000. It is concerned with raising the fee from \$0.95 to \$1.10 for domestic money orders valued up to \$500. Because money orders are a vehicle for people of modest means or limited access to financial alternatives to pay for necessary goods and services, the Commission recommends a fee of \$1.05 for domestic money orders up to \$500. The corresponding overall cost coverage is 150 percent.

25. Confirm (Fee Schedule 991)

[6166] Confirm service permits subscribing customers to obtain information electronically regarding when and where mailpieces undergo barcode scans in mail processing operations. Scan information is not guaranteed for every piece of qualifying mail. Destination Confirm is for a subscriber's outgoing mail while Origin Confirm is for reply mail incoming to the subscriber. Destination Confirm customers must electronically notify the Postal Service, or "start the clock," prior to entering mail into the system. Confirm service is available for First-Class Mail (including Priority), Standard, Periodicals, and Package Service automation compatible mail. USPS-T-40 at 15.

[6167] The Postal Service proposes classification changes, including the removal of the "start the clock" requirement, and a new pricing structure. Currently, Confirm service is available at three subscription levels for set fees: Silver for \$2,000, Gold for \$4,500, and Platinum for \$10,000. The Silver subscription has a term of three months and includes up to 15 million scans with the option to obtain additional scans in blocks of 2 million. The Gold subscription spans a 12-month period and permits up to 50 million scans with the option to obtain additional scans in blocks of 6 million. The Platinum subscription allows unlimited scans for three months. The Silver and Gold subscriptions include one identification (ID) code, while the Platinum subscription has three. Subscribers at any level may license additional ID codes for \$500 for a term of three months or until the subscription expires. *Id.* at 16.

[6168] The Postal Service proposes to replace the subscription-based pricing structure with a transaction-based structure that includes a flat subscription fee. A subscription will cost \$5,000 and consist of one ID code and 1 million units. One unit will not equal one scan, but rather will be the currency used to purchase scans at the following rates: one unit per scan of First-Class Mail pieces and five units per scan of other classes of mailpieces (5 to 1 ratio). Subscribers will buy additional units in one million blocks. The price of a block will decline as the scan's marginal cost approaches zero, such that a subscriber will pay \$70.00 per block for the first through ninth additional

blocks, \$35.00 per block for the tenth through 99th blocks, and \$17.50 per block for the 100th and more blocks. USPS-T-40 at 16-17. The Postal Service estimates that the number of Confirm subscriptions will remain the same under this transaction-based structure and that the demand for scans will decrease 10 percent from current usage. Tr. 14/3938, 3974. It calculates a cost coverage of 126.3 percent. USPS-T-40 at 19.

[6169] The Service seeks to modify the pricing structure for Confirm because the current tiered structure never produced sufficient revenue to cover costs. It explains that Confirm has fewer subscribers than anticipated as potential customers chose to obtain Confirm service through resellers. Due to the unlimited scan option, little incremental revenue is generated when customers use resellers as opposed to obtaining a Confirm subscription. Postal Service Brief at 379-380.

[6170] The Postal Service claims that increasing the fees of the current price structure will not enable Confirm to cover costs. It argues that subscribers will turn to resellers rather than retain their own subscription or will migrate to the Gold tier from the Platinum tier. USPS-RT-13 at 6. It asserts that the proposed pricing structure will provide revenue to cover costs while fulfilling the factors in §3622(b). The Postal Service also claims that its proposal provides flexibility for future enhancements and facilitates the addition of other information-based services, such as scanning containers. Postal Service Brief at 380-82.

[6171] The Postal Service finds the current structure unfair because subscribers within a tier pay the same subscription fee while using disparate numbers of scans. USPS-RT-13 at 6. It contends that its proposal improves fairness and equity by closing the gap between the price per scan paid by small volume users. The structure will shift more of the fee burden to the larger users, and will make Standard Mail customers pay a greater share of the cost relative to First-Class Mail customers. Postal Service Brief at 381. The Service explains that First-Class Mail provides greater value of service, which permits a lower fee for First-Class Mail scans. Postal Service Reply Brief at 296.

[6172] *Major Mailers Association's proposal.* The Major Mailers Association (MMA) proposes that the Postal Service offer First-Class presort mailers unlimited scans

for a fixed annual fee that covers the costs of establishing and maintaining the accounts. It acknowledges that its proposal is silent on fees for Standard Mail scans. MMA believes its proposal will encourage new subscribers and will help offset the cost of providing Confirm, which is minimal in comparison to the First-Class workshared mailers' large institutional cost contribution. It argues that offering Confirm at a lower cost will enable the Postal Service to establish a solid link with its most profitable class, the First-Class workshared mailers, and to match its competitors, which offer this tracking service as a feature of their delivery services. Because the costs of providing Confirm are mostly fixed, MMA asserts that its marketing approach makes sense. MMA Brief at 1-2, 24-26.

[6173] The Postal Service claims that MMA implicitly supports the Service's 5 to 1 cost ratio for scans because MMA argued that First-Class Mail's unit contribution, which is twice that of Standard Mail, justifies a lesser charge for First-Class scans. The Service contends that MMA's proposal is incomplete as it does not address many issues, such as whether mailers sending both First-Class and Standard Mail will need two subscriptions. USPS-RT-13 at 25-26. It states that MMA's proposal can not be adopted because MMA did not propose fees for Standard Mail scans or a classification change to bundle Confirm service with First-Class Mail. The Service asserts that the record lacks evidence that MMA's proposal will cover costs as required by statute. Postal Service Brief at 387.

[6174] MMA disputes the obstacles the Postal Service asserted to offering First-Class presort mailers unlimited scans for a reasonable fee. It contends that a classification change bundling Confirm service with classes of mail is unnecessary because First-Class mailers will still subscribe to the Confirm service and pay a fee. It believes that its proposal will meet costs because the Service is seeking excessive revenues while the MMA rate structure might attract subscribers to the service. MMA Reply Brief at 39-40. It explains that an increase to the annual fee will remedy any revenue shortfall. As an alternative to its proposal, MMA espouses retaining the current rate structure and urges a minimal rate increase. MMA Brief at 26.

[6175] The American Bankers Association (ABA) and GrayHair Software support MMA's proposal, with GrayHair further suggesting that the costs of scans be built into all market dominant classes. ABA Brief at 26; GrayHair Brief at 11.

[6176] *OCA's Proposal*. OCA proposes to keep the current pricing structure and to increase the subscription fees as follows: the Silver subscription fee will remain at \$2,000; the Gold subscription fee will increase 15.6 percent from \$4,500 to \$5,200; the Platinum subscription fee will increase 95 percent from \$10,000 to \$19,500; and the cost for additional quarterly ID codes will increase from \$500 to \$750. Annual ID codes remain at \$2,000. OCA Brief at 114, 116. Assuming that the number of subscribers remains constant at 16 Silver, 119 Gold, and 45 Platinum, OCA estimates its proposal will result in a 127.3 percent cost coverage. OCA Brief at 114, 116.

[6177] OCA asserts that based on the demonstrated behavior of current customers to oversubscribe, its assumption that the fee increases will not effect the subscription rates is reasonable. While the Postal Service contends that Platinum subscribers will seed mailings or switch to a Gold subscription, OCA counters that the Postal Service lacks understanding of the behavior of the current Platinum subscribers whose demand could be fulfilled by a Gold subscription. Because 29 current Platinum subscribers only use Gold-level volumes, OCA argues that subscribers are not as price sensitive as the Postal Service thinks. OCA contends that seeding is a response to transaction-based fees, not higher subscription-based fees as the Postal Service asserts. *Id.* at 117-19.

[6178] OCA argues that its proposal is likely to produce a cost coverage of 127.3 percent because subscribers support the proposed subscription-based fees and the purchase of additional ID codes will generate revenue not included in the estimated cost coverage. Based on the Postal Service's assumption that its transaction-based structure will result in a 10 percent reduction in scans, OCA estimates that this 10 percent reduction equals a shift of five subscribers from the Platinum tier to Gold tier under its proposal. It contends that shifting these five subscribers will reduce its projected cost coverage from 127.3 percent to 121.4 percent, and that eliminating these five subscribers from Confirm entirely will result in a cost coverage of 119.2 percent. It

claims that more than 22 subscribers must migrate from the Platinum tier to the Gold tier for the cost coverage to drop below 100 percent. OCA explains that a lower cost coverage will reflect decreased value of service if subscribers switch tiers or end their subscriptions. *Id.* at 119-22.

[6179] *Postal Service comments on OCA's proposal.* The Postal Service asserts that OCA's proposal is unlikely to generate adequate revenues to cover costs because OCA made risky assumptions about subscriber reaction to the proposed Platinum fee increase, such as: (1) no migration to a less expensive tier; (2) no elimination of subscriptions; (3) no decrease in demand; and (4) no impact from arbitrage. USPS-RT-13 at 6. The Postal Service contends that all the current subscribers must accept OCA's proposed increases for OCA's cost coverage to be met. Postal Service Brief at 383.

[6180] The Service argues that customers will not continue to oversubscribe. It contends that customers view scans as a discretionary good and will begin seeding, move to a less expensive tier, or switch to a reseller in response to the fee increases proposed by OCA. It argues that OCA's proposal depends on subscribers retaining Platinum subscriptions where the Gold tier will satisfy their demand despite the large fee increase. The Postal Service explains that as the price gap between the Gold and Platinum tiers increases under OCA's proposal, the number of scans for which a Gold subscription costs less than a Platinum subscription also increases. It notes that 29 Platinum subscribers will save at least \$12,800 by becoming Gold subscribers, and at least seven of these subscribers must remain Platinum subscribers for OCA's proposal to result in a cost coverage greater than 100 percent. USPS-RT-13 at 7-9, 12. The Service argues that if 30 subscribers migrate to Gold and purchase 1 block of 6 million scans each, the revenue will be \$406,500 less than OCA projected. Postal Service Brief at 384. It adds that three Silver subscribers that are purchasing four consecutive subscriptions will pay less by migrating to the Gold tier. Tr. 19/6791.

[6181] The Postal Service asserts that although OCA agrees the Service's proposal will decrease scan usage, OCA does not consider that its proposal will lead to a

reduction in subscriptions, a migration to a lower tier, or seeding. It contends that as more subscribers migrate to the Gold tier from Platinum, the Platinum subscription fee will have to be increased, which in turn will cause more subscribers to migrate.

USPS-RT-13 at 10-13; Postal Service Brief at 384. It notes that the scan fee under its proposal limits the impact of movement from the Platinum to the Gold tier. USPS-RT-13 at 14.

[6182] The Postal Service is concerned that OCA's proposal will promote pure arbitrage because a reseller who purchases unlimited scans for a fixed price can sell the scans at a price that is less than a subscription. It asserts that while pure arbitrage is not currently a problem because resellers are selling value added scans, Confirm's inability to cover costs is a problem that could be made worse if the potential for pure arbitrage is realized. The Service argues that increasing the Platinum subscription fee will increase the opportunity for pure arbitrage because the reseller can charge more for scans and have fewer customers. It contends that because OCA did not consider arbitrage, each customer that moves to a reseller under OCA's proposal results in a revenue loss that requires larger fee increases to offset, thereby imposing a greater cost burden on the remaining subscribers. In contrast, the Service notes that the revenue from those customers is not lost under its proposal because the reseller must purchase additional scans for each new customer it obtains. *Id.* at 14-17.

[6183] The Postal Service explains that under the current fee structure customers within a tier pay different costs per scan depending on the number of scans used. It contends that OCA's proposal exacerbates these differences and continues to favor high volume users. The Service asserts that its proposal charges customers using an equal number of scans the same fees, thus improving fairness and equity. It recognizes that a per-scan price difference still exists between large- and small-volume users under its proposal, but argues that the price gap is diminished. *Id.* at 18-19.

[6184] The Postal Service asserts that OCA's fee structure does not offer the flexibility to differentiate among the various types of data that future enhancements may make possible or the relative cost of gathering and distributing that data. In contrast, the

Service notes that its proposal to base fees on units rather than scans accommodates the potential of using Confirm to disseminate information made possible by technology. *Id.* at 23-24.

[6185] The Postal Service argues that its proposed transaction-based fee structure is simpler than a subscription-based structure with an unlimited tier because customers can not oversubscribe. It emphasizes that only 15 subscribers (8.3 percent), those using more than 92 million scans, receive value and benefit financially from the availability of an unlimited tier, and that most new subscribers will fall into the Gold, not Platinum, tier. *Id.* at 20-22.

[6186] *Intervenor comments.* OCA, MMA, GrayHair, ABA, the Mail Order Association of America (MOAA), the Association for Postal Commerce and the Mailing and Fulfillment Service Association (PostCom), The Flute Network, and ANM, et al.²⁸⁵ criticize the Postal Service on brief and argue that the Postal Service's proposal should be rejected. In support, the participants attack various aspects of the Postal Service's proposal arguing that: (1) the transaction-based structure will reduce scan usage; (2) the large increase in fees will decrease demand for scans; (3) the use of Confirm service as a performance measurement tool will decline; (4) the 5 to 1 ratio is arbitrary and discriminatory; (5) the proposal will not increase fairness and equity amongst subscribers; (6) the proposed structure is more complex; (7) the current structure can support future enhancements; (8) an unlimited tier has benefits that a transaction-based structure does not provide; (9) resellers enhance the Confirm service; and (10) a subscription-based structure can cover costs. Each of these contentions is discussed in turn below.

[6187] *Transaction-based structure will reduce scan usage.* OCA, ANM, et al., GrayHair, MOAA, and PostCom argue that charging a transaction-based fee for Confirm scans, which turns a scan into a discretionary good, will discourage the use of Confirm

²⁸⁵ Brief of the Alliance of Nonprofit Mailers, National Association of Presort Mailers, National Postal Policy Council, and Office of Consumer Advocate on Pricing of Confirm Service, December 21, 2006 (ANM, *et al.*).

and will generate less revenue than estimated. OCA Brief at 124, 126; ANM, et al. Brief at 24-35; GrayHair Brief at 2; MOAA Brief at 26; PostCom Brief at 42. Although the Postal Service acknowledges that its structure will decrease scan demand, OCA and ANM, et al. assert that the Postal Service's estimated 10 percent decline in scans is arbitrary and not supported by any market research. OCA Brief at 123; ANM, et al. Brief at 26-35. MOAA notes that the 10 percent reduction in volume under the proposed fee structure is greater than the reduction forecast for any of the classes of mail, and argues that a greater loss of scan volume or revenues under the existing fee structure is unlikely. MOAA Brief at 26. GrayHair argues that in addition to decreasing demand, any per-scan charge is likely to exceed the scan's cost, which is negligible. GrayHair Brief at 2.

[6188] *Large increases to fees will decrease demand for scans.* OCA, ANM, et al., MMA, and GrayHair claim that the large increases to subscription fees under the proposed structure will negatively affect demand for scans. OCA Brief at 125-6; ANM, et al. Brief at 24-35; MMA Brief at 5, 23; GrayHair Brief at 14. GrayHair contends it will face a 460 percent increase in fees. GHS-T-1 at 16. OCA argues that subscribers could experience the following increases in fees: 189 percent for Silver subscribers, 56 percent for Gold subscribers, and 102 percent for Platinum subscribers using 750 million scans, which the Postal Service claims is the maximum number currently being used. OCA-T-5, Attachment 1; Tr. 14/4144. MMA asserts that subscribers facing double and triple digit increases will curtail or eliminate their use of Confirm. MMA Brief at 23.

[6189] MOAA asserts that the Postal Service's 5 to 1 ratio produces widely differing rate increases or decreases for mailers regardless of their current subscription level. MOAA Brief at 23. OCA asserts that charging more for scans of Standard Mail than First-Class will depress demand for scans of Standard Mail. OCA Brief at 124, 126.

[6190] OCA, ANM, et al. and GrayHair argue that Confirm usage will not decline as dramatically under the rate increases proposed by OCA. OCA Brief at 125-6; GrayHair Brief at 14; ANM, et al. Brief at 24-35. The ABA offers that keeping Confirm at a

reasonable price under the current structure will increase the banking industry's use of Confirm. ABA Brief at 27.

[6191] The Postal Service disputes GrayHair's assertion that it will experience a 460 percent increase under the Postal Service's proposal, and asserts that the increase corresponds to potential business growth that would require GrayHair to purchase additional scans. Postal Service Reply Brief at 298.

[6192] *Use of Confirm service as a performance measurement tool will decline.* OCA, ANM, et al., MOAA, GrayHair, The Flute Network, and ABA assert that by suppressing scan usage through higher fees, the transaction-based structure will result in Confirm being much less comprehensive and useful as a performance measurement tool. OCA Brief at 113; ANM, et al. Brief at 10-11; ANM, et al. Reply Brief at 7-9; MOAA Brief at 23; GrayHair Brief at 3; Flute Brief at 29. MOAA further asserts that the Postal Service should maximize the use of Confirm because it provides a performance measurement tool at the mailers' expense. It emphasizes that the use of Confirm as a performance measurement tool has value to mailers, and argues that the decrease in Confirm scans will diminish the mailers' value of service at a time when mail volumes are a concern. MOAA urges the Commission to consider offering a Confirm service that provides the precise location of a given parcel, which the Service's competitors provide at no extra cost. MOAA Brief at 22-23, 26.

[6193] GrayHair asserts that the Postal Service's proposal, which will damage Confirm service, is untimely because new technology and new performance measurement requirements under the PAEA poise Confirm for success. GrayHair Brief at 3. ABA also argues that the Service's proposal moves away from making its system transparent and conflicts with the service standard provisions in the PAEA. ABA Brief at 25-26.

[6194] MMA, ABA and GrayHair support retaining the "start the clock" requirement, which enhances the data for analyzing performance. ABA Brief at 26; GrayHair Brief at 5; MMA Brief at 26-27. OCA announces that it came to an agreement with the Postal Service regarding the removal of the "start the clock" requirement from § 991.31 of the

DMCS. OCA Brief at 138. The Postal Service has agreed to abandon its proposal in favor of modifying the DMCA language by deleting the word “must” so that electronic notification is optional. *Id.* at 138-9; Postal Service Brief at 386.

[6195] The Postal Service explains that the current pricing structure was implemented based on the rationale that it would encourage the use of Confirm scans, thus generating data for analyzing the processing system. Postal Service Reply Brief at 284-85. It contends that the current structure did not produce sufficient usage to make Confirm a credible performance measurement tool as hoped. It notes that its informal agreement with OCA to refrain from seeking elimination of the “start the clock” requirement signals its intention not to reduce the utility of Confirm for assessing service performance. Postal Service Brief at 386. The Postal Service emphasizes that its proposed structure does nothing to change the potential role that Confirm may play in assessing service performance under the PAEA. Postal Service Reply Brief at 289.

[6196] *The 5 to 1 ratio is arbitrary and discriminatory.* OCA, ANM, et al. and GrayHair argue that the Postal Service’s proposal to charge higher rates for Standard Mail scans than for First-Class scans at a 5 to 1 ratio is arbitrary and discriminatory. OCA Reply Brief at 38; ANM, et al. Brief at 42-43, 45; GrayHair Brief at 18. ANM, et al. emphasize that the Postal Service admitted the costs were identical for all the classes and, thus, the ratio is not cost based. ANM, et al. Brief at 42-43, 45. OCA argues that the Postal Service arbitrarily set the ratio at 5 to 1 based on the income needed to generate enough revenue to maintain Confirm. OCA Reply Brief at 38.

[6197] OCA contends that the Postal Service’s argument that the ratio provides additional value to First-Class Mail is irrational because First-Class Mail has higher rates in return for service of greater value. It explains that charging less for First-Class scans without providing service of a greater value is unsound. OCA Reply Brief at 37. ANM, et al. also argue that the Postal Service’s observation that First-Class Mail has a higher value of service can not constitute reasonable ground for the differential treatment, because the observation would justify any price discrimination, including extreme fee differences. ANM, et al. Brief at 45.

[6198] ANM, et al. assert that the Postal Service has failed to show that a one to five price disparity between scans for First-Class and all the other classes of mail is consistent with the anti-discrimination provisions of 39 U.S.C. § 403(c). *Id.* at 43. They claim that price disparities violate § 403(c), unless the Postal Service demonstrates that the disparities are justified by the greater intrinsic value of the service being charged the higher price. ANM, et al. Reply Brief at 11. They argue that because the 5 to 1 ratio is not justified by any difference in the cost of a scan, the Postal Service failed to provide reasonable grounds for the substantial price discrimination. ANM, et al. Brief at 42-43, 45.

[6199] GrayHair argues that the Postal Service ratio constitutes value-pricing and is discriminatory. GrayHair Brief at 19, 22. It implies that value-pricing prejudices Standard Mail by decreasing demand for a class that needs accessible service performance measurement data because the service is less reliable and less consistent. GrayHair asserts that value-based pricing should not be applied to Confirm scans for the following reasons: (a) as the cost of scans approaches zero, any per-scan pricing will restrict demand; (b) the scans are a derivative product and should not be elevated to a primary product with a requirement to generate contribution; and (c) public interest in service performance exists. *Id.* at 22-24. ABA also contends that the 5 to 1 ratio is discriminatory because both classes need a reliable performance-tracking system. ABA Brief at 27.

[6200] (5) *The proposal will not increase fairness and equity amongst subscribers.* OCA, ANM, et al., GrayHair, MMA and MOAA argue that the Postal Service's proposed structure is not more fair and equitable than the current subscription-based fee structure. OCA Brief at 127; ANM, et al. Brief at 34; GrayHair Brief at 9; MMA Brief at 5; MOAA Brief at 24. In response to the Service's argument that the existing fee structure is unfair and inequitable to low volume Confirm users, GrayHair asserts that the Postal Service's proposal is just as unfair and inequitable to higher volume users. GrayHair Brief at 9.

[6201] OCA argues that the Postal Service's proposal, which will charge mailers one unit for First-Class Mail scans and five units for all other classes, is unfair and

inequitable because subscribers will pay different amounts for the same number of scans. Noting that the price per scan decreases as the number of scans purchased increases under both proposals, OCA argues that the current structure better serves the small volume users than the Postal Service's proposal, which significantly raises the price for the low volume subscribers. OCA Brief at 128-131.

[6202] ANM, et al. emphasize that in Docket No. MC2002-1 the Commission found the subscription-based structure to be fair and equitable and to be in accordance with title 39 of the United States Code. They assert that the Postal Service's argument that the subscription-based structure is unfair and inequitable because subscribers pay grossly different costs per scan is without merit. In support, they argue that the Service made erroneous assumptions concerning volume taper and subscription levels when calculating the price per scan under OCA's proposal. ANM, et al. claim that the Postal Service's argument is at odds with its position as to the reasonableness of declining block volume discounts in negotiated service agreements, and assert that the same reasoning for allowing block volume discounts in negotiated service agreements applies to the current rate structure for Confirm. ANM, et al. Brief at 34-38.

[6203] MOAA asserts that the Service's "fairness" argument, which is based on mailers choosing a Platinum subscription when a Gold subscription is financially better, can not be used to support a structural change to Confirm. It argues that mailers large enough to use Confirm do not require the Service's protection against oversubscribing. MOAA highlights that the Postal Service's fairness argument is totally at odds with its assertion that under OCA's proposal customers will downgrade their level of service due to the higher Platinum subscription fee. MOAA Brief at 24-25, 27.

[6204] *Proposed structure is more complex.* OCA, ANM, et al., and GrayHair argue that the Postal Service's transaction-based fee structure is more complex than OCA's subscription-based fee structure. OCA Brief at 132; ANM, et al. Brief at 39; GrayHair Brief at 10. OCA explains that the existing additional blocks of scans will be replaced with blocks of units, which is complicated because one unit does not equal one scan. It contends that determining the number of additional blocks of units needed is difficult

because the amount of units required is dependant on the class of mail scanned due to the 5 to 1 ratio and that subscribers will not be able to pre-determine the cost of a subscription. OCA Brief at 133.

[6205] OCA, ANM, et al., and GrayHair contend that eliminating the unlimited tier adds complexity and increases administrative costs and problems by giving rise to claims for defective scans, requiring the accurate recording and billing of the scanned mail by class, and necessitating a precise count of scans by subscribers to ensure the Service is not overcharging them. *Id.* at 134; ANM, et al. Brief at 39-40; GrayHair Brief at 10. ANM, et al. also argue that under the proposed structure Confirm revenue will be difficult to predict because it will fluctuate depending on the potentially volatile customer demand. ANM, et al. Brief at 40.

[6206] *Current structure can support future enhancements.* Countering the Postal Service's argument that potential future developments require a new fee structure, OCA, ANM, et al., MMA and GrayHair assert that the current subscription-based structure can accommodate enhancements and can be restated in terms of units. OCA Brief at 134; ANM, et al. Brief at 41-42; MMA Brief at 24; GrayHair Brief at 11-12. OCA emphasizes that the Service does not have any current plans for enhancements. It notes that even if future enhancements are made, the Postal Service fails to demonstrate that the scans will have dissimilar costs and prices compared to current scans. OCA contends that subscribers do not want to invest in programming required by enhancements that may never occur. OCA Brief at 135-37.

[6207] *Unlimited tier has benefits that a transaction-based structure can not provide.* OCA, ANM, et al., GrayHair, and PostCom support the retention of an unlimited scan tier. ANM, et al. emphasize the benefits that customers and the Postal Service derive from Confirm and its unlimited tier option, including better time management of mailings, an objective service performance measure, a valuable management tool that identifies deficient service, and the ability to attract and retain mail volume and revenue by enhancing the underlying mail service. They assert that the Postal Service, which argues that only a few mailers benefit directly from the unlimited scan option, ignores the

fact that most mailers benefit indirectly by purchasing Confirm scans from a value-added reseller and that the Postal Service benefits by receiving performance measurement data. ANM, et al. Brief at 6-7, 9, 15. PostCom argues that the unlimited tier under OCA's proposal will create enormous economies by encouraging increased usage and by promoting the resale of scans, which makes the service more accessible to additional users. PostCom Brief at 42.

[6208] GrayHair contends that the availability of unlimited scans benefits all postal customers due to the improved level of information on the Service's delivery and service performance. It claims that unlimited scans allow for unrestricted market growth, which has a synergistic effect on other OneCode services, and can positively affect subscriber business plans. GrayHair asserts that because Confirm scans are completely derivative upon the existence of mailpieces for their value, per-scan charges hurt mailers by making a mini-product out of mail scans. GrayHair Brief at 10-11.

[6209] *Resellers enhance Confirm.* GrayHair contends that the Postal Service's arguments about how resellers may concentrate the market share and reduce revenue are speculative because the Postal Service did not conduct market research or interviews. It asserts that higher Confirm fees under OCA's proposal will not increase arbitrage because resellers add value and do not engage in pure arbitrage. Because the maximum opportunity for arbitrage is \$19,500 under OCA's proposal, it argues that significant users of Confirm will purchase their own subscriptions rather than saving a minimal amount by buying scans from a reseller. GrayHair notes that arbitrage is a legitimate component of many markets. It argues that any potential loss in revenue may be mitigated by new users of the OneCode Address Correction Service or the four-state code becoming Confirm subscribers as well. *Id.* at 7-9.

[6210] ANM, et al. and PostCom argue that arbitrage by resellers will not increase in response to increased subscription fees and that the Postal Service's concerns about the potential negative effect from arbitrage of scans are unfounded. ANM, et al. at 29-30; PostCom Brief at 42-43. PostCom also contends that the resale of scans enhances the value of Confirm. PostCom Brief at 42-43. OCA adds that the Postal

Service's proposal will suppress the growth of value-added resellers. OCA Reply Brief at 36.

[6211] The Postal Service notes that while the elasticity of Confirm is unknown as the service is in its infancy, resellers are able to charge more for scans with added value. It maintains it accepts Confirm resellers, but argues that no principle requires it to lose money so that resellers can generate a profit. Postal Service Reply Brief at 292-294. Recognizing that pure arbitrage has not been a problem for Confirm to date, it argues that as fees for the unlimited tier increase to cover costs the risk of pure arbitrage also increases. Postal Service Brief at 385.

[6212] *Current structure can cover costs.* OCA, ANM, et al., GrayHair and MOAA claim that the Postal Service's position that the current rate structure can not generate sufficient revenue to cover costs is baseless. OCA Brief at 115-119; ANM, et al. at 16-18; MOAA Brief at 25-27; GrayHair Brief at 2-3. OCA, ANM, et al. and MOAA also argue that the Postal Service's contention that customers will choose a lower service level under OCA's proposal, resulting in a revenue shortfall, is unsupported by any empirical evidence. OCA at 115-18; ANM, et al. Brief at 22-23; MOAA Brief at 25-27.

[6213] MOAA asserts that the Postal Service failed to offer market research that retaining the existing rate structure and increasing fees will encourage arbitrage, which will lead to fewer Confirm subscribers and a failure to cover costs. MOAA contends that the financial harm from the Postal Service not covering costs is miniscule. *Id.* at 25-27.

[6214] ANM, et al. state that the Postal Service fails to assign a value to the increased postage revenue resulting from the greater demand for First-Class and Standard Mail service stimulated by Confirm because it mistakenly believes that 39 U.S.C. § 3622(b)(3) requires consideration of Confirm's costs and revenue in isolation from the underlying mail services. ANM, et al. argue that the cost coverage requirement of § 3622(b)(3) applies to the class of mail or type of mail service as a whole, and not to each individual component or ancillary service provided in conjunction with the class, such as return of undeliverable as addressed with First-Class Mail. They assert that the Service ignores the likely increase in demand for ID codes, which will develop as

resellers grow in the market, and made baseless “no-growth” assumptions on the number of mailers, postal delivery points, and the aggregate economic activity in the United States. According to ANM, et al., the Postal Service’s analyses ignore the increasing demand for Confirm and the resulting revenue due to the deployment of the four-state barcode. The Service also overlooked the possibility that service enhancements by third-party resellers and the Evolutionary Network Design (END) program might stimulate demand for Confirm. ANM, et al. contend that the Service also should assign a value to its own use of Confirm for internal performance measurement. ANM, et al. Brief at 16-22.

[6215] The Postal Service responds that under the current structure the Platinum subscription will make less economic sense for customers as its fee increases in the future. It argues that OCA’s assumption that customers will continue to oversubscribe is fiscally risky. It asserts that the revenue and volume projections in OCA’s proposal are unrealistic because the proposal does not make adjustments to recognize that a price increase can affect volume. The Postal Service claims that most customers will subscribe to the Gold tier, which will charge a much higher fee for scans than under a transaction-based structure. In response to the intervenors’ argument that customers will not resubscribe if the Service’s proposal is implemented, the Service counters that the assertion lacks credibility because the scans cost a minimal amount compared to creating a mailpiece and paying for postage. Postal Service Reply Brief at 290-92, 294.

[6216] *Miscellaneous.* Several intervenors provide additional arguments as to why the Commission should reject the Postal Service’s proposal. ANM, et al. and OCA assert that the Service failed to meet its burden of proof for eliminating the unlimited scan tier by showing that the current price structure is inferior to its proposed structure. OCA Brief at 110-11; ANM, et al. Brief at 12-13. Similarly, MOAA contends that the Service offered no valid reasons for proposing such a radically different structure. MOAA Brief at 23-24.

[6217] ANM, et al. and GrayHair note that the Service’s assertions are inconsistent with its May 2006 presentation at the International Conference on Postal Automation and

its previous position in Docket No MC2002-1 when it proposed Confirm and the subscription-based fee structure. ANM, et al. Brief at 13; GrayHair Brief at 14-15, 22; Tr. 33/11424-25. MOAA and ANM, et al. emphasize that the Postal Service is proposing drastic changes without having determined its customers' views regarding the current and proposed pricing structures. MOAA Brief at 27; ANM, et al. Brief at 5, 14. MMA asserts that the 49 percent increase in revenue generated by the Postal Service's proposal is excessive when compared to the average proposed increase of 8.5 percent in this omnibus rate case and is extreme for a service still in its infancy. MMA Brief at 23.

[6218] The Postal Service responds that most of the intervenors support retaining the unlimited tier because they represent Platinum subscribers and resellers. It acknowledges that the intervenors rely on arguments that the Service made in the past supporting subscription-based pricing. It explains that the subscription-based approach did not lead to the fiscal success that was necessary, intended and anticipated, thus requiring a new approach. Postal Service Reply Brief at 286-287.

[6219] *Commission analysis.* The Postal Service proposes a transaction-based price structure arguing that the existing structure can not accommodate future enhancements to the Confirm service and will not cover costs. The Commission finds that the Postal Service has not proven that its proposed transaction-based structure can cover costs better than the current subscription-based structure. It observes that the Postal Service's cost coverage for its proposed structure is unsound because the figures pertinent to the revenue calculation are not justified by any market research or studies.

[6220] The Service speculates that a 10 percent decrease in scan usage will result due to the large fee increases it proposes, but provides no evidentiary support for this figure. The Service also fails to substantiate its assumption that the percent of scans of First-Class and Standard Mail will remain at the existing price structure's levels of 55 percent and 45 percent respectively, even under its proposed structure where a First-Class scan will cost one unit and a Standard scan will cost five. The Service states that it assumed an across-the-board reduction of 10 percent because it could not determine what percent of an individual subscriber's scans will be used for First-Class.

Tr. 19/6793. In support of its proposal to charge five times as much for a Standard Mail scan as for a First-Class scan when the costs of scans are identical for all classes of mail, the Service states that First-Class's higher value of service allows for differential pricing. The Service does not expound on how this explanation equates to a 5 to 1 ratio specifically, or how it calculated the 5 to 1 ratio. The Commission concludes that switching to a transaction-based structure defined by arbitrary rate distinctions is neither justified nor appropriate.

[6221] The Commission notes that the Postal Service is not currently proposing any enhancements to the service and did not provide concrete examples as to how the existing price structure will be unable to accommodate the future changes. The Commission does not support changing price structures based on hypothetical future enhancements. No tangible justification exists for such modifications and users can not effectively comment.

[6222] The Commission is not persuaded that the current structure is too complex by the Postal Service's unsubstantiated claim that subscribers were unable to estimate their demand for scans and oversubscribed. The existing structure allows customers to subscribe to Gold and switch to Platinum mid-subscription if their demand projections were too low. It also finds the Postal Service's concern that the price disparity between low and high volume users is too large under the current structure overstated. The price per scan decreases as the number of scans purchased increases under both transaction-based and subscription-based price structures.

[6223] The Commission finds that increased fees under the current subscription-based price structure will provide adequate revenue to cover Confirm's costs. In recommending OCA's proposal, the Commission acknowledges the Postal Service's concerns that a revenue shortfall could result if the 29 Platinum subscribers currently oversubscribing migrate to the Gold tier. If 30 Platinum subscribers downgrade their subscriptions, and thus contribute less towards the revenue, OCA's proposal will fall short of covering costs by \$406,500.

[6224] To ensure that Confirm covers its costs, the Commission recommends increasing the fee for a Gold subscription 33 percent from \$4,500 to \$6,000, rather than to \$5,200 as proposed by OCA. In determining the appropriate rate for a Gold subscription, the Commission assumed that 30 Platinum subscribers will migrate to the Gold tier and purchase one block of 6 million units each, as postulated by the Postal Service. The Commission finds that a fee of \$6,000 for a Gold subscription offsets the potential loss in revenue from 30 Platinum subscribers downgrading and three Silver subscribers, who purchased four quarterly subscriptions, upgrading to the less expensive Gold tier. This fee will also recover the costs imposed on the system by new customers, who will likely subscribe to the Gold tier.

[6225] A 33 percent increase to the Gold fee is smaller than some Gold subscribers would have experienced under the Service's proposal. Subscribers using the service to scan Standard Mail are also spared from the large increase the Service's proposal would have imposed with its 5 to 1 price ratio.

[6226] The Commission concludes that customers who use the Silver service occasionally or would like to try Confirm for three months before investing in a yearly subscription will find Confirm more affordable with retention of the subscription-based price structure. Silver subscribers would have experienced a fee increase up to 189 percent under the Service's proposal.

[6227] MMA proposes a structure that offers First-Class presort mailers unlimited scans for a minimal annual fee that would cover the costs of establishing and maintaining the accounts. While the Commission is retaining the unlimited scan tier, it is recommending a larger rate increase to the Platinum tier than MMA desires. The Commission must charge more than a minimal annual fee because the cost of scans, while marginal, must be covered. The current structure offers the less expensive Gold tier for Confirm users whose scan demand does not financially justify a Platinum subscription.

[6228] The Commission recommends the fees proposed by OCA, except for a fee of \$6,000 for a Gold subscription. It estimates a cost coverage of 135.3 percent, which is

reasonable for a discretionary service that previously failed to cover its costs. The Commission calculates the cost coverage based on all subscribers retaining their current subscription levels.

[6229] The Commission recognizes that the Postal Service is no longer proposing to eliminate the “start the clock” requirement. It adopts the classification change agreed upon by OCA and the Service to make the electronic notification voluntary with a slight modification to the proposed language so that it conforms to their intent.

26. Miscellaneous Fees (Fee Schedule 1000)

a. Permit Fees

[6230] Permit fees are collected for: (1) First-Class presort; (2) Standard Mail; (3) Destination Entry Package Services; (4) Media Mail and Library Mail presort; (5) Parcel Return Services; (6) Business Reply Mail; (7) Bulk Parcel Return Service; (8) Merchandise Return service; and (9) permit imprints. While the permit imprint fee is a one-time only fee for mailings requiring permit indicia, the fee for all the other permits is collected on an annual basis.

[6231] The estimated test year cost for a permit is \$135.77. The Postal Service proposes to increase the permit fee from \$160 to \$175. USPS-T-39 at 53-54.

[6232] The Commission recommends the permit fee proposed by the Postal Service. The \$175 fee results in a cost coverage of 128.9 percent. By allowing mailers access to lower rates, permits provide a high value of service that justifies a modest contribution.

b. Account Maintenance Fee

[6233] The annual account maintenance fee pays for the service required to maintain advance deposits associated with certain postal services. Funds are deducted

from the account to pay for postage for Business Reply Mail; Merchandise Return service; Bulk Parcel Return Service; Shipper Paid Forwarding; and Parcel Return Services. *Id.* at 6, 8.

[6234] The Postal Service proposes a classification change for this service by replacing the term “accounting fee” with “account maintenance fee.” The Postal Service contends that the change in language clarifies that the fee pays for the service of maintaining an advance deposit account, rather than the accounting activities related to daily withdrawals from the account.

[6235] The Postal Service proposes to increase the account maintenance fee to \$550 from the current level of \$500. The estimated test year annual accounting cost is \$335.85 per service. *Id.* at 5, 7-8.

[6236] The Commission recommends the Service’s proposed fee of \$550, which produces a cost coverage of 163.8 percent. The Commission adopts the Postal Service’s proposal to modify the name of this service for clarification purposes.

c. Periodicals Application Fee

[6237] Four types of Periodicals Application Fees exist: (1) a one-time original entry fee; (2) an additional entry fee for new mailing locations; (3) a re-entry fee when the status of a publication is affected by a name change, frequency of issue change, preferential rate status change, or office of publication change; and (4) a news registration application fee for news agents who handle two or more periodicals by different publishers. The Postal Service proposes to increase the original entry fee, which has an estimated test year cost of \$468.29, from \$395.00 to \$500.00. It suggests increasing the re-entry fee from \$45.00 to \$55.00 to cover the test year cost of \$51.17. The Service proposes to increase the additional entry fee, which has a test year cost of \$68.56, from \$65.00 to \$75.00, and to increase the fee for the registration of new agents, which has an estimated test year cost of \$32.67, from \$40.00 to \$45.00. *Id.* at 49-50.

[6238] The Commission recommends the fees proposed by the Postal Service and calculates a cost coverage of 108.0 percent. The increases to all of the fees are necessary to cover the costs of the service and to contribute to institutional costs.

d. Change of Address Fee

[6239] The Change of Address fee is paid by customers choosing to change their addresses online or over the telephone rather than completing a PS Form 3575 and sending it back to the post office. To enhance security and to prevent fraudulent changes of addresses, the Postal Service requires identity validation by a credit card company when signatures are not collected. Postal Service Reply Brief at 309.

[6240] The Service asserts that the credit card companies charge a minimum fee of \$1 to perform identity validation. Tr. 18B/5473, 5615-16; Tr. 19/6932. The Postal Service argues that because the credit card companies require a minimum charge, the charge is the result of a third-party requirement rather than a fee for a postal service. The Service concludes, therefore, that the fee does not belong in the DMCS. Postal Service Reply Brief at 309.

[6241] Popkin asserts that the Change of Address Service is a postal service. As such, he argues that the fee must be approved by the Commission and appear in the DMCS regardless of the purpose of the \$1 fee. Popkin Brief at 15.

[6242] The Commission finds that the Change of Address Service is a postal service because it facilitates delivery by enabling the forwarding of mail. All postal services for which a rate or fee is charged must be included in the DMCS. Therefore, the Commission recommends adding the following language to the DMCS:

913 CHANGE OF ADDRESS SERVICE

913.1 Definition

913.1 Change of Address Service is available to customers who want their mail permanently or temporarily forwarded to a future or current address from a former address.

913.2 Fees

913.21 The fee for Change of Address Service is set forth in Fee Schedule 1000.

[6243] The Commission recommends a \$1 fee for Change of Address Service provided over the Internet or by telephone.

RATE SCHEDULES

RATE SCHEDULES 121, 122 AND 123

EXPRESS MAIL

Weight (lbs.)	Schedule 121	Schedule 122	Schedule 123	Schedule 123
	Same Day Airport Service	Custom Designed	Next Day & Second Day PO to PO	Next Day & Second Day PO to Addressee
0.5		\$14.15	\$13.85	\$16.25
1		17.40	17.10	19.50
2		19.30	19.00	21.40
3		22.40	22.10	24.50
4		25.50	25.20	27.60
5		28.60	28.30	30.70
6		31.70	31.40	33.80
7		34.80	34.50	36.90
8		37.90	37.60	40.00
9		41.00	40.70	43.10
10		43.15	42.85	45.25
11		45.30	45.00	47.40
12		47.45	47.15	49.55
13		49.60	49.30	51.70
14		51.75	51.45	53.85
15		53.90	53.60	56.00
16		56.05	55.75	58.15
17		58.20	57.90	60.30
18		60.35	60.05	62.45
19		62.50	62.20	64.60
20		64.65	64.35	66.75
21		66.80	66.50	68.90
22		68.95	68.65	71.05
23		71.10	70.80	73.20
24		73.25	72.95	75.35
25		75.40	75.10	77.50
26		77.55	77.25	79.65
27		79.70	79.40	81.80
28		81.85	81.55	83.95
29		84.00	83.70	86.10
30		86.15	85.85	88.25
31		88.30	88.00	90.40
32		90.45	90.15	92.55
33		92.60	92.30	94.70
34		94.75	94.45	96.85
35		96.90	96.60	99.00
36		99.05	98.75	101.15
37		101.20	100.90	103.30
38		103.35	103.05	105.45
39		105.50	105.20	107.60
40		107.65	107.35	109.75

EXPRESS MAIL (continued)

Weight (lbs.)	Schedule 121	Schedule 122	Schedule 123	Schedule 123
	Same Day Airport Service	Custom Designed	Next Day & Second Day PO to PO	Next Day & Second Day PO to Addressee
41		\$109.80	\$109.50	\$111.90
42		111.95	111.65	114.05
43		114.10	113.80	116.20
44		116.25	115.95	118.35
45		118.40	118.10	120.50
46		120.55	120.25	122.65
47		122.70	122.40	124.80
48		124.85	124.55	126.95
49		127.00	126.70	129.10
50		129.15	128.85	131.25
51		131.30	131.00	133.40
52		133.45	133.15	135.55
53		135.60	135.30	137.70
54		137.75	137.45	139.85
55		139.90	139.60	142.00
56		142.05	141.75	144.15
57		144.20	143.90	146.30
58		146.35	146.05	148.45
59		148.50	148.20	150.60
60		150.65	150.35	152.75
61		152.80	152.50	154.90
62		154.95	154.65	157.05
63		157.10	156.80	159.20
64		159.25	158.95	161.35
65		161.40	161.10	163.50
66		163.55	163.25	165.65
67		165.70	165.40	167.80
68		167.85	167.55	169.95
69		170.00	169.70	172.10
70		172.15	171.85	174.25

SCHEDULES 121, 122 AND 123 NOTES

1. The applicable 1/2-pound rate is charged for matter sent in a flat-rate envelope provided by the Postal Service.
2. Add \$14.25 for each Pickup On-Demand stop.
3. Add \$14.25 for each Custom Designed delivery stop.

**FIRST-CLASS MAIL
RATE SCHEDULE 221**

LETTERS AND SEALED PARCELS

	Rate
Single-piece	
First ounce	
Letters	\$0.410
Flats	0.800
Parcels	1.130
Additional ounces	0.170
Nonmachinable surcharge	0.170
Qualified Business Reply Mail	0.380
 Presorted	
First ounce	
Letters	0.373
Flats	0.699
Additional ounces	0.170
Nonmachinable surcharge	0.170
 Automation Letters	
Mixed AADC	0.360
AADC	0.341
3-digit	0.334
5-digit	0.312
Additional ounces	0.125
 Automation Flats	
Mixed ADC	0.686
ADC	0.567
3-digit	0.484
5-digit	0.383
Additional ounces	0.170
 Business Parcels	
ADC	0.891
3-digit	0.837
5-digit	0.704
Additional ounces	0.170

SCHEDULE 221 NOTES

1. A mailing fee of \$175.00 must be paid once each year at each office of mailing by any person who mails at presorted or automation rates. Payment of the fee allows the mailer to mail at any First-Class Mail rate.
2. First-Class Mail rates apply through 13 ounces. Heavier pieces are subject to Priority Mail rates.
3. Add \$0.005 per piece for Presorted, Automation Letters and Automation Flats pieces bearing a Repositionable Note as defined in DMCS Sections 221.223, 221.326, and 221.336.
4. For nonmachinable, non-barcoded, or less than 2 ounce business parcels (ADC and 3-digit) add \$0.05 per piece.
5. The rate for single-piece, first ounce letters also applies to sales of the Forever Stamp at the time of purchase.

**FIRST-CLASS MAIL
RATE SCHEDULE 222**

CARDS

	Rate
Regular	
Single-piece cards	\$0.260
Qualified Business Reply Mail	0.230
Presorted	0.241
Automation	
Mixed AADC	0.220
AADC	0.208
3-digit	0.204
5-digit	0.191

SCHEDULE 222 NOTES

1. A mailing fee of \$175.00 must be paid once each year at each office of mailing by any person who mails at presorted or automation rates. Payment of the fee allows the mailer to mail at any First-Class Mail rate.

**FIRST-CLASS MAIL
RATE SCHEDULE 223**

PRIORITY MAIL

Weight (lbs.)	Local, Zones	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Zone 8
	1, 2						
1	\$4.60	\$4.60	\$4.60	\$4.60	\$4.60	\$4.60	\$4.60
2	4.60	4.90	5.30	6.20	6.55	7.00	7.50
3	5.05	5.70	6.40	8.25	9.10	9.65	10.55
4	5.70	6.65	7.70	10.20	11.10	12.20	13.45
5	6.30	7.55	8.90	11.90	12.90	14.35	15.85
6	6.85	8.25	10.00	12.95	13.10	14.75	16.05
7	7.35	8.85	11.00	13.95	14.35	16.40	18.30
8	7.75	9.60	11.95	14.90	15.60	18.00	20.55
9	8.15	10.25	12.50	15.90	16.85	19.60	22.85
10	8.50	10.75	13.10	16.95	18.25	21.30	25.05
11	8.80	11.20	13.65	17.95	19.75	22.90	26.35
12	9.15	11.70	14.20	18.95	21.30	24.10	27.50
13	9.50	12.20	14.75	20.00	22.85	25.05	28.45
14	9.80	12.70	15.35	20.90	24.10	26.50	29.85
15	10.15	13.20	15.90	21.55	24.65	26.75	30.50
16	10.35	13.45	16.20	22.00	25.20	27.35	31.25
17	10.50	13.70	16.50	22.55	25.85	28.05	32.10
18	10.70	13.90	16.80	23.00	26.35	28.60	32.85
19	11.10	14.15	17.10	23.55	27.00	29.30	33.70
20	11.60	14.35	17.40	23.95	27.50	29.85	34.40
21	12.00	14.55	17.70	24.35	27.95	30.40	35.10
22	12.50	14.80	17.95	24.90	28.60	31.10	35.95
23	12.90	15.00	18.45	25.30	29.10	31.65	36.60
24	13.35	15.20	19.00	25.85	29.70	32.35	37.50
25	13.85	15.40	19.65	26.25	30.15	32.85	38.15
26	14.25	15.60	20.25	26.80	30.80	33.55	39.35
27	14.70	15.80	20.85	27.20	31.25	34.05	40.80
28	15.15	16.00	21.40	27.55	31.70	34.55	42.30
29	15.60	16.20	22.05	27.90	32.10	35.00	43.70
30	16.10	16.40	22.65	28.30	32.55	35.50	45.15
31	16.50	16.55	23.25	28.65	32.95	35.95	46.65
32	16.95	16.95	23.85	29.00	33.40	36.80	48.10
33	17.40	17.40	24.40	29.35	33.80	37.85	49.50
34	17.85	17.85	25.05	30.00	34.80	38.90	50.95
35	18.30	18.30	25.65	30.65	35.75	39.95	52.40
36	18.75	18.75	26.25	31.30	36.70	41.05	53.85
37	19.20	19.20	26.95	31.90	37.65	42.10	55.30
38	19.65	19.65	27.50	32.55	38.70	43.10	56.75
39	20.05	20.05	28.25	33.20	39.65	44.20	58.25
40	20.45	20.45	28.90	33.85	40.55	45.20	59.65

PRIORITY MAIL (continued)

Weight (lbs.)	Local, Zones	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Zone 8
	1, 2						
41	\$20.85	\$20.85	\$29.50	\$34.20	\$41.50	\$46.25	\$61.10
42	21.25	21.25	30.25	34.90	42.40	47.35	62.55
43	21.65	21.65	30.90	35.70	43.45	48.40	64.00
44	22.05	22.05	31.50	36.50	44.35	49.50	65.45
45	22.45	22.45	32.20	37.25	45.30	50.55	66.90
46	22.85	22.85	32.90	38.00	46.25	51.60	68.35
47	23.25	23.25	33.50	38.80	47.30	52.70	69.75
48	23.65	23.65	34.25	39.60	48.25	53.75	71.25
49	24.05	24.05	34.90	40.30	49.15	54.85	72.70
50	24.40	24.40	35.55	41.10	50.10	55.90	74.15
51	24.85	24.85	36.20	41.90	51.05	56.95	75.60
52	25.20	25.20	36.90	42.70	52.10	58.00	77.05
53	25.65	25.65	37.50	43.45	53.00	59.10	78.50
54	26.00	26.00	38.15	44.25	53.90	60.10	79.90
55	26.45	26.45	38.90	45.05	54.85	61.10	81.35
56	26.80	26.80	39.50	45.75	55.90	62.20	82.85
57	27.25	27.25	40.15	46.50	56.80	63.25	84.30
58	27.60	27.60	40.85	47.30	57.75	64.30	85.70
59	28.05	28.05	41.50	48.10	58.70	65.35	87.20
60	28.40	28.40	42.15	48.90	59.70	66.40	88.65
61	28.85	28.85	42.90	49.65	60.70	67.45	90.10
62	29.20	29.20	43.50	50.45	61.60	68.50	91.50
63	29.65	29.65	44.20	51.25	62.55	69.55	92.95
64	30.00	30.00	44.85	52.05	63.50	70.55	94.45
65	30.45	30.45	45.45	52.70	64.50	71.65	95.90
66	30.80	30.80	46.15	53.50	65.40	72.70	97.30
67	31.25	31.25	46.90	54.30	66.35	73.70	98.80
68	31.60	31.60	47.50	55.10	67.30	74.80	100.20
69	32.05	32.05	48.15	55.90	68.30	75.85	101.65
70	32.45	32.45	48.90	56.65	69.25	76.90	103.10

SCHEDULE 223 NOTES

1. The 1-pound rate is charged for matter sent in a flat-rate envelope provided by the Postal Service.
2. A rate of \$9.15 is charged for matter sent in a flat-rate box provided by the Postal Service.
3. Exception: In Zones 1 - 4 (including Local), parcels weighing less than 20 pounds but measuring more than 84 inches in combined length and girth (though not more than 108 inches) are charged the applicable rate for a 20-pound parcel (balloon rate).
4. Exception: In Zones 5 - 8, parcels exceeding one cubic foot are rated at the actual weight or the dimensional weight, whichever is greater.
5. Add \$14.25 for each Pickup On-Demand stop.

**STANDARD MAIL
RATE SCHEDULE 321A**

**REGULAR
NONAUTOMATION CATEGORIES**

	Rate
Letter, minimum piece rate	
Piece Rate	
Mixed ADC	\$0.255
AADC	0.246
Mixed ADC (Nonmachinable)	0.520
ADC (Nonmachinable)	0.440
3-digit (Nonmachinable)	0.411
5-digit (Nonmachinable)	0.328
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, minimum piece rate	
Piece Rate	
Mixed ADC	0.515
ADC	0.461
3-digit	0.427
5-digit	0.363
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, piece and pound rate	
Piece Rate	
Mixed ADC	0.365
ADC	0.311
3-digit	0.277
5-digit	0.213
Pound Rate	0.739
Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203

REGULAR
NONAUTOMATION CATEGORIES (continued)

Parcels, minimum piece rate

Piece Rate	
Mixed ADC (Nonmachinable Parcels)	\$1.129
ADC (Nonmachinable Parcels)	0.914
3-digit (Nonmachinable Parcels)	0.653
5-digit (Nonmachinable Parcels)	0.607
Destination Entry Discounts	
BMC	0.033
SCF	0.042
DDU	0.051

Parcels, piece and pound rate

Piece Rate	
Mixed BMC (Machinable Parcels)	0.909
BMC (Machinable Parcels)	0.716
5-digit (Machinable Parcels)	0.346
Mixed ADC (Nonmachinable Parcels)	0.979
ADC (Nonmachinable Parcels)	0.764
3-digit (Nonmachinable Parcels)	0.503
5-digit (Nonmachinable Parcels)	0.457
Pound Rate	0.739
Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203
DDU	0.248

NFM Pieces, minimum piece rate

Piece Rate	
Mixed ADC/Mixed BMC	1.028
ADC/BMC	0.767
3-digit	0.506
5-digit	0.460
Destination Entry Discounts	
BMC	0.033
SCF	0.042
DDU	0.051

**REGULAR
NONAUTOMATION CATEGORIES (continued)**

NFM Pieces, piece and pound rate

Piece Rate	
Mixed ADC/Mixed BMC	\$0.878
ADC/BMC	0.617
3-digit	0.356
5-digit	0.310
 Pound Rate	 0.739
 Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203
DDU	0.248

SCHEDULE 321A NOTES

1. A fee of \$175.00 must be paid each 12-month period for each bulk mailing permit.
2. For non-barcoded parcels and NFM pieces, add \$0.05 per piece. The surcharge does not apply to pieces sorted to 5-digit ZIP Codes.
3. For flats, parcels and NFMs, the mailer pays either the minimum piece rate or the pound rate, whichever is higher.
4. Letters forwarded as defined in DMCS section 353a are charged \$0.35 per piece. Flats forwarded as defined in DMCS section 353a are charged \$1.05 per piece. Mailpieces forwarded as defined in DMCS section 353b are charged the appropriate First-Class Mail Rate for the piece plus the rate multiplied by a weighted factor of 2.472.
5. Pieces entered as Customized Market Mail, as defined in DMCS section 321.5, pay \$0.460 per piece.
6. Add \$0.015 per piece for pieces bearing a Repositionable Note as defined in DMCS section 321.8.

**STANDARD MAIL
RATE SCHEDULE 321B**

**REGULAR
AUTOMATION CATEGORIES**

	Rate
Letters, minimum piece-rate	
Piece Rate	
Mixed AADC	\$ 0.252
AADC	0.238
3-digit	0.233
5-digit	0.218
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, minimum piece rate	
Piece Rate	
Mixed ADC	0.477
ADC	0.424
3-digit	0.392
5-digit	0.335
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, piece and pound rate	
Piece Rate	
Mixed ADC	0.328
ADC	0.275
3-digit	0.243
5-digit	0.186
Pound Rate	0.739
Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203

SCHEDULE 321B NOTES

1. A fee of \$175.00 must be paid once each 12-month period for each bulk mailing permit.
2. Letters that weigh more than 3.3 ounces but not more than 3.5 ounces pay the flats piece and pound rate but receive a discount off the piece rate equal to the applicable flats minimum piece rate minus the applicable letter minimum piece rate corresponding to the correct presort tier.
3. For flats, the mailer pays either the minimum piece rate or the pound rate, whichever is higher.
4. Add \$0.015 per piece for pieces bearing a Repositionable Note as defined in DMCS section 321.8.
5. Letters forwarded as defined in DMCS section 353a are charged \$0.35 per piece. Flats forwarded as defined in DMCS section 353a are charged \$1.05 per piece. Mailpieces forwarded as defined in DMCS section 353b are charged the appropriate First-Class Mail Rate for the piece plus the rate multiplied by a weighted factor of 2.472.

**STANDARD MAIL
RATE SCHEDULE 322**

ENHANCED CARRIER ROUTE

	Rate
Letters, minimum piece rate	
Piece Rate	
Basic	\$ 0.226
High density	0.186
Saturation	0.177
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, minimum piece rate	
Piece Rate	
Basic	0.249
High density	0.205
Saturation	0.187
Destination Entry Discounts	
BMC	0.033
SCF	0.042
DDU	0.051
Flats, piece and pound rate	
Piece Rate	
Basic	0.121
High density	0.077
Saturation	0.059
Pound Rate	0.621
Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203
DDU	0.248

ENHANCED CARRIER ROUTE (continued)

Parcels, minimum piece rate

Piece Rate	
Basic	\$0.499
High density	0.378
Saturation	0.369

Destination Entry Discounts

BMC	0.033
SCF	0.042
DDU	0.051

Parcels, piece and pound rate

Piece Rate	
Basic	0.371
High density	0.250
Saturation	0.241

Pound Rate	0.621
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Destination Entry Discounts (off pound rate)

BMC	0.159
SCF	0.203
DDU	0.248

SCHEDULE 322 NOTES

1. A fee of \$175.00 must be paid each 12-month period for each bulk mailing permit.
2. Pieces that do not qualify for letter or flats rate categories are subject to parcels rates.
3. For flats and parcels, the mailer pays either the minimum piece rate or the pound rate, whichever is higher.
4. Pieces that otherwise meet the requirements for high density and saturation letter rates that weigh more than 3.3 ounces but not more than 3.5 ounces pay the flats piece and pound rate but receive a discount off the piece rate equal to the applicable flats minimum piece rate minus the applicable letter minimum piece rate corresponding to the correct density tier.
5. For letter-size pieces, not meeting the automation requirements specified by the Postal Service, the mailer pays the flats rate for the applicable density tier.
6. Add \$0.015 per piece for pieces bearing a Repositionable Note as defined in DMCS section 322.8.
7. Add \$0.015 per piece for flat-shaped and parcel-shaped pieces addressed using detached address labels (DALs).
8. Letters forwarded as defined in DMCS section 353a are charged \$0.35 per piece. Flats forwarded as defined in DMCS section 353a are charged \$1.05 per piece. Mailpieces forwarded as defined in DMCS section 353b are charged the appropriate First-Class Mail Rate for the piece plus the rate multiplied by a weighted factor of 2.472.

**STANDARD MAIL
RATE SCHEDULE 323A**

**NONPROFIT
REGULAR NONAUTOMATION CATEGORIES**

	Rate
Letters, minimum piece rate	
Piece Rate	
Mixed AADC	\$0.164
AADC	0.155
Mixed ADC (Nonmachinable)	0.429
ADC (Nonmachinable)	0.349
3-digit (Nonmachinable)	0.320
5-digit (Nonmachinable)	0.237
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, minimum piece rate	
Piece Rate	
Mixed ADC	0.389
ADC	0.335
3-digit	0.301
5-digit	0.237
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, piece and pound rate	
Piece Rate	
Mixed ADC	0.263
ADC	0.209
3-digit	0.175
5-digit	0.111
Pound Rate	0.622
Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203

**NONPROFIT
REGULAR NONAUTOMATION CATEGORIES (continued)**

Parcels, minimum piece rate

Piece Rate	
Mixed ADC (Nonmachinable Parcels)	\$1.003
ADC (Nonmachinable Parcels)	0.788
3-digit (Nonmachinable Parcels)	0.527
5-digit (Nonmachinable Parcels)	0.481
Destination Entry Discounts	
BMC	0.033
SCF	0.042
DDU	0.051

Parcels, piece and pound rate

Piece Rate	
Mixed BMC (Machinable Parcels)	0.807
BMC (Machinable Parcels)	0.614
5-digit (Machinable Parcels)	0.244
Mixed ADC (Nonmachinable Parcels)	0.877
ADC (Nonmachinable Parcels)	0.662
3-digit (Nonmachinable Parcels)	0.401
5-digit (Nonmachinable Parcels)	0.355
Pound Rate	0.622
Destination Entry Discount (off pound rate)	
BMC	0.159
SCF	0.203
DDU	0.248

NFM Pieces, minimum piece rate

Piece Rate	
Mixed ADC/Mixed BMC	0.902
ADC/BMC	0.641
3-digit	0.380
5-digit	0.334
Destination Entry Discounts	
BMC	0.033
SCF	0.042
DDU	0.051

**NONPROFIT
REGULAR NONAUTOMATION CATEGORIES (continued)**

NFM Pieces, piece and pound rate

Piece Rate	
Mixed ADC/Mixed BMC	\$0.776
ADC/BMC	0.515
3-digit	0.254
5-digit	0.208
 Pound Rate	 0.622
 Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203
DDU	0.248

SCHEDULE 323A NOTES

1. A fee of \$175.00 must be paid each 12-month period for each bulk mailing permit.
2. For non-barcoded parcels and NFM pieces, add \$0.05 per piece. The surcharge does not apply to pieces sorted to 5-digit ZIP Codes.
3. For flats, parcels and NFMs, the mailer pays either the minimum piece rate or the pound rate, whichever is higher.
4. Letters forwarded as defined in DMCS section 353a are charged \$0.35 per piece. Flats forwarded as defined in DMCS section 353a are charged \$1.05 per piece. Mailpieces forwarded as defined in DMCS section 353b are charged the appropriate First-Class Mail Rate for the piece plus the rate multiplied by a weighted factor of 2.472.
5. Pieces entered as Customized Market Mail, as defined in DMCS section 321.5, pay \$0.334 per piece.
6. Add \$0.015 per piece for pieces bearing a Repositionable Note as defined in DMCS section 323.8.

**STANDARD MAIL
RATE SCHEDULE 323B**

**NONPROFIT REGULAR
AUTOMATION CATEGORIES**

	Rate
Letters, minimum piece rate	
Piece Rate	
Mixed AADC	\$ 0.161
AADC	0.147
3-digit	0.142
5-digit	0.127
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, minimum piece rate	
Piece Rate	
Mixed ADC	0.354
ADC	0.301
3-digit	0.269
5-digit	0.212
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, piece and pound rate	
Piece Rate	
Mixed ADC	0.228
ADC	0.175
3-digit	0.143
5-digit	0.086
Pound Rate	0.622
Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203

SCHEDULE 323B NOTES

1. A fee of \$175.00 must be paid each 12-month period for each bulk mailing permit.
2. Letters that weigh more than 3.3 ounces but not more than 3.5 ounces pay the flats piece and pound rate but receive a discount off the piece rate equal to the applicable flats minimum piece rate minus the applicable letter minimum piece rate corresponding to the correct presort tier.
3. For flats, the mailer pays either the minimum piece rate or the pound rate, whichever is higher.
4. Add \$0.015 per piece for pieces bearing a Repositionable Note as defined in DMCS section 323.8.
5. Letters forwarded as defined in DMCS section 353a are charged \$0.35 per piece. Flats forwarded as defined in DMCS section 353a are charged \$1.05 per piece. Mailpieces forwarded as defined in DMCS section 353b are charged the appropriate First-Class Mail Rate for the piece plus the rate multiplied by a weighted factor of 2.472.

**STANDARD MAIL
RATE SCHEDULE 324**

NONPROFIT ENHANCED CARRIER ROUTE

	Rate
Letters, minimum piece rate	
Piece Rate	
Basic	\$0.157
High density	0.117
Saturation	0.108
Destination Entry Discounts	
BMC	0.033
SCF	0.042
Flats, minimum piece rate	
Piece Rate	
Basic	0.180
High density	0.136
Saturation	0.118
Destination Entry Discounts	
BMC	0.033
SCF	0.042
DDU	0.051
Flats, piece and pound rate	
Piece Rate	
Basic	0.091
High density	0.047
Saturation	0.029
Pound Rate	0.432
Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203
DDU	0.248

NONPROFIT ENHANCED CARRIER ROUTE (continued)**Parcels, minimum piece rate**

Piece Rate	
Basic	\$0.430
High density	0.309
Saturation	0.300

Destination Entry discounts	
BMC	0.033
SCF	0.042
DDU	0.051

Parcels, piece and pound rate

Piece Rate	
Basic	0.341
High density	0.220
Saturation	0.211

Pound Rate	0.432
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Destination Entry Discounts (off pound rate)	
BMC	0.159
SCF	0.203
DDU	0.248

SCHEDULE 324 NOTES

1. A fee of \$175.00 must be paid each 12-month period for each bulk mailing permit.
2. Pieces that do not qualify for letter or flats rate categories are subject to parcels rates.
3. For flats and parcels, the mailer pays either the minimum piece rate or the pound rate, whichever is higher.
4. Pieces that otherwise meet the requirements for high density and saturation letter rates that weigh more than 3.3 ounces but not more than 3.5 ounces pay the flats piece and pound rate but receive a discount off the piece rate equal to the applicable flats minimum piece rate minus the applicable letter minimum piece rate corresponding to the correct density tier.
5. For letter-size pieces, not meeting the automation requirements specified by the Postal Service, the mailer pays the flats rate for the applicable density tier.
6. Add \$0.015 per piece for pieces bearing a Repositionable Note as defined in DMCS section 324.8.
7. Add \$0.015 per piece for flat-shaped and parcel-shaped pieces addressed using detached address labels (DALs).
8. Letters forwarded as defined in DMCS section 353a are charged \$0.35 per piece. Flats forwarded as defined in DMCS section 353a are charged \$1.05 per piece. Mailpieces forwarded as defined in DMCS section 353b are charged the appropriate First-Class Mail Rate for the piece plus the rate multiplied by a weighted factor of 2.472.

**PERIODICALS
RATE SCHEDULE 421**

OUTSIDE COUNTY (INCLUDING SCIENCE OF AGRICULTURE)

	Postage Rate Unit	Rate
Outside County Advertising		
Destination Delivery Unit	Pound	\$ 0.160
Destination SCF	Pound	0.209
Destination ADC	Pound	0.219
Zones 1 & 2	Pound	0.239
Zone 3	Pound	0.257
Zone 4	Pound	0.303
Zone 5	Pound	0.372
Zone 6	Pound	0.446
Zone 7	Pound	0.534
Zone 8	Pound	0.610
Nonadvertising		
Destination Delivery Unit	Pound	0.133
Destination SCF	Pound	0.174
Destination ADC	Pound	0.182
All other editorial (nonadvertising)	Pound	0.199
Science of Agriculture Advertising		
Destination Delivery Unit	Pound	0.120
Destination SCF	Pound	0.157
Destination ADC	Pound	0.164
Zones 1 & 2	Pound	0.179
Zone 3	Pound	0.257
Zone 4	Pound	0.303
Zone 5	Pound	0.372
Zone 6	Pound	0.446
Zone 7	Pound	0.534
Zone 8	Pound	0.610
Nonadvertising		
Destination Delivery Unit	Pound	0.133
Destination SCF	Pound	0.174
Destination ADC	Pound	0.182
All other editorial (nonadvertising)	Pound	0.199

OUTSIDE COUNTY (INCLUDING SCIENCE OF AGRICULTURE) (continued)**Piece Rates****Mixed ADC Bundle Pieces**

Nonautomation Nonmachinable	Piece	\$0.534
Nonautomation Machinable	Piece	0.431
Automation Nonmachinable	Piece	0.504
Automation Machinable	Piece	0.404
Automation Letter	Piece	0.327

ADC Bundle Pieces

Nonautomation Nonmachinable	Piece	0.432
Nonautomation Machinable	Piece	0.370
Automation Nonmachinable	Piece	0.412
Automation Machinable	Piece	0.350
Automation Letter	Piece	0.289

SCF/3-Digit Bundle Pieces

Nonautomation Nonmachinable	Piece	0.373
Nonautomation Machinable	Piece	0.348
Automation Nonmachinable	Piece	0.362
Automation Machinable	Piece	0.331
Automation Letter	Piece	0.275

5-digit Bundle Pieces

Nonautomation Nonmachinable	Piece	0.289
Nonautomation Machinable	Piece	0.276
Automation Nonmachinable	Piece	0.285
Automation Machinable	Piece	0.268
Automation Letter	Piece	0.211

Carrier Route Bundle Pieces

Basic	Piece	0.169
High Density	Piece	0.149
Saturation	Piece	0.131
Firm bundle\4	Bundle	0.169

Ride-Along Piece

Per Piece	Piece	0.155
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Discounts

Per-piece editorial discount\5	Piece	(0.091)
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OUTSIDE COUNTY (INCLUDING SCIENCE OF AGRICULTURE) (continued)**Bundle Rates****Mixed ADC Sack**

Mixed ADC bundle	Bundle	\$0.100
ADC bundle	Bundle	0.129
3-digit/SCF bundle	Bundle	0.134
5-digit bundle	Bundle	0.161
Firm Bundle	Bundle	0.079

ADC Sack or Pallet

ADC bundle	Bundle	0.038
3-digit/SCF bundle	Bundle	0.063
5-digit bundle	Bundle	0.095
Carrier Route bundle	Bundle	0.104
Firm bundle	Bundle	0.048

3-Digit/SCF Sack or Pallet

3-digit/SCF bundle	Bundle	0.039
5-digit bundle	Bundle	0.084
Carrier Route bundle	Bundle	0.095
Firm bundle	Bundle	0.045

5-digit Sack or Pallet

5-digit bundle	Bundle	0.008
Carrier Route bundle	Bundle	0.039
Firm bundle	Bundle	0.027

Sack Rates**Mixed ADC Sack**

OSCF Entry	Sack	0.42
OADC Entry	Sack	0.42

ADC Sack

OSCF Entry	Sack	1.80
OADC Entry	Sack	1.80
OBMC Entry	Sack	1.80
DBMC Entry	Sack	1.10
DADC Entry	Sack	0.60

3-Digit/SCF Sack

OSCF Entry	Sack	1.90
OADC Entry	Sack	1.90
OBMC Entry	Sack	1.90
DBMC Entry	Sack	1.20
DADC Entry	Sack	1.00
DSCF Entry	Sack	0.60

OUTSIDE COUNTY (INCLUDING SCIENCE OF AGRICULTURE) (continued)

5-Digit/Carrier Route Sack

OSCF Entry	Sack	\$2.24
OADC Entry	Sack	2.24
OBMC Entry	Sack	2.24
DBMC Entry	Sack	1.50
DADC Entry	Sack	1.30
DSCF Entry	Sack	0.90
DDU Entry	Sack	0.70

Pallet Rates

ADC Pallet

OSCF Entry	Pallet	18.61
OADC Entry	Pallet	18.61
OBMC Entry	Pallet	18.61
DBMC Entry	Pallet	13.00
DADC Entry	Pallet	8.90

3-Digit/SCF Pallet

OSCF Entry	Pallet	22.98
OADC Entry	Pallet	22.98
OBMC Entry	Pallet	22.98
DBMC Entry	Pallet	14.40
DADC Entry	Pallet	12.20
DSCF Entry	Pallet	6.70

5-Digit Pallet

OSCF Entry	Pallet	26.95
OADC Entry	Pallet	26.95
OBMC Entry	Pallet	26.95
DBMC Entry	Pallet	17.50
DADC Entry	Pallet	15.50
DSCF Entry	Pallet	8.00
DDU Entry	Pallet	1.20

SCHEDULE 421 NOTES

1. The rates in this schedule also apply to Nonprofit (DMCS Section 422.2) and Classroom rate categories. These categories receive a 5 percent discount on all components of postage except advertising pounds. Moreover, the 5 percent discount does not apply to commingled nonsubscriber, nonrequestor, complimentary, and sample copies in excess of the 10 percent allowance under DMCS sections 412.34 and 413.42, or to Science of Agriculture mail.
2. Rates do not apply to otherwise Outside County mail that qualifies for the Within County rates in Schedule 423.
3. Charges are computed by adding the appropriate per-piece charge, per-bundle charge, per-sack, and per-pallet charge to the sum of the editorial (nonadvertising) pound portion and the advertising pound portion, as applicable.
4. Firm bundles are charged a single piece charge.
5. For postage calculations, multiply the proportion of editorial (nonadvertising) content by this factor and subtract from the applicable piece rate.
6. Advertising pound rate is not applicable to qualifying Nonprofit and Classroom publications containing 10 percent or less advertising content.
7. For a Ride-Along item enclosed with or attached to a Periodical, add \$0.155 per copy.
8. Add \$0.015 per piece for pieces bearing a Repositionable Note as defined in DMCS section 424.

**PERIODICALS
RATE SCHEDULE 423**

WITHIN COUNTY

	Postage Rate Unit	Rate
Delivery Unit	Pound	\$ 0.132
All other zones	Pound	0.171
 Basic		
Nonautomation	Piece	0.122
Automation letter	Piece	0.055
Automation flat	Piece	0.107
 3-Digit		
Nonautomation	Piece	0.110
Automation letter	Piece	0.046
Automation flat	Piece	0.099
 5-Digit		
Nonautomation	Piece	0.098
Automation letter	Piece	0.044
Automation flat	Piece	0.093
 Carrier Route		
Basic	Piece	0.056
High density	Piece	0.041
Saturation	Piece	0.028
 Discounts		
Worksharing Discount DDU	Piece	(0.008)
Ride-Along	Piece	0.155

SCHEDULE 423 NOTES

1. Charges are computed by adding the appropriate per-piece charge to the appropriate pound charge.
2. For a Ride-Along item enclosed with or attached to a Periodical, add \$0.155 per copy.
3. Add \$0.015 per-piece for pieces bearing a Repositionable Note as defined in DMCS section 424.

**PACKAGE SERVICES
RATE SCHEDULE 521.2A**

**PARCEL POST
INTER-BMC RATES**

Weight (lbs.)	Zones						
	1 & 2	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Zone 8
1	\$4.38	\$4.50	\$4.50	\$4.50	\$4.50	\$4.50	\$4.50
2	4.50	4.80	5.20	5.67	6.00	6.15	6.15
3	4.95	5.60	6.30	7.02	7.05	7.33	7.93
4	5.60	6.55	7.47	7.78	8.04	8.45	9.25
5	6.20	7.45	8.23	8.59	8.98	9.50	10.50
6	6.75	8.15	8.97	9.36	9.83	10.48	11.77
7	7.25	8.61	9.67	10.09	10.64	11.44	12.88
8	7.65	8.94	10.36	10.79	11.41	12.32	14.08
9	8.05	9.27	10.99	11.47	12.14	13.14	15.21
10	8.40	10.37	11.62	12.12	12.84	13.92	16.17
11	8.70	10.69	12.22	12.75	13.52	14.68	17.08
12	8.96	10.97	12.80	13.36	14.17	15.40	17.96
13	9.14	11.22	13.37	13.95	14.80	16.10	18.80
14	9.32	11.53	13.91	14.53	15.41	16.77	19.61
15	9.48	11.79	14.44	15.09	15.99	17.43	20.40
16	9.62	12.04	14.96	15.64	16.56	18.06	21.16
17	9.80	12.25	15.46	16.18	17.12	18.67	21.89
18	9.93	12.48	15.78	16.70	17.66	19.27	22.61
19	10.10	12.71	16.13	17.21	18.18	19.85	23.30
20	10.22	12.92	16.42	17.71	18.70	20.41	23.98
21	10.37	13.14	16.72	18.20	19.19	20.96	24.64
22	10.49	13.31	17.02	18.69	19.68	21.50	25.28
23	10.63	13.55	17.33	19.16	20.16	22.02	25.90
24	10.73	13.72	17.58	19.62	20.62	22.54	26.51
25	10.87	13.90	17.85	20.08	21.08	23.04	27.11
26	10.97	14.07	18.10	20.53	21.53	23.53	27.69
27	11.12	14.25	18.33	20.97	21.97	24.01	28.26
28	11.21	14.42	18.60	21.40	22.39	24.48	28.82
29	11.34	14.60	18.84	21.83	22.81	24.94	29.36
30	11.44	14.74	19.05	22.24	23.23	25.39	29.90
31	11.57	14.89	19.27	22.66	23.63	25.83	30.42
32	11.65	15.05	19.49	23.06	24.03	26.27	30.94
33	11.75	15.21	19.71	23.46	24.42	26.69	31.44
34	11.87	15.31	19.88	23.86	24.81	27.11	31.93
35	11.97	15.48	20.09	24.25	25.19	27.53	32.42
36	12.06	15.61	20.31	24.63	25.56	27.93	32.90
37	12.16	15.73	20.46	25.01	25.92	28.33	33.37
38	12.25	15.90	20.64	25.38	26.28	28.72	33.83
39	12.36	15.99	20.81	25.76	26.64	29.11	34.28
40	12.45	16.15	21.00	26.12	26.99	29.49	34.73

**PARCEL POST
INTER-BMC RATES (continued)**

Weight (lbs.)	Zones 1 & 2	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Zone 8
41	\$12.57	\$16.28	\$21.15	\$26.48	\$27.33	\$29.87	\$35.17
42	12.65	16.39	21.32	26.84	27.67	30.23	35.60
43	12.71	16.51	21.49	27.19	28.01	30.60	36.03
44	12.81	16.60	21.63	27.53	28.34	30.96	36.45
45	12.90	16.74	21.80	27.88	28.66	31.31	36.86
46	12.99	16.85	21.96	28.22	28.98	31.66	37.27
47	13.10	16.98	22.09	28.42	29.30	32.00	37.67
48	13.17	17.08	22.26	28.59	29.62	32.34	38.06
49	13.23	17.20	22.39	28.76	29.92	32.67	38.46
50	13.31	17.28	22.50	28.93	30.23	33.01	38.84
51	13.42	17.41	22.66	29.09	30.53	33.33	39.22
52	13.48	17.51	22.79	29.24	30.83	33.65	39.59
53	13.59	17.59	22.88	29.39	31.12	33.97	39.97
54	13.65	17.73	23.04	29.54	31.41	34.28	40.33
55	13.72	17.77	23.17	29.69	31.70	34.60	40.69
56	13.82	17.93	23.28	29.84	31.98	34.90	41.05
57	13.90	18.01	23.41	29.97	32.26	35.20	41.40
58	13.96	18.10	23.52	30.11	32.54	35.50	41.75
59	14.05	18.19	23.65	30.24	32.82	35.80	42.09
60	14.13	18.28	23.78	30.37	33.09	36.09	42.43
61	14.24	18.41	23.87	30.49	33.36	36.38	42.77
62	14.30	18.47	23.99	30.62	33.62	36.67	43.10
63	14.35	18.58	24.10	30.73	33.88	36.95	43.42
64	14.42	18.64	24.19	30.85	34.14	37.23	43.75
65	14.50	18.75	24.31	30.97	34.40	37.51	44.07
66	14.60	18.84	24.40	31.07	34.66	37.78	44.39
67	14.68	18.93	24.52	31.19	34.91	38.05	44.70
68	14.73	19.01	24.64	31.29	35.16	38.32	45.01
69	14.79	19.07	24.73	31.40	35.41	38.59	45.32
70	14.89	19.19	24.83	31.49	35.65	38.85	45.62
Oversized	50.54	55.19	58.28	69.40	83.99	97.82	127.24

SCHEDULE 521.2A NOTES

1. For Origin Bulk Mail Center (OBMC) Presort Discount, deduct \$1.50 per piece.
2. For BMC Presort Discount, deduct \$0.26 per piece.
3. For barcode discount, deduct \$0.03 per piece (machinable parcels only).
4. For nonmachinable parcels, add \$3.89 per piece.
5. Regardless of weight, any piece that measures more than 108 inches (but not more than 130 inches) in combined length and girth must pay the oversized rate.
6. Pieces exceeding 84 inches in length and girth combined and weighing less than 20 pounds are subject to a rate equal to that for a 20-pound parcel for the zone to which the parcel is addressed.
7. For each Pickup On-Demand stop, add \$14.25.

**PACKAGE SERVICES
RATE SCHEDULE 521.2B**

**PARCEL POST
INTRA-BMC RATES**

Weight (lbs.)	Local Zone	Zones 1 & 2	Zone 3	Zone 4	Zone 5
1	\$3.42	\$3.67	\$3.70	\$3.78	\$3.96
2	3.80	4.34	4.38	4.47	4.72
3	4.15	4.96	5.00	5.11	5.46
4	4.47	5.37	5.58	5.69	6.13
5	4.76	5.74	6.07	6.21	6.76
6	5.03	6.09	6.53	6.67	7.32
7	5.24	6.42	6.94	7.10	7.86
8	5.42	6.95	7.33	7.50	8.34
9	5.60	7.24	7.69	7.90	8.79
10	5.77	7.55	8.07	8.53	9.21
11	5.93	7.82	8.38	8.86	9.59
12	6.09	8.10	8.69	9.18	9.96
13	6.25	8.28	8.97	9.48	10.30
14	6.39	8.44	9.22	9.81	10.61
15	6.53	8.59	9.49	10.07	10.90
16	6.68	8.74	9.76	10.33	11.20
17	6.80	8.92	10.01	10.61	11.45
18	6.93	9.05	10.25	10.84	11.70
19	7.05	9.20	10.49	11.08	11.94
20	7.19	9.35	10.73	11.28	12.15
21	7.30	9.46	10.95	11.49	12.36
22	7.42	9.62	11.17	11.71	12.55
23	7.53	9.72	11.40	11.93	12.76
24	7.65	9.85	11.61	12.15	12.93
25	7.76	9.96	11.81	12.35	13.11
26	7.86	10.10	12.00	12.56	13.26
27	7.97	10.21	12.21	12.76	13.42
28	8.07	10.31	12.41	12.94	13.59
29	8.18	10.43	12.60	13.13	13.79
30	8.29	10.54	12.78	13.31	13.97
31	8.38	10.65	12.94	13.49	14.17
32	8.46	10.76	13.13	13.67	14.34
33	8.57	10.86	13.29	13.83	14.52
34	8.63	10.96	13.40	14.00	14.69
35	8.70	11.05	13.55	14.16	14.86
36	8.78	11.14	13.66	14.31	15.02
37	8.83	11.26	13.78	14.47	15.18
38	8.89	11.35	13.91	14.62	15.34
39	8.98	11.45	14.04	14.76	15.49
40	9.06	11.52	14.14	14.91	15.64

**PARCEL POST
INTRA-BMC RATES (continued)**

Weight (lbs.)	Local Zone	Zones 1 & 2	Zone 3	Zone 4	Zone 5
41	\$9.14	\$11.65	\$14.29	\$15.00	\$15.79
42	9.20	11.71	14.39	15.11	15.93
43	9.28	11.79	14.50	15.18	16.07
44	9.37	11.90	14.61	15.26	16.20
45	9.43	11.96	14.70	15.48	16.33
46	9.48	12.09	14.82	15.55	16.57
47	9.57	12.18	14.91	15.63	16.96
48	9.63	12.25	15.03	15.68	17.37
49	9.69	12.35	15.13	15.74	17.77
50	9.75	12.39	15.22	15.80	18.19
51	9.84	12.51	15.30	15.87	18.61
52	9.88	12.60	15.44	15.93	19.05
53	9.95	12.64	15.51	15.96	19.50
54	10.04	12.71	15.56	16.03	19.96
55	10.10	12.79	15.63	16.09	20.15
56	10.14	12.88	15.68	16.16	20.23
57	10.21	12.97	15.70	16.19	20.37
58	10.28	13.04	15.76	16.24	20.46
59	10.35	13.12	15.80	16.29	20.56
60	10.37	13.21	15.83	16.32	20.67
61	10.49	13.29	15.89	16.38	20.76
62	10.52	13.36	15.93	16.46	20.85
63	10.60	13.43	15.95	16.55	20.94
64	10.66	13.51	15.98	16.63	21.04
65	10.71	13.59	16.03	16.71	21.11
66	10.75	13.68	16.06	16.80	21.22
67	10.86	13.75	16.09	16.90	21.29
68	10.91	13.78	16.12	16.95	21.37
69	10.92	13.88	16.15	17.04	21.46
70	10.93	13.95	16.19	17.13	21.54
Oversized	28.82	41.78	42.17	43.01	44.28

SCHEDULE 521.2B NOTES

1. For barcode discount deduct \$0.03 per piece (machinable parcels only).
2. For nonmachinable parcels, add \$2.87 per piece.
3. Regardless of weight, any piece that measures more than 108 inches (but not more than 130 inches) in combined length and girth must pay the oversized rate.
4. Pieces exceeding 84 inches in length and girth combined and weighing less than 20 pounds are subject to a rate equal to that for a 20-pound parcel for the zone to which the parcel is addressed.
5. For each Pickup On-Demand stop, add \$14.25.

**PACKAGE SERVICES
RATE SCHEDULE 521.2C**

**PARCEL POST
PARCEL SELECT DESTINATION BULK MAIL CENTER RATES**

Weight (lbs.)	Zones			
	1 & 2	Zone 3	Zone 4	Zone 5
1	\$2.38	\$2.72	\$3.05	\$3.91
2	2.68	3.35	3.99	4.67
3	2.96	3.95	4.85	5.41
4	3.24	4.52	5.58	6.08
5	3.49	5.05	6.10	6.71
6	3.73	5.54	6.53	7.27
7	3.95	5.99	6.92	7.81
8	4.17	6.43	7.28	8.29
9	4.38	6.84	7.66	8.74
10	4.58	7.24	8.48	9.16
11	4.77	7.63	8.81	9.54
12	4.96	8.00	9.13	9.91
13	5.14	8.33	9.43	10.25
14	5.32	8.59	9.76	10.56
15	5.49	8.87	10.02	10.85
16	5.65	9.14	10.28	11.15
17	5.81	9.35	10.56	11.40
18	5.96	9.54	10.79	11.65
19	6.12	9.71	11.03	11.89
20	6.26	9.89	11.23	12.10
21	6.41	10.07	11.41	12.31
22	6.55	10.22	11.60	12.50
23	6.68	10.40	11.77	12.71
24	6.82	10.55	11.93	12.88
25	6.95	10.70	12.08	13.06
26	7.08	10.82	12.23	13.21
27	7.21	10.99	12.37	13.37
28	7.33	11.15	12.49	13.51
29	7.45	11.28	12.65	13.64
30	7.57	11.41	12.76	13.79
31	7.69	11.51	12.86	13.92
32	7.81	11.65	12.98	14.05
33	7.92	11.76	13.10	14.15
34	8.03	11.88	13.19	14.27
35	8.14	12.00	13.31	14.38
36	8.26	12.58	13.40	14.48
37	8.37	12.68	13.49	14.58
38	8.47	12.80	13.58	14.68
39	8.58	12.91	13.66	14.77
40	8.68	13.02	13.74	14.84

PARCEL POST
PARCEL SELECT DESTINATION BULK MAIL CENTER RATES (continued)

Weight (lbs.)	Zones			
	1 & 2	Zone 3	Zone 4	Zone 5
41	\$8.78	\$13.15	\$13.81	\$14.93
42	8.88	13.25	13.90	15.01
43	8.98	13.36	13.98	15.38
44	9.07	13.44	14.05	15.74
45	9.17	13.52	14.24	16.14
46	9.26	13.64	14.30	16.52
47	9.36	13.73	14.36	16.91
48	9.44	13.84	14.44	17.32
49	9.53	13.92	14.50	17.72
50	9.63	14.02	14.54	18.14
51	9.71	14.10	14.60	18.56
52	9.80	14.21	14.66	19.00
53	9.89	14.27	14.71	19.45
54	9.97	14.33	14.77	19.91
55	10.05	14.38	14.83	20.10
56	10.14	14.42	14.86	20.18
57	10.22	14.46	14.90	20.32
58	10.30	14.51	14.95	20.41
59	10.38	14.54	14.99	20.51
60	10.46	14.58	15.02	20.62
61	10.54	14.62	15.07	20.71
62	10.62	14.66	15.16	20.80
63	10.69	14.69	15.24	20.89
64	10.77	14.72	15.30	20.99
65	10.85	14.76	15.38	21.06
66	10.92	14.80	15.48	21.17
67	10.99	14.82	15.54	21.24
68	11.06	14.83	15.61	21.32
69	11.14	14.86	15.68	21.41
70	11.21	14.89	15.77	21.49
Oversized	21.08	29.49	39.77	41.33

SCHEDULE 521.2C NOTES

1. For nonmachinable parcels, add \$2.14 per piece.
2. Regardless of weight, any piece that measures more than 108 inches (but not more than 130 inches) in combined length and girth must pay the oversized rate.
3. Pieces exceeding 84 inches in length and girth combined and weighing less than 20 pounds are subject to a rate equal to that for a 20-pound parcel for the zone to which the parcel is addressed.
4. A mailing fee of \$175.00 must be paid once each 12-month period for Parcel Select.

**PACKAGE SERVICES
RATE SCHEDULE 521.2D**

**PARCEL POST
PARCEL SELECT DESTINATION SECTIONAL CENTER FACILITY RATES**

Weight (lbs.)	Rate	Weight (lbs.)	Rate
1	\$1.90	36	\$5.81
2	2.11	37	5.88
3	2.30	38	5.94
4	2.47	39	6.02
5	2.63	40	6.08
6	2.79	41	6.14
7	2.93	42	6.22
8	3.07	43	6.28
9	3.21	44	6.34
10	3.33	45	6.40
11	3.45	46	6.47
12	3.57	47	6.53
13	3.69	48	6.58
14	3.79	49	6.64
15	3.92	50	6.70
16	4.03	51	6.76
17	4.14	52	6.80
18	4.24	53	6.85
19	4.35	54	6.90
20	4.45	55	6.97
21	4.54	56	7.02
22	4.64	57	7.07
23	4.73	58	7.12
24	4.83	59	7.18
25	4.91	60	7.22
26	5.00	61	7.26
27	5.09	62	7.31
28	5.18	63	7.36
29	5.26	64	7.42
30	5.34	65	7.45
31	5.42	66	7.50
32	5.51	67	7.55
33	5.58	68	7.58
34	5.66	69	7.64
35	5.74	70	7.68
		Oversized	13.56

SCHEDULE 521.2D NOTES

1. Regardless of weight, any piece that measures more than 108 inches (but not more than 130 inches) in combined length and girth must pay the oversized rate.
2. Pieces exceeding 84 inches in length and girth combined and weighing less than 20 pounds are subject to a rate equal to that for a 20-pound parcel for the zone to which the parcel is addressed.
3. A mailing fee of \$175.00 must be paid once each 12-month period for Parcel Select.
4. For nonmachinable parcels sorted to 3-digit ZIP Code areas, add \$0.96 per piece.

**PACKAGE SERVICES
RATE SCHEDULE 521.2E**

**PARCEL POST
PARCEL SELECT DESTINATION DELIVERY UNIT RATES**

Weight (lbs.)	Rate	Weight (lbs.)	Rate
1	\$1.40	36	\$2.60
2	1.47	37	2.62
3	1.52	38	2.64
4	1.58	39	2.66
5	1.63	40	2.69
6	1.68	41	2.71
7	1.72	42	2.73
8	1.76	43	2.75
9	1.81	44	2.77
10	1.85	45	2.79
11	1.88	46	2.81
12	1.92	47	2.83
13	1.96	48	2.85
14	1.99	49	2.87
15	2.03	50	2.89
16	2.06	51	2.90
17	2.09	52	2.92
18	2.13	53	2.94
19	2.16	54	2.95
20	2.19	55	2.96
21	2.22	56	2.98
22	2.25	57	2.99
23	2.27	58	3.00
24	2.30	59	3.01
25	2.33	60	3.02
26	2.36	61	3.04
27	2.38	62	3.05
28	2.41	63	3.06
29	2.43	64	3.07
30	2.46	65	3.08
31	2.48	66	3.10
32	2.51	67	3.11
33	2.53	68	3.12
34	2.55	69	3.13
35	2.58	70	3.14
		Oversized	7.36

SCHEDULE 521.2E NOTES

1. Regardless of weight, any piece that measures more than 108 inches (but not more than 130 inches) in combined length and girth must pay the oversized rate.
2. Pieces exceeding 84 inches in length and girth combined and weighing less than 20 pounds are subject to a rate equal to that for a 20-pound parcel for the zone to which the parcel is addressed.
3. A mailing fee of \$175.00 must be paid once each 12-month period for Parcel Select.

**PACKAGE SERVICES
RATE SCHEDULE 521.2F**

**PARCEL POST
PARCEL SELECT RETURN SERVICES
RETURN DELIVERY UNIT RATE CATEGORY**

Weight (lbs.)	Rate	Weight (lbs.)	Rate
1	\$2.20	36	\$2.20
2	2.20	37	2.20
3	2.20	38	2.20
4	2.20	39	2.20
5	2.20	40	2.20
6	2.20	41	2.20
7	2.20	42	2.20
8	2.20	43	2.20
9	2.20	44	2.20
10	2.20	45	2.20
11	2.20	46	2.20
12	2.20	47	2.20
13	2.20	48	2.20
14	2.20	49	2.20
15	2.20	50	2.20
16	2.20	51	2.20
17	2.20	52	2.20
18	2.20	53	2.20
19	2.20	54	2.20
20	2.20	55	2.20
21	2.20	56	2.20
22	2.20	57	2.20
23	2.20	58	2.20
24	2.20	59	2.20
25	2.20	60	2.20
26	2.20	61	2.20
27	2.20	62	2.20
28	2.20	63	2.20
29	2.20	64	2.20
30	2.20	65	2.20
31	2.20	66	2.20
32	2.20	67	2.20
33	2.20	68	2.20
34	2.20	69	2.20
35	2.20	70	2.20
		Oversized	8.08

SCHEDULE 521.2F NOTES

1. Regardless of weight, any parcel that measures more than 108 inches (but not more than 130 inches) in combined length and girth must pay the oversized rate.

**PACKAGE SERVICES
RATE SCHEDULE 521.2G**

**PARCEL POST
PARCEL SELECT RETURN SERVICE
RETURN BMC RATE CATEGORY
MACHINABLE PIECES**

Weight (lbs.)	Zones 1 & 2	Zone 3	Zone 4	Zone 5
1	\$2.22	\$2.25	\$2.33	\$2.51
2	2.89	2.93	3.02	3.27
3	3.51	3.55	3.66	4.01
4	3.92	4.13	4.24	4.68
5	4.29	4.62	4.76	5.31
6	4.64	5.08	5.22	5.87
7	4.93	5.49	5.65	6.41
8	5.50	5.88	6.05	6.89
9	5.79	6.24	6.45	7.34
10	6.04	6.62	7.08	7.76
11	6.19	6.93	7.41	8.14
12	6.38	7.24	7.73	8.51
13	6.55	7.52	8.03	8.85
14	6.71	7.77	8.36	9.16
15	6.84	8.04	8.62	9.45
16	6.98	8.31	8.88	9.75
17	7.15	8.56	9.16	10.00
18	7.26	8.80	9.39	10.25
19	7.42	9.04	9.63	10.49
20	7.54	9.23	9.83	10.70
21	7.66	9.41	10.04	10.91
22	7.79	9.56	10.26	11.10
23	7.90	9.77	10.48	11.31
24	8.00	9.91	10.70	11.48
25	8.11	10.07	10.90	11.66
26	8.23	10.21	11.11	11.81
27	8.34	10.37	11.31	11.97
28	8.42	10.52	11.45	12.14
29	8.53	10.68	11.58	12.34
30	8.64	10.80	11.71	12.52
31	8.74	10.91	11.82	12.72
32	8.86	11.05	11.95	12.89
33	8.93	11.18	12.05	13.07
34	9.04	11.28	12.16	13.21
35	9.11	11.42	12.25	13.33

SCHEDULE 521.2G NOTES

1. Parcels that weigh less than 20 pounds but measure more than 84 inches in combined length and girth are charged the applicable rate for a 20-pound parcel.

**PACKAGE SERVICES
RATE SCHEDULE 521.2G (continued)**

**PARCEL POST
PARCEL SELECT RETURN SERVICE
RETURN BMC RATE CATEGORY
NONMACHINABLE PIECES**

Weight (lbs.)	Zones 1 & 2	Zone 3	Zone 4	Zone 5
1	\$5.09	\$5.12	\$5.20	\$5.38
2	5.76	5.80	5.89	6.14
3	6.38	6.42	6.53	6.88
4	6.79	7.00	7.11	7.55
5	7.16	7.49	7.63	8.18
6	7.51	7.95	8.09	8.74
7	7.80	8.36	8.52	9.28
8	8.37	8.75	8.92	9.76
9	8.66	9.11	9.32	10.21
10	8.91	9.49	9.95	10.63
11	9.06	9.80	10.28	11.01
12	9.25	10.11	10.60	11.38
13	9.42	10.39	10.90	11.72
14	9.58	10.64	11.23	12.03
15	9.71	10.91	11.49	12.32
16	9.85	11.18	11.75	12.62
17	10.02	11.43	12.03	12.87
18	10.13	11.67	12.26	13.12
19	10.29	11.91	12.50	13.36
20	10.41	12.10	12.70	13.57
21	10.53	12.28	12.91	13.78
22	10.66	12.43	13.13	13.97
23	10.77	12.64	13.35	14.18
24	10.87	12.78	13.57	14.35
25	10.98	12.94	13.77	14.53
26	11.10	13.08	13.98	14.68
27	11.21	13.24	14.18	14.84
28	11.29	13.39	14.32	15.01
29	11.40	13.55	14.45	15.21
30	11.51	13.67	14.58	15.39
31	11.61	13.78	14.69	15.59
32	11.73	13.92	14.82	15.76
33	11.80	14.05	14.92	15.94
34	11.91	14.15	15.03	16.08
35	11.98	14.29	15.12	16.20
36	12.10	14.43	15.25	16.35
37	12.19	14.52	15.33	16.42

**PARCEL POST
 PARCEL SELECT RETURN SERVICE
 RETURN BMC RATE CATEGORY
 NONMACHINABLE PIECES (continued)**

Weight (lbs.)	Zones 1 & 2	Zone 3	Zone 4	Zone 5
38	\$12.24	\$14.61	\$15.39	\$16.48
39	12.31	14.71	15.45	16.54
40	12.36	14.77	15.49	16.61
41	12.45	14.88	15.54	16.67
42	12.48	14.95	15.60	16.72
43	12.53	15.03	15.66	16.75
44	12.60	15.10	15.71	16.79
45	12.64	15.16	15.89	16.84
46	12.72	15.25	15.93	16.87
47	12.78	15.30	15.96	16.91
48	12.82	15.39	15.99	16.95
49	12.89	15.46	16.02	16.98
50	12.90	15.52	16.05	17.02
51	12.99	15.57	16.08	17.07
52	13.03	15.67	16.12	17.10
53	13.05	15.71	16.13	17.14
54	13.11	15.73	16.17	17.17
55	13.15	15.76	16.20	17.21
56	13.20	15.78	16.23	17.25
57	13.26	15.78	16.23	17.29
58	13.31	15.81	16.25	17.33
59	13.35	15.82	16.27	17.37
60	13.41	15.83	16.27	17.40
61	13.45	15.84	16.30	17.44
62	13.49	15.85	16.36	17.47
63	13.54	15.85	16.42	17.52
64	13.59	15.85	16.45	17.56
65	13.62	15.89	16.50	17.59
66	13.68	15.89	16.56	17.63
67	13.73	15.90	16.63	17.67
68	13.73	15.90	16.66	17.70
69	13.80	15.90	16.72	17.75
70	13.84	15.90	16.77	17.79
Oversized	27.39	27.78	28.62	29.89

SCHEDULE 521.2G NOTES

1. Parcels that weigh less than 20 pounds but measure more than 84 inches in combined length and girth are charged the applicable rate for a 20-pound parcel. Regardless of weight, any parcel that measures more than 108 inches (but not more than 130 inches) in combined length and girth must pay the oversized rate.

**PACKAGE SERVICES
RATE SCHEDULE 522A**

**BOUND PRINTED MATTER
SINGLE-PIECE RATES**

Weight (lbs.)	Zones 1 & 2	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Zone 8
1.0	\$2.12	\$2.17	\$2.23	\$2.30	\$2.38	\$2.45	\$2.62
1.5	2.12	2.17	2.23	2.30	2.38	2.45	2.62
2.0	2.21	2.27	2.35	2.45	2.55	2.65	2.87
2.5	2.30	2.38	2.48	2.60	2.73	2.85	3.13
3.0	2.39	2.48	2.60	2.75	2.90	3.05	3.38
3.5	2.48	2.59	2.73	2.90	3.08	3.25	3.64
4.0	2.57	2.69	2.85	3.05	3.25	3.45	3.89
4.5	2.66	2.80	2.98	3.20	3.43	3.65	4.15
5.0	2.75	2.90	3.10	3.35	3.60	3.85	4.40
6.0	2.93	3.11	3.35	3.65	3.95	4.25	4.91
7.0	3.11	3.32	3.60	3.95	4.30	4.65	5.42
8.0	3.29	3.53	3.85	4.25	4.65	5.05	5.93
9.0	3.47	3.74	4.10	4.55	5.00	5.45	6.44
10.0	3.65	3.95	4.35	4.85	5.35	5.85	6.95
11.0	3.83	4.16	4.60	5.15	5.70	6.25	7.46
12.0	4.01	4.37	4.85	5.45	6.05	6.65	7.97
13.0	4.19	4.58	5.10	5.75	6.40	7.05	8.48
14.0	4.37	4.79	5.35	6.05	6.75	7.45	8.99
15.0	4.55	5.00	5.60	6.35	7.10	7.85	9.50

SCHEDULE 522A NOTES

1. For barcode discount, deduct \$0.03 per piece (machinable parcels and automatable flats only).
2. For flats, deduct \$0.16 per piece.

**PACKAGE SERVICES
RATE SCHEDULE 522B**

**BOUND PRINTED MATTER
PRESORTED AND CARRIER ROUTE RATES
FLATS, PARCELS, AND NONMACHINABLE PARCELS**

Flats

	Zones						
	1 & 2	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Zone 8
Per-Piece							
Presorted	\$1.289	\$1.289	\$1.289	\$1.289	\$1.289	\$1.289	\$1.289
Carrier Route	1.178	1.178	1.178	1.178	1.178	1.178	1.178
Per Pound	0.122	0.148	0.195	0.249	0.311	0.359	0.477

Parcels and Nonmachinable Parcels

	Zones						
	1 & 2	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Zone 8
Per-Piece							
Presorted	\$1.447	\$1.447	\$1.447	\$1.447	\$1.447	\$1.447	\$1.447
Carrier Route	1.336	1.336	1.336	1.336	1.336	1.336	1.336
Per Pound	0.122	0.148	0.195	0.249	0.311	0.359	0.477

SCHEDULE 522B NOTES

1. For barcode discount, deduct \$0.03 per piece (machinable parcels and automatable flats only).
Barcode discount is not available for Carrier Route rates.

**PACKAGE SERVICES
RATE SCHEDULE 522C**

**BOUND PRINTED MATTER
PRESORTED RATES, DESTINATION ENTRY
FLATS, PARCELS, AND NONMACHINABLE PARCELS**

Flats

	DBMC					
	DDU	DSCF	Zones 1 & 2	Zone 3	Zone 4	Zone 5
Per Piece	\$0.505	\$0.589	\$0.972	\$0.972	\$0.972	\$0.972
Per Pound	0.040	0.083	0.086	0.124	0.164	0.218

Parcels and Nonmachinable Parcels

	DBMC					
	DDU	DSCF	Zones 1 & 2	Zone 3	Zone 4	Zone 5
Per Piece	\$0.663	\$0.747	\$1.130	\$1.130	\$1.130	\$1.130
Per Pound	0.040	0.083	0.086	0.124	0.164	0.218

SCHEDULE 522C NOTES

1. For barcode discount, deduct \$0.03 per piece (machinable parcels and automatable flats only). Barcode discount is not available for carrier route parcels, or parcels entered at DDU or DSCF rates or DBMC mail entered at an ASF (except Phoenix, AZ, ASF); or flats entered at DDU rates, or carrier route rates.
2. A mailing fee of \$175.00 must be paid once each 12-month period to mail at any destination entry Bound Printed Matter rate.
3. The DDU rate is not available for flats that weigh 1 pound or less.

**PACKAGE SERVICES
RATE SCHEDULE 522D**

**BOUND PRINTED MATTER
CARRIER ROUTE RATES, DESTINATION ENTRY
FLATS, PARCELS, AND NONMACHINABLE PARCELS**

Flats

	DBMC					
	DDU	DSCF	Zones 1 & 2	Zone 3	Zone 4	Zone 5
Per Piece	\$0.394	\$0.478	\$0.861	\$0.861	\$0.861	\$0.861
Per Pound	0.040	0.083	0.086	0.124	0.164	0.218

Parcels and Nonmachinable Parcels

	DBMC					
	DDU	DSCF	Zones 1 & 2	Zone 3	Zone 4	Zone 5
Per Piece	\$0.552	\$0.636	\$1.019	\$1.019	\$1.019	\$1.019
Per Pound	0.040	0.083	0.086	0.124	0.164	0.218

SCHEDULE 522D NOTES

1. A mailing fee of \$175.00 must be paid once each 12-month period to mail at any destination entry Bound Printed Matter rate.

**PACKAGE SERVICES
RATE SCHEDULE 523**

MEDIA MAIL

	Rate
First Pound	
Single-Piece	\$2.13
5-Digit Presort	1.30
Basic Presort	1.80
Each additional pound, through 7 pounds	0.34
Each additional pound, over 7 pounds	0.34

SCHEDULE 523 NOTES

1. A mailing fee of \$175.00 must be paid once each 12-month period to mail at any Media Mail presorted rate.
2. For barcode discount, deduct \$0.03 per piece (machinable parcels only). Barcode discount is not available for pieces mailed at the 5-digit rate.

**PACKAGE SERVICES
RATE SCHEDULE 524**

LIBRARY MAIL

	Rate
First Pound	
Single-Piece	\$2.02
5-Digit Presort	1.24
Basic Presort	1.71
Each additional pound, through 7 pounds	0.32
Each additional pound, over 7 pounds	0.32

SCHEDULE 524

1. A mailing fee of \$175.00 must be paid once each 12-month period to mail at any Library Mail presorted rate.
2. For barcode discount, deduct \$0.03 per piece (machinable parcels only). Barcode discount is not available for pieces mailed at the 5-digit rate.

**NEGOTIATED SERVICE AGREEMENTS
CAPITAL ONE NSA
RATE SCHEDULE 610A**

Volume Block	Incremental Discounts
1,225,000,001 - 1,275,000,000	3.0¢
1,275,000,001 - 1,325,000,000	3.5¢
1,325,000,001 - 1,375,000,000	4.0¢
1,375,000,001 - 1,450,000,000	4.5¢
1,450,000,001 - 1,525,000,000	5.0¢
1,525,000,001 - 1,600,000,000	5.5¢
1,600,000,001 and above	6.0¢

**CAPITAL ONE NSA
RATE SCHEDULE 610B**

Volume Block	Incremental Discounts
1,025,000,001 - 1,075,000,000	1.0¢
1,075,000,001 - 1,125,000,000	1.5¢
1,125,000,001 - 1,175,000,000	2.0¢
1,175,000,001 - 1,225,000,000	2.5¢

**CAPITAL ONE NSA
RATE SCHEDULE 610C
FOR ADJUSTED THRESHOLD (A.T.)**

Volume Block	Incremental Discounts
A.T. + 1 - A.T. + 50,000,000	3.0¢
A.T. + 50,000,001 - A.T. + 100,000,000	3.5¢
A.T. + 100,000,001 - A.T. + 150,000,000	4.0¢
A.T. + 150,000,001 - A.T. + 225,000,000	4.5¢
A.T. + 225,000,001 - A.T. + 300,000,000	5.0¢
A.T. + 300,000,001 - A.T. + 375,000,000	5.5¢
A.T. + 375,000,001 and above	6.0¢

**CAPITAL ONE NSA
RATE SCHEDULE 610D
FOR ADJUSTED THRESHOLD (A.T.)**

Volume Block**Incremental Discounts**

A.T. + 1 - A.T. + 50,000,000	1.0¢
A.T. + 50,000,001 - A.T. + 100,000,000	1.5¢
A.T. + 100,000,001 - A.T. + 150,000,000	2.0¢
A.T. + 150,000,001 - A.T. + 200,000,000	2.5¢

**DISCOVER FINANCIAL SERVICES NSA
RATE SCHEDULE 611A**

Volume Block

Incremental Discounts

405,000,000 to 435,000,000	2.5¢
435,000,001 to 465,000,000	3.0¢
465,000,001 to 490,000,000	3.5¢
490,000,001 to 515,000,000	4.0¢
515,000,001 and above	4.5¢

**DISCOVER FINANCIAL SERVICES NSA
RATE SCHEDULE 611B
FOR ADJUSTED THRESHOLD (A.T.)**

Volume Block**Incremental Discounts**

A.T. to A.T. + 30,000,000	2.5¢
A.T. + 30,000,001 to A.T. + 60,000,000	3.0¢
A.T. + 60,000,001 to A.T. + 85,000,000	3.5¢
A.T. + 85,000,001 to A.T. + 110,000,000	4.0¢
A.T. + 110,000,001 and above	4.5¢

**BANK ONE NSA
RATE SCHEDULE 612A**

Volume Block

Incremental Discounts

535,000,001 to 560,000,000	2.5¢
560,000,001 to 585,000,000	3.0¢
585,000,001 to 610,000,000	3.5¢
610,000,001 to 645,000,000	4.0¢
645,000,001 to 680,000,000	4.5¢
680,000,001 and above	5.0¢

**BANK ONE NSA
RATE SCHEDULE 612B
FOR ADJUSTED THRESHOLD (A.T.)**

Volume Block	Incremental Discounts
A.T. to A.T. + 25,000,000	2.5¢
A.T. + 25,000,001 to A.T. + 50,000,000	3.0¢
A.T. + 50,000,001 to A.T. + 75,000,000	3.5¢
A.T. + 75,000,001 to A.T. + 110,000,000	4.0¢
A.T. + 110,000,001 to A.T. + 145,000,000	4.5¢
A.T. + 145,000,001 and above	5.0¢

**HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613A**

(FIRST YEAR OF AGREEMENT)

Volume Block	Incremental Discounts
615,000,001 to 655,000,000	2.5¢
655,000,001 to 675,000,000	3.0¢
675,000,001 to 695,000,000	3.5¢
695,000,001 to 715,000,000	4.0¢
715,000,001 to 735,000,000	4.5¢
735,000,001 and above	5.0¢

**HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613B**

(SECOND YEAR OF AGREEMENT)

Volume Block	Incremental Discounts
725,000,001 to 765,000,000	2.5¢
765,000,001 to 785,000,000	3.0¢
785,000,001 to 805,000,000	3.5¢
805,000,001 to 825,000,000	4.0¢
825,000,001 to 845,000,000	4.5¢
845,000,001 and above	5.0¢

**HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613C**

(THIRD YEAR OF AGREEMENT)

Volume Block	Incremental Discounts
810,000,001 to 850,000,000	2.5¢
850,000,001 to 870,000,000	3.0¢
870,000,001 to 890,000,000	3.5¢
890,000,001 to 910,000,000	4.0¢
910,000,001 to 930,000,000	4.5¢
930,000,001 and above	5.0¢

**HSBC NORTH AMERICA HOLDINGS INC. NSA
RATE SCHEDULE 613D
FOR ADJUSTED THRESHOLDS (A.T.)**

Volume Block	Incremental Discounts
A.T. to A.T. + 40,000,000	2.5¢
A.T. + 40,000,001 to A.T. + 60,000,000	3.0¢
A.T. + 60,000,001 to A.T. + 80,000,000	3.5¢
A.T. + 80,000,001 to A.T. + 100,000,000	4.0¢
A.T. + 100,000,001 to A.T. + 120,000,000	4.5¢
A.T. + 120,000,001 and above	5.0¢

**BOOKSPAN NSA
RATE SCHEDULE 620A**

(FIRST YEAR OF AGREEMENT)

Volume Block¹	Incremental Discounts
87,000,001 to 120,000,000	2.0¢
120,000,001 to 150,000,000	3.0¢

¹ Volume block beginning and ending thresholds are subject to adjustment for mergers or acquisitions by adding the new entities' volume in accordance with DMCS § 620.24.

**BOOKSPAN NSA
RATE SCHEDULE 620B**

(SECOND YEAR OF AGREEMENT)

Volume Block¹	Incremental Discounts
85,000,001 to 110,000,000	2.0¢
110,000,001 to 150,000,000	3.0¢

¹ Volume block beginning and ending thresholds are subject to adjustment for mergers or acquisitions by adding the new entities' volume in accordance with DMCS § 620.24.

**BOOKSPAN NSA
RATE SCHEDULE 620C**

(THIRD YEAR OF AGREEMENT)

Volume Block¹	Incremental Discounts
94,000,001 to 100,000,000	1.0¢
100,000,001 to 120,000,000	2.0¢
120,000,001 to 150,000,000	3.0¢

¹ Volume block beginning and ending thresholds are subject to adjustment for mergers or acquisitions by adding the new entities' volume in accordance with DMCS § 620.24.

FEE SCHEDULES**FEE SCHEDULE 911****ADDRESS CORRECTIONS**

Description	Fee
Manual correction, each	\$0.50
Electronic correction, each	
First-Class Mail	0.06
Other	0.25
Automated correction (Letters Only)	
First-Class Mail	
First two notices, each ¹	0.00
Additional notices, each ²	0.05
Standard Mail	
First two notices, each ¹	0.02
Additional notices, each ²	0.15

SCHEDULE 911 NOTES

1. For a given address change.
2. After the second notice for a given address change.

FEE SCHEDULE 912**ZIP CODING OF MAILING LISTS**

Description	Fee
Per 1,000 addresses, or fraction	\$110.00

CORRECTION OF MAILING LISTS

Description	Fee
Per submitted address	\$0.33
Minimum charge per list (30 items)	9.90

**ADDRESS CHANGES FOR ELECTION BOARDS
AND REGISTRATION COMMISSIONS**

Description	Fee
Per change of address	\$0.32

SEQUENCING OF ADDRESS CARDS

Description	Fee
Per correction	\$0.33
Insertion of blanks	0.00

SCHEDULE 912 NOTES

1. When rural routes have been consolidated or changed to another post office, no charge will be made for correction if the list contains only names of persons residing on the routes involved.

FEE SCHEDULE 921

POST OFFICE BOXES AND CALLER SERVICE

I. Post Office Boxes

Semi-annual Box Fees

Box Size	Fee Group							
	1	2	3	4	5	6	7	E
1	\$ 42.00	\$ 35.00	\$ 28.00	\$ 20.00	\$ 18.00	\$ 13.00	\$ 10.00	\$ 0.00
2	64.00	54.00	46.00	34.00	26.00	20.00	16.00	0.00
3	118.00	94.00	84.00	52.00	48.00	35.00	28.00	0.00
4	242.00	184.00	150.00	102.00	88.00	62.00	48.00	0.00
5	390.00	326.00	250.00	196.00	148.00	110.00	86.00	0.00

Key Duplication and Lock Charges

Description	Fee
Key duplication or replacement	\$ 6.00
Post office box lock replacement	14.00

II. Caller Service

Semi-annual Caller Service Fees

Group 1	630.00
Group 2	550.00
Group 3	485.00
Group 4	475.00
Group 5	465.00
Group 6	415.00
Group 7	370.00
Annual Call Number Reservation Fee	38.00

SCHEDULE 921 NOTES

1. When the Postal Service determines not to provide carrier delivery to a customer's physical address or business location that constitutes a potential carrier delivery point, as defined by the Postal Service, that customer becomes eligible for one post office box at the Group E fee.
2. Box Size 1 = under 296 cubic inches; 2 = 296-499 cubic inches; 3 = 500-999 cubic inches; 4 = 1000-1999 cubic inches; 5 = 2000 cubic inches and larger.

FEE SCHEDULE 931**BUSINESS REPLY MAIL**

Description	Fee
Regular (no account maintenance fee)	
Permit fee (per year)	\$175.00
Per-piece charge	0.70
Regular (with account maintenance fee)	
Permit fee (per year)	175.00
Account maintenance fee (per year)	550.00
Per-piece charge	0.08
Qualified Business Reply Mail, low-volume	
Permit fee (per year)	175.00
Account maintenance fee (per year)	550.00
Per-piece charge, basic	0.05
Qualified Business Reply Mail, high-volume	
Permit fee (per year)	175.00
Account maintenance fee (per year)	550.00
Quarterly fee	1,800.00
Per-piece charge, high-volume	0.005
Bulk Weight Averaged	
Permit fee (per year)	175.00
Account maintenance fee (per year)	550.00
Per-piece charge, bulk weight averaged	0.011
Monthly maintenance fee	900.00

FEE SCHEDULE 932

MERCHANDISE RETURN SERVICE

Description	Fee
Permit fee (per year)	\$175.00
Account maintenance fee (per year)	550.00
Per-piece charge	0.00

FEE SCHEDULE 933

RESERVED

FEE SCHEDULE 934

RESERVED

FEE SCHEDULE 935

BULK PARCEL RETURN SERVICE

Description	Fee
Permit fee (per year)	\$175.00
Account maintenance fee (per year)	550.00
Per-piece charge	2.10

FEE SCHEDULE 936

SHIPPER PAID FORWARDING

Description	Fee
Account maintenance fee (per year)	\$550.00

FEE SCHEDULE 937

PREMIUM FORWARDING SERVICE

Description	Fee
Enrollment fee	\$10.00
Weekly reshipment fee	\$ 2.85

Docket No. R2006-1

SCHEDULE 937 NOTE

1. The weekly reshipment fee is in addition to the postage applicable to a 3-pound parcel mailed to zone 6, as stated in Rate Schedule 223 (Priority Mail).

FEE SCHEDULE 941

CERTIFIED MAIL

Description	Fee
Fee per piece, in addition to postage	\$2.65

FEE SCHEDULE 942

REGISTERED MAIL

Declared Value	Fee	
	(in addition to postage)	
\$ 0.00	\$9.50	
0.01 to 100	10.15	
100.01 to 500	11.25	
500.01 to 1,000	12.35	
1,000.01 to 2,000	13.45	
2,000.01 to 3,000	14.55	
3,000.01 to 4,000	15.65	
4,000.01 to 5,000	16.75	
5,000.01 to 6,000	17.85	
6,000.01 to 7,000	18.95	
7,000.01 to 8,000	20.05	
8,000.01 to 9,000	21.15	
9,000.01 to 10,000	22.25	
10,000.01 to 11,000	23.35	
11,000.01 to 12,000	24.45	
12,000.01 to 13,000	25.55	
13,000.01 to 14,000	26.65	
14,000.01 to 15,000	27.75	
15,000.01 to 16,000	28.85	
16,000.01 to 17,000	29.95	
17,000.01 to 18,000	31.05	
18,000.01 to 19,000	32.15	
19,000.01 to 20,000	33.25	
20,000.01 to 21,000	34.35	
21,000.01 to 22,000	35.45	
22,000.01 to 23,000	36.55	
23,000.01 to 24,000	37.65	
24,000.01 to 25,000	38.75	
25,000.01 to \$15 million.....	38.75	plus \$1.10 handling charge for each \$1,000 or fraction thereof over \$25,000.00
Over \$15 million.....	16,511.25	plus amount determined by the Postal Service based on weight, space, and value

SCHEDULE 942 NOTES

1. Articles with a declared value of more than \$25,000 can be registered, but compensation for loss or damage is limited to \$25,000.

FEE SCHEDULE 943

INSURANCE

Description	Fee
Express Mail Insurance	
Merchandise coverage	
\$0.01 to 100.00	\$0.00
100.01 to 200.00	0.75
200.01 to 500.00	2.10
500.01 to 5,000.00	\$2.10 plus \$1.35 for each \$500 or fraction thereof over \$500.00
 Document reconstruction coverage	
\$0.00 to 100.00	0.00
 Regular Insurance	
Amount of coverage	
\$0.01 to 50.00	1.65
50.01 to 100.00	2.05
100.01 to 200.00	2.45
200.01 to 300.00	4.60
300.01 to 5,000.00	\$4.60 plus \$.90 for each \$100 or fraction thereof over \$300.00
 Bulk Insurance	
Amount of coverage	
\$0.01 to 50.00	0.85
50.01 to 100.00	1.25
100.01 to 200.00	1.65
200.01 to 300.00	3.80
300.01 to 5,000.00	\$3.80 plus \$.90 for each \$100 or fraction thereof over \$300.00

SCHEDULE 943 NOTES

1. Fees for bulk insurance represent a discount of \$0.80.

FEE SCHEDULE 944

COLLECT ON DELIVERY

Description	Fee
Amount to be collected, or Insurance Coverage Desired	
\$ 0.01 to \$ 50.....	\$5.10
50.01 to 100.....	6.25
100.01 to 200.....	7.40
200.01 to 300.....	8.55
300.01 to 400.....	9.70
400.01 to 500.....	10.85
500.01 to 600.....	12.00
600.01 to 700.....	13.15
700.01 to 800.....	14.30
800.01 to 900.....	15.45
900.01 to 1000.....	16.60
Notice of nondelivery	3.40
Alteration of COD charges	3.40
Designation of new addressee	3.40
Registered COD	4.55

FEE SCHEDULE 945**RETURN RECEIPTS**

Description	Fee
Return Receipt	
Requested at time of mailing	
Original signature	\$2.15
Copy of signature (electronic)	0.85
Requested after mailing	3.80
Return Receipt for Merchandise	
Requested at time of mailing	\$3.50
Delivery record	3.80

FEE SCHEDULE 946

RESTRICTED DELIVERY

Description	Fee
Per piece	\$4.10

FEE SCHEDULE 947**CERTIFICATE OF MAILING**

Description	Fee
Individual Pieces	
Original certificate of mailing for listed pieces of all classes of ordinary mail	\$1.05
Three or more pieces individually listed in a firm mailing book or an approved customer provided manifest (per piece)	0.35
Each additional copy of original certificate of mailing or original mailing receipt for registered, insured, certified, and COD mail (each copy)	1.05
Bulk	
Identical pieces of First-Class and Standard Mail paid with ordinary stamps, precanceled stamps, or meter stamps are subject to the following fees:	
Up to 1,000 pieces (one certificate for total number)	5.50
Each additional 1,000 pieces or fraction	0.60
Duplicate copy	1.05

FEE SCHEDULE 948

DELIVERY CONFIRMATION

Description	Fee
First-Class Mail Letters and Sealed Parcels	
Electronic	\$0.18
Retail	0.75
Priority Mail	
Electronic	0.00
Retail	0.65
Standard Mail	
Electronic	0.18
Package Services Parcel Select	
Electronic	0.00
Other Package Services	
Electronic	0.18
Retail	0.75

FEE SCHEDULE 949**SIGNATURE CONFIRMATION**

Description	Fee
First-Class Mail Letters and Sealed Parcels	
Electronic	\$1.75
Retail	2.10
Priority Mail	
Electronic	1.75
Retail	2.10
Package Services	
Electronic	1.75
Retail	2.10

FEE SCHEDULE 951

PARCEL AIR LIFT

Description	Fee
For pieces weighing:	
Not more than 2 pounds	\$0.50
Over 2 but not more than 3 pounds	\$1.00
Over 3 but not more than 4 pounds	\$1.45
Over 4 but not more than 30 pounds	\$2.00

FEE SCHEDULE 952

SPECIAL HANDLING

Description	Fee
For pieces weighing:	
Not more than 10 pounds	\$6.90
More than 10 pounds	9.60

FEE SCHEDULE 961

STAMPED ENVELOPES

Description	Fee
Plain stamped envelopes	
Basic, size 6-3/4, each	\$0.09
Basic, size 6-3/4, 500	14.50
Basic, over size 6-3/4, each	0.09
Basic, over size 6-3/4, 500	16.50
Personalized stamped envelopes	
Basic, size 6-3/4, 50	4.25
Basic, size 6-3/4, 500	20.00
Basic, over size 6-3/4, 50	4.25
Basic, over size 6-3/4, 500	23.00

FEE SCHEDULE 962

STAMPED CARDS

Description	Fee
Single card	\$0.02
Double reply-paid card	0.04
Sheet of 40 cards (uncut)	0.80

FEE SCHEDULE 971

MONEY ORDERS

Description	Fee
Domestic (\$0.01 to \$500.00)	\$1.05
Domestic (\$500.01 to \$1,000.00)	1.50
APO/FPO (\$0.01 to \$1,000.00)	0.30
Inquiry, including a copy of paid money order	5.00

FEE SCHEDULE 991**CONFIRM**

Description	Fee
Silver	
Subscription Fee (3 months)	\$2,000.00
Additional Scans (block of 2 million)	500.00
Gold	
Subscription Fee (12 months)	6,000.00
Additional Scans (block of 6 million)	750.00
Platinum	
Subscription Fee (12 months)	19,500.00
Additional ID Codes	
Annual	2,000.00
Quarterly	750.00

FEE SCHEDULE 1000

MISCELLANEOUS FEES

Description	Fee
First-Class Presorted Mailing Fee (per year)	\$175.00
Standard Mail Mailing Fee (per year)	175.00
Periodicals	
A. Original Entry	500.00
B. Additional Entry	75.00
C. Re-entry	55.00
D. Registration for News Agents	45.00
Parcel Select Mailing Fee (per year)	175.00
Bound Printed Matter: Destination Entry Mailing Fee (per year)	175.00
Media Mail Presorted Mailing Fee (per year)	175.00
Library Mail Presorted Mailing Fee (per year)	175.00
Authorization to Use Permit Imprint (one-time only)	175.00
Account Maintenance Fee (per year)	550.00
Permit Fee (per year)	175.00
Parcel Return Service Account Maintenance Fee (per year)	550.00
Parcel Return Service Permit Fee (per year)	175.00
Change of Address Service	1.00

EXPEDITED MAIL CLASSIFICATION SCHEDULE

110 DEFINITION

Expedited Mail is mail matter entered as Express Mail under the provisions of this Schedule. Any matter eligible for mailing may, at the option of the mailer, be mailed as Express Mail. Insurance is either included in Express Mail postage or is available for an additional charge, depending on the value and nature of the item sent by Express Mail.

120 DESCRIPTION OF SERVICES

121 Same Day Airport Service

Same Day Airport service is available between designated airport mail facilities.

122 Custom Designed Service

122.1 General. Custom Designed service is available between designated postal facilities or other designated locations for mailable matter tendered under a service agreement between the Postal Service and the mailer. Service under a service agreement shall be offered in a manner consistent with 39 U.S.C. 403(c).

122.2 Service Agreement. A service agreement shall set forth the following:

- a. The scheduled place for each shipment tendered for service to each specific destination;
- b. Scheduled place for claim, or delivery, at destination for each scheduled shipment;
- c. Scheduled time of day for tender at origin and for claim or delivery at destination.

122.3 Pickup and Delivery. Pickup at the mailer's premises, and/or delivery at an address other than the destination postal facility is provided under terms and conditions as specified by the Postal Service.

122.4 Commencement of Service Agreement. Service provided pursuant to a service agreement shall commence not more than 10 days after the signed service agreement is tendered to the Postal Service.

122.5 Termination of Service Agreement

122.51 Termination by Postal Service. Express Mail service provided pursuant to a service agreement may be terminated by the Postal Service upon 10 days prior written notice to the mailer if:

- a. Service cannot be provided for reasons beyond the control of the Postal Service or because of changes in Postal Service facilities or operations, or
- b. The mailer fails to adhere to the terms of the service agreement or this schedule.

122.52 Termination by Mailers. The mailer may terminate a service agreement, for any reason, by notice to the Postal Service.

123 Next Day Service and Second Day Service

123.1 Availability of Services. Next Day and Second Day Services are available at designated retail postal facilities to designated destination facilities or locations for items tendered by the time or times specified by the Postal Service. Next Day Service is available for overnight delivery. Second Day Service is available for delivery on the second day or, in certain circumstances, the second delivery day, as specified by the Postal Service. For purposes of this schedule, the “second delivery day” is the next delivery day following the second day.

123.2 Pickup Service. Pickup service is available for Next Day and Second Day Services under terms and conditions as specified by the Postal Service. Service shall be offered in a manner consistent with 39 U.S.C. 403(c).

130 PHYSICAL LIMITATIONS

Express Mail may not exceed 70 pounds or 108 inches in length and girth combined.

140 POSTAGE AND PREPARATION

Except as provided in Rate Schedules 121, 122 and 123, postage on Express Mail is charged on each piece. For shipments tendered in Express Mail pouches under a service agreement, each pouch is a piece.

150 DEPOSIT AND DELIVERY**151 Deposit**

Express Mail must be deposited at places designated by the Postal Service.

152 Receipt

A receipt showing the time and date of mailing will be provided to the mailer upon acceptance of Express Mail by the Postal Service. This receipt serves as evidence of mailing.

153 Service

Express Mail service provides a high speed, high reliability service. Same Day Airport Express Mail will be dispatched on the next available transportation to the destination airport mail facility. Custom Designed Express Mail will be available for claim or delivery as specified in the service agreement.

154 Forwarding and Return

When Express Mail is returned, or forwarded, as specified by the Postal Service, there will be no additional charge.

160 ANCILLARY SERVICES

The following services may be obtained in conjunction with mail sent under this classification schedule upon payment of applicable fees:

Service	Schedule
a. Address correction	911
b. Return receipts	945
c. COD	944
d. Express Mail Insurance	943

170 RATES AND FEES

The rates for Express Mail are set forth in the following rate schedules:

	Schedule
a. Same Day Airport	121
b. Custom Designed	122
c. Next Day Post Office-to-Post Office	123
d. Second Day Post Office-to-Post Office	123
e. Next Day Post Office-to-Addressee	123
f. Second Day Post Office-to-Addressee	123

180 REFUNDS

181 Procedure

Claims for refunds of postage must be filed within the period of time and under terms and conditions specified by the Postal Service.

182 Availability

182.1 Same Day Airport. Except as provided in 182.5, the Postal Service will refund the postage for Same Day Airport Express Mail not available for claim by the time specified.

182.2 Custom Designed. Except where a service agreement provides for claim, or delivery, of Custom Designed Express Mail more than 24 hours after scheduled tender at point of origin, the Postal Service will refund postage for such mail not available for claim, or not delivered, within 24 hours of mailing, except as provided in 182.5.

182.3 Next Day. Except as provided in 182.5, the Postal Service will refund postage for Next Day Express Mail not available for claim or not delivered:

- a. By 10:00 a.m., or earlier time(s) specified by the Postal Service, of the next delivery day in the case of Post Office-to-Post Office service; or
- b. By 3:00 p.m., or earlier time(s) specified by the Postal Service, of the next delivery day in the case of Post Office-to-Addressee service.

182.4 **Second Day.** Except as provided in 182.5, the Postal Service will refund postage for Second Day Express Mail not available for claim or not delivered:

- a. By 10:00 a.m., or earlier time(s) specified by the Postal Service, of the second delivery day in the case of Post Office-to-Post Office service; or
- b. By 3:00 p.m., or earlier time(s) specified by the Postal Service, of the second delivery day in the case of Post Office-to-Addressee service.

182.5 **Limitations**

182.51 Refunds may not be available if delivery was attempted within the times required for the specific service, or if the delay was caused by:

- a. proper detention for law enforcement purposes;
- b. strike or work stoppage;
- c. late deposit of shipment, forwarding, return, incorrect address, or incorrect ZIP code;
- d. delay or cancellation of flights;
- e. governmental action beyond the control of the Postal Service or air carriers;
- f. war, insurrection, or civil disturbance;
- g. breakdowns of a substantial portion of the USPS transportation network resulting from events or factors outside the control of the Postal Service; or
- h. acts of God.

FIRST-CLASS MAIL CLASSIFICATION SCHEDULE

210 DEFINITION

Any matter eligible for mailing, except Regular and Nonprofit Presort category mail entered as Customized Market Mail under sections 321.22 and 323.22, may, at the option of the mailer, be mailed as First-Class Mail. The following must be mailed as First-Class Mail, unless mailed as Express Mail or exempt under title 39, United States Code, or except as authorized under sections 344.12, 344.23 and 443:

- a. Mail sealed against postal inspection as set forth in section 5000;
- b. Matter wholly or partially in handwriting or typewriting except as specifically permitted by sections 312, 313, 520, 544.2, and 446;
- c. Matter having the character of actual and personal correspondence except as specifically permitted by sections 312, 313, 520, 544.2, and 446; and
- d. Bills and statements of account.

220 DESCRIPTION OF SUBCLASSES

221 Letters and Sealed Parcels Subclass

221.1 General. The Letters and Sealed Parcels subclass consists of First-Class Mail weighing 13 ounces or less that is not mailed under section 222 or 223.

221.2 Regular Rate Categories. The regular rate categories consist of Letters and Sealed Parcels subclass mail not mailed under section 221.3 or 221.4.

221.21 Single-Piece Rate Category. The single-piece rate category applies to regular rate Letters and Sealed Parcels subclass mail not mailed under section 221.22 or 221.24.

221.211 Letters. The letter rates apply to pieces that:

- a. Do not exceed 3.5 ounces in weight;
- b. Exhibit a length between 5.0 and 11.5 inches;

- c. Exhibit a height between 3.5 and 6.125 inches; and
- d. Exhibit a thickness between 0.007 and 0.25 inches.

221.212 **Flats.** The flat rates apply to pieces that:

- a. Exceed 3.5 ounces in weight, but otherwise meet the requirements specified in section 221.211 for letters; or
- b. Exhibit the following dimensions:
 - i. A length more than 11.5 inches, or a height more than 6.125 inches, or a thickness more than 0.25 inches; and
 - ii. A length not more than 15 inches, or a height not more than 12 inches, or a thickness not more than 0.75 inches.

221.213 **Parcels.** The parcel rates apply to single-piece rate category pieces that are not eligible for letter or flat rates as defined in sections 221.211 and 221.212.

221.22 **Presort Rate Category.** The presort rate category applies to Letters and Sealed Parcels subclass mail that:

- a. Is prepared in a mailing of at least 500 pieces;
- b. Is presorted, marked, and presented as specified by the Postal Service; and
- c. Meets the addressing and other preparation requirements specified by the Postal Service.

221.221 **Letters.** The letter rates apply to pieces that:

- a. Do not exceed 3.5 ounces in weight;
- b. Exhibit a length between 5.0 and 11.5 inches;
- c. Exhibit a height between 3.5 and 6.125 inches; and
- d. Exhibit a thickness between 0.007 and 0.25 inches.

221.222 **Flats.** The flat rates apply to pieces that:

- a. Exceed 3.5 ounces in weight, but otherwise meet the requirements specified in section 221.221 for letters; or
- b. Exhibit the following dimensions:
 - i. A length more than 11.5 inches, or a height more than 6.125 inches, or a thickness more than 0.25 inches; and
 - ii. A length not more than 15 inches, or a height not more than 12 inches, or a thickness not more than 0.75 inches.

221.22[1]3 Repositionable Notes. Repositionable Notes may be attached to the exterior of letter-size and flat-size presort rate category mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 3 to Rate Schedule 221.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such request.
- b. If the Postal Service determines not to file such request, this provision expires on such date as [specifiefd] specified by the Postal Service, but no later than April 3, 2007.

221.23 *Reserved*

221.24 **Qualified Business Reply Mail Rate Category.** The qualified business reply mail rate category applies to Letters and Sealed Parcels subclass mail that:

- a. Is provided to senders by the recipient, an advance deposit account business reply mail permit holder, for return by mail to the recipient;
- b. Bears the recipient's preprinted machine-readable return address, a barcode representing not more than 11 digits (not including "correction" digits), a Facing Identification Mark, and other markings specified and approved by the Postal Service; and

- c. Meets the letter machinability and other preparation requirements specified by the Postal Service.

221.25 *Reserved*

221.26 **Nonmachinable Surcharge.** Single-piece and presort letter-shaped mail as defined in section 221.211 or 221.221 weighing one ounce or less is subject to a surcharge if:

- a. Its aspect ratio does not fall between 1 to 1.3 and 1 to 2.5 inclusive; or
- b. It does not meet letter machinability requirements as specified by the Postal Service.

[**221.26** **Nonmachinable Surcharge.** Regular rate category Letters and Sealed Parcels subclass mail is subject to a surcharge if it is nonmachinable mail, as defined in section 232.]

[**221.27** **Presort Discount for Pieces Weighing More Than Two Ounces.** Presort rate category Letters and Sealed Parcels subclass mail is eligible for an additional presort discount on each piece weighing more than two ounces.]

221.3 **Automation Rate Categories — Letters and Flats**

221.31 **General.** The automation rate categories consist of Letters and Sealed Parcels subclass mail weighing 13 ounces or less that:

- a. Is presorted, marked, and presented as specified by the Postal Service;
- b. Bears a barcode representing not more than 11 digits (not including "correction" digits) as specified by the Postal Service; and
- c. Meets the machinability, addressing, barcoding, and other preparation requirements specified by the Postal Service.

221.32 **Letter Categories**

221.321 **General.** The letter rates apply to pieces that:

- a. Do not exceed 3.5 ounces in weight;
- b. Exhibit a length between 5.0 and 11.5 inches;

- c. Exhibit a height between 3.5 and 6.125 inches; and
- d. Exhibit a thickness between 0.007 and 0.25 inches.

221.32[1]2 Mixed AADC Rate Category. The Mixed AADC rate category applies to letter-size automation rate category mail not mailed under section [221.322,] 221.323, 221.324, or 221.325.

221.32[2]3 AADC Rate Category. The AADC rate category applies to letter-size automation rate category mail presorted to automated area distribution center destinations as specified by the Postal Service.

221.32[3]4 Three-Digit Rate Category. The three-digit rate category applies to letter-size automation rate category mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

221.32[4]5 Five-Digit Rate Category. The five-digit rate category applies to letter-size automation rate category mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.

[221.325 Carrier Route Rate Category. The carrier route rate category applies to letter-size automation rate category mail presorted to carrier routes. It is available only for those carrier routes specified by the Postal Service.]

221.326 Repositionable Notes. Repositionable Notes may be attached to the exterior of automation letter rate category mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 3 to Rate Schedule 221.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such request.
- b. If the Postal Service determines not to file such request, this provision expires on such date as specified by the Postal Service, but no later than April 3, 2007.

221.33 Flats Categories

221.331 **General.** The flat rates apply to pieces that exhibit:

- a. A length more than 11.5 inches, or a height more than 6.125 inches, or a thickness more than 0.25 inches; and
- b. A length not more than 15 inches, or a height not more than 12 inches, or a thickness not more than 0.75 inches.

221.33[1]2 **Mixed ADC Flats Rate Category.** The Mixed ADC flats rate category applies to flat-size automation rate category mail not mailed under section 221.33[2]3, 221.33[3]4, or 221.33[4]5.

221.33[2]3 **ADC Flats Rate Category.** The ADC flats rate category applies to flat-size automation rate category mail presorted to area distribution center destinations as specified by the Postal Service.

221.33[3]4 **Three-Digit Flats Rate Category.** The three-digit flats rate category applies to flat-size automation rate category mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

221.33[4]5 **Five-Digit Flats Rate Category.** The five-digit flats rate category applies to flat-size automation rate category mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.

[221.335 **Nonmachinable Surcharge.** Flat-size automation rate category pieces are subject to a surcharge if they are nonmachinable mail, as defined in section 232.]

221.336 **Repositionable Notes.** Repositionable Notes may be attached to the exterior of automation flats rate category mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 3 to Rate Schedule 221.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such[request] request.

- b. If the Postal Service determines not to file such request, this provision expires on such date as specified by the Postal Service, but no later than April 3, 2007.

[221.34 Presort Discount for Pieces Weighing More Than Two Ounces. Presorted automation rate category mail is eligible for an additional presort discount on each piece weighing more than two ounces.]

221.4 Business Parcels Categories.

221.41 General. The business parcels categories apply to Letters and Sealed Parcels subclass mail that:

- a. Is prepared in a mailing of at least 500 pieces;
- b. Is presorted, marked, and presented as specified by the Postal Service;
- c. Exhibit lengths between 3.5 and 18.0 inches;
- d. Exhibit heights between 3.0 and 15.0 inches;
- e. Exhibit thicknesses between 0.05 and 22.0 inches; and
- f. Meets the addressing and other preparation requirements as specified by the Postal Service.

221.42 Single-Piece Rate. The single-piece rate category as defined in 221.213 applies to pieces not qualifying under section 221.43, 221.44, or 221.45.

221.43 ADC Parcels Rate Category. The ADC parcels rate category applies to parcel rate category mail presorted to area distribution center destinations as specified by the Postal Service.

221.44 Three-Digit Parcels Rate Category. The three-digit parcels rate category applies to parcels rate category mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

221.45 Five-Digit Parcels Rate Category. The five-digit parcels rate category applies to parcels rate category mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.

221.46 Nonbarcoded and Nonmachinable Surcharge. Parcels rate category pieces qualifying for sections 221.43 and 221.44 are subject to a surcharge

if non-barcoded, less than 2 ounces, or nonmachinable as specified by the Postal Service.

222 Cards Subclass

222.1 Definition

222.11 Cards. The Cards subclass consists of Stamped Cards, defined in section 962.1, and postcards. A postcard is a privately printed mailing card for the transmission of messages. To be eligible to be mailed as a First-Class Mail postcard, a card must be of uniform thickness, prepared as specified by the Postal Service, and must not exceed any of the following dimensions:

- a. 6 inches in length;
- b. 4 1/4 inches in [width] height; or
- c. 0.016 inch in thickness.

222.12 Double Cards. Double Stamped Cards or double postcards may be mailed as Stamped Cards or postcards. Double Stamped Cards are defined in section 962.1. A double postcard consists of two attached cards, one of which may be detached by the receiver and returned by mail as a single postcard.

222.2 *Reserved*

222.3 Regular Rate Categories

222.31 Single-Piece Rate Category. The single-piece rate category applies to regular rate Cards subclass mail not mailed under section 222.32 or 222.34.

222.32 Presort Rate Category. The presort rate category applies to Cards subclass mail that:

- a. Is prepared in a mailing of at least 500 pieces;
- b. Is presorted, marked, and presented as specified by the Postal Service; and
- c. Meets the addressing and other preparation requirements specified by the Postal Service.

222.33 ***Reserved***

222.34 **Qualified Business Reply Mail Rate Category.** The qualified business reply mail rate category applies to Cards subclass mail that:

- a. Is provided to senders by the recipient, an advance deposit account business reply mail permit holder, for return by mail to the recipient;
- b. Bears the recipient's preprinted machine-readable return address, a barcode representing not more than 11 digits (not including "correction" digits), a Facing Identification Mark, and other markings specified and approved by the Postal Service; and
- c. Meets the card machinability and other preparation requirements specified by the Postal Service.

222.4 **Automation Rate Categories**

222.41 **General.** The automation rate categories consist of Cards subclass mail that:

- a. Is presorted, marked, and presented as specified by the Postal Service;
- b. Bears a barcode representing not more than 11 digits (not including "correction" digits) as specified by the Postal Service; and
- c. Meets the machinability, addressing, barcoding, and other preparation requirements specified by the Postal Service.

222.42 **Mixed AADC Rate Category.** The Mixed AADC rate category applies to automation rate category cards not mailed under section 222.43, 222.44, or 222.45[, or 222.46].

222.43 **AADC Rate Category.** The AADC rate category applies to automation rate category cards presorted to automated area distribution center destinations as specified by the Postal Service.

222.44 **Three-Digit Rate Category.** The three-digit rate category applies to automation rate category cards presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

- 222.45 Five-Digit Rate Category.** The five-digit rate category applies to automation rate category cards presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.
- [222.46 Carrier Route Rate Category.** The carrier route rate category applies to automation rate category cards presorted to carrier routes. It is available only for those carrier routes specified by the Postal Service.]
- 223 Priority Mail Subclass**
- 223.1 General.** The Priority Mail subclass consists of:
- a. First-Class Mail weighing more than 13 ounces; and
 - b. Any mailable matter which, at the option of the mailer, is mailed for expeditious handling and transportation.
- 223.2 Single-Piece Priority Mail Rate Category.** The single-piece Priority Mail rate category applies to Priority Mail subclass mail not mailed under section 223.3.
- 223.3 *Reserved***
- 223.4 Flat Rate Box**
- 223.41 General.** Priority Mail subclass mail sent in a “flat rate” box with an external size of 0.34 cubic feet, provided by the Postal Service, is charged the rate designated in Rate Schedule 223, note 2. [A “flat rate” box with an internal capacity of .34 cubic feet is charged the rate designated in note 5¹ for Rate Schedule 223.]
- [223.42 Duration of the Flat Rate Box Experiment.** The provisions of section 223.4 expire the later of:
- a. two years after the implementation date specified by the Postal Service Board of Governors, or
 - b. if, by the expiration date specified above, a request for the establishment of a permanent Flat Rate Box classification is pending before the Postal Rate Commission, the later of:

¹ [The expiration of provisions related to Docket No. MC2001-1 eliminated Note 4. Note 5 now becomes Note 4 in this new version.]

- (1) three months after the Commission takes action on such proposal under section 3624 of Title 39, or, if applicable,
- (2) on the implementation date for a permanent Flat Rate Box classification.]

223.5 Flat Rate Envelope. Priority Mail subclass mail sent in a “flat rate” envelope provided by the Postal Service is charged the one-pound rate.

223.6 Pickup On-Demand [Service]. Pickup On-Demand service is available for Priority Mail subclass mail under terms and conditions specified by the Postal Service.

223.7 [Bulk] Bulky Parcels. In zones 1 through 4 including Local). Priority Mail subclass mail weighing less than [15] 20 pounds[, and] but measuring [over] more than 84 inches [combined,] in combined length and girth is charged [a minimum rate equal to that] the applicable rate for a [15-pound] 20-pound parcel [for the zone to which the piece is addressed] (balloon rate).

223.8 Low-Density Parcels. In zones 5 through 8, Priority Mail subclass mail exceeding one cubic foot is rated at the actual weight or the dimensional weight, whichever is greater.

- a. For box-shaped parcels, the dimensional weight, in pounds, is calculated as the length times the width times the height, all in inches, divided by 194.
- b. For irregularly-shaped parcels (not appearing box-shaped), the dimensional weight, in pounds, is calculated as the length times the width times the height at their maximum cross-sections, all in inches, divided by 194, and multiplied by an adjustment factor of 0.785.

230 PHYSICAL LIMITATIONS

231 Size and Weight

First-Class Mail may not exceed 70 pounds or 108 inches in length and girth combined. Additional size and weight limitations apply to individual First-Class Mail subclasses.

[232 Nonmachinable Mail

Letters and Sealed Parcels subclass mail weighing one ounce or less is nonmachinable if:

- a. Its aspect ratio does not fall between 1 to 1.3 and 1 to 2.5 inclusive; it exceeds any of the following dimensions:
 - i. 11.5 inches in length;
 - ii. 6.125 inches in width; or
 - iii. 0.25 inch in thickness; or
- b. For letter-sized pieces:
 - i. it does not meet the machinability requirements of the Postal Service; or
 - ii. manual processing is requested.]

240 POSTAGE AND PREPARATION

Postage on First-Class Mail must be paid as set forth in section 3000. Postage is computed separately on each piece of mail. Pieces not within the same postage rate increment may be mailed at other than a single-piece rate as part of the same mailing only when specific methods approved by the Postal Service for determining and verifying postage are followed. All mail mailed at other than a single-piece rate must have postage paid in a manner not requiring cancellation.

241 FOREVER STAMP

Postage for the first ounce of a First-Class Mail single-piece letter may be paid through the application of a Forever Stamp. The Forever Stamp is sold at the prevailing rate for single-piece letters, first ounce, in Rate Schedule 221. Once purchased, the Forever Stamp may be used for first ounce letter postage at any time in the future, regardless of the prevailing rate at the time of use.

250 DEPOSIT AND DELIVERY

251 Deposit

First-Class Mail must be deposited at places and times designated by the Postal Service.

252 Service

First-Class Mail receives expeditious handling and transportation, except that when First-Class Mail is attached to or enclosed with mail of another class, the service of that class applies.

253 Forwarding and Return

First-Class Mail that is undeliverable-as-addressed is forwarded or returned to the sender without additional charge.

260 ANCILLARY SERVICES

The following services may be obtained in conjunction with mail sent under this classification schedule upon payment of applicable fees:

Service	Schedule
a. Address Correction	911
b. Business Reply Mail	931
c. Certificates of Mailing	947
d. Certified Mail	941
e. COD	944
f. Insurance	943
g. Registered Mail	942
h. Return Receipt (limited to merchandise sent by Priority Mail)	945
i. Merchandise Return	932
j. Delivery Confirmation (limited to parcel-shaped Letters and Sealed Parcels and Priority Mail)	948
k. Signature Confirmation (limited to parcel-shaped Letters and Sealed Parcels and Priority Mail)	949

270 RATES AND FEES

271 First-Class Mail. The rates and fees for First-Class Mail are set forth in the following rate schedules:

	Schedule
a. Letters and Sealed Parcels	221
b. Cards	222
c. Priority Mail	223

272 Keys and Identification Devices. Keys, identification cards, identification tags, or similar identification devices that:

- a. weigh no more than 2 pounds;
- b. are mailed without cover; and
- c. bear, contain, or have securely attached the name and address information, as specified by the Postal Service, of a person, organization, or concern, with instructions to return to the address and a statement guaranteeing the payment of postage due on delivery; are subject to the following rates and fees:
 - i. the applicable single-piece rates in schedules 221 or 223; and
 - ii. the fee set forth in Fee Schedule 931 for payment of postage due charges if an active business reply mail advance deposit account is not used; [; and
 - iii. if applicable, the surcharge for nonmachinable mail, as defined in section 232.]

280 AUTHORIZATIONS AND LICENSES

The mailing fee set forth in schedule 1000 must be paid once each year at each office of mailing or office of verification, as specified by the Postal Service, by or for mailers of other than single-piece First-Class Mail. Payment of the fee allows the mailer to mail at any First-Class rate.

**STANDARD MAIL
CLASSIFICATION SCHEDULE**

310 DEFINITION

311 General

Any mailable matter weighing less than 16 ounces may be mailed as Standard Mail except:

- a. Matter required to be mailed as First-Class Mail;
- b. Copies of a publication that is entered as Periodicals class mail, except copies sent by a printer to a publisher, and except copies that would have traveled at the former second-class transient rate. (The transient rate applied to individual copies of second-class mail (currently Periodicals class mail) forwarded and mailed by the public, as well as to certain sample copies mailed by publishers.)

312 Printed Matter

Printed matter, including printed letters which according to internal evidence are being sent in identical terms to several persons, but which do not have the character of actual and personal correspondence, may be mailed as Standard Mail. Printed matter does not lose its character as Standard Mail when the date and name of the addressee and of the sender are written thereon. For the purposes of the Standard Mail Classification Schedule, "printed" does not include reproduction by handwriting or typewriting.

313 Written Additions

Standard Mail may have the following written additions placed on the wrapper, on a tag or label attached to the outside of the parcel, or inside the parcel, either loose or attached to the article:

- a. Marks, numbers, name, or letters descriptive of contents;
- b. "Please Do Not Open Until Christmas," or words of similar import;
- c. Instructions and directions for the use of an article in the package;

- d. Manuscript dedication or inscription not in the nature of personal correspondence;
- e. Marks to call attention to any word or passage in text;
- f. Corrections of typographical errors in printed matter;
- g. Manuscripts accompanying related proof sheets, and corrections in proof sheets to include: corrections of typographical and other errors, alterations of text, insertion of new text, marginal instructions to the printer, and rewrites of parts if necessary for correction;
- h. Handstamped imprints, except when the added matter is itself personal or converts the original matter to a personal communication; or
- i. An invoice.

320 DESCRIPTION OF SUBCLASSES

321 Regular Subclass

321.1 **General.** The Regular subclass consists of Standard Mail that is not mailed under sections 322, 323, or 324. Eligibility for Regular subclass rate categories is based on the size or mail processing shape of the mailpiece as specified by the Postal Service. Mail processing shapes include letter-size mail, flat-size mail, parcels and not flat-machinable (NFM) mail.

321.2 [Presort] Nonautomation Rate Categories

- 321.21** **General.** The [presort] nonautomation rate categories apply to Regular subclass mail that:
- a. Is prepared in a mailing of at least 200 addressed pieces or 50 pounds of addressed pieces;
 - b. Is presorted, marked, and presented as specified by the Postal Service; [and]
 - c. Meets the machinability, addressing, and other preparation requirements specified by the Postal Service[.] ; and
 - d. Is not entered as Customized Market Mail under section 321.5.

[321.22 Basic Rate Categories. The basic rate categories apply to presort rate category mail not mailed under section 321.23, and to all mail entered as Customized Market Mail (CMM). CMM must be marked and bear endorsements as specified by the Postal Service, and must meet the preparation, addressing, and acceptance requirements specified by the Postal Service. Notwithstanding section 6020, Customized Market Mail may be nonrectangular in shape. The following size standards apply to Customized Market Mail:

- a. Thickness: at least 0.007 inch and no more than 0.75 inch;
- b. Length: at least 5 inches and no more than 15 inches, measured for nonrectangular shapes as specified by the Postal Service;
- c. Height: at least 3.5 inches and no more than 12 inches, measured for nonrectangular shapes as specified by the Postal Service.]

321.22 Mixed AADC Rate Category. The Mixed AADC rate category applies to nonautomation rate category letter-size mail that meets machinability criteria specified by the Postal Service and that is not mailed under section 321.23.

[321.23 Three- and Five-Digit Rate Categories. The three- and five-digit rate categories apply to presort rate category mail presorted to single or multiple three- and five-digit ZIP Code destinations as specified by the Postal Service.]

321.23 AADC Rate Category. The AADC rate category applies to letter-size nonautomation rate category mail that meets machinability criteria specified by the Postal Service and that has been presorted to automated area distribution center destinations as specified by the Postal Service.

321.24 Mixed ADC Rate Categories. The Mixed ADC rate categories apply to nonautomation rate category mail not mailed under sections 321.22, 321.23, 321.25, 321.26, 321.27, 321.28 or 321.29.

321.25 ADC Rate Categories. The ADC rate categories apply to nonautomation rate category mail that has been presorted to area distribution center destinations as specified by the Postal Service.

321.26 Three-Digit Rate Categories. The three-digit rate categories apply to nonautomation rate category mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

- 321.27** **Five-Digit Rate Categories.** The five-digit rate categories apply to nonautomation rate category mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.
- 321.28** **Mixed BMC Rate Category.** The Mixed BMC rate category applies to parcel-shaped nonautomation rate category mail that meets machinability criteria specified by the Postal Service and that is not mailed under section 321.29.
- 321.29** **BMC Rate Category.** The BMC rate category applies to parcel-shaped nonautomation rate category mail that meets machinability criteria specified by the Postal Service and that has been presorted to bulk mail center (or equivalent facility) destinations as specified by the Postal Service.
- 321.3** **Automation Rate Categories**
- 321.31** **General.** The automation rate categories apply to Regular subclass mail that:
- a. Is presorted, marked, and presented as specified by the Postal Service;
 - b. Bears a barcode representing not more than 11 digits (not including “correction” digits) as specified by the Postal Service; and
 - c. Meets the machinability, addressing, barcoding, and other preparation requirements specified by the Postal Service.
- 321.32** **Mixed AADC Rate Category.** The Mixed AADC rate category applies to letter-size automation rate category mail not mailed under section 321.33, 321.34, or 321.35.
- 321.33** **AADC Rate Category.** The AADC rate category applies to letter-size automation rate category mail presorted to automated area distribution center destinations as specified by the Postal Service.
- 321.34** **Three-Digit Barcoded Rate [Category] Categories.** The three-digit barcoded rate [category applies] categories apply to letter-size or flat-size automation rate category mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.
- 321.35** **Five-Digit Barcoded Rate [Category] Categories.** The five-digit barcoded rate [category applies] categories apply to letter-size or flat-size automation

rate category mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.

321.36 [Basic Barcoded Flats] Mixed ADC Rate Category. The [basic barcoded flats] Mixed ADC rate category applies to flat-size automation rate category mail not mailed under section 321.37.

321.37 [Three- and Five-Digit Barcoded Flats] ADC Rate Category. The [three- and five-digit barcoded flats] ADC rate category applies to flat-size automation rate category mail presorted to [single or multiple three- and five-digit ZIP Code] area distribution center destinations as specified by the Postal Service.

321.4 Destination Entry Discounts. The destination entry discounts apply to Regular subclass mail, except [Regular Presort category] mail entered as Customized Market Mail under section [321.22] 321.5, prepared as specified by the Postal Service and addressed for delivery within the service area of the BMC (or auxiliary service facility), [or] sectional center facility (SCF), or destination delivery unit (DDU) at which it is entered, as defined by the Postal Service.

[321.5 Residual Shape Surcharge. Regular subclass mail is subject to a surcharge if it is entered as Customized Market Mail under section 321.22 or is prepared as a parcel or if it is not letter or flat shaped.]

321.5 Customized Market Mail (CMM). CMM must be marked and bear endorsements as specified by the Postal Service, and must meet the preparation, addressing, and acceptance requirements specified by the Postal Service. Notwithstanding section 6020, Customized Market Mail may be nonrectangular in shape. The following size standards apply to Customized Market Mail:

- a. Thickness: at least 0.007 inch and no more than 0.75 inch;
- b. Length: at least 5 inches and no more than 15 inches, measured for nonrectangular shapes as specified by the Postal Service;
- c. Height: at least 3.5 inches and no more than 12 inches, measured for nonrectangular shapes as specified by the Postal Service; and
- d. Weight: not to exceed the maximum weight for CMM specified by the Postal Service.

321.6 **[Barcode Discount] Non-barcoded Surcharge.** [The barcode discount applies to Regular Subclass mail, except Regular Presort category mail entered as Customized Market Mail under section 321.22, that is subject to the residual shape surcharge in 321.5, is entered at designated facilities, bears a barcode specified by the Postal Service, is prepared as specified by the Postal Service, and meets all other preparation and machinability requirements of the Postal Service.] Regular nonautomation mailpieces not qualifying for letter-size or flat-size rate categories and that do not bear a barcode specified by the Postal Service are subject to a Non-barcoded Surcharge. The surcharge will not apply to pieces sorted to 5-digit ZIP Codes.

321.7 **Nonmachinable [Surcharge] Rate Categories.** The nonmachinable [surcharge applies] rate categories apply to Regular [presort] nonautomation category letter-size[d] pieces and pieces to which the parcel rate categories apply, [except Regular Presort category mail entered as Customized Market Mail under section 321.22, (i)] that do not meet the machinability requirements specified by the Postal Service[; or (ii) for which manual processing is requested].

321.8 **Repositionable Notes.** Repositionable Notes may be attached to the exterior of letter-size or flat-size Regular subclass mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 6 to Rate Schedule 321A or note 4 to Rate Schedule 321B.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such request.
- b. If the Postal Service determines not to file such request, this provision expires on such date as specified by the Postal Service, but no later than April 3, 2007.

321.9 **Standard Mail Forwarding.** As described in section 353, undeliverable-as-addressed Standard Mail Regular subclass mail that is forwarded on request of the mailer is charged the appropriate rate shown in note 4 to Rate Schedule 321A or note 5 to Rate Schedule 321B. Mail for which Standard Mail Forwarding is purchased must meet preparation requirements and bear endorsements as specified by the Postal Service. Payment for Standard

Mail Forwarding is made through an advance deposit account, or as specified by the Postal Service.

322 Enhanced Carrier Route Subclass

322.1 Definition. The Enhanced Carrier Route subclass consists of Standard Mail [weighing less than 16 ounces] that is not mailed under section 321, 323, or 324, and that:

- a. Is prepared in a mailing of at least 200 addressed pieces or 50 pounds of addressed pieces;
- b. Is prepared, marked, and presented as specified by the Postal Service;
- c. Is presorted to carrier routes as specified by the Postal Service;
- d. Is sequenced as specified by the Postal Service;
- e. Meets the machinability, addressing, and other preparation requirements specified by the Postal Service; and
- f. For high-density and saturation category letters, bears a barcode representing not more than 11 digits (not including “correction” digits) as specified by the Postal Service.

Eligibility for Enhanced Carrier Route subclass rate categories is based on the size or mail processing shape of the mailpiece as specified by the Postal Service. Mail processing shapes include letter-size mail, flat-size mail, parcels and not flat-machinable (NFM) mail.

322.2 Basic Rate Category. The basic rate category applies to Enhanced Carrier Route subclass mail not mailed under section 322.3[,] or 322.4 [or 322.5].

[322.3 Basic Pre-Barcoded Rate Category. The basic pre-barcoded rate category applies to letter-size Enhanced Carrier Route subclass mail which bears a barcode representing not more than 11 digits (not including “correction” digits), as specified by the Postal Service, and which meets the machinability, addressing, and barcoding specifications and other preparation requirements specified by the Postal Service.]

322.[4]3 High Density Rate Category. The high density rate category applies to Enhanced Carrier Route subclass mail presented in walk-sequence order and meeting the high density requirements specified by the Postal Service.

High density rate category letters must meet the applicable automation requirements specified by the Postal Service, and must bear a barcode representing not more than 11 digits (not including “correction” digits), as specified by the Postal Service.

- 322.[5]4 Saturation Rate Category.** The saturation rate category applies to Enhanced Carrier Route subclass mail presented in walk-sequence order and meeting the saturation requirements specified by the Postal Service. Saturation rate category letters must meet the applicable automation requirements specified by the Postal Service, and must bear a barcode representing not more than 11 digits (not including “correction” digits), as specified by the Postal Service.
- 322.[6]5 Destination Entry Discounts.** Destination entry discounts apply to Enhanced Carrier Route subclass mail prepared as specified by the Postal Service and addressed for delivery within the service area of the BMC (or auxiliary service facility), sectional center facility (SCF), or destination delivery unit (DDU) at which it is entered, as defined by the Postal Service. Letter-size mail is not eligible for the DDU discount.
- [322.7 Residual Shape Surcharge.** Enhanced Carrier Route subclass mail is subject to a surcharge if it is prepared as a parcel or if it is not letter or flat shaped.]
- 322.6 DAL Surcharge.** Flat-shaped and parcel-shaped Enhanced Carrier Route subclass mail are subject to a per-piece surcharge if they are addressed using a detached address label (DAL).
- 322.7 Standard Mail Forwarding.** As described in section 353, undeliverable-as-addressed Standard Mail Enhanced Carrier Route subclass mail that is forwarded on request of the mailer is charged the appropriate rate shown in note 8 to Rate Schedule 322. Mail for which Standard Mail Forwarding is purchased must meet preparation requirements and bear endorsements as specified by the Postal Service. Payment for Standard Mail Forwarding is made through an advance deposit account, or as specified by the Postal Service.
- 322.8 Repositionable Notes.** Repositionable Notes may be attached to the exterior of letter-size or flat-size Enhanced Carrier Route subclass mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 6 to Rate Schedule 322.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such request.
- b. If the Postal Service determines not to file such request, this provision expires on such date as specified by the Postal Service, but no later than April 3, 2007.

323 Nonprofit Regular Subclass

323.1 General. The Nonprofit Regular subclass consists of Standard Mail weighing less than 16 ounces that is not mailed under section 321, 322, or 324, and that is mailed by authorized nonprofit organizations or associations of the following types:

- a. Religious, as defined in section 1009;
- b. Educational, as defined in section 1009;
- c. Scientific, as defined in section 1009;
- d. Philanthropic, as defined in section 1009;
- e. Agricultural, as defined in section 1009;
- f. Labor, as defined in section 1009;
- g. Veterans', as defined in section 1009;
- h. Fraternal, as defined in section 1009;
- i. Qualified political committees; or
- j. State or local voting registration officials when making a mailing required or authorized by the National Voter Registration Act of 1993.

Eligibility for Nonprofit Regular subclass rate categories is based on the size or mail processing shape of the mailpiece as specified by the Postal Service. Mail processing shapes include letter-size mail, flat-size mail, parcels and not flat-machinable (NFM) mail.

323.11 Qualified Political Committees. The term "qualified political committee" means a national or State committee of a political party, the Republican and Democratic Senatorial Campaign Committees, the Democratic National Congressional Committee, and the National Republican Congressional Committee:

- a. The term "national committee" means the organization which, by virtue of the bylaws of a political party, is responsible for the day-to-day operation of such political party at the national level; and
- b. The term "State committee" means the organization which, by virtue of the bylaws of a political party, is responsible for the day-to-day operation of such political party at the State level.

323.12 Limitation on Authorization. An organization authorized to mail at the nonprofit Standard rates for qualified nonprofit organizations may mail only its own matter at these rates. An organization may not delegate or lend the use of its permit to mail at nonprofit Standard rates to any other person, organization or association.

323.2 [Presort] Nonautomation Rate Categories

323.21 General. The [presort] nonautomation rate categories apply to Nonprofit Regular subclass mail that:

- a. Is prepared in a mailing of at least 200 addressed pieces or 50 pounds of addressed pieces;
- b. Is presorted, marked, and presented as specified by the Postal Service; [and]
- c. Meets the machinability, addressing, and other preparation requirements specified by the Postal Service[.]; and
- d. Is not entered as Customized Market Mail under section 323.5.

[323.22 Basic Rate Categories. The basic rate categories apply to presort rate category mail not mailed under section 322.23, and to all mail entered as Customized Market Mail, as defined in section 321.22.]

[323.23 Three- and Five-Digit Rate Categories. The three- and five-digit rate categories apply to presort rate category mail presorted to single or multiple

three- and five-digit ZIP Code destinations as specified by the Postal Service.]

323.22 **Mixed AADC Rate Category.** The Mixed AADC rate category applies to nonautomation rate category letter-size mail that meets machinability criteria specified by the Postal Service and that is not mailed under section 323.23.

323.23 **AADC Rate Category.** The AADC rate category applies to letter-size nonautomation rate category mail that meets machinability criteria specified by the Postal Service and that has been presorted to automated area distribution center destinations as specified by the Postal Service.

323.24 **Mixed ADC Rate Categories.** The Mixed ADC rate categories apply to nonautomation rate category mail not mailed under sections 323.22, 323.23, 323.25, 323.26, 323.27, 323.28 or 323.29.

323.25 **ADC Rate Categories.** The ADC rate categories apply to nonautomation rate category mail that has been presorted to area distribution center destinations as specified by the Postal Service.

323.26 **Three-Digit Rate Categories.** The three-digit rate categories apply to nonautomation rate category mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

323.27 **Five-Digit Rate Categories.** The five-digit rate categories apply to nonautomation rate category mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.

323.28 **Mixed BMC Rate Category.** The Mixed BMC rate category applies to parcel-shaped nonautomation rate category mail that meets machinability criteria specified by the Postal Service and that is not mailed under section 323.29.

323.29 **BMC Rate Category.** The BMC rate category applies to parcel-shaped nonautomation rate category mail that meets machinability criteria specified by the Postal Service and that has been presorted to bulk mail center (or equivalent facility) destinations as specified by the Postal Service.

323.3 **Automation Rate Categories**

323.31 **General.** The automation rate categories apply to Nonprofit Regular subclass mail that:

- a. Is presorted, marked, and presented as specified by the Postal Service;
- b. Bears a barcode representing not more than 11 digits (not including “correction” digits) as specified by the Postal Service; and
- c. Meets the machinability, addressing, barcoding, and other preparation requirements specified by the Postal Service.

- 323.32 Mixed AADC Rate Category.** The Mixed AADC rate category applies to letter-size automation rate category mail not mailed under section 323.33, 323.34, or 323.35.
- 323.33 AADC Rate Category.** The AADC rate category applies to letter-size automation rate category mail presorted to automated area distribution center destinations as specified by the Postal Service.
- 323.34 Three-Digit Barcoded Rate [Category] Categories.** The three-digit barcoded rate [category applies] categories apply to letter-size or flat-size automation rate category mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.
- 323.35 Five-Digit Barcoded Rate [Category] Categories.** The five-digit barcoded rate [category applies] categories apply to letter-size or flat-size automation rate category mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.
- 323.36 [Basic Barcoded Flats] Mixed ADC Rate Category.** The [basic barcoded flats] Mixed ADC rate category applies to flat-size automation rate category mail not mailed under section 323.37.
- 323.37 [Three- and Five-Digit Barcoded Flats] ADC Rate Category.** The [three- and five-digit barcoded flats] ADC rate category applies to flat-size automation rate category mail presorted to [single or multiple three- and five-digit ZIP Code] area distribution center destinations as specified by the Postal Service.
- 323.4 Destination Entry Discounts.** Destination entry discounts apply to Nonprofit Regular subclass mail, except [Nonprofit Presort category] mail entered as Customized Market Mail under section 323.[22]5, prepared as specified by the Postal Service and addressed for delivery within the service area of the BMC (or auxiliary service facility), [or] sectional center facility (SCF), or destination delivery unit (DDU) at which it is entered, as defined by the Postal Service.

[323.5 Residual Shape Surcharge. Nonprofit subclass mail is subject to a surcharge if it is entered as Customized Market Mail under section 323.22 or is prepared as a parcel or if it is not letter or flat shaped.]

323.5 Customized Market Mail (CMM). Nonprofit Regular subclass mail may be entered as CMM as defined in section 321.5.

323.6 [Barcode Discount] Non-barcoded Surcharge. [The barcode discount applies to Nonprofit subclass mail, except Nonprofit Presort category mail entered as Customized Market Mail under section 323.22, that is subject to the residual shape surcharge in 323.5, is entered at designated facilities, bears a barcode specified by the Postal Service, is prepared as specified by the Postal Service and meets all other preparation and machinability requirements of the Postal Service.] Nonprofit Regular nonautomation mailpieces not qualifying for letter-size or flat-size rate categories and that do not bear a barcode specified by the Postal Service are subject to a Non-barcoded Surcharge. The surcharge will not apply to pieces sorted to 5-digit ZIP Codes.

323.7 Nonmachinable [Surcharge] Rate Categories. The nonmachinable [surcharge applies] rate categories apply to Nonprofit [presort] Regular nonautomation category letter-size[d] pieces and pieces to which the parcel rate categories apply, [except Nonprofit Presort category mail entered as Customized Market Mail under section 323.22,] [(i) that do not meet the machinability requirements specified by the Postal Service ; or (ii) for which manual processing is requested].

323.8 Repositionable Notes. Repositionable Notes may be attached to the exterior of letter-size or flat-size Nonprofit Regular subclass mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 6 to Rate Schedule 323A or note 4 to Rate Schedule 323B.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such request.

- b. If the Postal Service determines not to file such request, this provision expires on such date as specified by the Postal Service, but no later than April 3, 2007.

323.9 **Standard Mail Forwarding.** As described in section 353, undeliverable-as-addressed Standard Mail Nonprofit Regular subclass mail that is forwarded on request of the mailer is charged the appropriate rate shown in note 4 to Rate Schedule 323A or note 5 to Rate Schedule 323B. Mail for which Standard Mail Forwarding is purchased must meet preparation requirements and bear endorsements as specified by the Postal Service. Payment for Standard Mail Forwarding is made through an advance deposit account, or as specified by the Postal Service.

324 Nonprofit Enhanced Carrier Route Subclass

324.1 Definition. The Nonprofit Enhanced Carrier Route subclass consists of Standard Mail [[]weighing less than 16 ounces[]] that is not mailed under section 321, 322, or 323, that is mailed by authorized nonprofit organizations or associations (as defined in section 323) under the terms and limitations stated in section 323.12, and that:

- a. Is prepared in a mailing of at least 200 addressed pieces or 50 pounds of addressed pieces;
- b. Is prepared, marked, and presented as specified by the Postal Service;
- c. Is presorted to carrier routes as specified by the Postal Service;
- d. Is sequenced as specified by the Postal Service;
- e. Meets the machinability, addressing, and other preparation requirements specified by the Postal Service; and
- f. For high-density and saturation letters, bears a barcode representing not more than 11 digits (not including “correction” digits) as specified by the Postal Service.

Eligibility for Nonprofit Enhanced Carrier Route subclass rate categories is based on the size or mail processing shape of the mailpiece as specified by the Postal Service. Mail processing shapes include letter-size mail, flat-size mail, parcels and not flat-machinable (NFM) mail.

- 324.2 Basic Rate Category.** The basic rate category applies to Nonprofit Enhanced Carrier Route subclass mail not mailed under section 324.3[,] or 324.4 [, or 324.5].
- [324.3 Basic Pre-Barcoded Rate Category.** The basic pre-barcoded rate category applies to letter-size Nonprofit Enhanced Carrier Route subclass mail which bears a barcode representing not more than 11 digits (not including “correction” digits), as specified by the Postal Service, and which meets the machinability, addressing, and barcoding specifications and other preparation requirements specified by the Postal Service.]
- 324.[4]3 High Density Rate Category.** The high density rate category applies to Nonprofit Enhanced Carrier Route subclass mail presented in walk-sequence order and meeting the high density requirements specified by the Postal Service. High density rate category letters must meet the applicable automation requirements specified by the Postal Service, and must bear a barcode representing not more than 11 digits (not including “correction” digits), as specified by the Postal Service.
- 324.[5]4 Saturation Rate Category.** The saturation rate category applies to Nonprofit Enhanced Carrier Route subclass mail presented in walk-sequence order and meeting the saturation requirements specified by the Postal Service. Saturation rate category letters must meet the applicable automation requirements specified by the Postal Service, and must bear a barcode representing not more than 11 digits (not including “correction” digits), as specified by the Postal Service.
- 324.[6]5 Destination Entry Discounts.** Destination entry discounts apply to Nonprofit Enhanced Carrier Route subclass mail prepared as specified by the Postal Service and addressed for delivery within the service area of the BMC (or auxiliary service facility), sectional center facility (SCF), or destination delivery unit (DDU) at which it is entered, as defined by the Postal Service. Letter-size mail is not eligible for the DDU discount.
- 324.6 DAL Surcharge.** Flat-shaped and parcel-shaped Nonprofit Enhanced Carrier Route subclass mail are subject to a per-piece surcharge if they are addressed using a detached address label (DAL).
- [324.7 Residual Shape Surcharge.** Nonprofit Enhanced Carrier Route subclass mail is subject to a surcharge if it is prepared as a parcel or if it is not letter or flat shaped.]

324.7 **Standard Mail Forwarding.** As described in section 353, undeliverable-as-addressed Standard Mail Nonprofit Enhanced Carrier Route subclass mail that is forwarded on request of the mailer is charged the appropriate rate shown in note 8 to Rate Schedule 324. Mail for which Standard Mail Forwarding is purchased must meet preparation requirements and bear endorsements as specified by the Postal Service. Payment for Standard Mail Forwarding is made through an advance deposit account, or as specified by the Postal Service.

324.8 **Repositionable Notes.** Repositionable Notes may be attached to the exterior of letter-size or flat-size Nonprofit Enhanced Carrier Route subclass mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 6 to Rate Schedule 324.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such request.
- b. If the Postal Service determines not to file such request, this provision expires on such date as specified by the Postal Service, but no later than April 3, 2007.

330 PHYSICAL LIMITATIONS

331 Size

Standard Mail may not exceed 108 inches in length and girth combined. Additional size limitations apply to individual rate categories. The maximum size for mail in the Enhanced Carrier Route and Nonprofit Enhanced Carrier Route subclasses is [14 inches in length, 11.75 inches in width, and 0.75 inch in thickness] the same as the maximum size for flat-size mail in the Regular and Nonprofit Regular subclasses, except that merchandise samples mailed with detached address [cards] labels, prepared as specified by the Postal Service, may exceed those dimensions.

332 Weight

Standard Mail may not weigh more than 16 ounces.

340 POSTAGE AND PREPARATION

341 Postage

Postage must be paid as set forth in section 3000. When the postage is higher than the rate prescribed in any of the Package Services subclasses for which the piece also qualifies, the piece is eligible for the applicable lower rate. All mail mailed at a bulk or presort rate must have postage paid in a manner not requiring cancellation.

342 Preparation

All pieces in a Standard mailing must be separately addressed. All pieces in a Standard mailing must be identified as specified by the Postal Service, and must contain the ZIP Code of the addressee when specified by the Postal Service. All Standard mailings must be prepared and presented as specified by the Postal Service. Two or more Standard mailings may be commingled and mailed only when specific methods approved by the Postal Service for determining and verifying postage are followed.

343 Non-Identical Pieces

Pieces not identical in size and weight may be mailed at a bulk or presort rate as part of the same mailing only when specific methods approved by the Postal Service for determining and verifying postage are followed.

344 Attachments and Enclosures

344.1 General. First-Class Mail may be attached to or enclosed in Standard Mail, except Regular and Nonprofit [Presort] Regular subclass category mail entered as Customized Market Mail under sections 321.[22] 5 and 323.[22] 5. The piece must be marked as specified by the Postal Service. Except as provided in section 344.2, additional postage must be paid for the attachment or enclosure as if it had been mailed separately. Otherwise, the entire combined piece is subject to the First-Class rate for which it qualifies.

344.2 Incidental First-Class Attachments and Enclosures. First-Class Mail, as defined in subsections b through d of section 210, may be attached to or enclosed with Standard Mail containing merchandise, including books, but excluding merchandise samples, with postage paid on the combined piece at the applicable Standard rate, if the attachment or enclosure is incidental to the piece to which it is attached or with which it is enclosed.

350 DEPOSIT AND DELIVERY**351 Deposit**

Standard Mail must be deposited at places and times designated by the Postal Service.

352 Service

Standard Mail may receive deferred service.

353 Forwarding and Return

Undeliverable-as-addressed Standard Mail, except Regular and Nonprofit [Presort category] Regular subclass mail entered as Customized Market Mail under sections 321.[22]5 and 323.[22]5, will be returned on request of the mailer, or forwarded and returned on request of the mailer.

Undeliverable-as-addressed combined First-Class and Standard Mail pieces will be returned as specified by the Postal Service. Except as provided in section 935, the applicable First-Class Mail rate is charged for each piece receiving return only service. Except as provided in sections 935 and 936, charges for forwarding-and-return service are assessed [only on those pieces which cannot be forwarded and are returned. Except as provided in sections 935 and 936, the charge for those returned pieces is the appropriate First-Class Mail rate for the piece plus that rate multiplied by a factor equal to the number of Standard Mail pieces nationwide that are successfully forwarded for every one piece that cannot be forwarded and must be returned.] as follows:

- a. If used in conjunction with Address Correction Service (automated or electronic),
 - i. Returned pieces are charged the appropriate First-Class Mail rate.
 - ii. Forwarded pieces are charged as described in section 321.9, 322.7, 323.9, or 324.7.
- b. If used in conjunction with Address Correction Service (manual), or if no Address Correction Service requested,
 - i. Returned pieces are charged the appropriate First-Class Mail rate for the piece plus the rate multiplied by a factor equal to the number of Standard Mail pieces successfully forwarded (using this method

of payment) for every one piece that cannot be forwarded and must be returned.

360 ANCILLARY SERVICES

361 All Subclasses

All Standard Mail, except Regular and Nonprofit [Presort category] Regular subclass mail entered as Customized Market Mail under sections 321.[22]5 and 323.[22]5, will receive the following services upon payment of the appropriate fees:

Service	Schedule
a. Address correction	911
b. Certificates of mailing indicating that a specified number of pieces have been mailed	947

Certificates of mailing are not available for Standard Mail when postage is paid with permit imprint.

362 Regular and Nonprofit Regular

362.1 Regular and Nonprofit Regular subclass mail, except Regular and Nonprofit [Presort category] Regular subclass mail entered as Customized Market Mail under sections 321.[22]5 and 323.[22]5, will receive the following additional services upon payment of the appropriate fees.

Service	Schedule
a. Bulk Parcel Return Service	935
b. Shipper-Paid Forwarding	936

362.2 Regular and Nonprofit Regular subclass mail [subject to the residual shape surcharge in 321.5 and 323.6] to which the parcels or not flat-machinable (NFM) rate categories apply, [respectively, except Regular and Nonprofit Presort category mail entered as Customized Market Mail under sections

321.22 and 323.22,] will receive the following additional services upon payment of the appropriate fees.

Parcel Service	Schedule
a. Bulk Insurance	943
b. Return Receipt (merchandise only)	945
c. Delivery Confirmation	948
NFM Service	Schedule
a. Delivery Confirmation	948

Bulk Insurance may not be used selectively for individual pieces in a multi-piece Standard Mail mailing unless specific methods approved by the Postal Service for determining and verifying postage are followed.

370 RATES AND FEES

The rates and fees for Standard Mail are set forth as follows:

	Schedule
a. Regular subclass	
[Presort] <u>Nonautomation</u> categor[y] <u>ies</u>	321A
Automation categor[y] <u>ies</u>	321B
b. Enhanced Carrier Route subclass	322
c. Nonprofit <u>Regular</u> subclass	
[Presort] <u>Nonautomation</u> categor[y] <u>ies</u>	323A
Automation categor[y] <u>ies</u>	323B
d. Nonprofit Enhanced Carrier Route subclass	324
e. Fees	1000

380 AUTHORIZATIONS AND LICENSES

The mailing fee set forth in Schedule 1000 must be paid once each year at each office of mailing or office of verification, as specified by the Postal Service, by or for mailers of Standard Mail. Payment of the fee allows the mailer to mail at any Standard Mail rate.

**PERIODICALS
CLASSIFICATION SCHEDULE**

410 DEFINITION

411 General Requirements

411.1 Definition. A publication may qualify for mailing under the Periodicals Classification Schedule if it meets all the requirements in sections 411.2 through 411.5 and the requirements for one of the qualification categories in sections 412 through 415. Eligibility for specific Periodicals rates is prescribed in section 420.

411.2 Periodicals. Periodicals class mail is mailable matter consisting of newspapers and other periodical publications. The term "periodical publications" includes, but is not limited to:

- a. Any catalog or other course listing including mail announcements of legal texts which are part of post-bar admission education issued by any institution of higher education or by a nonprofit organization engaged in continuing legal education; and
- b. Any looseleaf page or report (including any index, instruction for filing, table, or sectional identifier which is an integral part of such report) which is designed as part of a looseleaf reporting service concerning developments in the law or public policy.

411.3 Issuance

411.31 Regular Issuance. Periodicals class mail must be regularly issued at stated intervals at least four times a year, bear a date of issue, and be numbered consecutively.

411.32 Separate Publication. For purposes of determining Periodicals rate eligibility, an "issue" of a newspaper or other periodical shall be deemed to be a separate publication when the following conditions exist:

- a. The issue is published at a regular frequency more often than once a month either on (1) the same day as another regular issue of the same publication; or (2) on a day different from regular issues of the same publication;

- b. More than 10 percent of the total number of copies of the issue is distributed on a regular basis to recipients who do not subscribe to it or request it; and
- c. The number of copies of the issue distributed to nonsubscribers or nonrequesters is more than twice the number of copies of any other issue distributed to nonsubscribers or nonrequesters on that same day, or, if no other issue that day, any other issue distributed during the same period. "During the same period" shall be defined as the periods of time ensuing between the distribution of each of the issues whose eligibility is being examined. Such separate publications must independently meet the qualifications for Periodicals eligibility.

411.4 Office of Publication. Periodicals class mail must have a known office of publication. A known office of publication is a public office where business of the publication is transacted during the usual business hours. The office must be maintained where the publication is authorized original entry.

411.5 Printed Sheets. Periodicals class mail must be formed of printed sheets. It may not be reproduced by stencil, mimeograph, or hectograph processes, or reproduced in imitation of typewriting. Reproduction by any other printing process is permissible. Any style of type may be used.

412 General Publications

412.1 Definition. To qualify as a General Publication, Periodicals class mail must meet the requirements in section 411 and in sections 412.2 through 412.4.

412.2 Dissemination of Information. A General Publication must be originated and published for the purpose of disseminating information of a public character, or devoted to literature, the sciences, art, or some special industry.

412.3 Paid Circulation

412.31 Total Distribution. A General Publication must be designed primarily for paid circulation. At least 50 percent or more of the copies of the publication must be distributed to persons who have paid above a nominal rate.

412.32 List of Subscribers. A General Publication must be distributed to a legitimate list of persons who have subscribed by paying or promising to pay at a rate above nominal for copies to be received during a stated time.

Copies mailed to persons who are not on a legitimate list of subscribers are nonsubscriber copies.

412.33 Nominal Rates. As used in section 412.31, nominal rate means:

- a. A token subscription price that is so low that it cannot be considered a material consideration; and
- b. A reduction to the subscriber, under a premium offer or any other arrangements, of more than 70 percent of the amount charged at the basic annual rate for a subscriber to receive one copy of each issue published during the subscription period. The value of a premium is considered to be its actual cost to the publishers, the recognized retail value, or the represented value, whichever is highest.

412.34 Nonsubscriber Copies

412.341 Up to Ten Percent. Nonsubscriber copies, including sample and complimentary copies, mailed at any time during the calendar year up to and including 10 percent of the total number of copies mailed to subscribers during the calendar year are mailable at the rates that apply to subscriber copies provided that the nonsubscriber copies would have been eligible for those rates if mailed to subscribers.

412.342 Over Ten Percent. Nonsubscriber copies, including sample and complimentary copies, mailed at any time during the calendar year, in excess of 10 percent of the total number of copies mailed to subscribers during the calendar year which are presorted and commingled with subscriber copies are charged the applicable rates for Outside County Periodicals, but are not eligible for preferred rate discounts. The 10 percent limitation for a publication is based on the total number of all copies of that publication mailed to subscribers during the calendar year.

412.35 Advertiser's Proof Copies. One complete copy of each issue of a General Publication may be mailed to each advertiser in that issue as an advertiser's proof copy at the rates that apply to subscriber copies, whether the advertiser's proof copy is mailed to the advertiser directly or, instead, to an advertising representative or agent of the publication. These copies count as subscriber copies.

412.36 Expired Subscriptions. For six months after a subscription has expired, copies of a General Publication may be mailed to a former subscriber at the rates that apply to copies mailed to subscribers, if the publisher has

attempted during that six months to obtain payment, or a promise to pay, for renewal. These copies do not count as subscriber copies.

412.4 Advertising Purposes

A General Publication may not be designed primarily for advertising purposes. A publication is "designed primarily for advertising purposes" if it:

- a. Has advertising in excess of 75 percent in more than one-half of its issues during any 12-month period;
- b. Is owned or controlled by individuals or business concerns and conducted as an auxiliary to and essentially for the advancement of the main business or calling of those who own or control it;
- c. Consists principally of advertising and editorial write-ups of the advertisers;
- d. Consists principally of advertising and has only a token list of subscribers, the circulation being mainly free;
- e. Has only a token list of subscribers and prints advertisements free for advertisers who pay for copies to be sent to a list of persons furnished by the advertisers; or
- f. Is published under a license from individuals or institutions and features other businesses of the licensor.

413 Requester Publications

413.1 Definition. A publication which is circulated free or mainly free may qualify for Periodicals class as a Requester Publication if it meets the requirements in sections 411, and 413.2 through 413.4.

413.2 Minimum Pages. It must contain at least 24 pages.

413.3 Advertising Purposes

413.31 Advertising Percentage. It must devote at least 25 percent of its pages to nonadvertising and not more than 75 percent to advertisements.

- 413.32 Ownership and Control.** It must not be owned or controlled by one or more individuals or business concerns and conducted as an auxiliary to and essentially for the advancement of the main business or calling of those who own or control it.
- 413.4 Circulated to Requesters**
- 413.41 List of Requesters.** It must have a legitimate list of persons who request the publication, and 50 percent or more of the copies of the publication must be distributed to persons making such requests. Subscription copies paid for or promised to be paid for, including those at or below a nominal rate may be included in the determination of whether the 50 percent request requirement is met. Persons will not be deemed to have requested the publication if their request is induced by a premium offer or by receipt of material consideration, provided that mere receipt of the publication is not material consideration.
- 413.42 Nonrequester Copies**
- 413.421 Up to Ten Percent.** Nonrequester copies, including sample and complimentary copies, mailed at any time during the calendar year up to and including 10 percent of the total number of copies mailed to requesters during the calendar year are mailable at the rates that apply to requester copies provided that the nonrequester copies would have been eligible for those rates if mailed to requesters.
- 413.422 Over Ten Percent.** Nonrequester copies, including sample and complimentary copies, mailed at any time during the calendar year, in excess of 10 percent of the total number of copies mailed to requesters during the calendar year which are presorted and commingled with requester copies are charged the applicable rates for Outside County Periodicals, but are not eligible for preferred rate discounts. The 10 percent limitation for a publication is based on the total number of all copies of that publication mailed to requesters during the calendar year.
- 413.43 Advertiser's Proof Copies.** One complete copy of each issue of a Requester Publication may be mailed to each advertiser in that issue as an advertiser's proof copy at the rates that apply to requester copies, whether the advertiser's proof copy is mailed to the advertiser directly or, instead, to an advertising representative or agent of the publication. These copies count as requester copies.

414 Publications of Institutions and Societies

414.1 Publisher's Own Advertising. Except as provided in section 414.2, a publication which meets the requirements of sections 411 and 412.4, and which contains no advertising other than that of the publisher, qualifies for Periodicals class as a publication of an institution or society if it is:

- a. Published by a regularly incorporated institution of learning;
- b. Published by a regularly established state institution of learning supported in whole or in part by public taxation;
- c. A bulletin issued by a state board of health or a state industrial development agency;
- d. A bulletin issued by a state conservation or fish and game agency or department;
- e. A bulletin issued by a state board or department of public charities and corrections;
- f. Published by a public or nonprofit private elementary or secondary institution of learning or its administrative or governing body;
- g. Program announcements or guides published by an educational radio or television agency of a state or political subdivision thereof, or by a nonprofit educational radio or television station;
- h. Published by or under the auspices of a benevolent or fraternal society or order organized under the lodge system and having a bona fide membership of not less than 1,000 persons;
- i. Published by or under the auspices of a trade(s) union;
- j. Published by a strictly professional, literary, historical, or scientific society; or,
- k. Published by a church or church organization.

414.2 General Advertising. A publication published by an institution or society identified in sections 414.1 h through k, may contain advertising of other persons, institutions, or concerns, if the following additional conditions are met:

- a. The publication is originated and published to further the objectives and purposes of the society;
- b. Circulation is limited to:
 - i. Copies mailed to members who pay either as a part of their dues or assessment or otherwise, not less than 50 percent of the regular subscription price;
 - ii. Other actual subscribers; and
 - iii. Exchange copies.
- c. The circulation of nonsubscriber copies, including sample and complimentary copies, does not exceed 10 percent of the total number of copies referred to in 414.2b.

415 Publications of State Departments of Agriculture

A publication which is issued by a state department of agriculture and which meets the requirements of sections 411 qualifies for Periodicals class as a publication of a state department of agriculture if it contains no advertising and is published for the purpose of furthering the objects of the department.

416 Foreign Publications

Foreign newspapers and other periodicals of the same general character as domestic publications entered as Periodicals class mail may be accepted on application of the publishers thereof or their agents, for transmission through the mail at the same rates as if published in the United States. This section does not authorize the transmission through the mail of a publication which violates a copyright granted by the United States.

420 DESCRIPTION OF SUBCLASSES

421 Outside County Subclass

421.1 *Reserved*

421.11 **Definition.** The Outside County subclass consists of Periodicals class mail that is not mailed under section 423 and that:

- a. Is presorted, marked, and presented as specified by the Postal Service; and
- b. Meets machinability, addressing, and other preparation requirements specified by the Postal Service.

421.12 Description of structure. The Outside County rate structure consists of pound, piece, bundle, sack, and pallet elements. The rate associated with the pound element is comprised of two main components. One, applicable to advertising content, is a zoned rate. The other, applicable to nonadvertising (editorial) content, is uniform across all zones, but may be reduced by certain destination entry discounts. The rate associated with the piece element is subject to presorting, pre-barcoding and machinability distinctions. Piece rates are reduced by a discount for the percentage of editorial content. Bundle charges generally are determined by the presort level of the pieces in the bundle.

421.2 Outside County Pound Rates

An unzoned pound rate applies to the nonadvertising portion of Outside County subclass mail and may be reduced by applicable destination entry discounts. A zoned pound rate applies to the advertising portion and may be reduced by applicable destination entry discounts. The pound rate postage is the sum of the nonadvertising portion charge and the advertising portion charges.

421.3 Outside County Piece Rates

421.31 **Reserved. [Basic Rate Category.** The basic rate category applies to all Outside County subclass mail not mailed under section 421.32, 421.33, or 421.34.]

421.311 **Mixed ADC Rate Category.** The Mixed ADC rate category applies to all Outside County subclass mail not mailed under section 421.312, 431.32, 421.33, or 421.34.

421.312 **ADC Rate Category.** The Mixed ADC rate category applies to all Outside County subclass mail not mailed under section 421.311, 431.32, 421.33, or 421.34.

421.32 **Three-Digit Rate Category.** The three-digit rate category applies to Outside County subclass mail presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

- 421.33 Five-Digit Rate Category.** The five-digit rate category applies to Outside County subclass mail presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.
- 421.34 Carrier Route Rate Category.** The carrier route rate category applies to Outside County subclass mail presorted to carrier routes as specified by the Postal Service. Firm bundles are included in this category.
- 421.4 Outside County [Subclass] Piece Discounts**
- 421.41 Barcoded Letter Discounts.** Barcoded letter discounts apply to letter size Outside County subclass mail mailed under sections [421.31] 421.311, 421.312, 421.32, and 421.33 which bears a barcode representing not more than 11 digits (not including "correction" digits) as specified by the Postal Service, and which meets the machinability, addressing, and barcoding specifications and other preparation requirements specified by the Postal Service.
- 421.42 Barcoded Flats Discounts.** Barcoded flats discounts apply to flat size Outside County subclass mail mailed under sections [421.31] 421.311, 421.312, 421.32, and 421.33 which bear a barcode representing not more than 11 digits (not including "correction" digits) as specified by the Postal Service, and meet the flats machinability, addressing, and barcoding specifications and other preparation requirements specified by the Postal Service.
- 421.43 High Density Discount.** The high density discount applies to Outside County subclass mail mailed under section 421.34, presented in walk sequence order, and meeting the high density and preparation requirements specified by the Postal Service.
- 421.44 Saturation Discount.** The saturation discount applies to Outside County subclass mail mailed under section 421.34, presented in walk-sequence order, and meeting the saturation and preparation requirements specified by the Postal Service.
- 421.45 Reserved. [Destination Entry Discounts.** Destination entry discounts apply to Outside County subclass mail which is prepared as specified by the Postal Service and addressed for delivery within the service area of the destination area distribution center (ADC), destination sectional center facility (SCF) or the destination delivery unit (DDU) at which it is entered, as defined by the Postal Service. The DDU discount only applies to Carrier Route rate category mail.]

- 421.46 Nonadvertising Discount.** The nonadvertising discount applies to all Outside County subclass mail and is determined by multiplying the proportion of nonadvertising content by the discount factor set forth in Rate Schedule 421 and subtracting that amount from the applicable piece rate.
- 421.47 Preferred Rate Discount.** Periodicals Mail qualifying as Nonprofit or Classroom mail under sections 422.2 and 422.3 is eligible for the Preferred rate discount set forth in Rate Schedule 421.
- 421.48 Reserved. [Pallet Discount.** The pallet discount applies to Outside Country subclass nonletter mail that is presented on pallets and meets the preparation requirements specified by the Postal Service.]
- 421.49 Reserved. [Dropship Pallet Discount.** The dropship pallet discount applies to Outside County subclass nonletter mail under section 421.45, that is presented on pallets and meets the preparation requirements specified by the Postal Service.]
- 421.50 Reserved. [Co-palletization Dropship Discounts.** Either a per-piece or a per-pound co-palletization dropship discount (but not both) applies to Outside County subclass nonletter mail qualifying under section 421.49, that is presented on sectional center facility (SCF) or area distribution center (ADC) pallets containing more than one publication, as specified by the Postal Service. The discount is limited to those pieces which could not be prepared on a qualifying pallet under section 421.48 or 421.49, if the mail had been prepared without such combining. The per-pound discounts apply only to editorial pounds, and are also limited to publications that weigh 9 ounces or more, which contain no more than 15 percent advertising matter, and which have a mailed circulation of no more than 75,000 copies per issue. A participating mailer or consolidator must provide pre-consolidation and post-consolidation documentation for all qualifying pieces, as specified by the Postal Service. This section expires the later of:
- a. October 3, 2006, or
 - b. if, by the expiration date specified in (a), a proposal for a permanent replacement for the co-palletization dropship discounts is pending before the Postal Rate Commission:
 - i. three months after the Commission takes action on such request under 39 U.S.C. § 3624 or, if applicable,

- ii. on the implementation date for a permanent replacement for the co-palletization dropship discounts.]

421.51 **Machinability Discounts.** Machinability discounts apply to Outside County subclass mail mailed under sections 421.311, 421.312, 421.32, and 421.33 which meet machinability, addressing, and barcoding specifications and other preparation requirements specified by the Postal Service.

421.6 **Outside County Bundle Rates (For Bundles in Sacks or on Pallets)**

421.61 **Bundles in Mixed ADC Sacks**

421.611 Mixed ADC Bundle rate. The Mixed ADC bundle rate applies to all Outside County subclass mail bundles mailed under section 421.61 which contain pieces presorted to Mixed ADC and meeting preparation requirements as specified by the Postal Service.

421.612 ADC Bundle rate. The ADC bundle rate applies to all Outside County subclass mail bundles mailed under section 421.61 which contain pieces presorted to ADC and meeting preparation requirements as specified by the Postal Service.

421.613 Three-Digit/SCF Bundle rate. The three-digit/SCF bundle rate applies to all Outside County subclass mail bundles mailed under section 421.61 which contain pieces presorted to three-digit/SCF and meeting preparation requirements as specified by the Postal Service.

421.614 Five-Digit Bundle rate. The five-digit bundle rate applies to all Outside County subclass mail bundles mailed under section 421.61 which contain pieces presorted to five-digit and meeting preparation requirements as specified by the Postal Service.

421.615 Firm Bundle rate. The firm bundle rate applies to all Outside County subclass mail bundles mailed under section 421.61 which contain firm pieces and meeting preparation requirements as specified by the Postal Service.

421.62 **Bundles in ADC Sacks or on ADC Pallets**

421.621 ADC Bundle rate. The ADC bundle rate applies to all Outside County subclass mail bundles mailed under section 421.62 which contain pieces presorted to ADC and meeting preparation requirements as specified by the Postal Service.

- 421.622** Three-Digit/SCF Bundle rate. The three-digit/SCF bundle rate applies to all Outside County subclass mail bundles mailed under section 421.62 which contain pieces presorted to three-digit/SCF and meeting preparation requirements as specified by the Postal Service.
- 421.623** Five-Digit Bundle rate. The five-digit bundle rate applies to all Outside County subclass mail bundles mailed under section 421.62 which contain pieces presorted to five-digit and meeting preparation requirements as specified by the Postal Service.
- 421.624** Carrier Route Bundle rate. The carrier route bundle rate applies to all Outside County subclass mail bundles mailed under section 421.62 which contain pieces presorted to carrier route and meeting preparation requirements as specified by the Postal Service.
- 421.625** Firm Bundle rate. The firm bundle rate applies to all Outside County subclass mail firm bundles mailed under section 421.62 and meeting preparation requirements as specified by the Postal Service.
- 421.63** **Bundles in Three-Digit/SCF Sacks or on Three-Digit/SCF Pallets**
- 421.631** Three-Digit/SCF Bundle rate. The three-digit/SCF bundle rate applies to all Outside County subclass mail bundles mailed under section 421.63 which contain pieces presorted to three-digit/SCF and meeting preparation requirements as specified by the Postal Service.
- 421.632** Five-Digit Bundle rate. The five-digit bundle rate applies to all Outside County subclass mail bundles mailed under section 421.63 which contain pieces presorted to five-digit and meeting preparation requirements as specified by the Postal Service.
- 421.633** Carrier Route Bundle rate. The carrier route bundle rate applies to all Outside County subclass mail bundles mailed under section 421.63 which contain pieces presorted to carrier route and meeting preparation requirements as specified by the Postal Service.
- 421.634** Firm Bundle rate. The firm bundle rate applies to all Outside County subclass mail firm bundles mailed under section 421.63 and meeting preparation requirements as specified by the Postal Service.

421.64 Bundles in Five-Digit Sacks or on Five-Digit Pallets

421.641 Five-Digit Bundle rate. The five-digit bundle rate applies to all Outside County subclass mail bundles mailed under section 421.64 which contain pieces presorted to five-digit and meeting preparation requirements as specified by the Postal Service.

421.642 Carrier Route Bundle rate. The carrier route bundle rate applies to all Outside County subclass mail bundles mailed under section 421.64 which contain pieces presorted to carrier route and meeting preparation requirements as specified by the Postal Service.

421.643 Firm Bundle rate. The firm bundle rate applies to all Outside County subclass mail firm bundles mailed under section 421.64 and meeting preparation requirements as specified by the Postal Service.

421.7 Outside County Sack Rates

421.71 Outside County Mixed ADC Sack Rates

421.711 OSCF Sack Category. The OSCF sack category rate applies to Outside County subclass sacks mailed under section 421.71 and presented at OSCF as specified by the Postal Service.

421.712 OADC Category. The OADC sack category rate applies to Outside County subclass mail sacks mailed under section 421.71 and presented at OADC as specified by the Postal Service.

421.72 Outside County ADC Sack Rates

421.721 OSCF Sack Category. The OSCF sack category rate applies to Outside County subclass sacks mailed under section 421.72 and presented at OSCF as specified by the Postal Service.

421.722 OADC Sack Category. The OADC sack category rate applies to Outside County subclass mail sacks mailed under section 421.72 and presented at OADC as specified by the Postal Service.

421.723 OBMC Sack Category. The OBMC sack category rate applies to Outside County subclass mail sacks mailed under section 421.72 and presented at OBMC as specified by the Postal Service.

- 421.724** **DBMC Sack Category.** The DBMC sack category rate applies to Outside County subclass mail sacks mailed under section 421.72 and presented at DBMC as specified by the Postal Service.
- 421.725** **DADC Sack Category.** The DADC sack category rate applies to Outside County subclass mail sacks mailed under section 421.72 and presented at DADC as specified by the Postal Service.
- 421.73** **Outside County Three-Digit/SCF Sack Rates**
- 421.731** **OSCF Sack Category.** The OSCF sack category rate applies to Outside County subclass sacks mailed under section 421.73 and presented at OSCF as specified by the Postal Service.
- 421.732** **OADC Sack Category.** The OADC sack category rate applies to Outside County subclass mail sacks mailed under section 421.73 and presented at OADC as specified by the Postal Service.
- 421.733** **OBMC Sack Category.** The OBMC sack category rate applies to Outside County subclass mail sacks mailed under section 421.73 and presented at OBMC as specified by the Postal Service.
- 421.734** **DBMC Sack Category.** The DBMC sack category rate applies to Outside County subclass mail sacks mailed under section 421.73 and presented at DBMC as specified by the Postal Service.
- 421.735** **DADC Sack Category.** The DADC sack category rate applies to Outside County subclass mail sacks mailed under section 421.73 and presented at DADC as specified by the Postal Service.
- 421.736** **DSCF Sack Category.** The DSF sack category rate applies to Outside County subclass mail sacks mailed under section 421.73 and presented at DSCF as specified by the Postal Service.
- 421.74** **Outside County 5-Digit Sack Rates**
- 421.741** **OSCF Sack Category.** The OSCF sack category rate applies to Outside County subclass sacks mailed under section 421.74 and presented at OSCF as specified by the Postal Service.
- 421.742** **OADC Sack Category.** The OADC sack category rate applies to Outside County subclass mail sacks mailed under section 421.74 and presented at OADC as specified by the Postal Service.

- 421.743** **OBMC Sack Category.** The OBMC sack category rate applies to Outside County subclass mail sacks mailed under section 421.74 and presented at OBMC as specified by the Postal Service.
- 421.744** **DBMC Sack Category.** The DBMC sack category rate applies to Outside County subclass mail sacks mailed under section 421.74 and presented at DBMC as specified by the Postal Service.
- 421.745** **DADC Sack Category.** The DADC sack category rate applies to Outside County subclass mail sacks mailed under section 421.74 and presented at DADC as specified by the Postal Service.
- 421.746** **DSCF Sack Category.** The DSF sack category rate applies to Outside County subclass mail sacks mailed under section 421.74 and presented at DSCF as specified by the Postal Service.
- 421.747** **DDU Sack Category.** The DDU sack category rate applies to Outside County subclass mail sacks mailed under section 421.74 and presented at DDU as specified by the Postal Service.
- 421.8** **Outside County Pallet Rates**
- 421.81** **Outside County ADC Pallet Rates**
- 421.811** **OSCF Pallet Category.** The OSCF pallet category rate applies to Outside County subclass Pallets mailed under section 421.81 and presented at OSCF as specified by the Postal Service.
- 421.812** **OADC Pallet Category.** The OADC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.81 and presented at OADC as specified by the Postal Service.
- 421.813** **OBMC Pallet Category.** The OBMC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.81 and presented at OBMC as specified by the Postal Service.
- 421.814** **DBMC Pallet Category.** The DBMC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.81 and presented at DBMC as specified by the Postal Service.
- 421.815** **DADC Pallet Category.** The DADC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.81 and presented at DADC as specified by the Postal Service.

421.82 **Outside County Three-Digit/SCF Pallet Rates**

421.821 **OSCF Pallet Category.** The OSCF pallet category applies to Outside County subclass Pallets mailed under section 421.82 and presented at OSCF as specified by the Postal Service.

421.822 **OADC Pallet Category.** The OADC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.82 and presented at OADC as specified by the Postal Service.

421.823 **OBMC Pallet Category.** The OBMC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.82 and presented at OBMC as specified by the Postal Service.

421.824 **DBMC Pallet Category.** The DBMC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.82 and presented at DBMC as specified by the Postal Service.

421.825 **DADC Pallet Category.** The DADC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.82 and presented at DADC as specified by the Postal Service.

421.826 **DSCF Pallet Category.** The DSF pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.82 and presented at DSCF as specified by the Postal Service.

421.83 **Outside County Five-Digit Pallet Rates**

421.831 **OSCF Pallet Category.** The OSCF pallet category applies to Outside County subclass Pallets mailed under section 421.83 and presented at OSCF as specified by the Postal Service.

421.832 **OADC Pallet Category.** The OADC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.83 and presented at OADC as specified by the Postal Service.

421.833 **OBMC Pallet Category.** The OBMC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.83 and presented at OBMC as specified by the Postal Service.

421.834 **DBMC Pallet Category.** The DBMC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.83 and presented at DBMC as specified by the Postal Service.

421.835 **DADC Pallet Category.** The DADC pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.83 and presented at DADC as specified by the Postal Service.

421.836 **DSCF Pallet Category.** The DSF pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.83 and presented at DSCF as specified by the Postal Service.

421.837 **DDU Pallet Category.** The DDU pallet category rate applies to Outside County subclass mail Pallets mailed under section 421.83 and presented at DDU as specified by the Postal Service.

422 **Preferred Qualification Categories**

422.1 **Definition.** Preferred Qualification Outside County Subclass Periodicals consist of Periodicals Mail, other than publications qualifying as Requester Publications, that meets applicable requirements in sections 422.2, 422.3, or 422.4.

422.2 **Nonprofit**

The Periodicals Outside County Subclass Nonprofit category consists of publications entered by authorized nonprofit organizations or associations of the following types:

- a. Religious, as defined in section 1009;
- b. Educational, as defined in section 1009;
- c. Scientific, as defined in section 1009;
- d. Philanthropic, as defined in section 1009;
- e. Agricultural, as defined in section 1009;
- f. Labor, as defined in section 1009;
- g. Veterans', as defined in section 1009;
- h. Fraternal, as defined in section 1009; and
- i. Associations of rural electric cooperatives, and the publications of the following types:

- i. one publication, which contains no advertising (except advertising of the publisher) published by the official highway or development agency of a state,
- ii. program announcements or guides published by an educational radio or television agency of a state or political subdivision thereof or by a nonprofit educational radio or television station, or
- iii. one conservation publication published by an agency of a state which is responsible for management and conservation of the fish or wildlife resources of such state.

422.3 Classroom

The Periodicals Outside County Subclass Classroom rate category consists of religious, educational, or scientific publications designed specifically for use in school classrooms or religious instruction classes.

422.4 Science of Agriculture

422.41 Definition. Science of Agriculture mail consists of Periodicals class mail devoted to the science of agriculture if the total number of copies of the publication furnished during any 12-month period to subscribers residing in rural areas amounts to at least 70 percent of the total number of copies distributed by any means for any purpose.

422.42 Rates. Science of Agriculture mail is subject to pound rates, piece rates, piece rate discounts (except for the discount set forth in section 421.47), bundle rates, sack rates, and pallet rates, for Outside County [Subclass] Periodicals [M]ail, except for DDU, DSCF, DADC, and Zone 1 & 2 pound rates. Rates for Science of Agriculture are set forth in Rate Schedule 421.

422.43 Nonadvertising Discount. The nonadvertising discount for Outside County Subclass Periodicals Mail applies to Science of Agriculture Periodicals, and is determined by multiplying the proportion of nonadvertising content by the discount factor set forth in Rate Schedule 421 and subtracting that amount from the applicable piece rate.

422.44 Destination Entry Discounts. Destination entry discounts apply to Science of Agriculture Periodicals mail which is prepared as specified by the Postal Service, and addressed for delivery within the service area of the destination area distribution center (ADC), destination sectional center facility (SCF) or the destination delivery unit (DDU) at which it is entered, as

defined by the Postal Service. The DDU discount only applies to Carrier Route rate category mail.

423 Within County Subclass

423.1 *Reserved*

423.2 General

423.21 Definition. Within County mail consists of Periodicals class mail, other than publications qualifying as Requester Publications, mailed in, and addressed for delivery within, the county where published and originally entered, from either the office of original entry or additional entry. In addition, a Within County publication must meet one of the following conditions:

- a. The total paid circulation of the issue is less than 10,000 copies; or
- b. The number of paid copies of the issue distributed within the county of publication is at least one more than one-half the total paid circulation of such issue.

423.22 Entry in an Incorporated City. For the purpose of determining eligibility for Within County mail, when a publication has original entry at an independent incorporated city which is situated entirely within a county or which is contiguous to one or more counties in the same state, such incorporated city shall be considered to be within the county with which it is principally contiguous. Where more than one county is involved, the publisher will select the principal county.

423.23 Pound Rate. One pound rate applies to Within County pieces presorted to carrier routes to be delivered within the delivery area of the originating post office, and another pound rate applies to all other pieces.

423.3 Within County Piece Rates

423.31 Basic Rate Category. The basic rate category applies to Within County Periodicals not mailed under section 423.32, 423.33, or 423.34.

423.32 Three-Digit Rate Category. The three-digit rate category applies to Within County Periodicals that are presorted to single or multiple three-digit ZIP Code destinations as specified by the Postal Service.

- 423.33 Five-Digit Rate Category.** The five-digit rate category applies to Within County Periodicals presorted to single or multiple five-digit ZIP Code destinations as specified by the Postal Service.
- 423.34 Carrier Route Rate Category.** The carrier route rate category applies to Within County Periodicals presorted to carrier routes as specified by the Postal Service.
- 423.4 Within County Discounts**
- 423.41 Barcoded Letter Discounts.** Barcoded letter discounts apply to letter size Within County Periodicals mailed under sections 423.31, 423.32, and 423.33 which bear a barcode representing not more than 11 digits (not including “correction” digits) as specified by the Postal Service, and which meet the machinability, addressing, and barcoding specifications and other preparation requirements specified by the Postal Service.
- 423.42 Barcoded Flats Discounts.** Barcoded flats discounts apply to flat size Within County Periodicals mailed under sections 423.31, 423.32, and 423.33 which bear a barcode representing not more than 11 digits (not including “correction” digits) as specified by the Postal Service, and meet the flats machinability, addressing, and barcoding specifications and other preparation requirements specified by the Postal Service.
- 423.43 High Density Discount.** The high density discount applies to Within County Periodicals mailed under section 423.34, presented in walk sequence order, and meeting the high density and preparation requirements specified by the Postal Service. Alternatively, Within County mail may qualify for such discount also by presenting otherwise eligible mailings containing pieces addressed to a minimum of 25 percent of the addresses per carrier route.
- 423.44 Saturation Discount.** The saturation discount applies to Within County Periodicals mailed under section 423.34, presented in walk sequence order, and meeting the saturation and preparation requirements specified by the Postal Service.
- 423.45 Destination Entry Discount.** A destination delivery unit discount applies to Within County carrier route category mail which is destined for delivery within the destination delivery unit (DDU) in which it is entered, as defined by the Postal Service.

424 **Repositionable Notes.** Repositionable Notes may be attached to the exterior of letter-size and flat-size Periodicals mail, as specified by the Postal Service. The additional charge for the Repositionable Note is specified in note 8 to Rate Schedule 421 or note 3 to Rate Schedule 423.

This provision for Repositionable Notes expires as provided below.

- a. If a request to continue to test or make Repositionable Notes permanent is filed, this provision expires on the implementation date for the replacement service, or if no replacement is implemented, three months after the Commission takes action under section 3624 of title 39, on such request.
- b. If the Postal Service determines not to file such request, this provision expires on such date as specified by the Postal Service, but no later than April 3, 2007.

430 **PHYSICAL LIMITATIONS**

Periodicals Mail may not weigh more than 70 pounds or exceed 108 inches in length and girth combined. Additional size limitations apply to individual Periodicals rate categories.

440 **POSTAGE AND PREPARATION**

441 **Postage.** Postage must be paid on Periodicals class mail as set forth in section 3000.

442 **Presortation.** Periodicals class mail must be presorted as specified by the Postal Service.

443 **Attachments and Enclosures**

443.1 **General.** First-Class Mail or Standard Mail may be attached to or enclosed with Periodicals class mail. The piece must be marked as specified by the Postal Service. Except as provided in section 443.2, additional postage must be paid for the attachment or enclosure as if it had been mailed separately. Otherwise, the entire combined piece is subject to the appropriate First-Class Mail, Standard Mail, or Package Services rate for which it qualifies (unless the rate applicable to the host piece is higher), or, if a combined piece with a Standard Mail attachment or enclosure weighs 16 ounces or more, the piece is subject to the Parcel Post rate for which it qualifies.

443.1a **“Ride-Along” Attachments and Enclosures.** A limit of one Standard Mail piece, not exceeding the weight of the host copy and weighing a maximum of 3.3 ounces, from any of the subclasses listed in section 321 (Regular, Enhanced Carrier Route, Nonprofit or Nonprofit Enhanced Carrier Route) may be attached to or enclosed with an individual copy of Periodicals Mail for an additional postage payment. Periodicals containing “Ride-Along” attachments or enclosures must maintain uniform thickness as specified by the Postal Service. The Periodicals piece with the “Ride-Along” must maintain the same shape and automation compatibility as it had before addition of the “Ride-Along” attachment or enclosure and meet other preparation requirements as specified by the Postal Service.

443.2 **Incidental First-Class Mail Attachments and Enclosures.** First-Class Mail that meets one or more of the definitions in section 210 b through d may be attached to or enclosed with Periodicals class mail, with postage paid on the combined piece at the applicable Periodicals rate, if the attachment or enclosure is incidental to the piece to which it is attached or with which it is enclosed.

444 **Identification**

Periodicals class mail must be identified as required by the Postal Service. Nonsubscriber and nonrequester copies, including sample and complimentary copies, must be identified as required by the Postal Service.

445 **Filing of Information**

Information relating to Periodicals class mail must be filed with the Postal Service under 39 U.S.C. 3685.

446 **Enclosures and Supplements**

Periodicals class mail may contain enclosures and supplements as specified by the Postal Service. An enclosure or supplement may not contain writing, printing or sign thereof or therein, in addition to the original print, except as authorized by the Postal Service, or as authorized under section 443.2.

450 **DEPOSIT AND DELIVERY**

451 **Deposit**

Periodicals class mail must be deposited at places and times designated by the Postal Service.

452 Service

Periodicals class mail is given expeditious handling insofar as is practicable.

453 Forwarding and Return

Undeliverable-as-addressed Periodicals class mail will be forwarded or returned to the mailer, as specified by the Postal Service. Undeliverable-as-addressed combined First-Class and Periodicals class mail pieces will be forwarded or returned, as specified by the Postal Service. Additional charges when Periodicals class mail is returned will be based on the applicable First-Class Mail rate.

470 RATES AND FEES

The rates and fees for Periodicals class mail are set forth as follows:

	Schedule
a. Outside County	421
b. Within County	423
c. Science of Agriculture	421
d. Fees	1000

480 AUTHORIZATIONS AND LICENSES

481 Entry Authorizations

Prior to mailing at Periodicals rates, a publication must be authorized for entry as Periodicals class mail by the Postal Service. Each authorized publication will be granted one original entry authorization at the post office where the office of publication is maintained. An authorization for the establishment of an account to enter a publication at an additional entry office may be granted by the Postal Service upon application by the publisher. An application for re-entry must be made whenever the publisher proposes to change the publication's title, frequency of issue or office of original entry.

482 Nonprofit, Classroom and Science of Agriculture Authorization

Prior to entering Nonprofit, Classroom, and Science of Agriculture Periodicals Mail, a publication must obtain an additional Postal Service entry authorization to mail at those rates.

483 Mailing by Publishers and News Agents

Periodicals class mail may be mailed only by publishers or registered news agents. A news agent is a person or concern engaged in selling two or more Periodicals publications published by more than one publisher. News agents must register at all post offices at which they mail Periodicals class mail.

484 Fees

Fees for original entry, additional entry, re-entry, and registration of a news agent are set forth in Schedule 1000.

**PACKAGE SERVICES
CLASSIFICATION SCHEDULE**

510 DEFINITION

511 General

Any mailable matter may be mailed as Package Services mail except:

- a. Matter required to be mailed as First-Class Mail;
- b. Regular and Nonprofit Presort category mail entered as Customized Market Mail under sections 321.22 and 323.22; and
- c. Copies of a publication that is entered as Periodicals class mail, except:
 - i. copies sent by a printer to a publisher;
 - ii. copies that would have traveled at the former second-class transient rate. (The transient rate applied to individual copies of second-class mail (currently Periodicals class mail) forwarded and mailed by the public, as well as to certain sample copies mailed by publishers.); and
 - iii. sample copies enclosed or attached with merchandise sent at Parcel Post or Bound Printed Matter rates.

512 Written Additions

Package Services mail may have the following written additions placed on the wrapper, on a tag or label attached to the outside of the parcel, or inside the parcel, either loose or attached to the article:

- a. Marks, numbers, name, or letters descriptive of contents;
- b. "Please Do Not Open Until Christmas," or words of similar import;
- c. Instructions and directions for the use of an article in the package;
- d. Manuscript dedication or inscription not in the nature of personal correspondence;

- e. Marks to call attention to any word or passage in text;
- f. Corrections of typographical errors in printed matter;
- g. Manuscripts accompanying related proof sheets, and corrections in proof sheets to include: corrections of typographical and other errors, alterations of text, insertion of new text, marginal instructions to the printer, and rewrites of parts if necessary for correction;
- h. Handstamped imprints, except when the added matter is itself personal or converts the original matter to a personal communication; or
- i. An invoice.

520 DESCRIPTION OF SUBCLASSES

521 Parcel Post Subclass

521.1 Definition. The Parcel Post subclass consists of Package Services mail that is not mailed under sections 522, 523, or 524.

521.2 Description of Rate Categories

521.21 Inter-BMC Rate Category. The inter-BMC rate category applies to all Parcel Post subclass mail not mailed under sections 521.22, 521.23, 521.24, 521.25, 521.26, 521.27, or 521.28.

521.22 Intra-BMC Rate Category. The intra-BMC rate category applies to Parcel Post subclass mail originating and destinating within a designated BMC or auxiliary service facility service area, Alaska, Hawaii or Puerto Rico.

521.23 Parcel Select—Destination Bulk Mail Center (DBMC) Rate Category. The Parcel Select—DBMC rate category applies to Parcel Post subclass mail barcoded (unless nonmachinable as defined in section 521.7) and prepared as specified by the Postal Service in a mailing of at least 50 pieces entered at a designated destination BMC, auxiliary service facility, or other equivalent facility, as specified by the Postal Service.

521.24 Parcel Select—Destination Sectional Center Facility (DSCF) Rate Category. The Parcel Select—DSCF rate category applies to Parcel Post subclass mail prepared as specified by the Postal Service in a mailing of at least 50 pieces sorted to five-digit destination ZIP Codes as specified by the Postal Service (except as described in Section 521.25) and entered at a

designated destination processing and distribution center or facility, or other equivalent facility, as specified by the Postal Service.

- 521.25 Surcharge for Parcel Select—Destination Sectional Center Facility (DSCF) Rate Nonmachinable Parcels sorted to 3-digit Zip Codes.** The Parcel Select—DSCF Surcharge applies, in addition to the appropriate DSCF Parcel Select Rate, to mail that does not meet the machinability criteria specified by the Postal Service and is prepared in a mailing of at least 50 pieces sorted to three-digit destination ZIP Codes as specified by the Postal Service and entered at a designated destination processing and distribution center or facility, or other equivalent facility, as specified by the Postal Service.
- 521.26 Parcel Select—Destination Delivery Unit (DDU) Rate Category.** The Parcel Select—DDU rate category applies to Parcel Post subclass mail prepared as specified by the Postal Service in a mailing of at least 50 pieces, and entered at a designated destination delivery unit, or other equivalent facility, as specified by the Postal Service.
- 521.27 Parcel Select Return Service—Return Delivery Unit (RDU) Rate Category.** The Parcel Select Return Service—RDU rate category applies to merchandise returned as Parcel Post subclass mail barcoded and prepared as specified by the Postal Service; entered as specified by the Postal Service; and retrieved in bulk at a designated delivery unit, or other equivalent facility, as specified by the Postal Service.
- 521.28 Parcel Select Return Service—Return BMC (RBMC) Rate Category.** The Parcel Select Return Service—RBMC rate category applies to merchandise returned as Parcel Post subclass mail barcoded and prepared as specified by the Postal Service; entered as specified by the Postal Service; and retrieved in bulk at a bulk mail center, or other equivalent facility, as specified by the Postal Service.
- 521.3 Bulk Parcel Post.** Bulk Parcel Post mail is Parcel Post mail consisting of properly prepared and separated single mailings of at least 300 pieces or 2000 pounds. Pieces weighing less than 15 pounds and measuring over 84 inches in length and girth combined or pieces measuring over 108 inches in length and girth combined are not mailable as Bulk Parcel Post mail.
- 521.31 Barcode Discount.** The barcode discount applies to Bulk Parcel Post mail that is entered at designated facilities, bears a barcode specified by the Postal Service, is prepared as specified by the Postal Service, and meets all other preparation and machinability requirements of the Postal Service.

521.4 Bulk Mail Center (BMC) Presort Discounts

521.41 BMC Presort Discount. The BMC presort discount applies to Inter-BMC Parcel Post subclass mail that is prepared as specified by the Postal Service in a mailing of 50 or more pieces, entered at a facility authorized by the Postal Service, and sorted to destination BMCs, as specified by the Postal Service.

521.42 Origin Bulk Mail Center (OBMC) Discount. The origin bulk mail center discount applies to Inter-BMC Parcel Post subclass mail that is prepared as specified by the Postal Service in a mailing of at least 50 pieces, entered at the origin BMC, and sorted to destination BMCs, as specified by the Postal Service.

521.5 Barcode Discount. The barcode discount applies to Inter-BMC, Intra-BMC, and Parcel Select—DBMC Parcel Post subclass mail that is entered at designated facilities, bears a barcode specified by the Postal Service, is prepared as specified by the Postal Service in a mailing of at least 50 pieces, and meets all other preparation and machinability requirements of the Postal Service.

521.6 Oversize Parcel Post

521.61 Excessive Length and Girth. Parcel Post subclass mail pieces exceeding 108 inches in length and girth combined, but not greater than 130 inches in length and girth combined, are mailable.

521.62 Balloon Rate. Parcel Post subclass mail pieces exceeding 84 inches in length and girth combined and weighing less than [15] 20 pounds are subject to a rate equal to that for a [15] 20 pound parcel for the zone to which the parcel is addressed.

521.7 Nonmachinable Surcharges

- a. Inter-BMC, Intra-BMC, and Parcel Select—DBMC Parcel Post mail that does not meet machinability criteria specified by the Postal Service is subject to a nonmachinable surcharge.
- b. Parcel Select—DSCF Parcel Post mail that does not meet machinability criteria specified by the Postal Service, and which is sorted to three-digit destination ZIP Codes as specified by the Postal Service, is subject to a nonmachinability surcharge for 3-digit nonmachinable DSCF Parcel Post.

- c. Parcel Select Return Service—RBMC Parcel Post mail that does not meet machinability criteria specified by the Postal Service is subject to a nonmachinable surcharge.

521.8 Pickup Service. Pickup service is available for Parcel Post subclass mail under terms and conditions specified by the Postal Service.

522 Bound Printed Matter Subclass

522.1 Definition. The Bound Printed Matter subclass consists of Package Services mail weighing not more than 15 pounds, which:

- a. Consists of advertising, promotional, directory, or editorial material, or any combination thereof;
- b. Is securely bound by permanent fastenings including, but not limited to, staples, spiral bindings, glue, and stitching; loose leaf binders and similar fastenings are not considered permanent;
- c. Consists of sheets of which at least 90 percent are imprinted with letters, characters, figures or images or any combination of these, by any process other than handwriting or typewriting;
- d. Does not have the nature of personal correspondence; and
- e. Is not stationery, such as pads of blank printed forms.

522.2 Description of Rate Categories

522.21 Single-Piece Nonpresort Rate Category. The single-piece rate category applies to Bound Printed Matter subclass mail which is not mailed under sections [522.3 or 522.4] 522.22, 522.23, 522.24, 522.25, or 522.26.

522.22 Basic Presort Rate Category. The basic presort rate category applies to Bound Printed Matter subclass mail prepared in a mailing of at least 300 pieces, prepared and presorted as specified by the Postal Service.

522.23 Carrier Route Presort Rate Category. The carrier route presort rate category applies to Bound Printed Matter subclass mail prepared in a mailing of at least 300 pieces of carrier route presorted mail, prepared and presorted as specified by the Postal Service.

- 522.24 Destination Bulk Mail Center (DBMC) Rate Category.** The destination bulk mail center rate category applies to Basic Presort Rate or Carrier Route Presort Rate Bound Printed Matter subclass mail prepared as specified by the Postal Service in a mailing entered at a designated destination BMC, auxiliary service facility, or other equivalent facility, as specified by the Postal Service.
- 522.25 Destination Sectional Center Facility (DSCF) Rate Category.** The destination sectional center facility rate category applies to Basic Presort Rate or Carrier Route Presort Rate Bound Printed Matter subclass mail prepared [as specified by the Postal Service in a mailing sorted to five-digit destination ZIP Codes as specified by the Postal Service] and entered at a designated destination processing and distribution center or facility, or other equivalent facility, as specified by the Postal Service.
- 522.26 Destination Delivery Unit (DDU) Rate Category.** The destination delivery unit rate category applies to Basic Presort Rate or Carrier Route Presort Rate Bound Printed Matter subclass mail prepared as specified by the Postal Service in a mailing entered at a designated destination delivery unit, or other equivalent facility, as specified by the Postal Service.
- 522.3 Barcode Discount.** The parcel barcoded discount or flats barcoded discount apply to single-piece rate and Basic Presort Rate Bound Printed Matter subclass parcel or flat mail, respectively, that is entered at designated facilities, bears a barcode specified by the Postal Service, is prepared as specified by the Postal Service in a mailing of at least 50 pieces, and meets all other preparation and machinability requirements of the Postal Service.
- 522.4 Flats Differential.** Flats-shaped single-piece rate, Basic Presort Rate, and Carrier Route Presort Rate Bound Printed Matter subclass mail that meets the preparation criteria specified by the Postal Service is eligible for a rate reduction in the form of a flats differential.
- 523 Media Mail Subclass**
- 523.1 Definition.** The Media Mail subclass consists of Package Services mail of the following types:
- a. Books, including books issued to supplement other books, of at least eight printed pages, consisting wholly of reading matter or scholarly bibliography or reading matter with incidental blank spaces for notations, and containing no advertising matter other than incidental announcements of books. Not more than three of the announcements

may contain as part of their format a single order form, which may also serve as a postcard. These order forms are in addition to and not in lieu of order forms which may be enclosed by virtue of any other provision;

- b. 16 millimeter or narrower width films which must be positive prints in final form for viewing, and catalogs of such films, of 24 pages or more, at least 22 of which are printed, except when sent to or from commercial theaters;
- c. Printed music, whether in bound form or in sheet form;
- d. Printed objective test materials and accessories thereto used by or in behalf of educational institutions in the testing of ability, aptitude, achievement, interests and other mental and personal qualities with or without answers, test scores or identifying information recorded thereon in writing or by mark;
- e. Sound recordings, including incidental announcements of recordings and guides or scripts prepared solely for use with such recordings. Not more than three of the announcements may contain as part of their format a single order form, which may also serve as a postcard. These order forms are in addition to and not in lieu of order forms which may be enclosed by virtue of any other provision;
- f. Playscripts and manuscripts for books, periodicals and music;
- g. Printed educational reference charts, permanently processed for preservation;
- h. Printed educational reference charts, including but not limited to
 - i. Mathematical tables,
 - ii. Botanical tables,
 - iii. Zoological tables, and
 - iv. Maps produced primarily for educational reference purposes;
- i. Looseleaf pages and binders therefor, consisting of medical information for distribution to doctors, hospitals, medical schools, and medical students; and

- j. Computer-readable media containing prerecorded information and guides or scripts prepared solely for use with such media.

523.2 Description of Rate Categories

523.21 Single-Piece Rate Category. The single-piece rate category applies to Media Mail not mailed under section 523.22 or 523.23 prepared as specified by the Postal Service.

523.22 Five-Digit Presort Rate Category. The Five-Digit presort rate category applies to mailings of at least 300 pieces in any Media Mail subclass presorted category, prepared and presorted to five-digit destination ZIP Codes as specified by the Postal Service.

523.23 Basic Presort Rate Category. The Basic Presort rate category applies to mailings of at least 300 pieces in any Media Mail subclass presorted category, prepared and presorted, as specified by the Postal Service, other than to five-digit destination ZIP Codes.

523.3 Barcode Discount. The barcode discount applies to single-piece rate and Basic Presort rate Media Mail that is entered at designated facilities, bears a barcode specified by the Postal Service, is prepared as specified by the Postal Service in a mailing of at least 50 pieces, and meets all other preparation and machinability requirements of the Postal Service.

524 Library Mail Subclass

524.1 Definition

524.11 General. The Library Mail subclass consists of Package Services mail of the following types:

- a. Matter designated in section 524.13, loaned or exchanged (including cooperative processing by libraries) between:
 - i. Schools or colleges, or universities;
 - ii. Public libraries, museums and herbaria, nonprofit religious, educational, scientific, philanthropic, agricultural, labor, veterans¹ or fraternal organizations or associations, or between such organizations and their members, readers or borrowers.

- b. Matter designated in section 524.14, mailed to or from schools, colleges, universities, public libraries, museums and herbaria and to or from nonprofit religious, educational, scientific, philanthropic, agricultural, labor, veterans' or fraternal organizations or associations; or
- c. Matter designated in section 524.15, mailed from a publisher or a distributor to a school, college, university or public library.

524.12 Definition of Nonprofit Organizations and Associations. Nonprofit organizations or associations are defined in section 1009.

524.13 Library Subclass Mail Under Section 524.11.a. Matter eligible for mailing as Library Mail under subsection a of section 524.11 consists of:

- a. Books consisting wholly of reading matter or scholarly bibliography or reading matter with incidental blank spaces for notations and containing no advertising other than incidental announcements of books;
- b. Printed music, whether in bound form or in sheet form;
- c. Bound volumes of academic theses in typewritten or other duplicated form;
- d. Periodicals, whether bound or unbound;
- e. Sound recordings;
- f. Other library materials in printed, duplicated or photographic form or in the form of unpublished manuscripts; and
- g. Museum materials, specimens, collections, teaching aids, printed matter and interpretative materials intended to inform and to further the educational work and interest of museums and herbaria.

524.14 Library Mail Under Section 524.11.b. Matter eligible for mailing as Library Mail under subsection b of section 524.11 consists of:

- a. 16-millimeter or narrower width films; filmstrips; transparencies; slides; microfilms; all of which must be positive prints in final form for viewing;
- b. Sound recordings;

- c. Museum materials, specimens, collections, teaching aids, printed matter, and interpretative materials intended to inform and to further the educational work and interests of museums and herbaria;
- d. Scientific or mathematical kits, instruments or other devices;
- e. Catalogs of the materials in subsections a through d of section 524.14 and guides or scripts prepared solely for use with such materials.

524.15 Library Mail Under Section 524.11.c. Matter eligible for mailing as Library subclass mail under subsection c of section 524.11 consists of books, including books to supplement other books, consisting wholly of reading matter or scholarly bibliography or reading matter with incidental blank spaces for notations, and containing no advertising matter other than incidental announcements of books.

524.2 Description of Rate Categories

524.21 Single-Piece Rate Category. The single-piece rate category applies to Library Mail not mailed under section 524.22 or 524.23 prepared as specified by the Postal Service.

524.22 Five-Digit Presort Rate Category. The Five-Digit Presort rate category applies to mailings of at least 300 pieces in any Library Mail subclass presorted category, prepared and presorted to five-digit destination ZIP Codes as specified by the Postal Service.

524.23 Basic Presort Rate Category. The Basic Presort rate category applies to mailings of at least 300 pieces in any Library Mail subclass presorted category, prepared and presorted as specified by the Postal Service, other than to five-digit destination ZIP Codes.

524.3 Barcode Discount. The barcode discount applies to Single-Piece Rate and Basic Presort Rate Library Mail that is entered at designated facilities, bears a barcode specified by the Postal Service, is prepared as specified by the Postal Service in a mailing of at least 50 pieces, and meets all other preparation and machinability requirements of the Postal Service.

530 PHYSICAL LIMITATIONS

531 Size

Except as provided in section 521.61, Package Services mail may not exceed 108 inches in length and girth combined. Additional size limitations apply to individual Package Services mail subclasses.

532 Weight

Package Services mail may not weigh more than 70 pounds. Additional weight limitations apply to individual Package Services mail subclasses.

540 POSTAGE AND PREPARATION

541 Postage

Postage must be paid as set forth in section 3000. All mail mailed at a bulk or presort rate must have postage paid in a manner not requiring cancellation.

542 Preparation

All pieces in a Package Services mailing must be separately addressed. All pieces in a Package Services mailing must be identified as specified by the Postal Service, and must contain the ZIP Code of the addressee when specified by the Postal Service. All Package Services mailings must be prepared and presented as specified by the Postal Service. Two or more Package Services mailings may be commingled and mailed only when specific methods approved by the Postal Service for determining and verifying postage are followed.

543 Non-Identical Pieces

Pieces not identical in size and weight may be mailed at a bulk or presort rate as part of the same mailing only when specific methods approved by the Postal Service for determining and verifying postage are followed.

544 Attachments and Enclosures

544.1 General. First-Class Mail or Standard Mail may be attached to or enclosed in Package Services mail. The piece must be marked as specified by the Postal Service. Except as provided in sections 544.2 and 544.3, additional

postage must be paid for the attachment or enclosure as if it had been mailed separately. Otherwise, the entire combined piece is subject to the First-Class, Standard Mail, or Package Services rate for which it qualifies unless the rate applicable to the host piece is higher.

544.2 Specifically Authorized Attachments and Enclosures. Package Services mail may contain enclosures and attachments as specified by the Postal Service and as described in subsections a and e of section 523.1, with postage paid on the combined piece at the Package Services rate applicable to the host piece.

544.3 Incidental First-Class Attachments and Enclosures. First-Class Mail that meets one or more of the definitions in subsections b through d of section 210, may be attached to or enclosed with Package Services mail, with postage paid on the combined piece at the Package Services rate applicable to the host piece, if the attachment or enclosure is incidental to the piece to which it is attached or with which it is enclosed.

550 DEPOSIT AND DELIVERY

551 Deposit

Package Services mail must be deposited at places and times designated by the Postal Service.

552 Service

Package Services mail may receive deferred service.

553 Forwarding and Return

Undeliverable-as-addressed Package Services mail will be forwarded on request of the addressee, returned on request of the mailer, or forwarded and returned on request of the mailer. Pieces which combine Package Services mail with First-Class Mail or Standard Mail will be forwarded if undeliverable-as-addressed, and returned if undeliverable, as specified by the Postal Service. When Package Services mail is forwarded or returned from one post office to another, additional charges will be based on the applicable single-piece Package Services mail rate.

560 ANCILLARY SERVICES

561 All Subclasses Except Parcel Select Return Service Categories

Package Services mail, except Parcel Select Return Service mail entered under sections 521.27 or 521.28 (which is eligible for Certificates of Mailing only), will receive the following services upon payment of the appropriate fees:

Service	Schedule
a. Address correction	911
b. Certificates of mailing	947
c. COD	944
d. Insurance	943
e. Special handling	952
f. Return receipt (merchandise only)	945
g. Merchandise return	932
h. Delivery Confirmation (limited to parcel-shaped Package Services Mail)	948
i. Shipper Paid Forwarding	936
j. Signature Confirmation limited to parcel-shaped Package Services Mail	949
k. Parcel Airlift	951

Insurance, special handling, and COD services may not be used selectively for individual pieces in a multi-piece Package Services mailing unless specific methods approved by the Postal Service for determining and verifying postage are followed.

562 Parcel Select Return Service

Parcel Post subclass mail entered under sections 521.27 or 521.28 will receive Certificate of Mailing service if the customer entering the returned parcel pays the appropriate fees at the time the mail is entered. Certificate of Mailing service may not be purchased by the addressee of the returned parcel.

570 RATES AND FEES

The rates and fees for Package Services Mail are set forth as follows:

	Schedule
a. Parcel Post subclass	
Inter-BMC	521.2A
Intra-BMC	521.2B
Parcel Select	
Destination BMC	521.2C
Destination SCF	521.2D
Destination Delivery Unit	521.2E
Parcel Select Return Services	
Return Delivery Unit	521.2F
Return BMC	521.2G
b. Bound Printed Matter subclass	
Single-Piece	522A
Basic Presort and Carrier Route	522B
Destination Entry Basic Presort	522C
Destination Entry Carrier Route Presort	522D
c. Media Mail subclass	523
d. Library Mail subclass	524
e. Fees	1000

580 AUTHORIZATIONS AND LICENSES**581 Parcel Post Subclass**

The mailing fee set forth in Schedule 1000 must be paid once each 12-month period at each office of mailing or office of verification, as specified by the Postal Service, by or for mailers of any Parcel Select rate category mail in the Parcel Post subclass. Payment of the fee allows the mailer to mail at any Parcel Select rate.

582 Bound Printed Matter Subclass

The mailing fee set forth in Schedule 1000 must be paid once each 12-month period at each office of mailing or office of verification, as specified by

the Postal Service, by or for mailers of Destination BMC, Destination SCF or Destination Delivery Unit rate category mail in the Bound Printed Matter subclass. Payment of the fee allows the mailer to mail at any destination entry Bound Printed Matter rate.

583 Media Mail Subclass

The mailing fee set forth in Schedule 1000 must be paid once each 12-month period at each office of mailing or office of verification, as specified by the Postal Service, by or for mailers of presorted Media Mail. Payment of the fee allows the mailer to mail at any presorted Media Mail rate.

584 Library Mail Subclass

The mailing fee set forth in Schedule 1000 must be paid once each 12-month period at each office of mailing or office of verification, as specified by the Postal Service, by or for mailers of presorted Library Mail. Payment of the fee allows the mailer to mail at any presorted Library Mail rate.

585 Parcel Return Service

585.1 A permit fee as set forth in Schedule 1000 must be paid once each 12-month period by mailers utilizing Parcel Select Return Service. In addition, the permit holder must pay the accounting fee specified in Fee Schedule 1000 once each 12-month period for each advance deposit account.

585.2 The Parcel Return Service permit may be canceled for failure to maintain sufficient funds in a trust account to cover postage and fees on returned parcels, for distributing labels that do not conform to Postal Service specifications, or for other reasons specified by the Postal Service.

**NEGOTIATED SERVICE AGREEMENTS
CLASSIFICATION SCHEDULE**

610 CAPITAL ONE NEGOTIATED SERVICE AGREEMENT

610.1 Eligible First-Class Mail

610.11 Capital One. Eligible First-Class Mail under this section is defined as Capital One's First-Class Mail customer correspondence with established account holders and First-Class Mail solicitations that bear the endorsement specified by the Postal Service. Eligible First-Class Mail does not include Business Reply Mail, Qualified Business Reply Mail, Cards, or Priority Mail.

610.12 Other Mailers. Comparable NSAs, involving adoption of electronic Address Correction Service in lieu of physical returns for First-Class Mail that qualifies for Standard Mail rates and declining block rates for First-Class Mail, may be entered into with other customers, as specified by the Postal Service, and implemented pursuant to proceedings under Chapter 36 of Title 39, of the United States Code.

610.2 Waiver of Address Correction Fees

The fees for address correction in Fee Schedule 911 are waived for those First-Class Mail solicitations on which Capital One uses the endorsement specified by the Postal Service, if:

- a. Capital One mails more than 750 million pieces of eligible First-Class Mail within the first year after implementation of this section, and
- b. updates its databases within 2 days after receipt of address correction information and uses the information in all future First-Class Mail marketing campaigns.

If, during the first year after implementation, Capital One mails fewer than 750 million pieces of eligible First-Class Mail, Capital One agrees to pay the greater of either (1) all address correction service fees under Fee Schedule 911, as specified by the Postal Service, for pieces receiving address correction service, or (2) \$1,000,000.

610.3 First-Class Mail Discounts

610.31 Discount Threshold. The Discount Threshold is defined as the greater of either 1.225 billion pieces of eligible First-Class Mail, or 90 percent of Capital One's average eligible First-Class Mail volume for FY2000, FY2001 and FY2002. The Discount Threshold may be adjusted in accordance with section 610.34.

610.32 Discounts. Capital One's eligible First-Class Mail is subject to the otherwise applicable First-Class Mail postage in Rate Schedule 221 less the discounts shown in Rate Schedule 610A, for each year in which Capital One meets the Discount Threshold. The discounts apply only to volume above the Discount Threshold. Each incremental discount applies only to the incremental volume within each volume block.

610.33 Additional Discounts (Year 2, Year 3, and Year 4). If eligible First-Class Mail volume for the first year is less than 1.025 billion pieces, the additional discount tiers shown in Rate Schedule 610B shall apply to the incremental volumes in the second, third, and fourth years in addition to the incremental discounts in Rate Schedule 610A.

610.34 Threshold Adjustment. In the event that Capital One merges with or acquires an entity with annual First-Class Mail volume in excess of 10 million pieces in the year preceding the acquisition or merger, or in the event that, in any Postal Service fiscal year, Capital One merges with or acquires multiple entities with combined annual First-Class Mail volume in excess of 25 million pieces, the discount threshold will be adjusted upward by the volume of First-Class Mail sent by the other entity (or entities) during the 12 months preceding the merger or acquisition. In that event, beginning in the succeeding fiscal quarter following the date of acquisition or merger, Rate Schedule 610C would apply in lieu of Rate Schedule 610A, and, if the conditions in section 610.33 are also met, Rate Schedule 610D would apply in lieu of Rate Schedule 610B.

610.35 Discount Limit. The maximum cumulative discount available to Capital One over the duration of this NSA shall not exceed \$40.637 million.

610.4 Rates

The rates applicable to this Agreement are set forth in the following rate schedules:

610A
610B
610C
610D

610.5 Expiration

The provisions of section 610 expire on September 1, 2007 at 12:01 a.m.

610.6 Precedence

To the extent any provision of section 610 is inconsistent with any other provision of the Domestic Mail Classification Schedule, section 610 shall control.

611 DISCOVER FINANCIAL SERVICES NEGOTIATED SERVICE AGREEMENT

611.1 Eligible First-Class Mail

Eligible First-Class Mail under this section is defined as: (1) Discover Financial Services' First-Class Mail customer correspondence related to credit and banking products and services account holders; and (2) First-Class Mail solicitations for credit and banking products that bear the endorsement specified by the Postal Service. Eligible First-Class Mail does not include Business Reply Mail, Qualified Business Reply Mail, Cards, or Priority Mail.

611.2 Waiver of Address Correction Fees

The fees for address correction in Fee Schedule 911 are waived for those First-Class Mail solicitations on which Discover Financial Services uses the endorsement specified by the Postal Service, if:

- a. Discover Financial Services mails more than 350 million pieces of eligible First-Class Mail within the first year after implementation of this section, and

- b. Discover Financial Services updates any databases it uses for solicitation mail, other than First-Class Mail customer correspondence related to account holders, as specified by the Postal Service.

If, during the first year after implementation, Discover Financial Services mails fewer than 350 million pieces of eligible First-Class Mail, Discover Financial Services agrees to pay the greater of either (1) all address correction service fees under Fee Schedule 911, as specified by the Postal Service, for pieces receiving address correction service, or (2) \$250,000.

611.3 First-Class Mail Discounts

611.31 Discount Threshold. The Discount Threshold is set at 405 million pieces of eligible First-Class Mail for the first year of the agreement.

611.32 Discounts. Discover Financial Services' Eligible First-Class Mail is subject to the otherwise applicable First-Class Mail postage in Rate Schedule 221 less the discounts shown in Rate Schedule 611A, for the first year of the agreement if Discover Financial Services meets the Discount Threshold. The discounts apply only to volume above the Discount Threshold. Each incremental discount applies only to the incremental volume within each volume block.

611.33 Annual Threshold Adjustment. The Postal Service shall annually adjust the Discount Threshold based on the percentage change, from year to year, of Discover Financial Services' domestic gross active accounts, as that figure is reported quarterly in SEC filings. The beginning and ending points for each volume block in Rate Schedule 611A will increase or decrease by the same number as the increase or decrease in the Discount Threshold. Rate Schedule 611B will be applicable in lieu of Rate Schedule 611A if there is such an adjustment.

611.34 Threshold Adjustment for Acquisition or Merger. In the event that Discover Financial Services merges with or acquires an entity with annual First-Class Mail volume in excess of 10 million pieces in the year preceding the acquisition or merger, or in the event that, in any Postal Service fiscal year, Discover Financial Services merges with or acquires multiple entities with combined annual First-Class Mail volume in excess of 25 million pieces, the Discount Threshold will be adjusted upward by the volume of First-Class Mail sent by the other entity (or entities) during the 12 months preceding the merger or acquisition. Rate Schedule 611B will be applicable in lieu of Rate Schedule 611A if there is such an adjustment.

611.35 Discount Limit. The maximum cumulative discount available to Discover Financial Services over the duration of this NSA shall not exceed \$13 million.

611.4 Rates

The rates applicable to this Agreement are set forth in Rate Schedules 611A and 611B.

611.5 Expiration

The provisions of section 611 expire at 12:01 a.m. on January 1, 2008.

611.6 Precedence

To the extent any provisions of section 611 is inconsistent with any other provision of the Domestic Mail Classification Schedule, the former shall control.

612 BANK ONE NEGOTIATED SERVICE AGREEMENT

612.1 Eligible First-Class Mail

Eligible First-Class Mail under this section is defined as: (1) all Bank One letter shape First-Class Mail customer account mail (statements and correspondence) related to credit and banking products and services account holders; and (2) First-Class Mail solicitations for credit and banking products that bear the endorsement specified by the Postal Service, except that no more than 35 million flat shape solicitation pieces will be counted annually toward the discount threshold or be eligible for discounts. Eligible First-Class Mail does not include Business Reply Mail, Qualified Business Reply Mail, Cards or Priority Mail.

612.2 Waiver of Address Correction Fees

The fees for address correction in Fee Schedule 911 are waived for those First-Class Mail solicitations on which Bank One uses the endorsement specified by the Postal Service.

In exchange for a waiver of ACS fees, Bank One will update any databases it maintains for solicitation mail, other than First-Class Mail customer correspondence related to account holders, and use the information in all future marketing campaigns.

If, during the first year after implementation, Bank One Corporation mails fewer than 25 million pieces of eligible First-Class Mail, Bank One agrees to pay \$200,000.

612.3 First-Class Mail Discounts

612.31 Discount Threshold. The Discount Threshold is set at 535 million pieces of eligible First-Class Mail for the first year of the agreement.

612.32 Discounts. Bank One's Eligible First-Class Mail is subject to the otherwise applicable First-Class Mail postage in Rate Schedule 221 less the discounts shown in Rate Schedule 612A, for the first year of this Agreement if Bank One meets the Discount Threshold. The discounts apply only to volume above the Discount Threshold. Each incremental discount applies only to the incremental volume within each volume block.

612.33 Annual Threshold Adjustment. The Postal Service shall annually adjust the Discount Threshold based on the percentage change from year to year in the sum of the number of Bank One's credit card and checking accounts, as listed in Bank One's annual report. This adjustment shall be determined as follows: if the percentage change is an increase or a decrease of greater than 5%, the threshold shall be adjusted upward or downward by the difference between the percentage change and 3%. No adjustment shall be made for a percentage change of 5% or less. If the percentage change is more than 5%, Rate Schedule 612B would apply in lieu of Rate Schedule 612A.

612.34 Threshold Adjustment for Mergers and Acquisitions; and Portfolio Purchases. In the event that:

- a. Bank One merges with and/or acquires an entity and/or purchases a portfolio with annual First-Class Mail volume in excess of 10 million pieces but less than 300 million pieces, the discount threshold will be adjusted to add the volume of First-Class Mail sent by the merged or acquired entity, or on behalf of the purchased portfolio during the 12 months preceding the merger, acquisition, or purchase. In that event, beginning in the succeeding fiscal quarter immediately following the date that mail volumes due to the merger, acquisition, or purchase begin to be mailed through the threshold permit accounts, Rate Schedule 612B would apply in lieu of Rate Schedule 612A.
- b. Bank One merges with, or acquires, another banking entity that has an annual First-Class Mail volume of over 300 million pieces, the discount

threshold will be adjusted upward to add the volume of the merged or acquired entity for the 12 months prior to the date the mail of the merged entity is first mailed through the threshold permit accounts. In that event, beginning in the succeeding fiscal quarter immediately following the date the mail of the merged entity is first mailed through the threshold permit accounts, Rate Schedule 612B would apply in lieu of Rate Schedule 612A.

- c. Bank One loses or sells a portfolio with annual First-Class Mail volume of at least 10 million pieces, the discount threshold will be adjusted downward by the product of the number of active accounts lost or sold multiplied by 12. In that event, beginning in the succeeding fiscal quarter immediately following the date that the mail volumes due to the loss or sale will no longer be mailed through the threshold permit accounts, Rate Schedule 612B will apply in lieu of Rate Schedule 612A.

612.35 Third Year Discounts. In the third year of the agreement, availability of the discounts in Rate Schedules 612A or 612B will be subject to the following provisions:

- a. If the cumulative financial impact of section 612 on the Postal Service at the end of the second year after implementation is positive, then the discounts in Rate Schedules 612A or 612B will be available.
- b. If the cumulative financial impact of section 612 on the Postal Service at the end of the second year after implementation is negative, and the incremental financial impact for volume entered under any rate discount block under section 612 is also negative, then mail that otherwise qualified for that discount shall instead be eligible for the deepest block discount that produces a positive incremental financial impact.
- c. Determination of the cumulative financial impact within the meaning of paragraph (a) shall be based on the financial analysis submitted into the record as Appendix A to USPS-T-1 by the Postal Service in Postal Rate Commission Docket No. MC2004-3, adjusted solely to reflect the return, forwarding and ACS success rates actually experienced by the Postal Service on eligible letter-shaped solicitations (as defined in section 612.1) entered as First-Class Mail under this provision during the first two years after implementation.
- d. Determination of the incremental financial impact for volume entered under each rate discount block within the meaning of paragraph (b) shall be based on a financial analysis comparable to that specified in

paragraph (c), except that the analysis shall report separately the net incremental contribution per piece for volume within each rate discount block, rather than the cumulative financial impact of section 612 in the aggregate, and shall be based on inputs from the second year only.

- e. The Postal Service shall submit its determination under this section, along with the Postal Service's supporting analysis, within two years and three months from the implementation date of this provision.
- f. If the Postal Service fails to submit the analysis described in this subsection within 2 years and 3 months after implementation, this provision (section 612) will expire 2 years and 3 months from the implementation date set by the Board of Governors, rather than at the end of the third year, as otherwise provided by section 612.5.

612.36 Discount Limit. The maximum cumulative discount available to Bank One Corporation over the duration of this negotiated service agreement shall not exceed \$11.508 million.

612.4 Rates

The rates applicable to this Agreement are set forth in Rate Schedules 612A and 612B.

612.5 Expiration

The provisions of section 612 expire on April 1, 2008.

612.6 Precedence

To the extent any provision of section 612 is inconsistent with any other provision of the Domestic Mail Classification Schedule, the former shall control.

613 HSBC NORTH AMERICA HOLDINGS INC. NEGOTIATED SERVICE AGREEMENT

613.1 Eligible First-Class Mail

Eligible First-Class Mail under this section is defined as: (1) HSBC's First-Class Mail customer correspondence related to credit and banking products and services account holders; and (2) First-Class Mail solicitations for credit and banking products that bear an endorsement specified by the Postal

Service. Eligible First-Class Mail does not include Business Reply Mail, Qualified Business Reply Mail, Cards, Priority Mail, or pieces that are not letter-shaped.

613.2 Waiver of Address Correction Fees

The fees for address correction in Fee Schedule 911 are waived for those First-Class Mail solicitations on which HSBC uses the endorsement specified by the Postal Service, if:

- a. HSBC mails more than 525 million pieces of eligible First-Class Mail within the first year after implementation of this section, and
- b. HSBC updates any databases it maintains for solicitation mail, other than First-Class Mail customer correspondence related to account holders, as specified by the Postal Service.

If, during the first year after implementation, HSBC mails fewer than 525 million pieces of eligible First-Class Mail, HSBC agrees to pay the greater of either (1) all address correction service fees under Fee Schedule 911, as specified by the Postal Service, for pieces receiving address correction service, or (2) \$200,000.

613.3 First-Class Mail Discounts

613.31 Discount Thresholds. The First-Class Mail Volume Threshold is set at 615 million pieces of eligible First-Class Mail for the first year of the agreement, 725 million pieces for the second year of the agreement, and 810 million pieces for the third year of the agreement.

613.32 Discounts. HSBC's eligible First-Class Mail is subject to the otherwise applicable First-Class Mail postage in Rate Schedule 221, less the discounts shown in Rate Schedule 613A for the first year of the agreement, in Rate Schedule 613B for the second year of the agreement, and in Rate Schedule 613C for the third year of the agreement, if HSBC meets the applicable Discount Threshold in any of those years. The discounts apply in each year only to volume above the Discount Threshold for that year. Each incremental discount applies only to the incremental volume within each volume block.

613.33 Annual Threshold Adjustments. The discount thresholds specified in section 613.31 for the second and third years of the agreement may be adjusted upward or downward based on the relationship between mail

volumes forecasted by HSBC for the first and second years of the agreement, and the mail volumes actually tendered by HSBC in those years. To determine whether any adjustment is warranted under this provision, at the end of the first and second years of the agreement, percentage deviations will be calculated between the before-rates forecasts of HSBC's First-Class Mail and Standard Mail volumes for the year, and HSBC's actual volume in each category. An upward adjustment will be triggered if the actual volume of First-Class Mail exceeds the forecasted volume by more than 20 percent, and the actual volume of Standard Mail exceeds the forecasted volume by more than 5 percent. For years in which the upward adjustment is triggered, the discount threshold specified in section 613.31 for the next year will be increased by a percentage amount equal to the First-Class Mail volume percentage surplus, less 15 percent. A downward adjustment will be triggered if the forecasted volume of First-Class Mail exceeds the actual volume of First-Class Mail by more than 15 percent. For years in which a downward adjustment is triggered, the discount threshold specified in section 613.31 for the next year will be decreased by a percentage amount equal to the First-Class Mail volume percentage deficit, less 15 percent. Any new annual threshold amounts calculated under this provision will be rounded to the nearest whole million pieces of mail. For any year for which a new annual threshold amount has been derived pursuant to this provision, Rate Schedule 613D will be applicable in lieu of Rate Schedule 613B or 613C.

613.34 Threshold Adjustment for Mergers and Acquisitions; and Portfolio Activity.

In the event that:

- a. HSBC merges with and/or acquires an entity and/or purchases a portfolio with annual First-Class Mail volume in excess of 10 million pieces, the discount threshold will be adjusted to add the volume of First-Class Mail sent by the merged or acquired entity, or on behalf of the purchased portfolio, during the 12 months preceding the merger, acquisition, or purchase. In that event, beginning in the succeeding fiscal quarter immediately following the date that mail volumes due to the merger, acquisition, or purchase begin to be mailed through the threshold permit accounts, Rate Schedule 613D would apply in lieu of Rate Schedule 613A, 613B, or 613C.
- b. HSBC in the first or second year of the agreement merges with or acquires multiple entities, or purchases multiple portfolios, that have combined annual First-Class Mail volume in excess of 25 million pieces,

the discount thresholds for all succeeding years of the agreement will be adjusted upward to add the First-Class Mail volume sent by the merged or acquired entities, or on behalf of the acquired portfolios, for the 12 months prior to the date the mail of the merged entity is first mailed through the threshold permit accounts. In that event, in all succeeding years of the agreement, Rate Schedule 613D would apply in lieu of Rate Schedule 613B or 613C.

- c. HSBC loses or sells a portfolio with annual First-Class Mail volume of at least 10 million pieces, the discount threshold will be adjusted downward by the product of the number of active accounts lost or sold, multiplied by 12. In that event, beginning in the succeeding fiscal quarter immediately following the date that the mail volumes due to the loss or sale will no longer be mailed through the threshold permit accounts, Rate Schedule 613D will apply in lieu of Rate Schedule 613A, 613B, or 613C.
- d. In order to avoid double counting, any volumes used to make adjustments pursuant to these merger, acquisition, and portfolio activity provisions shall be excluded from calculation of the corresponding annual threshold adjustment pursuant to section 613.33.

613.35 Discount Limit. The maximum cumulative discount available to HSBC over the duration of this NSA shall not exceed \$9 million.

613.36 Implementation Date Threshold Adjustments.

The discount threshold specified in section 613.31 for the first year of the agreement shall be increased by the difference between the thresholds specified for the first year and the second year, pro-rated on a monthly basis from January 1, 2005, to the first day of the month of the actual date of implementation, and then rounded to the nearest whole million pieces of mail. The discount threshold specified for the second year of the agreement shall be similarly increased, by applying the same proportional factor to the difference between the thresholds specified for the second and third year. The discount threshold specified for the third year shall be increased by the same absolute amount of volume added to the threshold for the second year. Similarly, for purposes of determining any applicable annual threshold adjustments as specified in section 613.33, the before-rates forecasts of HSBC's First-Class Mail for the first and second years of the agreement shall be increased by applying the same proportional factor to the differences between, respectively, the before-rates forecasts for the first and second years, and the before-rates forecasts for the second and third years.

613.4 Rates

The rates applicable to this Agreement are set forth in Rate Schedules 613A, 613B, 613C, and 613D.

613.5 Expiration

The provisions of section 613 expire on January 1, 2009.

613.6 Precedence

To the extent any provision of section 613 is inconsistent with any other provision of the Domestic Mail Classification Schedule, the former shall control.

620 BOOKSPAN NEGOTIATED SERVICE AGREEMENT

620.1 Eligible Standard Mail

620.11 Bookspan. Eligible Standard Mail under this section is defined as Standard Mail letter-shaped pieces sent by Bookspan for the purpose of soliciting book club membership: (1) of persons who are not current subscribers to the book club or clubs Bookspan is promoting in the mailing; or (2) of book club members whose membership is expiring. Such pieces may be sent by Bookspan, by entities in which Bookspan holds controlling shares, or by their vendors on their behalf. Such pieces may include up to two inserts promoting Bookspan's strategic business alliances. Under no circumstances are periodic Current Member club mailings which offer the cycle's Featured Selection, as well as other club selections and offerings, eligible to be counted and receive discounts under the Agreement, even if they contain solicitations to renew membership in that club or to join other clubs.

620.12 Other Mailers. Functionally equivalent NSAs, involving declining block rates for Standard Mail letters for the purpose of acquiring customers for programs involving recurring mailings offering merchandise, may be entered into with other customers demonstrating a similar or greater multiplier effect and implemented pursuant to proceedings under Chapter 36 of Title 39, of the United States Code. For a mailer to have a similar or greater multiplier effect, at least six times per year, that mailer must send a continuing series of marketing mail, send products to a list of people who have agreed to purchase some stipulated minimum number of items on a more or less

regular basis and use at least one other subclass for merchandise fulfillment.

620.2 Standard Mail Declining Block Rates

620.21 Volume Commitments. The following volume commitments for otherwise eligible letter-shaped Standard Mail pieces must be met before any discounts under this section are payable:

- a. 94 million for the first year of the Agreement;
- b. 95 million for the second year of the Agreement, subject to adjustment as specified below; and,
- c. 105 million for the third year of the Agreement, subject to adjustment as specified below.

If Bookspan does not mail at least 73 million pieces during the first year of this Agreement, it will pay the Postal Service a one-time transaction fee of \$200,000.

620.22 Volume Commitment Adjustment Mechanism. At the end of each year of the Agreement other than its final year, the volume commitment for the following year will be adjusted, as follows:

- a. If, at the end of the year, actual volume is 12 percent or more above that year's volume commitment, the following year's commitment will be revised to be the average of the completed year's actual volume and the original volume commitment for the following year.
- b. If, at the end of the year, actual volume is 5 percent or more below that year's volume commitment, the following year's commitment will be decreased by the percentage difference between the completed year's original volume commitment and its actual volume, but in no case to lower than 90 million.

620.23 Incremental Discounts. Bookspan's eligible Standard Mail is subject to the otherwise applicable Standard Mail postage in Rate Schedule 321A, 321B, or 322 less the discounts shown in Rate Schedule 620A for the first year of the Agreement, in Rate Schedule 620B for the second year of the Agreement, and in Rate Schedule 620C for the third year of the Agreement, if Bookspan meets the applicable volume commitments specified in 620.21,

or as adjusted in accordance with 620.22. Each incremental discount applies only to the incremental volume within each volume block.

620.24 Volume Block Adjustments for Mergers and Acquisitions. In the event that Bookspan merges with and/or acquires an entity or entities and/or purchases a portfolio with annual Standard Mail volume in excess of 5 million pieces, the volume blocks will be adjusted to add the volume of Standard Mail sent by the merged or acquired entity during the 12 months preceding the merger, acquisition, or purchase. The adjustment becomes effective for the succeeding fiscal quarter immediately following the date that mail volumes due to the merger, acquisition, or purchase begin to be mailed through the threshold permit accounts.

620.25 Termination. The Agreement automatically terminates and eligibility for all discounts under this section ceases if Bookspan's Standard Mail letter solicitation volume exceeds 150,000,000, or if the Agreement is terminated by either party with 30 days' written notice to the other party.

620.4 Rates

The rates applicable to this Agreement are set forth in Rate Schedules 620A, 620B, and 620C.

620.5 Expiration

The provisions of section 620 expire on June 1, 2009.

620.6 Precedence

To the extent any provision of section 620 is inconsistent with any other provision of the Domestic Mail Classification Schedule, the former shall control.

**SPECIAL SERVICES
CLASSIFICATION SCHEDULE**

910 ADDRESSING

911 ADDRESS CORRECTION SERVICE

911.1 Definition

911.11 Address Correction Service provides a mailer both an addressee's former and current address, if the correct address is known to the Postal Service. If the correct address is not known to the Postal Service, Address Correction Service provides the reason why the Postal Service could not deliver the mailpiece as addressed.

911.2 Availability

911.21 Address Correction service is available to mailers of postage prepaid mail of all classes, except for mail addressed for delivery by military personnel at any military installation and Regular and Nonprofit Presort category mail entered as Customized Market Mail under sections 321.22 and 323.22. Address Correction Service is mandatory for Periodicals class mail.

911.22 Automated or Electronic Address Correction Service is available to mailers who can receive computerized address corrections and meet the barcoding and other requirements specified by the Postal Service. Automated Address Correction Service is limited to mailers who meet address hygiene requirements, as specified by the Postal Service.

911.3 Mailer Requirements

911.31 Mail, other than Periodicals class mail, sent under this section must bear a request for Address Correction service.

911.4 Other Services

911.41 Address Correction Service serves as a prerequisite for Shipper Paid Forwarding, and for Standard Mail Forwarding Service for mailpieces defined in Section 353a.

911.5 Fees

911.51 The fees for Address Correction Service are set forth in Fee Schedule 911. These fees do not apply when the correction is provided incidental to the return of the mail piece to the sender. The “Automated” fees are available to customers meeting address hygiene requirements, as specified by the Postal Service.

912 MAILING LIST SERVICES

912.1 Definition

912.11 Mailing List services enable an eligible mailer to obtain the following services:

- a. Correction of Mailing Lists;
- b. Change-of-Address Information for Election Boards and Registration Commissions;
- c. ZIP Coding of Mailing Lists; and
- d. Sequencing of Address Cards.

912.2 Description of Services

a. Correction of Mailing Lists. This service provides current information concerning name and address mailing lists or correct information concerning occupant mailing lists. New names will not be added to a name and address mailing list, and street address numbers will not be added or changed for an occupant mailing list.

(1) The Postal Service provides the following corrections to name and address lists:

- i. deletion of names to which mail cannot be delivered or forwarded;
- ii. correction of incorrect house, rural, or post office box numbers; and

- iii. furnishing of new addresses, including Zip Codes, when permanent forwarding orders are on file for customers who have moved.

This service does not include the addition of new names.

(2) The Postal Service provides the following corrections to occupant lists:

- i. deletion of numbers representing incorrect or non-existent street addresses;
 - ii. identification of business addresses and rural route addresses, to the extent known; and
 - iii. grouping of corrected cards or sheets by route.
- b. Change-of-Address Information for Election Boards and Registration Commissions. This service provides election boards and voter registration commissions with the current address of a resident addressee, if known to the Postal Service.
 - c. ZIP Coding of Mailing Lists. This service provides sortation of addresses to the finest possible ZIP Code level.
 - d. Sequencing of Address Cards. This service provides for the removal of incorrect addresses, notation of missing addresses and addition of missing addresses.

912.3 Requirements of Customer

912.31 Correction of Mailing List service is available only to the following owners of name and address or occupant mailing lists:

- a. Members of Congress
- b. Federal agencies
- c. State government departments
- d. Municipalities
- e. Religious organizations

- f. Fraternal organizations
- g. Recognized charitable organizations
- h. Concerns or persons who solicit business by mail

912.32 A customer desiring correction of a mailing list or arrangement of address cards in sequence of carrier delivery must submit the list or cards as specified by the Postal Service.

912.33 Gummed labels, wrappers, envelopes, Stamped Cards, or postcards indicative of one-time use will not be accepted as mailing lists.

912.4 Fees

912.41 The fees for Mailing List services are set forth in Fee Schedule 912.

913 CHANGE OF ADDRESS SERVICE

913.1 Definition

913.11 Change of Address Service is available to customers who want their mail permanently or temporarily forwarded to a future or current address from a former address.

913.2 Fees

913.21 The fee for Change of Address Service is set forth in Fee Schedule 1000.

920 DELIVERY ALTERNATIVES

921 POST OFFICE BOX AND CALLER SERVICE

921.1 Post Office Box Service

921.11 Definition

921.111 Post Office Box service provides the customer with a private, locked receptacle for the receipt of mail during the hours specified by the Postal Service.

921.12 Limitations

921.121 The Postal Service may limit the number of post office boxes occupied by any one customer.

921.122 Post Office Box service is not available to a customer whose sole purpose for using this service is to obtain free forwarding or transfer of mail by filing change-of-address orders.

921.13 Fees

921.131 Fees for Post Office Box service are set forth in Fee Schedule 921.

921.132 In postal facilities primarily serving academic institutions or the students of such institutions, fees for post office boxes are:

Period of box use	Fee
95 days or less	½ semiannual fee
96 to 140 days	¾ semiannual fee
141 to 190 days	Full semiannual fee
191 to 230 days	1¼ semiannual fee
231 to 270 days	1½ semiannual fee
271 days to full year	Twice semiannual fee

921.133 No refunds will be made for post office box fees paid under section 921.132.

921.134 Two box keys are available upon payment of a refundable deposit, as specified by the Postal Service. Additional keys, including replacement keys, will be provided, as specified by the Postal Service, only upon payment of the key fee set forth in Fee Schedule 921. Changing the lock on a box is available upon request of the primary box customer and payment of the lock replacement fee set forth in Fee Schedule 921.

921.2 Caller Service**921.21 Definition**

921.211 Caller service provides a means for receiving mail, and enables an eligible customer to have properly addressed mail delivered through a call window or loading dock.

921.22 Availability

921.221 Caller service is provided to customers at the discretion of the Postal Service, based on mail volume received and capacity and utilization of post office boxes at any one facility.

921.222 Caller service is not available to a customer whose sole purpose for using this service is to obtain free forwarding or transfer of mail by filing change-of-address orders.

921.23 Fees

921.231 Fees for Caller service are set forth in Fee Schedule 921.

930 PAYMENT ALTERNATIVES

931 BUSINESS REPLY MAIL

931.1 Definitions

931.11 Business Reply Mail service enables a Business Reply Mail permit holder, or the permit holder's authorized representative, to distribute Business Reply Mail cards, envelopes, cartons and labels, which can then be used by mailers for sending First-Class Mail without prepayment of postage to an address chosen by the distributor. The permit holder guarantees payment on delivery of postage and fees for the Business Reply Mail pieces that are returned to the addressee, including any pieces that the addressee refuses.

931.2 Mailer Requirements

931.21 Business reply cards, envelopes, cartons and labels must meet the addressing and preparation requirements specified by the Postal Service. Qualified Business Reply Mail must in addition meet the requirements presented in sections 221.24 or 222.34 for the First-Class Mail Qualified Business Reply Mail rate categories.

931.22 To qualify for the advance deposit account per-piece fees, the customer must maintain sufficient money in an advance deposit account to cover postage and fees due for returned Business Reply Mail.

931.23 To qualify for the nonletter-size weight-averaging per-piece and monthly fees set forth in Fee Schedule 931, the permit holder must be authorized for weight averaging, and receive Business Reply Mail pieces that meet the

addressing and other preparation requirements specified by the Postal Service, but do not meet the machinability requirements specified by the Postal Service for mechanized or automation letter sortation.

931.3 Other Services

931.31 *Reserved*

931.4 Fees

931.41 The fees for Business Reply Mail are set forth in Fee Schedule 931.

931.42 To qualify for any service level except regular (no account[ing] maintenance fee) Business Reply Mail, the annual account[ing] maintenance fee set forth in Fee Schedule 1000 must be paid each year for each business reply advance deposit account at each facility where the mail is to be received.

931.43 The nonletter-size weight averaging monthly fee set forth in Fee Schedule 931 must be paid each month during any part of which the permit holder is authorized to use the weight averaging fees.

931.5 Authorizations and [Licenses] Permits

931.51 In order to distribute business reply cards, envelopes, cartons or labels, the distributor must obtain a [license] permit or [licenses] permits from the Postal Service and pay the appropriate fee as set forth in Fee Schedule 1000.

931.52 Except as provided in section 931.53, the [license] permit to distribute business reply cards, envelopes, cartons, or labels must be obtained at each office from which the mail is offered for delivery.

931.53 If the Business Reply Mail is to be distributed from a central office to be returned to branches or dealers in other cities, one [license] permit obtained from the post office where the central office is located may be used to cover all Business Reply Mail.

931.54 The [license to mail] permit to distribute Business Reply Mail may be canceled for failure to pay business reply postage and fees when due, and for distributing business reply cards or envelopes that do not conform to prescribed form, style or size.

931.55 Authorization to pay nonletter-size weight-averaging Business Reply Mail fees as set forth in Fee Schedule 931 may be canceled for failure of a

Business Reply Mail advance deposit trust account holder to meet the standards specified by the Postal Service for the weight averaging accounting method.

932 MERCHANDISE RETURN SERVICE

932.1 Definition

932.11 Merchandise Return service enables a Merchandise Return service permit holder to authorize [its customers to return a] a mailer to send parcels with the postage and fees paid by the permit holder.

932.2 Availability

932.21 Merchandise Return service is available to all Merchandise Return service permit holders who guarantee payment of postage and fees for all [returned] authorized parcels.

932.22 Merchandise Return service is available for the [return] sending of any parcel under the following classification schedules:

- a. First-Class Mail; and
- b. Package Services, except Parcel Post subclass mail entered under section 521.27 or 521.28.

932.3 Mailer Requirements

932.31 Merchandise return labels must be prepared as specified by the Postal Service, and be made available to the permit holder's customers.

932.4 Other Services

932.41 The following services may be purchased in conjunction with Merchandise Return Service:

Service	Fee Schedule
a. Certificate of Mailing	947
b. Insurance	943
c. Registered Mail	942
d. Special Handling	952

932.5 Fees

932.51 The permit holder must pay the account[ing] maintenance fee specified in Fee Schedule 1000 once each 12-month period for each advance deposit account.

932.6 Authorizations and Licenses

932.61 A permit fee as set forth in Schedule 1000 must be paid once each 12-month period by shippers utilizing Merchandise Return service.

932.62 The merchandise return permit may be canceled for failure to maintain sufficient funds in a trust account to cover postage and fees on returned parcels or for distributing merchandise return labels that do not conform to Postal Service specifications.

933 Reserved [On-Site Meter Service]**[933.1 Definition**

933.11 On-Site Meter service enables a mailer or meter manufacturer to obtain the following meter-related services from the Postal Service at the mailer's or meter manufacturer's premises:

- a. checking a meter in or out of service; and
- b. setting or examining a meter.

933.2 Availability

933.21 On-Site Meter service is available on a scheduled basis, and meter setting may be performed on an emergency basis for those customers enrolled in the scheduled on-site meter setting or examination program.

933.3 Fees

933.31 The fees for On-Site Meter service are set forth in Fee Schedule 933. The basic meter service fee is charged whenever a postal employee is available to provide a meter-related service in section 933.11 at the mailer's or meter manufacturer's premises, even if no particular service is provided.]

934 Reserved

935 BULK PARCEL RETURN SERVICE

935.1 Definition

935.11 Bulk Parcel Return Service provides a method whereby high-volume parcel mailers may have machinable Standard Mail parcels returned to designated postal facilities for pickup by the mailer at a predetermined frequency specified by the Postal Service or delivered by the Postal Service in bulk in a manner and frequency specified by the Postal Service. Such parcels are being returned because they:

- a. are undeliverable-as-addressed;
- b. have been opened, resealed, and redeposited into the mail for return to the mailer using the return label described in section 935.36 below; or
- c. are found in the mailstream, having been opened, resealed, and redeposited by the recipient for return to the mailer, and it is impracticable or inefficient for the Postal Service to return the mailpiece to the recipient for payment of return postage.

935.2 Availability

935.21 Bulk Parcel Return Service is available only for the return of machinable parcels, as defined by the Postal Service, initially mailed under the following Standard Mail subclasses: Regular and Nonprofit.

935.3 Mailer Requirements

935.31 Mailers must receive authorization from the Postal Service to use Bulk Parcel Return Service.

935.32 To claim eligibility for Bulk Parcel Return Service at each facility through which the mailer requests Bulk Parcel Return Service, the mailer must demonstrate receipt of 10,000 returned machinable parcels at a given delivery point in the previous postal fiscal year or must demonstrate a high likelihood of receiving 10,000 returned parcels in the postal fiscal year for which the service is requested.

935.33 Payment for Bulk Parcel Return Service is made through advance deposit account, or as otherwise specified by the Postal Service.

- 935.34** Mail for which Bulk Parcel Return Service is requested must bear endorsements specified by the Postal Service.
- 935.35** Bulk Parcel Return Service mailers must meet the documentation and audit requirements of the Postal Service.
- 935.36** Mailers of parcels endorsed for Bulk Parcel Return Service may furnish the recipient a return label, prepared at the mailer's expense to specifications set forth by the Postal Service, to authorize return of opened, machinable parcels at the expense of the original mailer. There is no additional fee for use of the label.

935.4 Other Services

- 935.41** The following services may be purchased in conjunction with Bulk Parcel Return Service:

Service	Fee Schedule
a. Address Correction Service	911
b. Certificate of Mailing	947
c. Shipper-Paid Forwarding	936

935.5 Fees

- 935.51** The per return fee for Bulk Parcel Return Service is set forth in Fee Schedule 935.
- 935.52** The permit holder must pay the account[ing] maintenance fee specified in Fee Schedule 1000 once each 12-month period for each advance deposit account.
- 935.6 Authorizations and Licenses**
- 935.61** A permit fee as set forth in Schedule 1000 must be paid once each 12-month period by mailers utilizing Bulk Parcel Return Service.
- 935.62** The Bulk Parcel Return Service permit may be canceled for failure to maintain sufficient funds in an advance deposit account to cover postage and fees on returned parcels or for failure to meet the specifications of the Postal Service, including distribution of return labels that do not conform to Postal Service specifications.

936 SHIPPER-PAID FORWARDING

936.1 Definition

936.11 Shipper-Paid Forwarding enables mailers to have undeliverable-as-addressed machinable Standard Mail parcels forwarded at applicable First-Class Mail rates for up to one year from the date that the addressee filed a change-of-address order. If Shipper-Paid Forwarding is elected for a parcel that is returned, the mailer will pay the applicable First-Class Mail rate, or the Bulk Parcel Return Service fee, if that service was elected.

936.2 Availability

936.21 Shipper-Paid Forwarding is available only for the forwarding of machinable parcels, as defined by the Postal Service, initially mailed under the following Standard Mail subclasses: Regular and Nonprofit.

936.22 Shipper-Paid Forwarding is available only if automated Address Correction Service, as described in section 911, is used.

936.3 Mailer Requirements

936.31 Mail for which Shipper-Paid Forwarding is purchased must meet the preparation requirements of the Postal Service.

936.32 Payment for Shipper-Paid Forwarding is made through advance deposit account, or as otherwise specified by the Postal Service.

936.33 Mail for which Shipper-Paid Forwarding is requested must bear endorsements specified by the Postal Service.

936.4 Other Services

936.41 The following services may be purchased in conjunction with Shipper-Paid Forwarding:

Service	Fee Schedule
a. Certificate of Mailing	947
b. Bulk Parcel Return Service	935

936.5 Applicable Rates and Fees

936.51 Except as provided in section 935, single-piece rates under the Letters and Sealed Parcels subclass or the Priority Mail subclass of First-Class Mail, as set forth in Rate Schedules 221, and 223, apply to pieces forwarded or returned under this section.

936.52 The account[ing] maintenance fee specified in Fee Schedule 1000 must be paid once each 12-month period for each advance deposit account.

937 PREMIUM FORWARDING SERVICES**937.1 Definition**

937.11 Premium Forwarding Service provides residential delivery customers, and certain post office box customers, the option to receive substantially all classes of mail addressed to a primary address instead at a temporary address by means of a weekly Priority Mail shipment. Parcels that are too large for the weekly shipment, mail pieces that require a scan upon delivery or arrive postage due at the office serving the customer's primary address, and certain Priority Mail pieces may be re-routed as specified by the Postal Service. Re-routed Express Mail, First-Class Mail, and Priority Mail pieces incur no additional reshipping charges. Re-routed Standard Mail and Package Service pieces may be re-routed postage due, primarily Priority Mail postage due, as specified by the Postal Service. Mail sent to a primary address for which an addressee has activated Premium Forwarding Service is not treated as undeliverable-as-addressed.

937.2 Availability

937.21 Premium Forwarding Service is available for a period of at least two weeks and not more than twelve months, as specified by the Postal Service. Customers may not use Premium Forwarding Service simultaneously with temporary or permanent forwarding orders. Premium Forwarding Service is not available to customers whose primary address consists of a size three, four or five post office box, subject to exceptions allowed by the Postal Service, or a centralized delivery point.

937.3 Customer Requirements

937.31 A customer must complete and submit a Premium Forwarding Service application together with all postage and fees for the full duration of service

to the post office responsible for delivery to that customer's primary address, as specified by the Postal Service.

937.4 Other Services

937.41 Premium Forwarding Service may not be combined with any ancillary or special services beyond those purchased by the original mailer.

937.5 Rates and Fees

937.51 The postage rate for mail reshipped by Premium Forwarding Service consists of the rate specified in Rate Schedule 223 for a three-pound parcel mailed to zone 6 on the enrollment date.

937.52 Fees for Premium Forwarding Service are specified in Fee Schedule 937.

937.6 Duration of the Premium Forwarding Service Experiment

937.61 The provisions of section 937 expire the later of:

- a. August 7, 2007, or
- b. if, by the expiration date specified above, a request for the establishment of a permanent Premium Forwarding Service is pending before the Postal Rate Commission, the later of:
 - (1) three months after the Commission takes action on such proposal under section 3624 of title 39, or, if applicable,
 - (2) the implementation date for a permanent Premium Forwarding Service classification.

940 ACCOUNTABILITY AND RECEIPTS

941 CERTIFIED MAIL

941.1 Definition

941.11 Certified Mail service provides a mailer with evidence of mailing and, upon request, electronic confirmation that an article was delivered or that a delivery attempt was made, and guarantees retention of a record of delivery by the Postal Service for a period specified by the Postal Service.

941.2 Availability

941.21 Certified Mail service is available for matter mailed as First-Class Mail.

941.3 Included Services

941.31 If requested by the mailer, the Postal Service will indicate the time of acceptance on the mailing receipt. A mailer may obtain a copy of the mailing receipt on terms specified by the Postal Service.

941.32 If the initial attempt to deliver the mail is not successful, a notice of attempted delivery is left at the mailing address, and the date and time of the attempted delivery is made available to the mailer.

941.33 The date and time of delivery is made available to the mailer electronically.

941.4 Mailer Requirements

941.41 Certified Mail must be deposited in a manner specified by the Postal Service.

941.42 The mailer must mail the article at a post office, branch, or station, or give the article to a rural carrier, in order to obtain a mailing receipt.

941.5 Other Services

941.51 The following services may be obtained in conjunction with mail sent under this section upon payment of the applicable fees:

Service	Fee Schedule
a. Restricted Delivery	946
b. Return Receipt	945

941.6 Fees

941.61 The fee for Certified Mail service is set forth in Fee Schedule 941.

942 REGISTERED MAIL**942.1 Definition**

942.11 Registered Mail service provides added protection to mail sent under this section and indemnity in case of loss or damage. The amount of indemnity

depends upon the actual value of the article at the time of mailing, up to a maximum of \$25,000, and is not available for articles of no value.

942.2 Availability

942.21 Registered Mail service is available for prepaid First-Class Mail of any value, if the mail meets the minimum requirements for length and width specified by the Postal Service.

942.22 Registered Mail service is not available for:

- a. All delivery points because of the high security required for Registered Mail; in addition, liability is limited in some geographic areas;
- b. Mail of any class sent in combination with First-Class Mail; and
- c. Two or more articles tied or fastened together, unless the envelopes are enclosed in the same envelope or container.

942.3 Included Services

942.31 The following services are provided as part of Registered Mail service at no additional cost to the mailer:

- a. A mailing receipt;
- b. Electronic confirmation, upon request, that an article was delivered or that delivery attempt was made;
- c. A record of delivery, retained by the Postal Service for a specified period of time;
- d. A notice of attempted delivery, left at the mailing address if the initial delivery attempt is unsuccessful; and
- e. A notice of nondelivery, when Registered Mail is undeliverable-as-addressed and cannot be forwarded.

942.32 Registered Mail is forwarded and returned without additional registry charge.

942.4 Mailer Requirements

942.41 Registered Mail must be deposited in a manner specified by the Postal Service.

942.42 Indemnity claims for Registered Mail must be filed within a period of time, specified by the Postal Service, from the date the article was mailed. A claim concerning complete loss of registered articles may be filled by the mailer only. A claim concerning damage to or partial loss of registered articles may be filed by either the mailer or addressee.

942.5 Other Services

942.51 The following services may be obtained in conjunction with mail sent under this section upon payment of applicable fees:

Service	Fee Schedule
a. Collect on Delivery	944
b. Restricted Delivery	946
c. Return Receipt	945
d. Merchandise Return (shippers only)	932

942.6 Fees

942.61 The fees for Registered Mail are set forth in Fee Schedule 942.

942.62 There are no additional Registered Mail fees for forwarding and return of Registered Mail.

943 INSURANCE**943.1 Express Mail Insurance****943.11 Definition**

943.111 Express Mail Insurance provides the mailer with indemnity for loss of, rifling of, or damage to items sent by Express Mail.

943.12 Availability

943.121 Express Mail Insurance is available only for Express Mail.

943.13 Limitations and Mailer Requirements

943.131 Insurance coverage is provided, for no additional charge, up to \$100 per-piece for document reconstruction, up to \$5,000 per occurrence, regardless of the number of claimants. Insurance coverage for merchandise is also provided, for no additional charge, up to \$100 per-piece. Additional merchandise insurance coverage may be purchased for a fee. The maximum liability for merchandise is \$5,000 per-piece. For negotiable items, currency, or bullion, the maximum liability is \$15.

943.132 Indemnity claims for Express Mail must be filed within a specified period of time from the date the article was mailed.

943.133 Indemnity will be paid under terms and conditions specified by the Postal Service.

943.134 Among other limitations specified by the Postal Service, indemnity will not be paid by the Postal Service for loss, damage or rifling:

- a. Of nonmailable matter;
- b. Due to improper packaging;
- c. Due to seizure by any agency of government; or
- d. Due to war, insurrection or civil disturbances.

943.14 Other Services

943.141 *Reserved*

943.15 Fees

943.151 The fees for Express Mail Insurance service are set forth in Fee Schedule 943.

943.2 General Insurance

943.21 Definition

943.211 General Insurance provides the mailer with indemnity for loss of, rifling of, or damage to mailed items. General Insurance provides a bulk option for mail

meeting the conditions described below and specified further by the Postal Service.

943.22 Availability

943.221 General Insurance is available for mail sent under the following classification schedules:

- a. First-Class Mail, if containing matter that may be mailed as Standard Mail or Package Services;
- b. Package Services, except Parcel Post subclass mail entered under section 521.27 or 521.28; and
- c. Regular and Nonprofit subclasses of Standard Mail, for Bulk Insurance only, for mail [subject to residual shape surcharge] paying parcel rates.

943.222 General Insurance is not available for matter offered for sale, addressed to prospective purchasers who have not ordered or authorized their sending. If such matter is received in the mail, payment will not be made for loss, rifling, or damage.

943.223 The Bulk Insurance option of General Insurance service is available for mail entered in bulk at designated facilities and in a manner specified by the Postal Service, including the use of electronic manifesting.

943.23 Included Services

943.231 For General Insurance, the mailer is issued a receipt for each item mailed. For items insured for more than \$[50] 200, a record of delivery is retained by the Postal Service for a specified period.

943.232 For items insured for more than \$[50] 200, a notice of attempted delivery is left at the mailing address when the first attempt at delivery is unsuccessful.

943.233 Mail undeliverable as addressed will be returned to the sender as specified by the sender or by the Postal Service.

943.24 Limitations and Mailer Requirements

943.241 Mail insured under section 943.2 must be deposited as specified by the Postal Service.

- 943.242** Bulk Insurance must bear endorsements and identifiers specified by the Postal Service. Bulk Insurance mailers must meet the documentation requirements of the Postal Service.
- 943.243** By insuring an item, the mailer guarantees forwarding and return postage.
- 943.244** General Insurance, other than Bulk Insurance, provides indemnity for the actual value of the article at the time of mailing. Bulk Insurance provides indemnity for the lesser of (1) the actual value of the article at the time of mailing, or (2) the wholesale cost of the contents to the sender.
- 943.245** For General Insurance, other than Bulk Insurance, a claim for complete loss may be filed by the mailer only, and a claim for damage or for partial loss may be filed by either the mailer or addressee. For Bulk Insurance, all claims must be filed by the mailer.
- 943.246** Indemnity claims must be filed within a specified period of time from the date the article was mailed.
- 943.247** For negotiable items, currency, or bullion, the maximum liability is \$15.

943.25 Other Services

943.251 The following services, if applicable to the subclass of mail, may be obtained in conjunction with mail sent under this section upon payment of the applicable fees:

Service	Fee Schedule
a. Parcel Airlift	951
b. Restricted Delivery (for items insured for more than \$[50] <u>200</u>)	946
c. Return Receipt (for items insured for more than \$[50] <u>200</u>)	945
d. Special Handling	952
e. Merchandise Return (shippers only)	932

943.26 Fees

943.261 The fees for General Insurance are set forth in Fee Schedule 943.

944 COLLECT ON DELIVERY**944.1 Definition**

944.11 Collect on Delivery (COD) service allows a mailer to mail an article for which full or partial payment has not yet been received and have the price, the cost of postage and fees, and anticipated or past due charges collected by the Postal Service from the addressee when the article is delivered.

944.2 Availability

944.21 COD service is available for collection of \$1,000 or less upon the delivery of postage prepaid mail sent under the following classification schedules:

- a. Express Mail;
- b. First-Class Mail; and
- c. Package Services, except Parcel Post subclass mail entered under section 521.27 or 521.28.

944.22 Service under this section is not available for:

- a. Collection agency purposes;
- b. Return of merchandise about which some dissatisfaction has arisen, unless the new addressee has consented in advance to such return;
- c. Sending only bills or statements of indebtedness, even though the sender may establish that the addressee has agreed to collection in this manner; however, when the legitimate COD shipment consists of merchandise or bill of lading, the balance due on a past or anticipated transaction may be included in the charges on a COD article, provided the addressee has consented in advance to such action;
- d. Parcels containing moving-picture films mailed by exhibitors to moving-picture manufacturers, distributors, or exchanges; and
- e. Goods that have not been ordered by the addressee.

944.3 Included Services

944.31 COD service provides the mailer with insurance against loss, rifling and damage to the article as well as failure to receive the amount collected from the addressee. This provision insures only the receipt of the instrument issued to the mailer after payment of COD charges, and is not to be construed to make the Postal Service liable upon any such instrument other than a Postal Service money order.

944.32 A receipt is issued to the mailer for each piece of COD mail. Additional copies of the original mailing receipt may be obtained by the mailer.

944.33 Delivery of COD mail will be made in a manner specified by the Postal Service. If a delivery to the mailing address is not attempted or if a delivery attempt is unsuccessful, a notice of attempted delivery will be left at the mailing address.

944.34 The mailer may receive a notice of nondelivery if the piece mailed is endorsed appropriately and the appropriate fee as set forth in Fee Schedule 944 is paid.

944.35 The mailer may designate a new addressee or alter the COD charges by submitting the appropriate form and by paying the appropriate fee as set forth in Fee Schedule 944.

944.4 Limitations and Mailer Requirements

944.41 The mailer must identify COD mail as COD mail, as specified by the Postal Service.

944.42 COD mail must be deposited in a manner specified by the Postal Service.

944.43 A mailer of COD mail guarantees to pay any return postage, unless otherwise specified on the piece mailed.

944.44 For COD mail sent as Package Services mail, postage at the applicable rate will be charged to the addressee:

- a. When an addressee, entitled to delivery to the mailing address under Postal Service regulations, requests delivery of COD mail that was refused when first offered for delivery; and

- b. For each delivery attempt, to an addressee entitled to delivery to the mailing address under Postal Service regulations, after the second such attempt.

944.45 A claim for complete loss may be filed by the mailer only. A claim for damage or for partial loss may be filed by either the mailer or addressee.

944.46 COD indemnity claims must be filed within a specified period of time from the date the article was mailed, and meet the requirements specified by the Postal Service.

944.5 Other Services

944.51 The following services, if applicable to the subclass of mail, may be obtained in conjunction with mail sent under this section upon payment of the applicable fee:

Service	Fee Schedule
a. Registered Mail, if sent as First-Class	942
b. Restricted Delivery	946
c. Special Handling	952

944.6 Fees

944.61 Fees for COD service are set forth in Fee Schedule 944.

945 RETURN RECEIPT

945.1 Regular Return Receipt

945.11 Definition

945.111 Return Receipt service provides evidence to the mailer that an article has been received at the delivery address, including an original or copy of the recipient's signature. Mailers requesting Return Receipt service at the time of mailing will be provided, as appropriate, an original or copy of the signature of the recipient, the date delivered, and the address of delivery, if different from the address on the mailpiece. Mailers requesting Return Receipt service after mailing will be provided a copy of the recipient's signature, the date of delivery, and the name of the person who signed for the article.

945.12 Availability

945.121 Return Receipt service is available for mail sent under the following sections or classification schedules:

Service	Fee Schedule
a. Certified Mail	941
b. COD Mail	944
c. Insurance (if insured for more than \$[50] <u>200</u>)	943
d. Registered Mail	942
e. Express Mail	

945.122 Return Receipt service is available at the time of mailing or, when purchased in conjunction with Certified Mail, COD, Insurance (if for more than \$[50] 200), Registered Mail, or Express Mail, after mailing.

945.13 Included Services

945.131 If the mailer does not receive a return receipt within a specified period of time from the date of mailing, the mailer may request evidence of delivery from the delivery record, at no additional fee.

945.14 Other Services

945.141 *Reserved*

945.2 Return Receipt For Merchandise

945.21 Definition

945.211 Return Receipt for Merchandise service provides evidence to the mailer that an article has been received at the delivery address. A Return Receipt for Merchandise also supplies the recipient's actual delivery address if it is different from the address used by the sender. A Return Receipt for Merchandise may not be requested after mailing.

945.22 Availability

945.221 Return Receipt for Merchandise is available for merchandise sent under the following sections or classification schedules:

- a. Priority Mail;

- b. Standard Mail pieces [subject to the residual shape surcharge] paying parcel rates, except Regular and Nonprofit Presort category mail entered as Customized Market Mail under sections 321.22 and 323.22; and
- c. Package Services, except Parcel Post subclass mail entered under section 521.27 or 521.28.

945.23 Mailer Requirements

945.231 Return Receipt for Merchandise must be deposited in a manner specified by the Postal Service.

945.232 Return Receipt for Merchandise mail may be addressed for delivery only in the United States and its territories and possessions, through Army/Air Force (APO) and Navy (FPO) post offices, or through the United Nations Post Office, New York.

945.24 Other Services

945.241 *Reserved*

945.3 Fees

945.31 The fees for Return Receipt service are set forth in Fee Schedule 945.

946 RESTRICTED DELIVERY

946.1 Definition

946.11 Restricted Delivery service enables a mailer to direct the Postal Service to limit delivery to the addressee or to someone authorized by the addressee to receive such mail.

946.2 Availability

946.21 This service is available for mail sent under the following sections:

Service	Fee Schedule
a. Certified Mail	941
b. COD Mail	944
c. Insurance (if insured for more than \$[50] <u>200</u>)	943
d. Registered Mail	942

946.22 Restricted Delivery is available to the mailer at the time of mailing or after mailing.

946.23 Restricted Delivery service is available for delivery only to natural persons specified by name.

946.3 Included Services

946.31 A record of delivery will be retained by the Postal Service for a period specified by the Postal Service.

946.4 Other Services

946.41 *Reserved*

946.5 Fees

946.51 The fee for Restricted Delivery service is set forth in Fee Schedule 946.

946.52 The fee (or communications charges) will not be refunded for failure to provide restricted delivery service when requested after mailing, due to prior delivery.

947 CERTIFICATE OF MAILING

947.1 Definition

947.11 Certificate of Mailing service furnishes evidence that mail has been presented to the Postal Service for mailing.

947.2 Availability

947.21 Certificate of Mailing service is available for matter sent using any class of mail, except Regular and Nonprofit Presort category mail entered as Customized Market Mail under sections 321.22 and 323.22.

947.22 Service under this section for Parcel Post subclass mail entered under section 521.27 or 521.28 is restricted to the mailer that enters the returned parcel. The addressee may not purchase this service.

947.3 Included Service

947.31 The mailer may obtain a copy of a Certificate of Mailing on terms specified by the Postal Service.

947.4 Limitations

947.41 The service does not entail retention of a record of mailing by the Postal Service and does not provide evidence of delivery.

947.5 Other Services

947.51 The following services, if applicable to the subclass of mail, may be obtained in conjunction with mail sent under this classification schedule upon payment of the applicable fees:

Service	Fee Schedule
a. Parcel Airlift	951
b. Special Handling	952

947.6 Fees

947.61 The fees for Certificate of Mailing service are set forth in Fee Schedule 947.

948 DELIVERY CONFIRMATION**948.1 Definition**

948.11 Delivery Confirmation service provides, upon request, electronic confirmation to the mailer that an article was delivered or that a delivery attempt was made.

948.2 Availability

948.21 Delivery Confirmation service is available for First-Class Letters and Sealed Parcels subclass mail that is parcel-shaped, as specified by the Postal Service; Priority Mail; Standard Mail, in the Regular and Nonprofit subclasses, that [is subject to the residual shape surcharge] pays parcel or not flat-machinable (NFM) rates, except Regular and Nonprofit Presort category mail entered as Customized Market Mail under sections 321.22 and 323.22; and Package Services mail that is parcel-shaped, as specified by the Postal Service, except Parcel Post subclass mail entered under section 521.27 or 521.28.

948.3 Mailer Requirements

948.31 Delivery Confirmation service may be requested only at the time of mailing.

948.32 Mail for which Delivery Confirmation service is requested must meet preparation requirements specified by the Postal Service, and bear a Delivery Confirmation barcode specified by the Postal Service.

948.33 Matter for which Delivery Confirmation service is requested must be deposited in a manner specified by the Postal Service.

948.4 Other Services

948.41 *Reserved*

948.5 Fees

948.51 The fees for Delivery Confirmation service are set forth in Fee Schedule 948.

949 SIGNATURE CONFIRMATION

949.1 Definition

949.11 Signature Confirmation service provides, upon request, electronic confirmation to the mailer that an article was delivered or that a delivery attempt was made, and a copy of the signature of the recipient.

949.2 Availability

949.21 Signature Confirmation is available for Letters and Sealed Parcels subclass mail that is parcel-shaped, as specified by the Postal Service; Priority Mail;

and Package Services mail that is parcel-shaped, as specified by the Postal Service, except Parcel Post or Bound Printed Matter subclass mail entered under section 521.27, 521.28, or 522.27.

949.3 Mailer Requirements

949.31 Signature Confirmation service may be requested only at the time of mailing.

949.32 Mail for which Signature Confirmation service is requested must meet preparation requirements specified by the Postal Service, and bear a Delivery Confirmation barcode specified by the Postal Service.

949.33 Matter for which Signature Confirmation is requested must be deposited in a manner specified by the Postal Service.

949.4 Other Services

949.41 *Reserved*

949.5 Fees

949.51 The fees for Signature Confirmation service are set forth in Fee Schedule 949.

950 PARCEL HANDLING

951 PARCEL AIRLIFT (PAL)

951.1 Definition

951.11 Parcel Airlift service provides for air transportation of parcels on a space available basis to or from military post offices outside the contiguous 48 states.

951.2 Availability

951.21 Parcel Airlift service is available for mail sent under the Package Services Classification Schedule, except Parcel Post subclass mail entered under section 521.27 or 521.28.

951.3 Mailer Requirements

951.31 The minimum physical limitations established for the mail sent under the classification schedule for which postage is paid apply to Parcel Airlift mail. In no instance may the parcel exceed 30 pounds in weight, or 60 inches in length and girth combined.

951.32 Mail sent under this section must be endorsed as specified by the Postal Service.

951.33 Parcel Airlift mail must be deposited in a manner specified by the Postal Service.

951.4 Forwarding and Return

951.41 Parcel Airlift mail sent for delivery outside the contiguous 48 states is forwarded as set forth in section 2030 of the General Definitions, Terms and Conditions. Parcel Airlift mail sent for delivery within the contiguous 48 states is forwarded or returned as set forth in section 353 as appropriate.

951.5 Other Services

951.51 The following services, if applicable to the subclass of mail, may be obtained in conjunction with mail sent under this section upon payment of the applicable fees:

Service	Fee Schedule
a. Certificate of Mailing	947
b. Insurance	943
c. Restricted Delivery (if insured for more than \$[50] <u>200</u>)	946
d. Return Receipt (if insured for more than \$[50] <u>200</u>)	945
e. Special Handling	952

951.6 Fees

951.61 The fees for Parcel Airlift service are set forth in Fee Schedule 951.

952 SPECIAL HANDLING

952.1 Definition

952.11 Special Handling service provides preferential handling to the extent practicable during dispatch and transportation.

952.2 Availability

952.21 Special Handling service is available for mail sent under the following classification schedules:

- a. First-Class Mail; and
- b. Package Services, except Parcel Post subclass mail entered under section 521.27 or 521.28.

952.3 Mailer Requirements

952.31 Mail sent under this section must be identified as specified by the Postal Service.

952.32 Mail sent under this section must be deposited in a manner specified by the Postal Service.

952.33 Special Handling service is mandatory for matter that requires special attention in handling, transportation and delivery.

952.4 Forwarding and Return

952.41 If undeliverable as addressed, Special Handling mail that is forwarded to the addressee is given special handling without requiring payment of an additional handling fee. However, additional postage at the applicable Standard Mail rate is collected on delivery.

952.5 Other Services

952.51 The following services, if applicable to the subclass of mail, may be obtained in conjunction with mail sent under this section upon payment of the applicable fees:

Service	Fee Schedule
a. COD Mail	944
b. Insurance	943
c. Parcel Airlift	951
d. Merchandise Return (shippers only)	932

952.6 Fees

952.61 The fees for Special Handling service are set forth in Fee Schedule 952.

960 STAMPED PAPER

961 STAMPED ENVELOPES

961.1 Definition

961.11 Plain Stamped Envelopes and printed Stamped Envelopes are envelopes with postage thereon offered for sale by the Postal Service.

961.2 Availability

961.21 Stamped Envelopes are available for:

- a. First-Class Mail within the first rate increment[.]; and
- b. Standard Mail mailed at a minimum per-piece rate as specified by the Postal Service.

961.22 Printed Stamped Envelopes may be obtained by special request.

961.3 Fees

961.31 The fees for Stamped Envelopes are set forth in Fee Schedule 961.

962 STAMPED CARDS**962.1 Definition**

962.11 Stamped Cards are cards with postage imprinted or impressed on them, and supplied by the Postal Service for the transmission of messages. Double Stamped Cards consist of two attached cards, one of which may be detached by the receiver and returned by mail as a single Stamped Card.

962.2 Availability

962.21 Stamped Cards are available for First-Class Mail.

962.3 Fees

962.31 The fees for Stamped Cards are set forth in Fee Schedule 962.

970 POSTAL MONEY ORDERS**971 MONEY ORDER SERVICE****971.1 Definition**

971.11 Money Order service provides the customer with an instrument for payment of a specified sum of money.

971.2 Limitations

971.21 The maximum value for which a domestic postal money order may be purchased is \$1,000. Other restrictions on the number or dollar value of postal money order sales, or both, may be imposed by law or under regulations prescribed by the Postal Service.

971.3 Included Services

971.31 A receipt of purchase is provided at no additional cost.

971.32 The Postal Service will replace money orders that are spoiled or incorrectly prepared, regardless of who caused the error, without charge if replaced on the date originally issued.

971.33 If a replacement money order is issued after the date of original issue because the original was spoiled or incorrectly prepared, the applicable money order fee may be collected from the customer.

971.34 Inquiries or claims may be filed by the purchaser, payee, or endorsee.

971.4 Other Services

971.41 *Reserved*

971.5 Fees

971.51 The fees for Money Order service are set forth in Fee Schedule 971.

990 MAILPIECE INFORMATION

991 CONFIRM

991.1 Definition

991.11 Confirm service permits subscribing customers to obtain information, electronically in near real time, regarding when and where mailpieces undergo barcode scans in mail processing operations. Scan information is not guaranteed for every piece of qualifying mail. Destination Confirm is for a subscriber's outgoing mail; Origin Confirm is for reply mail incoming to the subscriber.

991.12 Mailers may purchase Confirm service by subscribing to one or more of the following service levels: Silver, Gold, or Platinum.

991.121 Silver Subscription. The Silver subscription has a term of three months and includes the use of one identification (ID) code and up to 15 million scans. Subscribers may license the use of additional ID codes for a term of three months or until expiration of the subscription, whichever occurs first. Subscribers may license the use of additional scans in blocks of 2 million scans at any time prior to expiration of the subscription.

991.122 Gold Subscription. The Gold subscription has a term of twelve months and includes the use of one ID code and up to 50 million scans. Subscribers may license the use of additional ID codes for a term of three months or until expiration of the subscription, whichever occurs first. Subscribers may license the use of additional scans in blocks of 6 million scans at any time prior to expiration of the subscription.

991.123 Platinum Subscription. The Platinum subscription has a term of twelve months and includes the use of three ID codes and unlimited scans. Subscribers may license the use of additional ID codes for a term of three months or until expiration of the subscription, whichever occurs first.

991.2 Availability

991.21 Confirm service is available to subscribers authorized by the Postal Service under schedule 991 for automation compatible mail entered under the following classification schedules:

Classification Schedule

a. First-Class Mail, including Priority	210
b. Standard Mail	310
c. Periodicals	410
d. Package Services	510

991.3 Mailer Requirements

991.31 Mailers [must become Confirm subscribers by] may subscribe to Confirm after applying to, and being authorized by the Postal Service. Authorization requires that a customer demonstrate the capabilities of producing [mail pieces] mailpieces with Confirm-compatible barcodes as specified by the Postal Service. Destination Confirm mailers may provide electronic notice of entering Confirm mail prior to or contemporaneous with mail entry [all as specified by the Postal Service].

991.32 Qualifying mail must bear [PLANET] a barcode[s] or other coding, as specified by the Postal Service.

991.4 Other Services

991.41 Confirm neither precludes nor requires any other special services.

991.5 Fees

991.51 The fees for Confirm are set forth in Fee Schedule 991.

991.52 A Gold subscription may be upgraded to a Platinum subscription at any time prior to the expiration of the Gold subscription by paying the difference in the respective subscription fees. Upgrading does not extend the term of the underlying subscription.

GENERAL DEFINITIONS, TERMS AND CONDITIONS

1000 GENERAL DEFINITIONS

As used in this Domestic Mail Classification Schedule, the following terms have the meanings set forth below.

1001 Advertising

Advertising includes all material for the publication of which a valuable consideration is paid, accepted, or promised, that calls attention to something for the purpose of getting people to buy it, sell it, seek it, or support it. If an advertising rate is charged for the publication of reading matter or other material, such material shall be deemed to be advertising. Articles, items, and notices in the form of reading matter inserted in accordance with a custom or understanding that textual matter is to be inserted for the advertiser or his products in the publication in which a display advertisement appears are deemed to be advertising. If a publisher advertises his own services or publications, or any other business of the publisher, whether in the form of display advertising or editorial or reading matter, this is deemed to be advertising.

1002 Aspect Ratio

Aspect ratio is the ratio of width to length.

1003 Bills and Statements of Account

1003.1 A bill is a request for payment of a definite sum of money claimed to be owing by the addressee either to the sender or to a third party. The mere assertion of an indebtedness in a definite sum combined with a demand for payment is sufficient to make the message a bill.

1003.2 A statement of account is the assertion of the existence of a debt in a definite amount but which does not necessarily contain a request or a demand for payment. The amount may be immediately due or may become due after a certain time or upon demand or billing at a later date.

1003.3 A bill or statement of account must present the particulars of an indebtedness with sufficient definiteness to inform the debtor of the amount he is required for acquittal of the debt. However, neither a bill nor a statement of account need state the precise amount if it contains sufficient

information to enable the debtor to determine the exact amount of the claim asserted.

1003.4 A bill or statement of account is not the less a bill or statement of account merely because the amount claimed is not in fact owing or may not be legally collectible.

1004 Girth

Girth is the measurement around a piece of mail at its thickest part.

1005 Invoice

An invoice is a writing showing the nature, quantity, and cost or price of items shipped or sent to a purchaser or consignor.

1006 Permit Imprints

Permit imprints are printed indicia indicating postage has been paid by the sender under the permit number shown.

1007 Preferred Rates

Preferred rates are the reduced rates established pursuant to 39 U.S.C. 3626.

1008 ZIP Code

The ZIP Code is a numeric code that facilitates the sortation, routing, and delivery of mail.

1009 Nonprofit Organizations and Associations

Nonprofit organizations or associations are organizations or associations not organized for profit, none of the net income of which benefits any private stockholder or individual, and which meet the qualifications set forth below for each type of organization or association. The standard of primary purpose applies to each type of organization or association, except veterans' and fraternal. The standard of primary purpose requires that each type of organization or association be both organized and operated for the primary purpose. The following are the types of organizations or associations that may qualify as authorized nonprofit organizations or associations.

- a. Religious. A nonprofit organization whose primary purpose is one of the following:
 - i. To conduct religious worship;
 - ii. To support the religious activities of nonprofit organizations whose primary purpose is to conduct religious worship; or
 - iii. To perform instruction in, to disseminate information about, or otherwise to further the teaching of particular religious faiths or tenets.
- b. Educational. A nonprofit organization whose primary purpose is one of the following:
 - i. The instruction or training of the individual for the purpose of improving or developing his capabilities; or
 - ii. The instruction of the public on subjects beneficial to the community.

An organization may be educational even though it advocates a particular position or viewpoint so long as it presents a sufficiently full and fair exposition of the pertinent facts to permit an individual or the public to form an independent opinion or conclusion. On the other hand, an organization is not educational if its principal function is the mere presentation of unsupported opinion.

- c. Scientific. A nonprofit organization whose primary purpose is one of the following:
 - i. To conduct research in the applied, pure or natural sciences; or
 - ii. To disseminate systematized technical information dealing with applied, pure or natural sciences.
- d. Philanthropic. A nonprofit organization primarily organized and operated for purposes beneficial to the public. Philanthropic organizations include, but are not limited to, organizations that are organized for:
 - i. Relief of the poor and distressed or of the underprivileged;
 - ii. Advancement of religion;

- iii. Advancement of education or science;
- iv. Erection or maintenance of public buildings, monuments, or works;
- v. Lessening of the burdens of government;
- vi. Promotion of social welfare by organizations designed to accomplish any of the above purposes or:
 - (A) To lessen neighborhood tensions;
 - (B) To eliminate prejudice and discrimination;
 - (C) To defend human and civil rights secured by law; or
 - (D) To combat community deterioration and juvenile delinquency.
- e. Agricultural. A nonprofit organization whose primary purpose is the betterment of the conditions of those engaged in agriculture pursuits, the improvement of the grade of their products, and the development of a higher degree of efficiency in agriculture. The organization may advance agricultural interests through educational activities; the holding of agricultural fairs; the collection and dissemination of information concerning cultivation of the soil and its fruits or the harvesting of marine resources; the rearing, feeding, and management of livestock, poultry, and bees, or other activities relating to agricultural interests. The term agricultural nonprofit organization also includes any nonprofit organization whose primary purpose is the collection and dissemination of information or materials relating to agricultural pursuits.
- f. Labor. A nonprofit organization whose primary purpose is the betterment of the conditions of workers. Labor organizations include, but are not limited to, organizations in which employees or workmen participate, whose primary purpose is to deal with employers concerning grievances, labor disputes, wages, hours of employment and working conditions.
- g. Veterans'. A nonprofit organization of veterans of the armed services of the United States, or an auxiliary unit or society of, or a trust or foundation for, any such post or organization.
- h. Fraternal. A nonprofit organization that meets all the following criteria:

- i. Has as its primary purpose the fostering of brotherhood and mutual benefits among its members;
- ii. Is organized under a lodge or chapter system with a representative form of government;
- iii. Follows a ritualistic format; and
- iv. Is comprised of members who are elected to membership by vote of the members.

2000 DELIVERY OF MAIL

2010 Delivery Services

The Postal Service provides the following modes of delivery:

- a. Caller service. The fees for caller service are set forth in Fee Schedule 921.
- b. Carrier delivery service.
- c. General delivery.
- d. Post office box service. The fees for post office box service are set forth in Fee Schedule 921.
- e. Parcel Select Return Service. The rates for Parcel Select Return Service are set forth in Rate Schedules 521.2F and 521.2G.

2020 Conditions of Delivery

2021 General. Except as provided in section 2022, 2030, and 3030, mail will be delivered as addressed unless the Postal Service is instructed otherwise by the addressee in writing.

2022 Refusal of Delivery. The addressee may control delivery of his mail. The addressee may refuse to accept a piece of mail that does not require a delivery receipt at the time it is offered for delivery or after delivery by returning it unopened to the Postal Service. For mail that requires a delivery receipt, the addressee or his representative may read and copy the name of the sender of registered, insured, certified, COD, return receipt, and Express Mail prior to accepting delivery. Upon signing the delivery receipt the piece

may not be returned to the Postal Service without the applicable postage and fees affixed.

- 2023** **Receipt.** If a signed receipt is required, mail will be delivered to the addressee (or competent member of his family), to persons who customarily receive his mail or to one authorized in writing to receive the addressee's mail.
- 2024** **Jointly Addressed Mail.** Mail addressed to several persons may be delivered to any one of them. When two or more persons make conflicting orders for delivery for the same mail, the mail shall be delivered as determined by the Postal Service.
- 2025** **Commercial Mail Receiving Agents.** Mail may be delivered to a commercial mail receiving agency on behalf of another person. In consideration of delivery of mail to the commercial agent, the addressee and the agent are considered to agree that:
- a. No change-of-address order will be filed with the post office when the agency relationship is terminated; and
 - b. When remailed by the commercial agency, the mail is subject to payment of new postage.
- 2026** **Mail Addressed to Organizations.** Mail addressed to governmental units, private organizations, corporations, unincorporated firms or partnerships, persons at institutions (including but not limited to hospitals and prisons), or persons in the military is delivered as addressed or to an authorized agent.
- 2027** **Held Mail.** Mail will be held for a specified period of time at the office of delivery upon request of the addressee, unless the mail:
- a. Has contrary retention instructions;
 - b. Is perishable; or
 - c. Is registered, COD, insured, return receipt, certified, or Express Mail for which the normal retention period expires before the end of the specified holding period.

2030 Forwarding and Return

2031 Forwarding. Forwarding is the transfer of undeliverable-as-addressed mail to an address other than the one originally placed on the mailpiece. All post offices will honor change-of-address orders for a period of time specified by the Postal Service.

2032 Return. Return is the delivery of undeliverable-as-addressed mail to the sender. Parcel Select Return Service mail does not constitute returned mail within the meaning of this section.

2033 Applicable Provisions. The provisions of sections 150, 250, 350, 450, 550, 935 and 936 apply to forwarding and return.

2034 Forwarding for Postal Service Adjustments. When mail is forwarded due to Postal Service adjustments (such as, but not limited to, the discontinuance of the post office of original address, establishment of rural carrier service, conversion to city delivery service from rural, readjustment of delivery districts, or renumbering of houses and renaming of streets), it is forwarded without charge for a period of time specified by the Postal Service.

3000 POSTAGE AND PREPARATION

3010 Packaging

Mail must be packaged so that:

- a. The contents will be protected against deterioration or degradation;
- b. The contents will not be likely to damage other mail, Postal Service employees or property, or to become loose in transit;
- c. The package surface must be able to retain postage indicia and address markings; and
- d. It is marked by the mailer with a material that is neither readily water soluble nor easily rubbed off or smeared, and the marking will be sharp and clear.

3020 Envelopes

Paper used in the preparation of envelopes may not be of a brilliant color. Envelopes must be prepared with paper strong enough to withstand normal handling.

3030 Payment of Postage and Fees

3031 Postage Payment. Postage must be fully prepaid on all mail at the time of mailing, except as authorized by law or this Schedule. The Forever Stamp, described in section 3032, is intended for the prepayment of postage for the first ounce of First-Class Mail single-piece letter mail, and otherwise may be used for the prepayment of postage. Except as authorized by law or this Schedule, mail deposited without prepayment of sufficient postage shall be delivered to the addressee subject to payment of deficient postage, returned to the sender, or otherwise disposed of as specified by the Postal Service. Mail deposited without any postage affixed will be returned to the sender without any attempt at delivery.

3032 Forever Stamp. The Forever Stamp is sold at the prevailing rate for single-piece letters, first ounce, in Rate Schedule 221. The Forever Stamp is an adhesive stamp within the meaning of section 3040. Once purchased, the Forever Stamp may be used for postage equal to the prevailing rate, at the time of use, for single-piece letters, first ounce, in Rate Schedule 221.

3040 Methods for Paying Postage and Fees

Postage for all mail may be prepaid with postage meter indicia, adhesive stamps, permit imprint, or other payment methods specified by the Postal Service. Prior authorization for use of certain payment methods may be required, as specified by the Postal Service. A fee is charged for authorization to use a permit imprint, as set forth in Schedule 1000.

3050 Parcel Select Return Service and Bound Printed Matter Return Service Postage

Parcel Select Return Service mail that is entered under section 521.27 or 521.28 may be retrieved by the permit holder prior to payment of postage. With the exception of fees charged for Certificate of Mailing service, postage on mail in these categories will be determined and paid by the permit holder following receipt, in a manner and within a time specified by the Postal Service.

For Parcel Select Return Service mail that is entered under section 521.27 or 521.28, Certificate of Mailing service may be purchased and fees paid by the mailer entering the returned parcel.

3060 Special Service Fees

Fees for special services may be prepaid in any manner appropriate for the class of mail indicated or as otherwise specified by the Postal Service.

3070 Marking of Unpaid Mail

Matter authorized for mailing without prepayment of postage must bear markings identifying the class of mail service. Matter so marked will be billed at the applicable rate of postage set forth in this Schedule. Matter not so marked will be billed at the applicable First-Class rate of postage.

3080 Refund of Postage

When postage and special service fees have been paid on mail for which no service is rendered for the postage or fees paid, or collected in excess of the lawful rate, a refund may be made. There shall be no refund for registered, COD, general insurance, and Express Mail Insurance fees when the article is withdrawn by the mailer after acceptance. In cases involving returned articles improperly accepted because of excess size or weight, a refund may be made.

3090 Calculation of Postage

When a rate schedule contains per-piece and per-pound rates, the postage shall be the sum of the charges produced by those rates. When a rate schedule contains a minimum per-piece rate and a pound rate, the postage shall be the greater of the two. When the computation of postage yields a fraction of a cent in the charge, the next higher whole cent must be paid.

4000 POSTAL ZONES

4010 Geographic Units of Area

In the determination of postal zones, the earth is considered to be divided into units of area 30 minutes square, identical with a quarter of the area formed by the intersecting parallels of latitude and meridians of longitude. The distance between these units of area is the basis of the postal zones.

4020 Measurement of Zone Distances

The distance upon which zones are based shall be measured from the center of the unit of area containing the dispatching sectional center facility or multi-ZIP coded post office not serviced by a sectional center facility. A post office of mailing and a post office of delivery shall have the same zone relationship as their respective sectional center facilities or multi-ZIP coded post offices, but this shall not cause two post offices to be regarded as within the same local zone.

4030 Definition of Zones

4031 Local Zone. The local zone applies to mail mailed at any post office for delivery at that office; at any city letter carrier office or at any point within its delivery limits for delivery by carriers from that office; at any office from which a rural route starts for delivery on the same route; and on a rural route for delivery at the office from which the route starts or on any rural route starting from that office.

4032 First Zone. The first zone includes all territory within the quadrangle of entry in conjunction with every contiguous quadrangle, representing an area having a mean radial distance of approximately 50 miles from the center of a given unit of area. The first zone also applies to mail between two post offices in the same sectional center.

4033 Second Zone. The second zone includes all units of area outside the first zone lying in whole or in part within a radius of approximately 150 miles from the center of a given unit of area.

4034 Third Zone. The third zone includes all units of area outside the second zone lying in whole or in part within a radius of approximately 300 miles from the center of a given unit of area.

4035 Fourth Zone. The fourth zone includes all units of area outside the third zone lying in whole or in part within a radius approximately 600 miles from the center of a given unit of area.

4036 Fifth Zone. The fifth zone includes all units of area outside the fourth zone lying in whole or in part within a radius of approximately 1,000 miles from the center of a given unit of area.

4037 **Sixth Zone.** The sixth zone includes all units of area outside the fifth zone lying in whole or in part within a radius of approximately 1,400 miles from the center of a given unit of area.

4038 **Seventh Zone.** The seventh zone includes all units of area outside the sixth zone lying in whole or in part within a radius of approximately 1,800 miles from the center of a given unit of area.

4039 **Eighth Zone.** The eighth zone includes all units of area outside the seventh zone.

4040 **Zoned Rates**

Except as provided in section 4050, rates according to zone apply for zone-rated mail sent between Postal Service facilities including armed forces post offices, wherever located.

4050 **APO/FPO Mail**

4051 **General.** Except as provided in section 4052, the rates of postage for zone-rated mail transported between the United States, or the possessions or territories of the United States, on the one hand, and Army, Air Force and Fleet Post Offices on the other, or among the latter, shall be the applicable zone rates for mail between the place of mailing or delivery and the city of the postmaster serving the Army, Air Force or Fleet Post Office concerned.

4052 **Transit Mail.** The rates of postage for zone-rated mail that is mailed at or addressed to an Armed Forces post office and is transported directly to or from Armed Forces post offices at the expense of the Department of Defense, without transiting any of the 48 contiguous states (including the District of Columbia), shall be the applicable local zone rate; provided, however, that if the distance from the place of mailing to the embarkation point or the distance from the point of debarkation to the place of delivery is greater than the local zone for such mail, postage shall be assessed on the basis of the distance from the place of mailing to the embarkation point or the distance from the point of debarkation to the place of delivery of such mail, as the case may be. The word "transiting" does not include enroute transfers at coastal gateway cities which are necessary to transport military mail directly between military post offices.

5000 PRIVACY OF MAIL

5010 First-Class and Express Mail

Matter mailed as First-Class Mail or Express Mail shall be treated as mail which is sealed against postal inspection and shall not be opened except as authorized by law.

5020 All Other Mail

Matter not paid at First-Class Mail or Express Mail rates must be wrapped or secured in the manner specified by the Postal Service so that the contents may be examined. Mailing of sealed items as other than First-Class Mail or Express Mail is considered consent by the sender to the postal inspection of the contents.

6000 MAILABLE MATTER

6010 General

Mailable matter is any matter which:

- a. Is not mailed in contravention of 39 U.S.C. Chapter 30, or of 17 U.S.C. 109;
- b. While in the custody of the Postal Service is not likely to become damaged itself, to damage other pieces of mail, to cause injury to Postal Service employees or to damage Postal Service property; and
- c. Is not mailed contrary to any special conditions or limitations placed on transportation or movement of certain articles, when imposed under law by the U.S. Department of the Treasury; U.S. Department of Agriculture; U.S. Department of Commerce; U.S. Department of Health and Human Services, U.S. Department of Transportation; and any other Federal department or agency having legal jurisdiction.

6020 Minimum Size Standards

Except as provided in sections 321.22 and 323.22, the following minimum size standards apply to all mailable matter:

- a. all items must be at least 0.007 inch thick; and
- b. all items, other than keys and identification devices, which are 0.25 inch thick or less must be
 - i. rectangular in shape;
 - ii. at least 3.5 inches in width; and
 - iii. at least 5 inches in length.

6030 Maximum Size and Weight Standards

Where applicable, the maximum size and weight standards for each class or subclass of mail are set forth in sections 130, 230, 330, 430, 521.6, and 530. Additional limitations may be applicable to specific subclasses, and rate and discount categories as provided in the eligibility provisions for each subclass or category.

