

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

RECEIVED

FEB 11 4 46 PM '00

POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES, 2000

Docket No. R2000-1

RESPONSE OF UNITED STATES POSTAL SERVICE
WITNESS TAYMAN TO INTERROGATORIES OF
THE DIRECT MARKETING ASSOCIATION, INC.
(DMA/USPS-T9-1-19)

The United States Postal Service hereby provides the responses of witness Tayman to the following interrogatories of the Direct Marketing Association, Inc.: DMA/USPS-T9-1-19, filed on January 28, 2000. Interrogatories DMA/USPS-20-21 were redirected to witness Kashani.

Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.

Chief Counsel, Ratemaking



Scott L. Reiter

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-1. On page 2 of your testimony you state, "This absence of additional obligations to the Federal Government, coupled with the benefits of the 1992 restructuring and debt refinancing, moderate increases in the cost of labor and other resources, improved service, and continued growth in mail volume and revenue, have enabled the Postal Service to reverse the historical pattern of rate cycle losses." Please explain how improved service has help enable "the Postal Service to reverse the historical pattern of rate cycle losses."

RESPONSE:

In my opinion, the statement is intuitive. Improved service results in satisfied customers, which results in more revenue than would have been the case if service had not improved.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-2. Table 1 on pages 2 and 3 of your testimony shows the net income and the equity of the Postal Service from 1989-1998. Please provide a version of this table that starts in 1989 but includes 1999.

RESPONSE:

Please refer to Exhibit USPS 9L.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-3. For each year in Table 1, please provide the book value of the real estate that the Postal Service owns. Please also provide an estimate of the market value of the real estate.

RESPONSE:

Please refer to the attached workpaper for the book value of Postal Service buildings. I have no basis to estimate the market value of USPS land and buildings.

Book Value of USPS Real Property
Dollars in Millions

Attachment to Response
to DMA/USPS-T9-3.

Fiscal Year	Real Property		Accumulated Depreciation	Book Value	Source
	Buildings	Land			
FY 89	6,955	1,210	1,830	6,335	Docket R90-1, USPS Exhibit 15B
FY 90	7,434	1,302	2,017	6,719	USPS Financial Records
FY 91	8,401	1,492	2,230	7,663	Docket R94-1, USPS Exhibit 8B
FY 92	9,481	1,649	2,466	8,665	Docket R94-1, USPS Exhibit 8B
FY 93	9,951	1,715	2,742	8,924	Docket R94-1, USPS Exhibit 8B
FY 94	11,280	1,901	3,026	10,155	Docket R97-1, USPS LR H-12 Ch. 13
FY 95	11,917	1,997	3,359	10,555	Docket R97-1, USPS LR H-12 Ch. 13
FY 96	12,923	2,107	3,717	11,314	Docket R97-1, USPS LR H-12 Ch. 13
FY 97	13,911	2,178	4,161	11,928	Docket R2000-1, USPS LR I-127 Ch. 13
FY 98	15,123	2,286	4,559	12,850	Docket R2000-1, USPS LR I-127 Ch. 13
FY 99	16,513	2,407	5,023	13,897	Docket R2000-1, USPS LR I-127 Ch. 13

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-4. Speaking of the period 1989-1998 on page 3 of your testimony, you say "Despite the fact that this ten year period includes this unprecedented four-year string of net incomes and the three highest net incomes ever earned by the Postal Service, a cumulative \$346 million net loss was incurred. This means the Postal Service failed to make ground against its prior years' losses recovery objective during the last decade." Please assume that net income for FY 2000 is the 66 million that the Postal Service has estimated. On this assumption, please provide the net loss or gain for the ten-year period 1991 – 2000. Did equity increase in this period?

RESPONSE:

Assuming a net income of \$65.603 million for FY 2000, the ten year period FY 91-2000 would have a net income of \$897.480 million. I would also note that equity would still remain negative through FY 2000 under this assumption and most importantly, cumulative losses are still \$2.414 billion (see Table 53 on page 48 of my testimony).

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-5. Table 5 on page 6 of your testimony compares total assets and liabilities of the Postal Service. Are all assets of the Postal Service valued at book value? For real estate, does market value exceed book value?

RESPONSE:

Yes. All assets are valued at book value. As indicated in my response to T9-3, I have no basis to estimate market value.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-6. On page 7 of your testimony you say, "As reflected in Table 6, key national indicators of service performance from the Residential Customer Satisfaction Measurement System have all shown improvement since Quarter II of Fiscal Year 1994. In general, the attributes of customer satisfaction which make up the Residential Customer Satisfaction Measurement System have consistently improved at the same time unprecedented financial results have been achieved." What are "the attributes of customer satisfaction" which make up the Residential Customer Satisfaction system? What percentage of the revenues of the USPS do residential customers pay? By business mailers? Please provide any information or data you having bearing on the satisfaction of business mailers. Do you think business mailers are pleased that the USPS has proposed rate increase that are larger than the inflation rate?

RESPONSE:

The attributes of the customer satisfaction measurement system focus on the customer's experience with our services, products, and personnel. The measurement includes specific questions on timely delivery, reliability, value of products and services, and overall satisfaction. The information requested pertaining to the satisfaction of business mailers can be found on page 48 of the "1998 Comprehensive Statement on Postal Operations". Similar data for FY 97 can be found on page 46 of the "1997 Comprehensive Statement on Postal Operations".

I am not aware of any source for the percentage of revenues that residential and business customers pay. Regarding the last part of this question, I would assume that all mailers would prefer rate increases below the rate of inflation.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-7. On page nine of your testimony you say, "Estimated expenses of \$62.400 billion used in this filing were within 0.06 percent of the actual FY 1999 expenses of \$62.363 billion." Does this mean that costs for 1999 were \$36 million less than estimated by the roll forward program?

RESPONSE:

No. The \$62.363 billion reflected on page 11 of my testimony as actual FY 99 expenses should be \$62.392 billion. This is a difference of only \$8 million or .01 % from the amount estimated by the rollforward process. See errata filed on January 28, 2000.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-8. Table 10 on page 13 of your testimony shows cost reductions saving of \$475,374 for Clerks and Mailhandlers in the Test Year. How many labor hours does this represent?

RESPONSE:

Please note that Table 10 is on page 14 of my testimony. As reflected in USPS LR I-127, Chapter Va., page 197, estimated clerk/mailhandler workhour savings for the test year are 16.975 million.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-9. Table 10 on page 13 of your testimony shows cost reductions saving of \$151,374 for Carriers in the Test Year. How many labor hours does this represent?

RESPONSE:

Please note that Table 10 is on page 14 of my testimony. As reflected in USPS LR I-127, Chapter Va., page 197, estimated city carrier workhour savings for the test year are 5.123 million.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-10. On page 15 of your testimony you say, "Reduced program expense reflects management's commitment to control costs. There is long term risk, however, in this strategy, as it requires deferral and cancellation of programs that would otherwise be planned to improve the quality of service, increase responsiveness to customers, and build and maintain our infrastructure." Please describe all deferrals and cancellations caused by cost control. Are there also risks in failing to control costs? If so, please describe them.

RESPONSE:

Please note that the quoted statement appears on page 16 of my testimony. My testimony and the Postal Service's filing in this case directly recognize that there are risks in failing to control costs and address those risks by severely curtailing cost growth. As I noted at page 16 of USPS-T-9, the "Other Programs" expense growth in the last rate case was \$3.7 billion over the two years forecast in the last rate case, compared to the \$1.5 billion expense growth projected in this case over Fiscal Years 2000 and 2001. I further noted that the "Other Programs" expense growth in the current case is concentrated in corporatewide personnel costs, depreciation and interest expense. Corporatewide personnel cost growth is primarily driven by factors such as inflation, actuarial changes and labor contracts that are not subject to management control. Depreciation and interest expense are primarily driven by the Postal Service's capital program, which funds productivity improvements and maintenance and expansion of infrastructure. By limiting "Other Programs" cost growth to expenditures that are driven by exogenous factors, and expenditures

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-10. continued

are needed to maintain ongoing operations or to achieve cost savings, the Postal Service has reduced its exposure to the risks of not controlling costs.

Specific operating and capital programs that were deferred or cancelled include the following:

1. Associate Office Infrastructure – 524 Phase I sites were deferred to Phase II, completion of Phase II was deferred, and the Phase II target was reduced from 8,376 to 7,635.
2. Corporate Call Management – The implementation schedule has been extended to nearly two years. Full national coverage will now be achieved in FY 2004 instead of FY 2002.
3. International Service Centers – Eliminating future funding cancelled plans to activate the Dulles International Service Center.
4. Point of Service – Deployment schedule deferred 18 months.
5. Remitco – Permanently closed.
6. Miscellaneous Headquarters Programs – expenditures reduced by \$130 million in FY 2000.
7. Priority Mail Processing Centers – No facility deployments beyond existing geographic coverage.

The principal risks associated with failing to control costs relate to not serving customers well, weakened financial performance and reduced competitiveness.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-11. On page 15 of your testimony you say "Clerk overtime is assumed to continue at the FY 1998 level through the Test Year." How much overtime was there in 1998? What is the cost of clerk overtime in the Test Year? In 2000? Given the increased productivity of systems described by witness Kingsley, why is overtime not declining.

RESPONSE:

The statement to which you have referred can be found on page 17. The statement means that the level of overtime workyears as a percentage of total workyear and work related workyears, is assumed to remain at the FY 1998 level through the test year. While the productivity improvements discussed by witness Kingsley impact the total number of workyears, they do not affect the mix of workyears. A variety of factors, including operational and scheduling constraints and the flexibility needed to effectively manage fluctuations in workload, requires a certain amount of overtime. I believe that the assumptions regarding overtime levels are reasonable and appropriate.

The table below shows the amount of clerk overtime workyears for FY 1998 through the Test Year. The absolute number of total, work related, and overtime clerk workyears increases slightly in FY 99, and then declines through the test year. The proportion of overtime workyears to the other totals remains constant. To see the impact of cost reductions and other sources of change on total workyears please refer to Exhibit USPS-9P.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-11. continued

	FY 1998	FY 1999	FY 2000	FY 2001 BR	FY 2001 AR
Total Workyears	324,745	326,762	326,421	322,450	317,519
Work Related Workyears	282,354	283,891	283,660	280,494	276,151
Overtime Workyears	25,615	25,959	25,932	25,624	25,252
Overtime as a % of Work Related Workyears	9.1%	9.1%	9.1%	9.1%	9.1%

Source: USPS LR I-127, Chapter 10e.

Note: FY 98 excludes Special Delivery

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-12. When were the inflation estimates in Table 14 prepared? Has DRI provided you with more recent estimates? If so, please provide them.

RESPONSE:

Please refer to page 21, line 8 of USPS T-9. The reference of "1199" translates to "November 1999". DRI updates its forecasts periodically and makes this information available to its subscribers. DRI can be contacted at:

Standard & Poor's DRI
1200 G St. NW
Washington, DC 2005

Phone: 202- 663-7600

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-13. On page 42 of your testimony you say, "To achieve our net income plan for the year required significant cost cutting. This was in addition to funding greater than expected costs associated with the year 2000 computer transition." Is "year 2000 computer transition " synonymous with Y2K? If not, please explain how it is different. How much did the Postal Service spend on year 2000 computer transition in FY 98? In FY 99? What is the estimated cost for year 2000 computer transition in FY 00? In TYAR?

RESPONSE:

Yes, "year 2000 computer transition" is synonymous with Y2K. The Postal Service incurred costs of approximately \$88.6 million in FY 98 and \$267.0 million in FY 99 for Y2K. The FY 00 estimate for Y2K costs included in this filing is \$42.6 million. There are no costs estimated for Y2K in TYAR in this filing.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-14. Please refer to the first paragraph of page 27 of LR-I-126:

- a. Please confirm that this paragraph implies that from FY 1999 to FY 2000 the rate of growth in the costs for the "Year 2000 Software" program will outstrip inflation by \$1.558 million.

- b. Please confirm that there is no "Year 2000 Software" cost reduction or other program adjustment for FY 2001.

Please confirm that costs for "Year 2000 Software" are in cost Segment 16. If they are not, please provide the cost segment and component where they are.

RESPONSE:

- a. Not confirmed. The paragraph was in error and has been deleted.
See errata filed on January 28, 1999.

- b. Not confirmed. See my response to part a.

Virtually all the costs related to the "Year 2000 software" program are in cost segment 16.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-15. In discussing the size of the contingency you selected, on page 42 you state, " The outlook for the future is even more challenging. Volume growth is below historical norms and projections of Fiscal Year 2000 require workyears be held at the Fiscal Year 1999 level while mail volume and the delivery network continue to grow. In the Test Year after rates, a 1.5 percent workyear reduction is projected. It will be a challenge to achieve this reduction. Many other uncertainties exist and there also appear to be significant new pressures on salary and benefit cost levels. " Please confirm that volume growths below historic norms have been accounted for in your projection of both Test Year costs and revenues. Please confirm that mail volume and delivery network growth have been accounted for in your projection of both Test Year costs and revenues. Please describe the "other uncertainties" you cite. Please confirm that you projection of Test Year costs takes into account higher levels of *employee benefits than the USPS currently experiences.*

RESPONSE:

Please note that the quoted statement appears on page 43 of my testimony. I confirm that estimated volume and delivery network changes and changes in the level of costs in employee benefits have been accounted for in the estimation of test year revenues and expenses. A number of significant uncertainties are discussed specifically on pages 43 and 44 of my testimony. There is also the uncertainty surrounding totally unknown adverse events against which the Postal Service must be protected.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-16. In discussing the size of the contingency you state, "It also keeps the cumulative rate increases over the last two rate cycles below the cumulative rate of general inflation." Please provide calculations supporting your assertion that cumulative rate increases are below the rate of general inflation.

RESPONSE:

As reflected in the Table below, prices as measured by CPI-U (All Urban Consumers) rose 9.3% from January 1995 through January 1999 and are projected to rise an additional 4.8% from January 1999 through January 2001. This produces a cumulative 14.6% for the combined periods. The rates filed in this case request an average price increase of 6.4% and the rates from R97-1 averaged 2.9%. The cumulative rate increase would then be 9.5%, which is a full five percentage points below inflation. [9.5% is the geometric product of 2.9% and 6.4%, i.e., .094 = (1.029)(1.064)-1.]

Rate Cycle	Time Period	Cumulative Inflation	Average Rate Increase	CPI-U
R94-1 to R97-1	Jan 95 – Jan 99	9.3%	2.9%	450.30
R97-1 to R2000-1	Jan 99 – Jan 01	4.8%	6.4%	492.30
R97-1 to R2000-1	Jan 95 – Jan 01	14.6%	9.5%	516.13

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-17. Please describe all segments for your market in which foreign postal operations are competing. Please provide an estimate of how much of your revenues they have captured. Please provide an estimate of how much of your market they will have captured in the Test Year.

RESPONSE:

A number of foreign postal administrations have been competing aggressively against the USPS in the printed matter and letter mail segments in the United States. They also compete in the small packet market. In the parcel market, the postal competition has been minimal to date but we expect this to grow.

Following are the major postal competitors:

- **Royal Mail (UK)**
Royal Mail is incorporated in the US and is headquartered in New York, NY. It operates 13 sales offices around the country through which it markets worldwide distribution services.
- **Deutsche Post AG (Germany)**
The US headquarters of Deutsche Post is located in Fairfax, VA. Deutsche Post purchased two of the leading international mailing companies in the US, Global Mail of Sterling, VA and Yellowstone International of Elk Grove Village, IL. In addition, it purchased one of the country's largest freight forwarding companies, Air Express International. Deutsche Post provides worldwide distribution services.
- **TPG (Netherlands)**
TPG is a unit of PTT Post and is the result of the consolidation of TNT and Interpost. Although its organizational structure has evolved over the years, the Dutch postal administration has been active in the US market longer than any other competitor, providing a variety of worldwide distribution and value-added services.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-17. continued

- **Scandinavian Publication Distribution Service - SPDS (Denmark)**
This company, headquartered near Newark, NJ, has traditionally marketed its worldwide distribution services through wholesalers.

- **Canada Post Corporation**
Canada Post offers its Canadian distribution services directly to US customers through sales representatives that cover assigned geographic territories around the country.

Other foreign postal administrations known to have sales representation in the US include Swiss Post (Switzerland), La Poste (France) and Nordic.

I am unable to calculate how much Postal Service revenue has been or will be diverted as a result of foreign postal administration initiatives.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T9-18. Please explain how "the increasingly competitive environment in which the Postal Service operates" requires a higher contingency. Might a business in an increasingly competitive environment find ways to reduce their costs so they can remain competitive?

RESPONSE:

I did not say that an "increasingly competitive environment " requires a higher contingency. I did say that "the increasingly competitive environment in which the Postal Service operates" "further supports" the judgment that a contingency closer to the historical norm is warranted.

The purpose of the contingency provision is to provide a cushion for adverse events. The rapidly changing and increasingly competitive environment since the last rate case filing makes the Postal Service's financial performance more uncertain. At the same time, the Postal Service, like other businesses, is finding ways to control costs so that it may maintain its competitiveness. As an example of this, please refer to USPS-T-9 at page 16 where I describe the drop in the growth of "Other Programs" expense and indicate that this cost growth has been more than offset by cost reduction programs. So yes, I agree that businesses in increasingly competitive environments might find ways to decrease costs in order to stay competitive and I also believe the Postal Service is doing that.

**RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
DIRECT MARKETING ASSOCIATION, INC.**

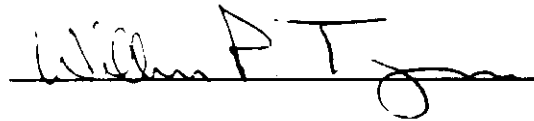
DMA/USPS-T9-19. Please refer to page 44 of your testimony where you state, "I am convinced that variance analysis cannot be relied upon in a vacuum as the basis for determining an appropriate contingency level. Variance analysis can only show us what happened in the past, and should not be relied upon exclusively to determine the prudent amount of cushion against unforeseen events in the Test Year." Do these two sentences mean that variance analysis does have a role to play in determining the size of the contingency? If not, please reconcile this view with these two sentences.

RESPONSE:

These two sentences, which can be found on page 45 of my testimony, mean that management may choose to review past performance when determining the appropriate size of the contingency. However, past performance would play a very minor role, if any, "cannot be relied upon in a vacuum", and "should not be relied upon exclusively", in determining the size of the contingency. As I also state on page 45 of my testimony, "no matter what results an historical variance analysis produces, it is not appropriate to use historical data to determine the size of the contingency in lieu of management's judgment about the future".

DECLARATION

I, William P. Tayman, declare under penalty of perjury that the foregoing answers are true and correct, to the best of my knowledge, information, and belief.

A handwritten signature in black ink, appearing to read "William P. Tayman", is written over a horizontal line.

Dated: 2-11-2000

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

Scott L. Reiter / EMB
Scott L. Reiter

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1137
(202) 268-2999 Fax -5402
February 11, 2000