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

RECEIVED
MAR 3 4 42 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 ALLIANCE OF NONPROFIT MAILERS (ANM/USPS-T9-29-44)

The United States Postal Service hereby provides the responses of witness Tayman to the following interrogatories of the Alliance of Nonprofit Mailers: ANM/USPS-T9-29-44, filed on February 18, 2000.

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

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1137
(202) 268-2999; Fax -5402
March 3, 2000

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-29. Please refer to your response to ANM/USPS-T9-1, where you state that "Exhibit 9F indicates that $3.704 billion in new debt is required to finance capital outlays without a rate increase. Under the proposed rate increase, no borrowing would be necessary." Since Exhibit USPS-9F indicates that depreciation and amortization in FY 2001 will amount to only $2.154 billion, while purchase of property and equipment will be $3.746 billion, is it reasonable to infer that monies derived from the provision for contingency will be used to fund the $1.592 billion difference? Please explain any answer that is not an unqualified affirmative.

RESPONSE:

Your inference is incorrect. As discussed on page 43 of my testimony, the contingency is to protect against unforeseen events. In both the before and after rate scenarios, it is assumed that the amount included for the contingency provision is spent. Accordingly, there are no contingency funds available to finance capital outlays. As reflected in the Postal Service's cash flow forecast (LR I-127 p. 232), the contingency is reflected as a test year expense and cash requirement. In the after rates scenario, enough cash is generated from operations to fully finance the purchase of property and equipment.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-30. In reference to your response to ANM/USPS-T9-2, please provide the following information:

a. What is the highest level of total debt that the Postal Service has ever incurred? That is, what is the closest the Postal Service has ever come to its $15 billion debt ceiling? In what year did that occur?

b. At the end of FY 1999, what was the Postal Service's current debt level in relation to its debt ceiling?

c. Have the Postal Service's capital expenditures for modernization and automation ever been restrained by the $2 billion limitation on the annual net increase in debt for capital expenditures? If so, in what year(s)? If the Postal Service has never been so constrained, then what have been the three years with the highest annual increase in debt for capital expenditures, and how much did the debt increase in those three years?

RESPONSE:

a. Postal Service debt reached its highest level of total debt in FY 93 ($9.7 billion).

b. At the end of FY 1999, the debt level was 46% ($6.9 billion/$15.0 billion) of the debt ceiling. This information is reflected on page 739 of LR I-127 and in my response to ANM/USPS-T9-2.

c. As explained in the response to ANM/USPS-T9-27, I am informed that the annual $2.0 billion capital investment borrowing limit (which was effective beginning with FY 92) has not constrained the capital investment program. For the period covered by the annual debt increase limitation of $2.0 billion, the level of debt increased in FY's 92, 98, and 99. The amounts of increase, which

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF
ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-30. continued

all resulted from capital borrowing, were $1.483 billion, $552 million, and $504 million, respectively. Debt declined in FY's 93-97.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-31. Please refer to your response to ANM/USPS-T9-4.

(a) Are the "two financing plans" referred to in that response identical to the attachment to ANM/USPS-T9-8? If not, please produce the missing documents.

(b) Are the "two financing plans" referred to in your response to ANM/USPS-T9-4 the only documents in the Postal Service's possession, custody or control that are responsive to the question?

RESPONSE:

(a) ANM/USPS-T9-4 requested information on debt financing and ANM/USPS-T9-8 requested information on the capital program and major program initiative. Accordingly, my response to ANM/USPS-T9-4 provided a copy of the financing plan and my response to ANM/USPS-T9-8 provided a copy of the capital plan.

(b) Yes.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-32. Please refer to your response to ANM/USPS-T9-5.

(a) Are the documents referred to in that response identical to the attachment to ANM/USPS-T9-8? If not, please produce the missing documents.

(b) Are the documents referred to in your response to ANM/USPS-T9-5 the only documents in the Postal Service's possession, custody or control that are responsive to the question?

RESPONSE:

(a) See my response to ANM/USPS-T9-31(a).

(b) See my response to ANM/USPS-T9-31(b).

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-33. This is a follow-up to ANM/USPS-T9-7(e). In your response, you state that the asset lives assumed by the Postal Service for personal property range from "3 to 10 years depending on the type of equipment and risk of technological obsolescence," and the asset lives assumed for motor vehicles range from "6 to 12 years depending on the type of vehicle."

(a) Please specify each kind of personal property that corresponds with each life within the range of 3 to 10 years.

(b) Please specify each kinds of motor vehicles that corresponds with each life within the range of 6 to 12 years.

RESPONSE:

(a & b)Please see LR-I-224, Personal Property and Motor Vehicle Asset Life Listing.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-34. This is a follow-up to ANM/USPS-T9-7(f). The question asked for "all documents containing" the justification for the asset lives assumed by the Postal Service. In response, you assert that the asset lives are based on six factors, but you have produced no documents.

(a) Please produce the documents requested by the original question.

(b) Please produce studies, analyses, and similar documents sufficient to enable a third party to verify whether the criteria identified in response to ANM/USPS-T9-7(f) justify lives as short as the specific lives referred in question ANM/USPS-T9-7(e).

RESPONSE:

(a) – (b) It is my understanding that service life estimates are developed at the time of the initial equipment buy in conjunction with the criteria defined in my response to ANM/USPS-T9-7(f). A review of the response to ANM/USPS-T9-33 which provides a listing of certain assets and their service lives and salvage values should be sufficient for a third party to assess the reasonableness of established asset lives.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-35. In the last sentence of your answer to ANM/USPS-T9-7(f), you state that the Postal Service's "[d]epreciation expense and the basis for its calculation is reviewed annually in conjunction with the audit conducted by our external auditors and has been found to be in compliance with Generally Accepted Accounting Principles."

(a) Does the Postal Service contend that depreciation lives that satisfy GAAP match the full period during which the depreciated assets are expected to provide service (the regulatory "matching principle")? If so, please produce all documentation on which you rely in support of your position.

(b) Have the Postal Service's "external auditors" – or anyone else – analyzed whether the depreciation lives assumed by the Postal Service in its cost of service studies comply with the matching principle? If so, please produce all documentation.

RESPONSE:

(a) Yes. GAAP requires the matching of revenue and expense. In Accounting Research Bulletin 43, the American Institute of Certified Public Accountants has defined depreciation accounting as "a system of accounting that aims to distribute the cost or other basic value of tangible capital assets, less salvage (if any), over the estimated useful life of the unit (which may be a group of assets) in a systematic and rational manner. It is a process of allocation, not of valuation."

(b) As part of the audit of the Postal Service financial statements, the auditors review the reasonableness of service life estimates for assets. The Postal Service has never received a qualified audit opinion based on service life estimates and to my knowledge has never received a management letter finding from the auditors relative to service life estimates. Accordingly, it would appear that the depreciation

ANM/USPS-T9-35. continued

lives assumed by the Postal Service comply with the matching principle.

Documentation on the auditors review would be contained in their workpapers. These records are not the property of the Postal Service and therefore, the postal Service does not have access to them.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-36. This is a follow-up to question ANM/USPS-T9-9. The question was, inter alia, a request for production of documents. Please produce the requested documents, or verify that no responsive documents exist.

RESPONSE:

I am unaware that any such documents exist.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-37. Your testimony at page 10, lines 16-17, states that "Planning to operate at a loss, to defer equity restoration, and to borrow for operations would be to plan for financial failure."

a. Would you agree that the Postal Service should distinguish between (i) borrowing for operations and (ii) borrowing for capital investment with anticipated future payoff in the form of, say, cost reductions? If you do not agree, please explain fully any reservations which you may have.

b. Since the Postal Service cannot fund its capital investment program by raising equity in the capital markets, would you agree that failure to borrow for necessary capital investment and infrastructure can be equivalent to planning for financial failure? If you do not agree, please explain fully.

RESPONSE:

a. As covered in my response to ANM/USPS-T9-2 and ANM/USPS-T9-27(b), Title 39 provides separate borrowing restrictions for defraying operating expense and capital improvements. The Postal Service has not borrowed for operations since 1976. Please note that some capital investments are made mainly for reasons other than measurable cost savings such as service, safety, or infrastructure. Other capital investment programs, such as many of the ones detailed on pages 93, 95, and 97 of LR I-127, do generate savings, and budgets are adjusted downward to reflect and capture the expected savings.

b. I disagree. Although the Postal Service cannot raise capital in the equity markets, as demonstrated in my response to ANM/USPS-T9-29, investments can be funded through operating income as well as debt.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-38. Exhibit USPS-9A estimates FY 2000 revenues at $64,761.8 million, with total accrued costs of $64,761.8 million and net income of $65.6 million. If we assume that the target for recovery of prior years' losses ("RPYL") in FY 2000 is equal to the amount established in Docket No. R97-1, $446.9 million, [Op. & Rec. Decision, ¶ 2032], would you concur that FY 2000 has an estimated deficiency of $381.3 ($65.6 - $446.9) million? Please explain any answer that is not an unqualified affirmative.

RESPONSE:

No. The $446.9 million amount you have used was the amount reflected in the Postal Service's original filing. The amount reflected in the Recommended Decision was $377.1 million (see Appendix C of Appendices to Opinion and Recommended Decision). Please refer to Exhibit USPS-9N for an analysis of Recovery of Prior Years' Losses relative to the Board of Governors policy on equity restoration. As reflected on that Exhibit, a net income of $66 million in FY 2000 would result in the Postal Service being $311 million behind, based on the calculations you have made.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-39. Exhibit USPS-9A estimates FY 2001 revenues at $66,328.4 million before rates, with total accrued costs of $68,046.6 million and net operating loss of $1,718.2 million. If we use the $446.9 million target for recovery of prior years' losses ("RPYL") established in Docket No. R97-1, would it be fair to say that the Before Rates revenue deficiency for "break even" in FY 2001 amounts to an estimated $2,165.1 ($1,718.2 + 446.9) million? Please explain any answer that is not an unqualified affirmative.

RESPONSE:

No. As specified on Exhibit USPS 9A, the before rates deficiency is $3.688 billion. As is also shown in Exhibit A, this amount is calculated by adding the contingency ($1.702 billion) and the prior years' loss recovery ($268.3), to the before rates test year net loss ($1.718 billion). Please note that the recovery of prior year's losses is recalculated each time an omnibus rate case is prepared to account for actual financial performance since the previous rate case. Please refer to Table 53, on page 48 of my testimony for the calculation of prior years' loss recovery.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-40. At page 16 of your testimony, lines 1-5, you state that the Other Programs expense for Test Year is $1.1 billion, and "is substantially less than the $3.7 billion in Other Programs expense growth estimated for FY 1997 and the Test Year in Docket No. R97-1."

a. Of the $3.7 billion for Other Programs expense that was estimated for FY 1997 and Test Year in Docket No. R97-1, how much was actually spent by the end of FY 1997?

b. How much of the $3.7 billion was spent in years after FY 1997?

c. How much of the $3.7 billion remains unspent, and how much has been canceled or dropped from the current and future budgets?

RESPONSE:

a. Please note that most of the $3.7 billion estimated growth for Other Programs expense was estimated to be spent in the test year, FY 1998. In FY 1997, approximately $700 million of the estimated increase was spent.

b. In FY 1998, approximately $2.0 billion of the increase was spent.

c. It is not possible to determine how much of this amount is unspent beyond FY 1998. Estimates beyond FY 1998 were not part of the R97-1 rate filing, however, if we examine these same categories for FY 1999, we finished the year approximately $114 million under our plan for the year. This under-run was used to partially offset the shortfall to our revenue plan of approximately $620 million in FY 1999. Through AP 6 of FY 2000, these expense categories are essentially on plan, however, revenue through AP 6 FY 2000 is $345 million below plan.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-41. Please provide a copy of the Fiscal Year 1999 Performance Plan and the Fiscal Year 2000 Performance Plan.

RESPONSE:

($ in millions)	**FY 1999**	**FY 2000**
Revenue	$ 63,395	$ 65,424
Expense	63,195	65,324
Net Income	$ 200	$ 100

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-42. The Postal Service has announced various rounds of spending cuts, including but not necessarily limited to the seven capital programs identified in your response to DMA/USPS-T9-10 and those announced by John Ward at the February 2 MTAC meeting.

(a) For all announced spending reductions, please identify by program (i) the change in cash expenditures in fiscal years 1999, 2000, and 2001, (ii) for those programs subject to being capitalized and amortized, the change in accrued expenses in fiscal years 1999, 2000, and 2001, and (iii) the effect that each program reduction is expected to have on your Test Year projected savings that were included in the roll-forward model.

(b) Produce all studies, analyses and similar documents underlying your answer to part (a).

RESPONSE:

(a) In FY 1999 as well as in the current year, spending reductions were and are being made to offset actual and forecasted revenue shortfalls. In the rate case filing, the FY 1999 estimated total expenses were approximately equal to actual FY 1999 results. (See my response to DMA/USPS-T9-7). For FY 2000, the revenue estimate included in the rate filing is approximately $600 million less than the revenue included in the FY 2000 operating budget. Accordingly, the expense reductions that are in the process of being made to the operating budget are to offset the forecasted revenue shortfall to the revenue plan. This is necessary to preserve the FY 2000 net income plan that approximates the FY 2000 net income estimated in the rate case filing.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-42. continued

as such, these changes do not impact the estimates in the rate case filing for either FY 2000 or FY 2001.

(b) None.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-43. In response to DMA/USPS-T9-10, you stated that "Corporate wide personnel cost growth is primarily driven by factors such as inflation, actuarial changes and labor contracts that are not subject to management control." Please confirm the following statements. Explain any failure to confirm fully.

a. The amount of overtime labor is subject to management control.

b. Within contractual limits, the number of casual and transitional employees is subject to management control.

c. The number of supervisors of any activity is subject to management control.

d. The number, responsibility, and job descriptions of headquarters and field management and support personnel are subject to management control.

e. The number and scheduling of equipment, building and vehicle maintenance employees are subject to management control.

f. The decision to purchase and install labor-saving equipment such as automated letter sorting machines, flat sorting machines, robots, tray management systems, etc., is subject to management control.

g. The decision to contract entire facilities, such as PMPCs, is subject to management control.

h. The decision to hire contract carriers for rural routes is subject to management control.

i. The decision to install new management systems designed to improve efficiency and reduce costs, such as the Corporate Call Management Program, is subject to management control.

RESPONSE:

a – i. According to Websters New World Dictionary, the definition of control includes "to exercise authority over; direct; command." From this context, management

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-43. continued

has control over the various items you have listed, but mostly in terms of authority over. For example, management authorizes the use of overtime. However, overtime usage can be driven, caused by or in fact controlled by weather, mail volumes or transportation arrival times. For hiring casual employees, local labor markets can dictate the availability of potential employees. To purchase equipment, in the past, Congress has even passed legislation that restricted the amount of capital spending the Postal Service could incur in a given year. Obviously management has various degrees of control or approval authority, but, just as you have referenced in your question, management's control may be limited by the provisions of labor contracts as well as approval in some of the examples sited in this question by the Board of Governors.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-44. This question concerns plant managers, and all supervisory personnel under the level of plant manager.

(a) Please identify all incentives, including but not necessarily limited to salary and bonus, which these personnel have to reduce the number of employees under their immediate supervision.

(b) Please identify all incentives, including but not necessarily limited to salary and bonus, which these personnel have to maintain or increase the number of employees under their immediate supervision.

(c) Please state whether, and to what extent, which plant managers and subordinate supervisory personnel are penalized for backlogs in mail processing (or given positive incentives for avoiding such backlogs).

(d) Please produce all studies, analyses, and similar documents generated by or for the Postal Service since July 1, 1998, concerning the effectiveness of efforts by Postal Service management to limit the size of its mail processing work force to the actual mail processing workload.

RESPONSE:

Plant managers and supervisors are covered under the EVA variable pay program. Under this program, incentives are earned in the form of lump sum payments for achieving both financial and service performance goals. Financial performance is measured between achieving productivity improvements and performing within operating budgets. Service is measured through EXFC overnight, EXFC two and three day and Priority Mail. To promote continuous improvement only 1/3 of a given years' incentive is paid out. The balance is paid out in subsequent years' based on continuing to achieve out year financial, service and employee goals.

RESPONSE OF WITNESS TAYMAN TO INTERROGATORIES OF ALLIANCE OF NON PROFIT MAILERS

ANM/USPS-T9-44. continued

(b) See response to part (a).

(c) See response to part (a) above. In addition, a daily mail condition report is issued that track backlogs in mail processing. This report is provided to various organizational levels, including the Chief Operating Officer. Action is taken to resolve backlog situations. Backlogs could lead to failure to achieve service goals, which in turn would lead to reductions in or loss of EVA incentives.

(d) I am unaware of any studies or analyses related to limiting the size of the mail processing work force.

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.

William P. Tayman

Dated: 3.3.2000

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

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260–1137
March 3, 2000