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

POSTAL RATE AND FEE CHANGES, 2000 | Docket No. R2000-1

DIRECT MARKETING ASSOCIATION, INC.
NOTICE OF REVISIONS TO TESTIMONY OF
LAWRENCE G. BUC (DMA-T-1)
(JUNE 23, 2000)

The Direct Marketing Association, Inc. ("DMA") hereby provides notice of revisions to the testimony of witness Lawrence G. Buc, DMA-T-1 (filed May 22, 2000).

These revisions correct an error in the "Direct Cost per Handling" for "IS - Manual, Delivery Unit," shown in Attachment C. See Response of DMA witness Buc to USPS/DMA-T1-13, filed June 23, 2000. The number originally shown in Attachment C was 3.273; the corrected number is 3.339. The effect of this change is to increase the size of the understated AFSM 100 cost reductions from $199.6 million to $202.1 million in the Test Year. The resulting size of the aggregate of the adjustments proposed by witness Buc in the Test Year revenue requirement is $(1,305,862,000).

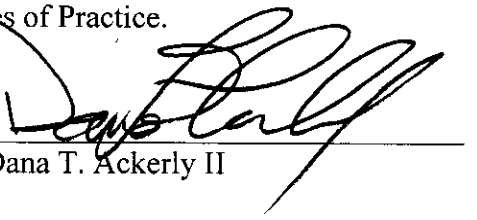
Respectfully submitted,

Dana T. Ackerly II, Esq.
COVINGTON & BURLING
1201 Pennsylvania Avenue, N.W.
Washington, D.C. 20004-2401
(202) 662-5296

Counsel for the Direct Marketing
Association, Inc.

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document in accordance with Section 12 of the Commission's Rules of Practice.



Dana T. Ackerly II

Dated: June 23, 2000

I. PURPOSE AND SCOPE OF TESTIMONY

In this testimony, I analyze the revenue requirement of the Postal Service. In particular, I analyze the proposed contingency and cost reduction and other programs presented by witness Tayman in USPS T-9. I show that the Postal Service has overstated its revenue requirement by at least $1.31 billion, by overstating the contingency by $1.01 billion and understating cost reduction and other programs by $295 million. Table 1, below, shows the adjustments I make to the Postal Service's proposed revenue requirement.

TABLE 1

TEST YEAR AFTER RATES

REVENUE REQUIREMENT ADJUSTMENTS

	USPS ($Thousands)	DMA ($Thousands)	ADJUSTMENT ($Thousands)
Contingency[1]	$1,679,766	$ 668,978	$ (1,010,788)
Rollforward Flaw[2]			(92,943)
AFSM 100[3]	169,379	371,510	(202,131)
Total Adjustment			$ (1,305,862)

[1]Attachment A, pg 1.
[2]Attachment B, pg 1.
[3]Attachment C, pg 1.

The Postal Service has requested a contingency of $1.68 billion in the Test Year, which is two and one half percent of the total costs (including final adjustments). Section II of my testimony shows that this request is neither reasoned nor reasonable and that the logic described by the Commission in previous rate cases for determining a reasonable contingency would result in a contingency of one percent of total costs, which is $669 million (after adjusting for two other overstatements to the revenue requirement, discussed next.)

Thus, the Postal Service has overstated its contingency requirement by $1.01 billion.

In addition to the unreasonable request for contingency, there are also two errors in cost reduction and other programs that lead witness Tayman to overstate the revenue requirement by an additional $295 million. In Section III, I describe and then correct these errors. The first is a flaw in the rollforward program for supervisors of clerks and mailhandlers and carriers, which the Commission corrected in the last case, but which the Postal Service has apparently not yet adopted. The second is an error in cost reduction programs for the Advanced Flat Sorting Machine 100 (AFSM 100).

II. CONTINGENCY

Under the Postal Reorganization Act, the revenue requirement includes "a reasonable provision for contingencies". 39 U.S.C. §3621. As the Commission wrote in its R76-1 Opinion and Recommended Decision, the purpose of the contingency is to cover "expenses which could be neither foreseen nor prevented through the exercise of honest, efficient, and economical management..." Op. R76-1 at 52. In this case, the Postal Service requests a contingency of 2.5 percent of its costs, or $1.68 billion.

Although the Commission has accepted all but one of the Postal Service's previous contingency requests, the Commission has also said that the requirement for a reasonable provision for contingency "requires that the amount be reasoned." Op. R97-1 at 21.

In the following section of this testimony, I will first review the Commission's body of writing pertaining to the contingency. I will next summarize the Postal Service's support for its request in this case. I will then show that witness Tayman provides little support for a contingency of 2.5 percent and that this request is neither reasoned nor reasonable given the Commission's past decisions. By contrast, a contingency of one percent is both.

540, 542, and 543. Further, in spite of all attempts at explanations, witness Tayman did not provide any underlying calculations showing the derivation of the cost reductions.

Because witness Tayman's explanations are so unsatisfying, I estimated savings for the AFSM 100 based on other available information, including the number of AFSM 100 sorts in the Test Year, sorting productivity on the AFSM 100, and savings per AFSM 100 sort, which is provided in the testimony and Library References of Postal Service witnesses. I also used a conservative estimate of savings. First, consistent with witness Tayman's and witness Yacobucci's (USPS-T-25) cost estimating methods, I used an average wage rate to determine cost savings. This completely ignores the additional savings that will result from paying AFSM 100 clerks at a lower wage rate than the manual clerks and keyers that the AFSM 100s will partially replace. Kingsley, Tr. 5/1803-1804,1840-1842,1941. Second, I assumed that one half of the sorts the AFSM 100 will replace are low-cost sorts when the Postal Service will at least partially use these machines to replace higher-cost sorts in the Test Year. Third, I included savings only from the original set of machines and did not include any savings from the portion of the additional 363 machines the Postal Service will install during the test year. O'Tormey, Tr. 21/8349-8351.

For the Test Year, it was possible to develop cost reduction estimates directly from information on the record rather than relying on estimates from "Program Mangers". Attachment C provides the derivation of my estimates.

Table 8, below, provides witness Tayman's estimates and my estimates. As the table shows, witness Tayman has understated AFSM 100 cost reductions by at least $202.1 million in the Test Year.

TABLE 8

COMPARISON OF USPS AND DMA

AFSM 100 TYAR COST SAVINGS ESTIMATE[1]

	USPS ($Thousands)	DMA ($Thousands)	Difference ($Thousands)
Clerk and MH Savings	$ 169,379	$ 371,510	$ (202,131)

[1]Attachment C, pg 1.

IV. CONCLUSION

As I have demonstrated, the Postal Service ignores the Commission's principles for setting a reasonable contingency and consequently overstates their contingency request by $1.01 billion dollars. Correcting the flaw in the rollforward program per the Commission's Opinion in R97-1 reduces the revenue request by an additional $93 million dollars. And calculating cost savings for the AFSM 100 using the Postal Service's own data increases these cost savings by $202 million. Thus, the revenue requirement should be reduced by $1.31 billion.

AFSM 100 Savings Comparison

Attachment C
Revised 6/23/00

AFSM 100 Cost Savings Comparison
(all numbers in thousands)

	DMA	USPS	Difference
	[1]	[2]	[3]=[1]-[2]
Total Savings	$ 371,510	$ 169,379	$ 202,131

Sources:

[1] Attachment C, pg 2.

[2] Attachment C, pg 3.

USPS AFSM 100 Clerks TY Savings

Attachment C
Revised 6/23/00

USPS AFSM 100 Clerks Test Year Savings

Clerks Workhour Savings (hours)	Hourly Clerk Wage Rate	Clerks Workhour Cost Savings (thousands)
[1]	[2]	[3]=[1]*[2]
6,052,003	$ 27.99	$ 169,379

Sources:

[1] Docket No. R2000-1, Tayman, Tr. 2/322.

[2] Docket No. R2000-1, USPS-LR-I-126, PRG_ANAL-revised.xls, 'Data'. Hourly wage rate obtained from dividing Clerk/Mailhandler Avg. Personnel Cost (50,125) by Workhours Per Workyear (1,791).

DMA AFSM 100 Clerks TY Savings

Attachment C
Revised 6/23/00

DMA AFSM Clerks Test Year Savings

		[1] Direct Cost per Handling (cents)	[2] Plant/Delivery Unit Manual IS Factor	[3] AFSM Productivity (units/hour)	[4] Number of Machines	[5] Operational Hours per Workday	[6] Operational Days per Year	[7] Total Sorts Per Year (millions)	[8] Allocated Sorts (millions)	[9] Total Cost Savings
IS	IS - Manual, Plant	6.184	26.10%							
	IS - Manual, Delivery Unit	3.339	73.90%							
	IS - AFSM 100	0.941	N/A							
	Difference*	3.140		15,000	166.5	20	313	15,634	5,916	$ 185,755

		Direct Cost per Handling	AFSM Productivity (units/hour)	Number of Machines	Operational Hours per Workday	Operational Days per Year	Total Sorts Per Year (millions)	Allocated Sorts (millions)	Total Cost Savings
IP	IP - FSM 881 OCR/BCR	2.853							
	IP - AFSM 100	0.941							
	Difference**	1.911	15,000	166.5	20	313	15,634	9,718	$ 185,755

TOTAL SAVINGS **$ 371,510**

Sources:

* Difference (IS only) is calculated by taking 26.10% of the difference between IS - Manual, Plant and IS - AFSM 100 added to 73.90% of the difference between IS - Manual, Delivery Unit and IS - AFSM 100 per Docket No. R2000-1, LR-I-90, R2000_1_Flats Cost Model_Final USPS.xls, 'Data', Plant/Delivery Unit Manual IS Factor.

** Difference (IP only) selected as conservative estimate as smallest difference between cost of current sort and cost of AFSM 100 sort.

[1] Docket No. R2000-1, LR-I-90, R2000_1_Flats Cost Model_Final USPS.xls, 'Mailflow Model Costs', Cents per Piece Handling, with a modification to set a volume variability factor equal to 1.00.

[2] Docket No. R2000-1, LR-I-90, R2000_1_Flats Cost Model_Final USPS.xls, 'Data', Plant/Delivery Unit Manual IS Factor.

[3] Docket No. R2000-1, LR-I-90, R2000_1_Flats Cost Model_Final USPS.xls, 'Productivities', Footnotes [7] and [8]

[4] LR-I-83, page I-12

[5] Kingsley, TR.5/1961.

[6] Kingsley, TR.5/1960.

[7] = [3]*[4]*[5]*[6]

[8] = Allocated Sorts is the number of sorts allocated to each scenario to yield equal cost savings, Kingsley, TR.5/1660.

[9] = [8]*[1]