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

POSTAL RATE AND FEE CHANGES, 2001 | Docket No. R2001-1

RESPONSE OF UNITED STATES POSTAL SERVICE
WITNESS HATFIELD TO INTERROGATORIES OF
UNITED PARCEL SERVICE
(UPS/USPS-T18-12-15)

The United States Postal Service hereby provides the responses of witness Hatfield to the following interrogatories of United Parcel Service: UPS/USPS-T18-12-15, filed on December 4, 2001.

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

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys

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December 20, 2001

UPS/USPS-T18-12. Refer to your answer to interrogatory UPS/USPS-T18-11 where you state that "FY 2001 through FY 2003 Air Taxi costs by class and subclass of mail are estimated by applying cost and volume adjustment to the Base Year Air Taxi costs by class and subclass of mail." Confirm that this answer refers to the methodology used to estimate the "Status Quo" costs rather than the "FedEx Scenario" costs. If not confirmed, explain.

RESPONSE:

Confirmed.

UPS/USPS-T18-13. Refer to Table USPS-T-18A, on page 13 of your testimony, and Table USPS-T-18E, on page 33 of your testimony.

(a) Confirm that the status quo cost for Parcel Post is $12,280,000 in FY2002 (see Table USPS-T-18A). If you do not confirm, provide the correct number.

(b) Confirm that under the FedEx contract, the cost is expected to decrease to $4,129,000 in FY2002 for a net decrease of $8,151,000 (see Table USPS-T-18E). If you do not confirm, provide the correct numbers.

(c) Explain completely all of the reasons for the projected decrease in Parcel Post costs in FY2002 under the FedEx contract.

RESPONSE:

(a), (b) Confirmed

(c) As shown in Table USPS-T-18G, the overall net decrease in Parcel Post purchased transportation costs of $8.151 million is comprised of three distinct items: air transportation (-$8.301 million), ground handling ($.142 million), and additional highway transportation ($0.008 million). Of the three items, the only one that decreases Parcel Post costs is air transportation. The net decrease in air transportation costs is also comprised of various factors that, taken individually, would tend to both increase and decrease Parcel Post costs. Because these factors are inter-related, no analysis has been done to separate or quantify their individual impact. The factors that contribute to the decrease in Parcel Post air transportation costs are described below.

The primary driver of the net decrease in Parcel Post purchased air transportation costs is the elimination of the Air Taxi cost pool. As shown in Table USPS-T-18A, the FY2002 Parcel Post costs are $12.280 million in the *status quo* scenario, of which $7.891 million are from the Air Taxi cost pool. The analysis described in my testimony assumes that the FedEx transportation agreement replaces the need for the transportation included in the Air Taxi cost pool. The $12.280 million of Parcel Post costs in the *status quo* scenario are replaced by a combination of FedEx and Passenger Air transportation totalling $4.129 million. Therefore, the elimination of the Air Taxi cost pool causes a significant reduction in Parcel Post costs.

Another factor that would tend to decrease the costs of Parcel Post under the FedEx scenario is the fact that FedEx air transportation tends to be less expensive than the transportation that it replaces. As described on page 3 of my testimony, the cost to move a given amount of mail on FedEx is less than the cost to move an equivalent amount of mail on *status quo* air transportation.

RESPONSE OF POSTAL SERVICE WITNESS
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UPS/USPS-T18-14. Refer to Table USPS-T-18B, on page 14 of your testimony, and Table USPS-T-18F, on page 34 of your testimony.

(a) Confirm that the status quo cost for Parcel Post is $13,136,000 in FY2003 (see Table USPS-T-18B). If you do not confirm, provide the correct number.

(b) Confirm that under the FedEx contract, the cost is expected to decrease to $4,272,000 in FY2003 for a net decrease of $8,864,000 (see Table USPS-T-18F). If you do not confirm, provide the correct numbers.

(c) Explain completely all of the reasons for the projected decrease in Parcel Post costs in FY2003 under the FedEx contract.

RESPONSE:

(a), (b) Confirmed

(c) As calculated from Tables USPS-T-18B and USPS-T-18F, the overall net decrease in Parcel Post purchased transportation costs of $8.864 million is comprised of three distinct items: air transportation (-$9.022 million), ground handling ($.149 million), and additional highway transportation ($0.008 million). Of the three items, the only one that decreases Parcel Post costs is air transportation. The net decrease in air transportation costs is also comprised of various factors that, taken individually, would tend to both increase and decrease Parcel Post costs. Because these factors are inter-related, no analysis has been done to separate or quantify their individual impact. The factors that contribute to the decrease in Parcel Post air transportation costs are described below.

As described in my response to UPS/USPS-T-18-13 (c), the primary driver of the net decrease in Parcel Post purchased air transportation costs is the elimination of the Air Taxi cost pool. As shown in Table USPS-T-18B, the FY2003 Parcel Post costs are $13.136 million in the *status quo* scenario, of which $8.441 million are a result of the Air Taxi cost pool. The analysis described in my testimony assumes that the FedEx transportation agreement replaces the need for the transportation included in the Air Taxi cost pool. The $13.136 million of Parcel Post costs in the *status quo* scenario are replaced by a combination of FedEx and Passenger Air transportation totalling $4.271 million. Therefore, the elimination of the Air Taxi cost pool causes a significant reduction in Parcel Post costs.

Another factor that would tend to decrease the costs of Parcel Post under the FedEx scenario is the fact that FedEx air transportation tends to be less expensive than the transportation that it replaces. As described on page 3 of my testimony, the cost to move a given amount of mail on FedEx is less than the cost to move an equivalent amount of mail on *status quo* air transportation.

UPS/USPS-T18-15. Refer to your answer to interrogatory UPS/USPS-T18-10, where you confirm that 100 percent of FY 2002 and FY 2003 air taxi costs will be replaced by the FedEx contract.

(a) Confirm that, according to Table USPS-T-18A, on page 13 of your testimony, 9.5 percent of FY 2002 Air Taxi costs are attributed to Parcel Post. If you do not confirm, provide the correct number.

(b) Confirm that, according to Table USPS-T-18B, on page 14 of your testimony, 9.8 percent of FY 2003 Air Taxi costs are attributed to Parcel Post. If you do not confirm, provide the correct number.

(c) Does your methodology assume that all Parcel Post volume that is transported via Air Taxi in the "Status Quo" scenario will be carried by the FedEx transportation contract?

(i) If your answer is yes, explain why FY 2002 Parcel Post transportation costs fall by 66 percent from the "Status Quo" scenario to the "FedEx Scenario" ($12,280,000 to $4,129,000), and why FY 2003 Parcel Post transportation costs fall by 67 percent from the "Status Quo" scenario to the "FedEx Scenario" ($13,136,000 to $8,864,000).

(ii) If your answer is no, provide corrected "FedEx Scenario" costs for FY 2002 and FY 2003 that reflect the volume that is currently carried on Air Taxis.

RESPONSE:

(a), (b) Confirmed

(c) No, the methodology used to develop the FedEx Rollforward Adjustment does not assume that all Parcel Post volume transported via Air Taxi in the *status quo* scenario will be carried by the FedEx transportation agreement. Rather, as stated in my responses to UPS/USPS-T-18-13 (c) and UPS/USPS-T-18-14 (c), the analysis included in my testimony assumes that the FedEx transportation agreement will replace the need for the transportation included in the Air Taxi cost pool, not necessarily the volume. As shown on Table 305 of USPS LR-J-94, the total pounds of mail flown by ACT type are the same in both the *status quo* and FedEx scenarios. Because FedEx is planned to carry First-Class, Priority, and express ACT types only, the analysis included in my testimony does not preclude the possibility that volume which previously traveled on Air Taxi transportation might migrate to Passenger Air transportation. However, the transportation that underlies the Parcel Post costs for Air Taxi transportation in the *status quo* scenario has not been accounted for in the FedEx scenario.

Specifically, as described in Section 14.1.1.4 of USPS-LR-J-1, Air Taxi costs are "distributed to classes and subclasses of mail on the basis of the composite of the costs of the other domestic air categories." In the Base Year, these other air categories included the Alaska Non-Pref cost pool. Because the Alaska Non-Pref cost pool has considerable costs attributable to Parcel Post, inclusion of this cost pool in the development of the Air Taxi distribution key tends to increase the amount of Air Taxi cost attributable to Parcel Post. It is my understanding that the original rationale for the inclusion of the Alaska Non-Pref cost pool in the development of the Air Taxi distribution key was that some portion of Air Taxi costs were related to intra-Alaska air transportation. If that were the case, then the assumption that the FedEx transportation agreement replaces the need for all Air Taxi costs would be incorrect insofar as FedEx is not planned to provide intra-Alaska air transportation.

However, in preparing my answers to these interrogatories, I investigated this issue and uncovered new information. Through discussions with the USPS Network Operations Management employee in charge of Alaska air transportation, I learned that the Air Taxi accounts no longer include any costs for intra-Alaska air transportation. Therefore, the Alaska Non-Pref cost pool should not be included in the development of the Air Taxi distribution key because Air Taxi costs do not include intra-Alaska air transportation. With this new information, the original assumption that FedEx will replace the need for Air Taxi transportation remains reasonable.

In conclusion, removal of the Alaska Non-Pref cost pool from the development of the Air Taxi distribution key would significantly decrease the Air Taxi costs attributable to Parcel Post in the Base Year and in my *status quo* scenario. However, this new understanding does not affect my estimation of costs under the FedEx scenario. Therefore, the net impact on Parcel Post transportation costs would be the same as it is now (using the current Base Year costs and the current FedEx Rollforward Adjustment). Specifically, the FedEx Rollforward Adjustment would show a smaller reduction in Parcel Post transportation costs because *status quo* Parcel Post costs would fall while the FedEx Parcel Post costs would remain unchanged. This smaller reduction in Parcel Post costs in the Rollforward Adjustment would be offset by lower Parcel Post costs in the Base Year as a result of changing the Air Taxi distribution key.

(i) Not applicable.

(ii) As described above, the issues addressed in this interrogatory have not led me to revise my estimates of FedEx scenario costs and do not impact the net Parcel Post air transportation costs in FY2002 or FY2003. Therefore, there are no "corrected" cost estimates to provide.

DECLARATION

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

Philip C Hatfield

Dated: 12/20/01

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.

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