

DOCKET SECTION

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

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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES, 1997

Docket No. R97-1

RESPONSE OF UNITED STATES POSTAL SERVICE
WITNESS TAYMAN TO INTERROGATORIES OF
THE OFFICE OF THE CONSUMER ADVOCATE
(OCA/USPS-T9-38-40)

The United States Postal Service hereby provides responses of witness Tayman to the following interrogatories of the Office of the Consumer Advocate: OCA/USPS-T9-38, filed on September 15; OCA/USPS-T9-39, filed on September 17; and OCA/USPS-T9-40, filed on September 19, 1997.

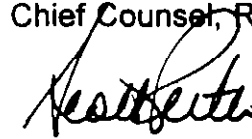
Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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September 29, 1997

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO INTERROGATORIES OF THE CONSUMER ADVOCATE
REDIRECTED FROM WITNESS TAYMAN**

OCA/USPS T9-38. According to a recent newspaper article in The Philadelphia Inquirer (August 8, 1997, page A1 and A16, attached), the Postal Service is permitted to contract out mail delivery as highway contract routes in areas it deems to be virgin territory and can do so at a cost of about 24.5 cents per delivery per day, only slightly over one-half the cost of delivery by employees. The article also states that in rapidly growing communities the Postal Service considers and compares a highway contract route on new routes and does a cost comparison every time.

- a. Please confirm that the Postal Service is permitted to contract out mail delivery as highway contract routes in areas deemed to be virgin territory. If you can not confirm, please describe the areas in which the Postal Service may enter into highway contract routes.
- b. What do the Postal Service contracts with the employees unions provide regarding the establishment of highway contract routes?
- c. At what organizational level in the Postal Service are initial decisions made to establish a highway contract route? At what organizational level in the Postal Service are final decisions made to establish a highway contract route?
- d. Please confirm that, nationally, the average cost of highway-contract delivery is 24.5 cents per delivery per day. If you do not confirm, please provide the nationwide average cost of highway contract delivery for FY 1996 and FY 1987.
- e. Please confirm that the average cost of highway contract delivery is a little over one-half the cost of delivery with postal employees. If you do not confirm, please provide the nationwide average cost of mail delivery with postal employees.
- f. Please provide the number of delivery points for each of the years FY 1990 through FY 1997.
- g. Please provide the actual number of city delivery, rural delivery and highway contract routes for each of the years FY 1990 through FY 1997.
- h. What proportion of new delivery routes for each of years FY 1990 through FY 1997 were highway contract routes?
- i. How many existing city or rural delivery routes were converted to highway contract routes for each of the years FY 1990 through FY 1997?

- j. Please provide the number of city delivery, rural delivery and highway contract routes for FY 1997 and FY 1998 assumed in the rate filing and indicate where those numbers are located in the documentation.
- k. Please provide the assumptions for the cost model underlying the estimate of the number of highway contract routes in FY 1997 and FY 1998.
- l. How have you taken into account in the roll-forward cost model for FY 1997 and FY 1998 the increasing number of highway contract routes relative to routes serviced by Postal employees.
- m. Please state the input adjustments that would need to be made to the cost model for FY 1997 and FY 1998 if a greater proportion of new routes were established during FY 1997 and FY 1998 as highway contract routes than was assumed in the rate filing.
- n. Are there any costs related to growth in highway contract routes included in the "Cost Reduction" or "Other Program" categories in your exhibit USPS 9B?

RESPONSE:

- a: Confirmed
- b: See Article 32 of the National Rural Letter Carriers Association Agreement and Article 32 of the National Association of Letter Carriers Agreement, which can be found in Library Reference H-88.
- c: The initial decision is made at the Post Office level. Concurrence is required at the District level and final approval is required at the headquarters' level.
- d: Not confirmed. The nationwide average is 27¢ as of the end of PFY 1996.
- e: Not confirmed. The cost of city delivery is 51¢ and the cost of rural delivery is 42¢ per delivery as of the end of PFY 1996.
- f: For FY 90-96 this information can be found in the Comprehensive Statement on Postal Operations, which is available in either the Postal Service library or the Commission's library. The estimated number of rural boxes and possible city

deliveries for FY 1997 can be found on page 74 of Library Reference H-12. The number of highway contract routes for FY 97 was not estimated in the development of this case.

- g: For FY 1996 and earlier this information is available in the Comprehensive Statement on Postal Operations, which is available in the Commission's library and the Postal Service's library. The number of routes for FY 1997 was not estimated in the development of this case.
- h: This can be calculated using the data provided in part g. above.
- i: This information is not readily available. However, since the criteria for converting rural routes to highway contract routes are very strict, the number is most likely relatively small.
- j: The number of city, rural, and highway routes were not used in the development of the revenue requirement.
- k: See part j., above.
- l: See part j., above.
- m: See part j., above. To estimate such an impact, assumptions would have to be made, and a methodology developed to estimate cost impacts and incorporate them into the rollforward model.
- n: No.

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OCA/USPS-T9-39. In your response to OCA/USPS-T9-37 you stated that the Postal Service believes no adjustments are necessary to reflect the unexpectedly high FY 1997 earnings of the Postal Service and that, "updating could result in a revenue requirement that is inconsistent with management's goals and objectives and infringes upon management's prerogative to determine financial policy." You further state that, "If updating is considered...it must not be done selectively."

- a. Please state how updating the filing to reflect actual earnings for FY 1997 could result in a revenue requirement that is inconsistent with management's goals and objectives?
- b. What goals and objectives of management are inconsistent with the utilization of actual numbers to establish the appropriate revenue requirement of the Postal Service?
- c. Please state how recognition of the actual FY 1997 earnings would infringe upon management's prerogative to determine financial policy? Does it mean that it is management's prerogative to use earnings in excess of its own recent estimates in a way which is totally disregarded in determining the future revenue needed to meet the costs of the Postal Service?
- d. Are there any other currently known changes in the costs or revenue estimates of a magnitude similar to the approximately \$40 million adjustment to the amount for the recovery for past year losses resulting from FY 1997 experience?
- e. If the PRC were to determine that updating should be considered, what updates would you recommend so that the updating would not be done selectively?

RESPONSE:

- a. If changes to the revenue requirement were to result in a Recommended Decision that significantly changed the amount of net revenue requested by the Postal Service in this filing, management's current goals and objectives could be undermined, especially if the revisions were to result in significant departure from the Postal Service's proposals. As I have tried to explain, management's assessment of the

overall revenue requirement is the result of balancing a complex array of quantitative and subjective considerations. The entire filing, furthermore, including the specific pricing and classification proposals, embodies management's judgment about how those considerations should be balanced, and about the appropriate financial policy goals for the Postal Service. This is not to say that any departure from specific proposals or estimates would necessarily compromise management's financial policy. I do believe, however, that any mechanical adjustment of the revenue goals in the case due to more recent information, in a way that would lead to substantial change in the Postal Service's pricing and other proposals, would be a mistake and would likely subvert the Postal Service's policy objectives. Accordingly, any changes in estimates due to actual performance or other events should be assessed comprehensively, and not selectively, and should be evaluated in the context of the entire filing. In this respect, it would not be unreasonable, nor unprecedented, for the Postal Service to conclude that the effects of particular changes, including actual financial performance, caused a reassessment of the elements of the revenue requirement in a way that permitted the Postal Service to determine that its financial and other policy objectives were still best served by adherence to its original revenue requirement. In fact, this is exactly the reasoning that has led the Postal Service to conclude in past cases that unforeseen expenses or liabilities that came to light during the litigation did not alter its proposals. For example, this is what happened in Docket No. R90-1, with the passage of the Omnibus Budget Reconciliation Act (OBRA) of 1990. In that case, the Postal Service evaluated the effects of the change and decided that the increased expenses

in the interim and test years should not alter the overall amount of revenue sought in the case. Rather, the Postal Service would settle for a reduction in the amount available for contingencies, which in the context of the entire filing was judged to be a reasonable adjustment. A similar reassessment might be appropriate on the particular facts of this case.

b. See the answer to a. Actual numbers would not necessarily conflict with management's goals as long as they did not substantially affect the proposals in this case. My current assessment is that the revenue requirement requested by the Postal Service in this filing remains appropriate.

c. See my response to parts a&b. Please note that a recommendation of rates providing the amount of net revenue requested by the Postal Service in this filing does not mean that improved FY 1997 net income will be "disregarded in determining the future revenue needed to meet the costs of the Postal Service".

d. I am not aware of changes beyond those already specified in my response to ANM/USPS-T9-1e. that would result in a change to the estimated net income of approximately \$1.0 billion which did not include the impact of the UPS strike. A rough preliminary estimate of the UPS strike's impact on FY 1997 is an improvement in net income of **about \$200 million**. Inclusion of this estimate increases the Postal Service's estimate of **net income** for FY 1997 to approximately \$1.2 billion. I do not expect the UPS strike to have a material impact on FY 1998.

e. I do not believe changes are necessary or required in this case to arrive at a reasonable and appropriate revenue requirement. See my responses to parts a. & b. However, should the Commission choose to update the Postal Service's revenue

requirement, all subsequent events should be considered including the use of a larger contingency. Please see my responses to UPS/USPS-T9-3b.-d.

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OCA/USPS-T9-40. Your responses to OCA/USPS-T9-33 and T9-34 have indicated that the Augmented Sales Force program is being re-evaluated and the Tactical Sales Force strategy is revised. As filed, the estimated increased expense for those two "Other Programs" for FY 1998 as shown in library reference H-10, exhibit B, totals \$64.841 million (Augmented Sales Force with \$38.175 million and Tactical Sales Force strategy with \$26.666 million), yet your responses have accounted for only \$18.2 million (\$2 million for the New York pilot program for the Augmented Sales Force, \$6 million for the Manifest Mailing System, and \$10.2 for the Customized Packaging System).

- a. Please confirm that the revised estimated expenditure for the programs that encompass the Tactical Sales Force strategy and the Augmented Sales Force program for FY 1998 is \$18.2 million. If you do not confirm, please explain.
- b. Are any other programs being funded from the excess FY 1998 expenditure increase estimates for the Augmented Sales Force program or the Tactical Sales Force strategy program? If so, please explain and provide the estimated FY 1998 increased costs for those programs.
- c. Please confirm that witness Patelunas utilizes the amounts from exhibit B in his roll forward model, exhibit 15A, pages 3-4. If not, please explain.

RESPONSE:

- a. Not confirmed. As I stated in my response to OCA/USPS-T9-34, the Tactical Sales Force Strategy encompasses several programs including Tactical Sales Force, Augmented Sales Force, Customized Packaging, and Manifest Mailing System. The estimated FY 98 cost of the Tactical Sales Force program (as opposed to the Tactical Sales Force strategy which encompasses the four programs listed above), remains \$26.666 million. The revised cost of the Augmented Sales Force program is \$2.0 million, however this could be increased depending upon the success of the pilot. In addition \$16.2 million has been redirected from the Augmented Sales Force Program to

the Manifest Mailing System program (\$6.0 million) and the Customized Packaging program (\$10.2 million).

b. The remaining Augmented Sales Force program funds are being held as unallocated funds pending the results of the pilot or possible redirection to some other initiative.

c. The primary source of the other program cost factors reflected in Patelunas Exhibit 15A is LR H-12. However, the same amounts are also reflected in Exhibit B of LR H-10.

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: SEPT. 29, 1997

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.

A handwritten signature in black ink, appearing to read "Scott L. Reiter", is written over a horizontal line.

Scott L. Reiter

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September 29, 1997