

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

POSTAL RATE AND FEE CHANGES
PURSUANT TO PUBLIC LAW 108-18

Docket No. R2005-1

ERRATA TO RESPONSES OF POSTAL SERVICE WITNESS TAYMAN
TO INTERROGATORIES OF VALPAK DIRECT MARKETING SYSTEMS, INC. AND
VALPAK DEALERS' ASSOCIATION, INC. (VP/USPS-T6-1-9)

The United States Postal Service hereby provides errata to the responses of witness Tayman to VP/USPS-T6-1-9, originally filed on June 7, 2005. The only correction is to the heading on each page to change the erroneous label attributing the interrogatories to the OCA, rather than to Val-Pak, their true and proper source.

Respectfully submitted,

UNITED STATES POSTAL SERVICE
By its attorneys:

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RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS TAYMAN
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VP/USPS-T6-1. According to the Postal Service's 2004 Annual Report, page 27, the Postal Service "estimated the 2004 present value of future premium payments [for retiree health care] to be between \$48 billion and \$59 billion."

- a. Please confirm that as of the end of Fiscal Year (FY) 2004 with respect to these future retiree health care liabilities discussed in the Annual Report, the Postal Service had not (i) accumulated any financial reserves, nor (ii) reflected any accrued expense in its income statement, nor (iii) reflected any liability on its balance sheet. If you do not confirm any part of the above, please explain fully.
- b. To what extent were any of these future health care liabilities incurred during the ten-year period from 1995 through 2004?
- c. Are you aware of any other estimate by any other party (e.g., Congressional Budget Office, Government Accountability Office, Office of Management and Budget, Office of Personnel Management) of the Postal Service's unfunded liabilities for retiree health care? If so, please provide those current estimates, along with the source.

Response:

- a. Confirmed.
- b. To my knowledge, this information is not available.
- c. I am aware that both the Congressional Budget Office and the Office of Personnel Management have calculated retiree health care liabilities that they have attributed to the Postal Service. In the Cost Estimate for H.R. 22, Postal Accountability and Enhancement Act, dated April 25, 2005, CBO estimates the "net present value of the unfunded liability for the health care costs of retirees would be \$49 billion at the end of 2006." This value is net of an anticipated \$21.2 billion asset transfer in 2006 from the Civil Service Retirement and Disability Fund and Postal Service payments in 2006 of \$6.4 billion.

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VP/USPS-T6-2. According to the Postal Service's 2004 Annual Report, page 27, the Postal Service spent \$1,313 million for health care benefits for existing retirees in Fiscal Year (FY) 2004.

- a. Please indicate whether any of this \$1,313 million spent for health care benefits for existing retirees in FY 2004 was treated as volume variable. If any were so treated, please state the amount, and state the rationale for treating health care costs for existing retirees as volume variable.
- b. Were any of the expenditures of \$1,313 million for health care benefits for existing retirees in FY 2004 treated as attributable? If so, please indicate (i) the amount of the attribution, (ii) the rationale justifying such attribution, and (iii) the key used to distribute the attributable portion to the classes of mail.
- c. In addition to the \$1,313 million of expenditures for health care benefits for existing retirees in FY 2004, did the Postal Service's income statement for FY 2004 include any accrued expense for future health care benefits? If so, please indicate the amount and explain what benefits this amount was accrued for.

Response:

a & b. \$743.329 million of the FY 2004 retiree health care costs were treated as volume variable. Annuitant health benefit costs are, and always have been, distributed to the same degree as all volume variable postal labor costs. This treatment is used because health care benefits for retirees are considered part of labor costs since we do not accrue costs for future health benefits of current employees.

c. No.

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VP/USPS-T6-3.

- a. Please estimate the amount that the Postal Service expects to spend for health care benefits for existing retirees in FY 2005.
- b. Please provide the projected amount of the Postal Service's unfunded health care liabilities at the end of FY 2005.

Response:

- a. \$1,539,773,000.
- b. This information is being developed and will be provided as soon as available.

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VP/USPS-T6-4.

- a. Please provide an estimate of the amount that the Postal Service expects to spend for health care benefits for existing retirees in TY 2006, and indicate whether this amount is included in the roll-forward model for this item.
- b. Will any of the anticipated expenditures for retiree health care benefits in TY 2006 be treated as (i) volume variable, and (ii) attributable? If so, please indicate the amount and the basis for attribution.
- c. Please provide the projected amount of the Postal Service's unfunded, off balance sheet health care liabilities at the end of TY 2006.
- d. During TY 2006, does the Postal Service currently plan to accrue any expense — and set aside any money — for its currently unfunded future retiree health care liabilities?
- e. As a hypothetical, please assume that in TY 2006, or some future year shortly thereafter, the Postal Service were to start accruing expenses and setting aside funds for its future health care liabilities. Please (i) state the extent to which you would expect any portion of such accrued expenses to be treated as volume variable or attributable, and (ii) provide the rationale for either attributing or not attributing such expenses.

Response:

- a. \$1,736,364,000 have been included in the roll-forward model for TY 2006 retiree health care premium expense. See page 274 of LR-K-50.
- b. \$974,691,000 before rates and \$968,562,000 after rates have been treated as volume variable. See response to VP/USPS-T6-2, a.
- c. This information is being developed and will be provided as soon as available.
- d. No.
- e. A change in treatment as proposed under this hypothetical could only be determined after careful review of the language and intent of the governing doctrine establishing a change in accounting treatment of these costs.

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VP/USPS-T6-5.

- a. Please confirm that on September 30, 2003, in response to a request by Congress, the Postal Service submitted "Postal Service Proposal: Use of Savings for Fiscal Years after 2005, P.L. 108-18," containing two alternate proposals, labeled Proposals I and II, respectively, on purposes to which any money accumulated in the escrow fund should be allocated. Please provide a copy of the Postal Service's September 30, 2003 submission to Congress.
- b. Please confirm that under Proposal I (which assumes that the existing escrow requirement would be eliminated), beginning in FY 2006, the Postal Service would make annual payments into a new Retiree Health Fund, estimated at \$1.2 billion in FY 2006, which would be used to pay for retiree health insurance premiums in the future. If you do not confirm, please explain.
- c. Please assume that Congress were to accept the Postal Service's Proposal I. That is, please assume (i) the escrow requirement would be eliminated, and (ii) a new Retiree Health Fund were established to pay future health care liabilities. Would you expect that any future payments into such a Retiree Health Fund would be treated as (i) volume variable, and/or (ii) attributable? Please explain the rationale for either attributing or not attributing such expenses.

Response:

- a. Confirmed. Copy attached.
- b. Not confirmed. The FY 2006 payment for retiree health benefits under Proposal I was \$5.0 billion.
- c. See response to VP/USPS-T6-4(e).

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VP/USPS-T6-6. The GAO report on the Postal Service's proposed options for disposition of the "savings" (Report No. GAO-04-238, p. 3, issued November 26, 2003) states that: the legislation [P.L. 108-18] stated that the Service should also consider the work of the President's Commission on the United States Postal Service (the Commission), whose report, issued in July 2003, identified the need for the Service to operate more efficiently.⁴ [Footnote 4 omitted.] The Commission's report recommended, among other things, that:

- "the Service should review its current policy relating to the accounting treatment of retiree health care benefits, and work with its independent auditor to determine the most appropriate treatment of such costs in accordance with applicable accounting standards and in consideration of the Postal Service's need for complete transparency in the reporting of future liabilities; and
 - the Postal Service should consider funding a reserve account for unfunded retiree health care obligations to the extent that its financial condition allows...."
- a. Has the Postal Service reviewed and prepared a report on its current policy relating to the accounting treatment of retiree health care benefits, and determined the most appropriate treatment of such costs in accordance with applicable accounting standards? If so, please provide a copy of such report and the current policy relating to the accounting treatment of retiree health care benefits.
- b. Please explain what consideration, if any, the Postal Service has given to funding of a reserve account for retiree health care obligations since release of the above-referenced GAO report.

Response:

- a. The quote cited above was taken out of context in the GAO report. The above statement was directed to "the new Board of Directors." Further, on page 124 of the Commission's report, they recognized the following:

[T]he retiree health care obligation is funded on a "pay-as-you-go" basis that focuses on obligations due today rather than the larger figure of obligations earned by and owed to employees today. The Commission wishes to make clear that the Postal Service's independent auditor has indicated that such an approach is in compliance with current applicable accounting standards governing the reporting of retiree health care costs.

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b. As referenced in the "Postal Service Proposal: Use of Savings for Fiscal Years after 2005, P.L. 108-18," two alternate proposals, labeled Proposals I and II presents consideration given to funding a reserve account for retiree health care obligations. Proposal I requires that the retroactive transfer of CSRS military service costs imposed on the Postal Service under Public Law 108-18 is returned to the U.S. Treasury. Under this proposal, the Postal Service would fund the current service cost of post-retirement health benefits and the net interest on the unfunded obligation. Proposal II is based on the Postal Service's funding of \$27 billion in CSRS military service costs. With this added burden, the Postal Service proposed funding the current service cost for Postal Service employees hired after FY2002.

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VP/USPS-T6-7. Please suppose the Postal Service is viewed as having two kinds of expense obligations, regular operating expense obligations and escrow expense obligations. Suppose further that the appropriate procedure for covering these expenses is in two steps. First, rates are set in a normal Commission proceeding to cover the regular operating expenses. Second, layered on top of the first step, a uniform proportionate surcharge is applied to cover the escrow.

- a. If at some point in the future the escrow expense were removed, please explain why it would not be appropriate to remove the proportionate surcharge as well.
- b. If the government placed a 10 percent surcharge on all postal rates in order to help pay for a war, please explain why you would not expect the surcharge to be removed after the war ended.
- c. If the escrow obligation was not removed and additional revenues were needed, please explain whether the analysis supporting the rate change should focus on the base rates or on the rates plus the surcharge.

Response:

- a. It would not be appropriate if the regular and escrow rates were not covering Postal Service operating costs.
- b. Based on past experience with the federal budget process, it might be more likely that the size of the federal budget deficit, as opposed to the end of the war, would determine if the surcharge were removed. It could also be possible that the surcharge would not be removed, and a new requirement would be established for funds generated from the surcharge to be held in "escrow."
- c. The analysis supporting the rate change would be based on all sources of revenue and expense.

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VP/USPS-T6-8.

Please suppose that the Postal Service is viewed as having two kinds of expense obligations: (i) regular operating expenses; and (ii) escrow expenses.

- a. Can you envision any outcome in which the escrow funds ultimately would not be expended for a purpose that otherwise would appropriately be funded by ordinary (non-escrow) revenues?
- b. If you can envision such a possibility, please explain and indicate the likelihood of such an outcome. If you cannot envision such a possible outcome, then why is it reasonable to view the requirement to set aside escrow funds as different from any other expense obligation? Please explain.

Response:

a & b. In accordance with Public Law 108-18's provision that Congress shall decide how the escrow funds will be expended, it is possible that these funds could be expended for a purpose that otherwise would not be funded by ordinary (non-escrow) revenues. A case in point would be the retroactive charge for CSRS military service costs that by law were previously the responsibility of the U.S. Treasury and transferred by Public Law 108-18 to the Postal Service. Another example would be the transfer of Post Office Department workers' compensation costs to the Postal Service.

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VP/USPS-T6-9.

- a. As a hypothetical, please assume Congress were to enact legislation that relieved the Postal Service of its \$3.1 billion obligation to the escrow account, but required that \$1.2 billion be paid into a new Retiree Health Care Fund, as suggested by the Postal Service in its Report to Congress "Postal Service Proposal: Use of Savings for Fiscal Years after 2005, P.L. 108-18," September 30, 2003.
- (i) Under these circumstances, would you see good reason for the Postal Service to amend and reduce the revenue requirement to reflect the lower Congressional mandate?
 - (ii) Regardless of whether you were to see good reason to reduce the revenue requirement or keep it unchanged, would you still consider an across-the-board rate increase to be appropriate under these circumstances? Please explain why or why not.
 - (iii) Under what legislative scenario would there be good reason for withdrawing the pending request and resubmitting a more traditional rate case; i.e., one that did not reflect an across-the-board rate increase?
- b. As a second hypothetical, please assume Congress were to enact legislation requiring that the entire \$3.1 billion payment in FY 2006 be paid to a new Retiree Health Care Fund. Under the circumstances of this hypothetical, would you still consider an across-the-board rate increase to be appropriate?

Response:

- a. (i) Assuming that the \$1.2 billion payment cited above relates to the difference between our proposed funding of \$5.0 billion less former CSRS and retiree health benefit premium payments, it would be appropriate for the Postal Service to withdraw this case and file a new case.
- (ii) See response to part (i). The timing of when such legislation were enacted and other provisions contained in that legislation would determine what course of action the Postal Service would take.
- (iii) See response to part (i).
- b. See response to part (a)(ii).

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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