

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

POSTAL RATE AND FEE CHANGES

Docket No. R2006-1

RESPONSE OF THE UNITED STATES POSTAL SERVICE WITNESS SMITH (USPS-T-13) TO INTERROGATORY OF VALPAK DIRECT MARKETING SYSTEMS, INC. AND VALPAK DEALERS' ASSOCIATION, INC. (VP/USPS-T13-1)
(June 27, 2006)

The United States Postal Service hereby provides the response of Witness Smith (USPS-T-13) to the following interrogatory of Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc.: VP/USPS-T13-1, filed on June 13, 2006.

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

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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June 27, 2006

**RESPONSE OF POSTAL SERVICE WITNESS MARC A. SMITH TO
INTERROGATORY OF VALPAK DIRECT MARKETING SYSTEMS, INC.
AND VALPAK DEALERS ASSOCIATION**

VP/USPS-T13-1.

Please refer to the attachment to this interrogatory. Column 1 contains Base Year volume variable costs, as shown in USPS-LR-L-3. Columns 2 and 3 distinguish those volume variable costs that are considered to be indirect from those that are considered to be direct. The separation between direct and indirect costs was obtained from USPS-LR-L-93, PRCBY05.xls, pages 4-6. Column 4 shows the USPS piggyback factors applied to direct costs, and Column 5 shows the total piggybacked costs.

- a. Please review the costs in columns 2 and 3 and either (i) confirm that they are correct and in the correct columns, as shown, or (ii) for each cost segment, provide the correct distribution of volume variable costs as between direct and indirect costs.
- b. The piggyback factors shown in column 4 are from USPS-T-13, Attachment 8, row 41, and are for TY2008BR – USPS Version. Please confirm that these are the correct piggyback factors to apply to the Base Year volume variable direct costs, or supply the correct piggyback factor for each Base Year volume variable direct cost shown in the attachment.
- c. Please confirm that the total piggybacked costs, \$10,002,532,000, shown at the bottom of column 5 on page 2 of the attachment is correct, or supply the correct figure for the total indirect costs that are piggybacked onto the volume variable direct costs in column 3 (*i.e.*, \$27,597,332,000 in the attachment).
- d. Please explain why the procedures that you use to develop piggyback factors result in total piggybacked indirect costs (*i.e.*, \$10,002,532,000) that fail to account for a portion (*i.e.*, 19.3 percent) of total indirect volume variable costs (*i.e.*, \$12,393,563,000).
- e. Please explain whether the piggyback factors used to compute cost differentials between rate categories should be increased by an amount sufficient to account for all, or nearly all, of the Postal Service's indirect volume variable costs.

Seg. No.		(1) Volume Variable Costs	(2) Indirect	(3) Direct	(4) USPS Piggy- back	(5) USPS Piggy'd Costs
1	Postmasters	379,979	379,979	0	1.223	0
2	Supervisors and Technicians	2,122,210	2,122,210	0	1.000	0
2.1.1	Mail processing	813,076	813,076	0		
2.1.2	Central mail markup	37,508	37,508	0		
2.2	Window service	99,795	99,795	0		
2.3	Admin & support	40,031	40,031	0		
2.4.1	City delivery	556,482	556,482	0		
2.4.2	Rural delivery	44,358	44,358	0		
2.4.3	Vehicle svc drivers	23,239	23,239	0		
2.5.2	Higher level	68,492	68,492	0		
2.5.5	Training	24,071	24,071	0		
2.5.6	Qual control/Rev prot	40,344	40,344	0		
2.5.7	Joint supervision	374,813	374,813	0		
3	Clerks and mailhandlers, CAG A-J Offices	14,424,203	663,556	13,760,648		7,655,464
3.1	Mail processing	12,703,875	0	12,703,875	1.570	7,241,208
3.2	Window service	1,056,773	0	1,056,773	1.392	414,255
3.3.1	Administrative clerks	629,633	629,633	0		
3.3.2	Time and attendance	33,922	33,922	0		
4	Clerks, CAG K Offices	3,335	0	3,335	1.000	0
6	City Delivery Carriers, Office Activity	4,201,813	1,003,740	3,198,073	1.264	844,291
6.1	In-office direct	3,198,073	0	3,198,073		
6.2.2	In-office support overhead	734,063	734,063	0		
6.2.3	In-office support other	269,676	269,676	0		
7	City Delivery Carriers, Street Activity	3,909,622	455,695	3,453,927	1.264	911,837
7.2	Delivery activities	3,453,927	0	3,453,927		
7.3	Delivery support	455,695	455,695	0		
8	Vehicle Service Drivers	367,029	0	367,029	1.482	176,908
10	Rural Carriers	2,214,077	0	2,214,077	1.187	414,032
	Evaluated routes	2,035,578	0	2,035,578		
	Other routes	178,499	0	178,499		
11	Custodial & Maint. Services	2,027,950	2,027,950	0	1.000	0
11.1.1	Custodial personnel	654,669	654,669	0		
11.1.2	Contract cleaners	54,515	54,515	0		
11.2	Op. equipment maintenance	1,005,109	1,005,109	0		
11.3	Custodial & maint. Services	313,657	313,657	0		
12	Motor Vehicle Service	268,037	268,037	0	1.000	0
12.1	Personnel	104,190	104,190	0		
12.2	Supplies & materials	157,245	157,245	0		
12.3	Vehicle hire	6,602	6,602	0		

Seg. No.	(1) Volume Variable Costs	(2) Indirect	(3) Direct	(4) USPS Piggy- back	(5) USPS Piggy'd Costs
13 Miscellaneous Local Operations	4,148	4,148	0	1,000	0
13.1 Carfare	1,694	1,694	0		
13.2 Driveout -- city carriers	2,455	2,455	0		
14 Transportation	4,564,206	0	4,564,206	1,000	0
14.1.1 Domestic air	1,598,314	0	1,598,314		
14.1.1 Domestic air -- Alaska	8,005	0	8,005		
14.1.2 Highway	2,122,924	0	2,122,924		
14.1.3 Railroad	118,014	0	118,014		
14.1.4 Domestic water	25,038	0	25,038		
14.2 International	691,911	0	691,911		
15 Building Occupancy	1,217,936	1,217,936	0	1,000	0
15.1 Rents	863,364	863,364	0		
15.2 Fuel & utilities	354,572	354,572	0		
16 Supplies and Services	1,278,496	1,272,629	5,867	1,000	0
16.1.1 Stamps	87,098	87,098	0		
16.1.2 Money orders	5,867	0	5,867		
16.1.3 Stamped cards & envelopes	7,306	7,306	0		
16.3.1 Custodial & building	101,250	101,250	0		
16.3.2 Equipment	309,630	309,630	0		
16.3.3 Track & trace	423	423	0		
16.3.4 Other miscellaneous	766,923	766,923	0		
17 Research & Development	0	0	0	1,000	0
18 Administration & Area Operations	1,441,253	1,441,172	81	1,000	0
18.1 Postal Inspection Service	43,325	43,325	0		
18.2.7 Commissions, non-U.S. Mos	81	0	81		
18.3.1 Repriced annual leave	49,056	49,056	0		
18.3.2 Holiday leave	533	533	0		
18.3.4 Workers compensation	454,940	454,940	0		
18.3.5 Unemployment compensation	23,930	23,930	0		
18.3.6 Annuitant health insurance	863,186	863,186	0		
18.3.7 Annuitant life insurance	6,202	6,202	0		
19 General Management Systems	0	0	0	1,000	0
20 Other Accrued Expenses	1,566,601	1,536,512	30,090	1,000	0
20.1 Equipment depreciation	738,572	738,572			
20.2 Vehicle depreciation	35,989	35,989			
20.3 Bldg & leasehold depreciation	760,767	760,767			
20.4 Indemnities	30,090		30,090		
20.5 Interest expense	1,183	1,183			
TOTAL	39,990,895	12,393,563	27,597,332		10,002,532

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RESPONSE:

- a. As indicated by witness Milanovic, USPS-T-9, in his response to VP/USPS-T9-1, the Postal Service does not separate base year costs into “direct” and “indirect” categories.¹ I have no opinion on the division of costs into “direct” and “indirect” as contained in USPS-LR-L-93, PRCBY05.xls, pages 4-6. The line between “direct” and “indirect” can be a matter of judgment and would depend on the purpose for making the distinction.
- b. Not confirmed. To address the questions you raise I have developed an attachment to this response that splits volume variable costs into: labor costs upon which costs are piggybacked, piggybacked costs, and other non-personnel costs. Base Year piggyback factors are provided in this attachment. These piggyback factors are from LR-L-52, spreadsheet BYPBack.USPS.xls. In addition, three additional sets of piggyback factors for Training, Supervisors Training, and Data Collection & Other Administrative are provided in LR-L-146, in spreadsheet BYPBack.All.USPS.xls.
- c. Not confirmed. See the Attachment to this response.

¹ In my testimony I reference costs that appear in the numerator of the piggyback factors, but not in the denominator, as “indirect costs.” These piggybacked costs are indirect or support costs for the purposes of the construction of the piggyback factors.

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- d. As shown in the attachment of this response, the full amount (except for rounding) of volume variable costs are accounted for by labor costs upon which piggyback factors are based, piggybacked costs and other non-personnel costs. The spreadsheet in LR-L-146 shows (in the sheets marked Summary of Outputs and Summary of Inputs) that the total costs for the cost segments which are included in piggybacked costs are accounted for in the development of the piggyback factors.
- e. As shown in the attachment of this response, the full amount (except for rounding) of volume variable costs are accounted for by labor costs upon which piggyback factors are based, piggybacked costs and other non-personnel costs.

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Division of FY 2005 Volume Variable Costs Into Labor, Piggyback and Other Non-Personnel Cost

Comp	Component Title	C/S	Labor Costs	Piggyback Factor	Piggyback Costs	Other Costs	Total Costs
0035	Mail Processing	3.1	12,703,875	1.510	6,475,352		19,179,226
0042	Clerks CAG K Offices	4.1	3,335	1.510	1,700		5,035
0040	Window Services	3.2	1,056,773	1.410	432,824		1,489,597
0256	C/S 6 City Delivery Carriers – Office Activity	6.0	4,201,813	1.251	1,054,458		5,256,271
0257	C/S 7 City Delivery Carriers – Street Activity	7.0	3,909,622	1.251	981,132		4,890,754
0057	Vehicle Service Drivers	8.1	367,029	1.454	166,809		533,838
0260	C/S 10 Rural Carriers	10.0	2,214,077	1.179	396,449		2,610,527
0251	C/S 1 Postmasters	1.0	379,979	1.223	84,556		464,535
0066	Claims & Inquiry	3.3.1.1	3,060	1.349	1,067		4,127
	Supervisors Training		24,071	1.082	1,965		26,037
421 & 41	Data Collection & Other Admin.	3.3.1.2 & 3.3.1.3	120,288	1.261	31,447		151,735
0470	Training	3.3.1.5	94,065	1.121	11,342		105,407
	Post Office Box Space- Related					487,622	487,622
0264	C/S 14 Transportation	14.0				4,564,206	4,564,206
0180	Stamps & Dispensers	16.1.1				87,098	87,098
181 & 244	Money Orders	16.1.2				5,948	5,948
0248	Stamped Cards & Embossed Stamped Envelopes	16.1.3				7,306	7,306
0196	Comprehensive Tracking & Tracing	16.3.3				423	423
0187	Misc Attrib PMPC / Intl / DC Supplies & Services	16.3.4.5				91,108	91,108
0397	Indemnities	20.4				30,090	30,090
	Total Volume Variable Costs		25,077,987		9,639,101	5,273,800	39,990,888

Source: See USPS LR-L-146.

CERTIFICATE OF SERVICE

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

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