

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

ANNUAL COMPLIANCE REPORT, 2007

Docket No. ACR2007

RESPONSES OF THE UNITED STATES POSTAL SERVICE
TO QUESTIONS 10, 12, 13, 16, 17, 18, 19, 20, AND 21 OF COMMISSION
INFORMATION REQUEST NO. 1
(February 1, 2008)

Commission Information Request No. 1 was posted on January 25, 2008. The request sought answers "as soon as they are developed." Attached are the Postal Service's responses to questions 10, 12, 13, 16, 17, 18, 19, 20, and 21. One of the responses refers to materials which are being separately provided to the Commission as part of the non-public annex of materials relating to this proceeding. A separate notice regarding such materials is also being filed today. Responses to additional questions will be submitted as they are developed.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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10. The supplement to the preface for USPS-FY07-2 describes the treatment of Annuitant Health and CSRS Benefits costs and states that the Postal Accountability and Enhancement Act (PAEA) requires that "...OPM will determine the amount of the new obligations incurred each year..." and that OPM's determination for FY 2007 is the source of the current portion of the Annuitant Health Benefits.

Please provide the report from OPM which determines the FY 2007 estimate of the Annuitant Health Benefits obligations, highlighting the current portion of the Annuitant Health Benefits of \$3.175 billion.

RESPONSE:

The relevant determination by OPM (which is also reproduced on page 26, second table, of the Postal Services' 2007 Annual Report) was not transmitted to the Postal Service in any formal report, but instead was sent via e-mail. The text of that email (including the two embedded tables) is reproduced below.

The Valuation of Post Retirement Health Liabilities and Normal Costs is performed consistent with Federal Accounting Standards Advisory Board (FASAB) Statement of Federal Financial Accounting Standards (SFFAS) No. 5 and uses an Aggregate Entry Age Normal Cost Method. Demographic assumptions and an interest rate assumption of 6.25% are consistent with the pension valuation assumptions, but decrements are based upon counts or number rather than dollars. The Normal cost which is on a per participant basis is computed to increase annually by a constant medical inflation rate which is assumed to be 7% per annum. Normal costs are derived from the current Federal Employees Health Benefits Program (FEHBP) on-roll population with an accrual period from entry into FEHBP to assumed retirement. Entry into the FEHBP is generally later than entry into the Federal retirement systems. The Accrued Liability is equal to the Total Liability less Future Normal Payments. The Liabilities and Normal Costs that appear in the USOPM financial statements and are used in Agency Reporting are based upon annuitant medical costs (including administration costs) less annuitant premium payments. The values that are being provided to the Postal Service are based the same methodology and assumptions as for the Financial Statements except the average government share of premium payments for annuitants is substituted for annuitant medical costs less annuitant premium payments. This government share of premium payments has been adjusted downward since our June 2007 estimate to reflect premium payments levels that correspond to actual costs. As before, this amount is

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assumed to increase at 7% per annum. For current Postal Annuitants this government share of premium payments is adjusted to reflect the pro-rata share of civilian service to total service for which the Postal Service is responsible. The pro-rata adjustment is made by applying calculated factors based upon actual payments that vary by age and Medicare status of the enrollments. For Postal Actives the pro-rata share in retirement is assumed to be 93% of the total.

The results of a sensitivity run assuming an 8% trend is also provided.

Postal Valuation as of 9/30/2006

Trend Assumption 7%

Postal Actives 618,712

Postal Annuitants 483,448

Per Participant Normal Cost \$4,801.52

Postal Liability (\$millions)

Liability for Actives

PV Future Premium Payments \$78,435

PV Future Normal Payments \$35,238

Accrued Liability for Actives \$43,197

Liability for Annuitants \$31,618

Total Liability as of 9/30/2006 \$74,815

FY 2007 Interest \$4,676

FY 2007 Normal Payments \$3,175

FY 2007 Premium Payments \$1,880

Total Liability as of 9/30/2007 \$80,786

Postal Valuation as of 9/30/2006

Trend Assumption 8%

Postal Actives 618,712

Postal Annuitants 483,448

Per Participant Normal Cost \$6,185.69

Postal Liability (\$millions)

Liability for Actives

PV Future Premium Payments \$100,424

PV Future Normal Payments \$49,501

Accrued Liability for Actives \$50,924

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Liability for Annuitants	\$35,690
Total Liability as of 9/30/2006	\$86,614
FY 2007 Interest	\$5,413
FY 2007 Normal Payments	\$4,129
FY 2007 Premium Payments	\$1,902
Total Liability as of 9/30/2007	\$94,254

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12. Please provide an explanation [with respect to USPS-FY07-19] for what is an apparently significant increase in direct city carrier casing costs.

a. Please confirm that direct city carrier casing costs have increased approximately 60.4 percent from FY 2005 to FY 2007 for the following rate categories for both First-Class Presort and Standard Mail: Non-automation – Nonmachinable Mixed ADC; Non-automation – Nonmachinable ADC; Non-automation – Nonmachinable 3-Digit; and Non-automation – Nonmachinable 5-Digit between FY05 and FY07. (See e.g., cell E46, worksheet “17.In-Office Detail,” file UDCmodel071211.xls and cell E18, worksheet “17.In-Office Detail,” file UDCmodel.PRC.xls).

b. Please explain why casing costs have increased to this extent for these rate categories.

RESPONSE:

a. Not confirmed. The table below provides the direct casing costs for FY2007 and FY2005 and the percentage change in the direct casing costs for each rate category within First Class Presort and Standard Regular subclasses.

The specific rate categories referenced in the question are in bold type.

Therefore, the statement presented for confirmation is true with regard to First-Class Mail, but not with regard to Standard Mail.

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Rate Category	2007 Direct Casing Costs (000)	2005 Direct Casing Costs (000)	%Change 2007/2005 Casing Costs
First Class Presort			
Nonautomation – Nonmach Mixed ADC	\$804	\$501	60%
Nonautomation – Nonmach ADC	\$380	\$237	60%
Nonautomation – Mach Mixed AADC	\$5,149	\$6,121	-16%
Nonautomation – Mach AADC	\$1,717	\$2,041	-16%
Nonautomation – Nonmach 3-Digit	\$487	\$304	60%
Nonautomation – Nonmach 5-Digit	\$98	\$61	60%
Nonautomation – Mach 3-Digit	\$4,059	\$4,647	-13%
Nonautomation – Mach 5-Digit	\$879.29	\$1,006	-13%
Automation Mixed AADC	\$27,368	\$28,215	-3%
Automation AADC	\$19,859	\$21,501	-8%
Auto 3-Digit Letters	\$170,319	\$184,463	-8%
Auto 5-Digit Letters CSBCS/Manual Sites	\$120,559	\$ 90,611	33%
Auto 5-Digit Letters Other Sites	\$17,131	\$25,721	-33%
Auto 5-Digit Letters	\$137,690	\$116,332	18%
Auto CR Letters	\$10,538	\$15,751	-33%
Presort Letters Subtotal*	\$379,353	\$381,185	0%
	2007 Direct Casing Costs	2005 Direct Casing Costs	%Change 2007/2005 Casing Costs
Standard Mail Regular			
Nonautomation – Nonmach Mixed ADC	\$2,735	\$1,602	71%
Nonautomation – Nonmach ADC	\$932	\$261	257%
Nonautomation – Mach Mixed AADC	\$6,707	\$643	943%
Nonautomation – Mach AADC	\$4,156	\$217	1818%
Nonautomation – Nonmach 3-Digit	\$3,959	\$34,031	-88%
Nonautomation – Nonmach 5-Digit	\$1,374	\$8,089	-83%
Nonautomation – Mach 3-Digit	\$4,604	\$7,203	-36%
Nonautomation – Mach 5-Digit	\$1,743	\$2,919	-40%
Automation Mixed AADC	\$21,410	\$20,002	7%
Automation AADC	\$20,173	\$18,822	7%
Automation 3-Digit Letters	\$148,598	\$123,362	20%
Automation 5-Digit Letters	\$141,561	\$101,579	39%
Regular Letters	\$357,953	\$318,728	12%
Standard Letters Subtotal	\$357,953	\$318,728	12%

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b. The direct casing costs for the Nonautomation – nonmachinable rate categories within the First Class Presort subclass rose 60 percent from FY2005 to FY2007. The direct casing costs increased by this amount because the mail flow models (which are used to derive DPS percentages by rate category) estimated that city carrier cased volume dropped 30 percent, while First Class Presort subclass direct casing costs dropped 0.5 percent from FY2005 to FY2007. In FY2007, the mail flow models estimated that 89 percent of First Class Presort mail was DPS'd as compared to 84 percent in FY2005. Multiplying one minus the DPS percentage by their respective city carrier volumes (30.3B in FY07 and 30.0B in FY05) results in approximately 1.4 billion less First Class Presort cased pieces on city routes in FY07 as compared to FY05. As a result, the unit direct casing cost (per city carrier delivered piece) is 11.2 cents in FY07 as compared to 7.9 cents in FY05. Applying the FY07 unit casing cost to the First Class Presort cased volumes by rate category resulted in a 60 percent increase in direct casing costs for First Class Presort Nonautomation – nonmachinable rate categories between FY05 and FY07.

For Standard Regular, the mail flow models also indicated an increase in the subclass DPS percentage (89% in FY07 as compared to 83% in FY05). Direct casing costs also rose over the same period, by 12 percent. As a result, the unit direct casing cost (per city carrier delivered piece) was 9.9 cents in FY07 as compared to 5.9 cents in FY05. As with First Class Presort, the unit casing cost is multiplied by city carrier estimated cased volume to calculate the direct casing costs by rate category within Standard Regular. However, the city carrier

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Standard Regular volumes (which are derived from RPW proportions) by rate category did not change uniformly for all Nonautomation nonmachinable and Nonautomation machinable rate categories as they did within First Class Presort. (For example, First Class presort volume increased eight percent for each Nonautomation nonmachinable rate category, while volume decreased nine percent for each Nonautomation machinable rate category). As a result, the percentage changes in direct casing costs are not the same for all Nonautomation nonmachinable rate categories nor for all Nonautomation machinable rate categories within Standard Regular mail, as the table provided in response to part a. of this question reflects.

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13. Please explain [with respect to USPS-FY07-19] the reason Special Purpose Route flat and parcel delivery costs for bound printed matter and media mail are not included in delivery activities in USPS-LR-L-67, DCModel.USPS.xls, but are included in UDCmodel071211.xls.

RESPONSE:

The Special Purpose Route flat and parcel delivery costs for Bound Printed Matter and Media Mail were erroneously omitted from USPS-LR-L-67 in Docket No. R2006-1. That inadvertent omission has been corrected, and the Special Purpose Delivery flat and parcel delivery costs for Bound Printed Matter and Media Mail are properly included in the unit delivery costs for their respective categories in USPS-FY07-19.

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16. In Docket No. R2006-1, MODS productivities for AFSM100 ATHS sorting operations were not available. Therefore, proxies were constructed using the MODS productivity data for each corresponding AFSM100 (non-ATHS) operations, assuming 20 percent fewer workhours in the denominator. In USPS-FY07-23, YRscrub2007.xls, 'Table' sheet, rows 35-40, what appear to be actual MODS productivities for AFSM100 AFHS operations are presented. Please confirm that these are actual MODS productivities for AFSM100 AFHS operations, and discuss whether it would be reasonable to utilize them in the flats cost avoidance models. If it would not be reasonable to utilize them in the flats cost avoidance models, please explain.

RESPONSE:

Confirmed that USPS-FY07-23 provides actual ATHS productivities. As of R2006-1, the state of ATHS deployment was such that there was insufficient data from ATHS operations to provide reliable productivities. For FY2007, the Postal Service regards the ATHS data as reliable; indeed, the data reflect complete deployment of ATHS equipment.

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17. In Docket No. R2006-1, the cost avoidance models for flats and letters used a single productivity for REC Mixed-Shape Keying. USPS-FY07-23, YRscrub2007.xls, 'Table' sheet, row 11, where this productivity would appear, instead instructs to "See REC productivity worksheet." USPS-FY07-23, RECprods2007.xls presents an apparent breakout of REC productivities between APPS, Flats, Letters, COA, and PARS as well as productivities that are "Adjusted for Overhead." It is the adjusted, shape-specific productivities that are used in the cost avoidance models.

- a. Please explain the rationale for the change to shape-specific REC productivities.
- b. Please explain and identify the difference between the total console hours in row 13, and the "Hours Including Overhead" in row 16, and include a discussion of the rationale for the adjustment.
- c. Please also identify the figure that corresponds to the "REC Mixed-Shape Keying" productivity used in Docket No. R2006-1.

RESPONSE:

a.-b. The changes in REC productivity methodology were motivated by the addition of flat, APPS, and PARS image keying to REC operations. The Postal Service investigated REC clocking practices and found that because Data Conversion Operators (DCOs) frequently switch from one system to another during the course of their shifts, REC managers do not have employees re-clock for work assignment changes to minimize non-productive time. Additionally, the implementation of MODS operation 388 ("REC Mixed VCS Keying") creates a mismatch of REC image volumes and REC workhours in MODS. The images keyed in operation 388 are credited to the appropriate shape-related operation(s) for the system(s) where the DCOs worked (e.g., 775 for letters, 389 for flats, 387 for APPS). However, REC workhours are reliable in the aggregate.

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Using console hours remedies the workhour-volume alignment issue, since DCOs must be logged into the system they are working and must log out before changing work assignments. However, productivities based on console hours alone would not be equivalent to productivities based on MODS workhours. The console hours reflect the time the DCOs are logged into an image processing system and keying mail. The MODS workhours include on-the-clock time during which DCOs are not logged into an image processing system, notably “variable overheads” such as hourly ergonomic breaks and time spent moving between workstations. Those overheads tend to be generated in proportion to the “direct” keying labor. The overhead adjustment, then, allocates the full on-the-clock time recorded in MODS to the shape-specific console hours.

- c. The previous “REC Mixed-Shape Keying” productivity was derived from data for MODS operation 775. While that operation is entitled “RBCS Keying” without a shape specification, it is used for keying letter-shape mail, so the R2006 productivity was misnamed. In USPS-FY07-23, file RECprods.xls, the productivity for the “Letters” product is the closest conceptual equivalent to the operation 775 productivity.

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18. In the preface to the FY 2007 Cost Segments and Components Report (filename "USPS-FY07-2 Preface.doc"), the description of attributable cost changes for Segment 16 notes that "a new general ledger expense account for eBay fees was generated, and these costs were attributed based on the contract fees and the classes of mail that paid the contract fees." Please confirm that the general ledger account entitled "Retail Merchandise, Cost of Goods Sold," account number 52410.901, is the expense account for eBay fees. If not, please provide the applicable general ledger account number used that shows the \$27,580,416 total expense for eBay fees.

RESPONSE:

General ledger account number 52410.901 was the expense account for eBay fees in FY 2007. The name of the account was changed in FY 2007 to "eBay fees" as shown in the FY 2007 Cost Segment & Components Reconciliation to Financial Statements and Account Reallocations, which is being filed electronically in response to question 20 of this information request. In FY 2008, the "eBay fees" account got a slightly different number, and account number 52410.901 reverted to the "cost of goods sold" account suggested in your question.

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19. In the Cost Segment “B” workpapers file I_Forms.xls at tab worksheet CS16.1.3, please identify the source of the “WT Postage” values that are used to develop the distribution key for eBay expenses. If the WT Postage values were calculated, please provide their derivation and cite all sources. If the source documents have not been previously provided in this docket, please include a copy in your response.

RESPONSE:

The total postage paid values for the USPS/eBay agreement are obtained from the USPS National Metered Activity Tracking System (NMATS). The NMATS file contains the total fiscal year revenue and special services for each mail class included in the USPS/eBay revenue sharing alliance. The FY 2007 NMATS file containing eBay postage is included as an Excel file in USPS-FY07-NP11 (Materials Relating to eBay Filed in Response to CIR No. 1, Q. 19), being filed today as part of the Non-Public Annex.

The weighted postage values that were used to develop the distribution key for eBay expenses were calculated by scaling the total eBay postage paid for each domestic and international postal product covered in the USPS/eBay Agreement. On May 14 of FY 2007, the terms of the revenue sharing provisions changed. Because this change occurred during the fiscal year, it was deemed appropriate that the total eBay revenues be scaled by different factors for the portion of the year between October 1, 2006 to May 13, 2007, and for the portion of the year between May 14, 2007 to September 30, 2007. The relevant calculations are shown in the Excel workbook “eBay2007worksheet.xls” which is also included in USPS-FY07-NP11. A narrative description of the methodology

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appears in the Summary Costing EBAY Word document, likewise included in
USPS-FY07-NP11.

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- 20.** Please provide the file containing the FY 2007 “Cost Segment and Components Reconciliation to Financial Statements and Account Reallocations.”

RESPONSE:

The requested file has been attached electronically as CIR.1.Q.20.ReAITB07.xls.

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21. Please provide a copy of the latest updated issue of *Handbook F-8, the USPS Chart of Accounts*.

RESPONSE:

Historically, the function of Handbook F-8 has been to set forth the Postal Service's general classification of accounts. An Excel spreadsheet (CIR.1.Q.21.Class.Accounts.xls) setting forth the current (Jan. 2008) classification of accounts is attached electronically.

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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