

OFFICIAL TRANSCRIPT OF PROCEEDINGS BEFORE THE POSTAL REGULATORY COMMISSION

In the Matter of:)
)
RATE ADJUSTMENT DUE TO) Docket No. R2010-4
EXTRAORDINARY OR)
EXCEPTIONAL CIRCUMSTANCES)

VOLUME #2

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POSTAL REGULATORY COMMISSION

In the Matter of:)
)
 RATE ADJUSTMENT DUE TO) Docket No. R2010-4
 EXTRAORDINARY OR)
 EXCEPTIONAL CIRCUMSTANCES)

Hearing Room
 Postal Regulatory Commission
 901 New York Avenue, N.W.
 Washington, D.C.

Volume 2
 Wednesday, August 11, 2010

The above-entitled matter came on for hearing
 pursuant to notice, at 9:34 a.m.

BEFORE:

HON. RUTH Y. GOLDWAY, CHAIRMAN
 HON. TONY HAMMOND, VICE-CHAIRMAN
 HON. DAN G. BLAIR, COMMISSIONER
 HON. NANCY E. LANGLEY, COMMISSIONER
 HON. MARK ACTON, COMMISSIONER

APPEARANCES:

On behalf of the United States Postal Service:

ERIC KOETTING, Esquire
 DAVID H. RUBIN, Esquire
 United States Postal Service
 475 L'Enfant Plaza, S.W.
 Washington, D.C. 20260

APPEARANCES: (cont'd.)

On behalf of the Office of the Consumer Advocate:

JIM WACLOWSKI, Esquire
PAM THOMPSON, Esquire
NATALIE REA, Esquire
Postal Regulatory Commission
Office of Consumer Advocate
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Washington, D.C.
(202) 789-6833

On behalf of Greeting Card Association:

(No Appearance.)

On behalf of National Association of Postmasters of the United States:

(No Appearance.)

On behalf of National Association of Letter Carriers:

(No Appearance.)

On behalf of David B. Popkin:

(No Appearance.)

On Behalf of National Rural Letter Carriers Association:

(No Appearance.)

C O N T E N T S

WITNESSES APPEARING:

STEPHEN J. MASSE

<u>WITNESSES:</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>	<u>VOIR DIRE</u>
Stephen J. Masse	136	--	--	--	--

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E X H I B I T S

<u>EXHIBITS AND/OR TESTIMONY</u>	<u>IDENTIFIED</u>	<u>RECEIVED</u>
Corrected statement of Stephen J. Masse on behalf of the United States Postal Service with associated library references, Exhibit 1	136	139
Answers of Stephen J. Masse to Presiding Officer Information Requests, Exhibit 2	139	140
Detailed Breakdown of the USPS Financial Information Reports	171	171

1 fellow Commissioners thought it might be appropriate
2 to acknowledge our sadness and perhaps provide a
3 moment of silence.

4 Before I suggest a moment of silence, I
5 thought perhaps some of my fellow Commissioners might
6 want to say something about Senator Stevens.
7 Commission Blair, I know that you worked with him
8 closely.

9 COMMISSIONER BLAIR: Thank you, Madam Chair.
10 It's a sad day for the country and the postal
11 community. Senator Stevens was such a champion on the
12 Postal Service's behalf and the community's behalf.

13 I've had the chance to work with him and his
14 staff since I first came to Washington on a number of
15 issues not only at the Postal Service, but he was also
16 a champion of civil service.

17 I know that we share in the grief over his
18 death and would extend our best wishes and prayers to
19 the family.

20 CHAIRMAN GOLDWAY: Thank you.

21 COMMISSIONER LANGLEY: And I, too, wish to
22 give my fond aloha to Senator Stevens. I worked with
23 him and his staff for just under 25 years. Hawaii and
24 Alaska share many commonalities, and I can say without
25 a doubt that the Alaska delegation and the Hawaii

1 delegation is quite close, and I know that he will be
2 missed.

3 He was definitely a tiger when it came to
4 postal issues, as well as federal employee issues, and
5 there was nothing finer than seeing him wearing his
6 Hulk tie. He had different ties that he wore when he
7 was going into battle, and the Hulk tie was reserved
8 for appropriations battles. I do remember that
9 fondly.

10 And also remembering Wayne Schley, I guess I
11 would say our former colleague here at the
12 Commissioner. Commissioner Schley moved to Alaska
13 when he was quite young and worked for Senator Stevens
14 for many years, so I know that right now Wayne and the
15 rest of the Stevens family, extended family, is
16 feeling deep sorrow, and I join them in my thoughts
17 and prayers. Thank you.

18 CHAIRMAN GOLDWAY: Thank you. Commissioner
19 Hammond?

20 VICE CHAIRMAN HAMMOND: Thank you, Madam
21 Chairman. I think that you and I are the only two
22 still on the Commission who had the opportunity at the
23 request of Senator Stevens and the rest of the Alaska
24 delegation about five, six years ago possibly to go
25 and see firsthand the Alaska postal situation.

1 CHAIRMAN GOLDWAY: That's right.

2 VICE CHAIRMAN HAMMOND: We went to some
3 really remote places while we were up there. Yes,
4 indeed. I recall that he changed his schedule when we
5 got back to Anchorage so that he could take time and
6 spend it with us, and we went to his office for about
7 an hour's worth of discussion on issues before the
8 Postal Service in Alaska.

9 I know everyone appreciates his impact on
10 the Postal Service and the care that he took for
11 people in Alaska.

12 CHAIRMAN GOLDWAY: Thank you. Mr. Acton?
13 No? All right.

14 Well, if we just take a moment to remember
15 him? I think that would be a nice thing to do for all
16 of us.

17 (Whereupon, a moment of silence was had.)

18 CHAIRMAN GOLDWAY: And now we'll get back to
19 the business at hand, which I'm sure he would be
20 interested in as well.

21 Yesterday we heard from Joseph Corbett,
22 Executive Vice President and Chief Financial Officer
23 of the Postal Service. Today we shall receive into
24 evidence the written statement of Stephen J. Masse,
25 Vice President, Finance and Planning, for the Postal

1 Service.

2 Tomorrow the Postal Service will present
3 Frank Neri, Manager of Processing Operations in the
4 Headquarters Network Operations Group, and James M.
5 Kiefer, a pricing economist.

6 Only the Commission will question the Postal
7 Service representative. Nevertheless, interested
8 parties have been given the opportunity to suggest
9 questions to the Commission, and a number of groups
10 and entities have filed suggested questions.

11 Once again, I and my fellow Commissioners
12 wish to express our appreciation for the effort that
13 has gone into the preparation of these questions.
14 Some of these questions will be asked today.

15 Others, however, are questions that were
16 submitted by participants more likely to elicit
17 meaningful responses if presented in the form of
18 written information requests. Accordingly, we
19 anticipate that additional presiding officer
20 information requests will include some of the
21 suggested questions, as well as followup from these
22 hearings.

23 At this point I would like to give my
24 colleagues any opportunity to offer remarks on today's
25 hearing. Commissioner Langley?

1 COMMISSIONER LANGLEY: I just have a very,
2 very brief comment. I think yesterday's hearing
3 demonstratēd our reasoned and balanced approach that
4 we are trying to take to what I see as an extremely
5 complex issue and one in which we have to balance the
6 financial needs of the Postal Service with the intent
7 of the law.

8 This is not an easy decision that we're
9 moving towards. I do believe that we are on the right
10 path, however. Thank you.

11 CHAIRMAN GOLDWAY: Thank you. Do any of my
12 other colleagues wish to say anything at this time?

13 (No response.)

14 CHAIRMAN GOLDWAY: All right. Mr. Koetting
15 from the Postal Service, would you identify your
16 postal witness?

17 MR. KOETTING: Thank you, Madam Chairman.
18 Eric Koetting for the United States Postal Service,
19 and the next official representing the Postal Service
20 will be Stephen J. Masse.

21 CHAIRMAN GOLDWAY: Would you please stand,
22 Mr. Masse?

23 //

24 //

25 //

1 Whereupon,

2 STEPHEN J. MASSE

3 having been duly sworn, was called as a
4 witness and was examined and testified as follows:

5 CHAIRMAN GOLDWAY: Thank you.

6 DIRECT EXAMINATION

7 BY MR. KOETTING:

8 Q Mr. Masse, for the record, could you please
9 state your full name and your title?

10 A I'm Stephen J. Masse, the Vice President of
11 Finance and Planning for the U.S. Postal Service.

12 (The document referred to was
13 marked for identification as
14 Exhibit No. 1.)

15 BY MR. KOETTING:

16 Q Mr. Masse, I'm handing you a copy of a
17 document titled Statement of Stephen J. Masse on
18 behalf of the United States Postal Service. Are you
19 familiar with this document?

20 A Yes, I am.

21 Q Was it prepared by you or under your
22 supervision?

23 A Yes, it was.

24 Q Does the copy that I've handed you include
25 the revisions filed last Friday, August 6, on page 6,

1 page 11 and a revised set of attachments?

2 A Yes, it does.

3 Q I believe you were in the hearing room
4 yesterday morning when Mr. Corbett introduced a set of
5 slides he had presented to the Board of Governors
6 regarding the Quarter 3 financial actual results. Are
7 you familiar with those slides as well?

8 A Yes, I am.

9 Q With the understanding that the
10 Commissioners may wish to revisit that matter in their
11 questions as well, could you very briefly summarize
12 the significance of the Quarter 3 results on the
13 statement you submitted on July 6?

14 A The Quarter 3 results included a very
15 significant adjustment for workers' compensation
16 which, as Mr. Corbett explained yesterday, is a
17 noncash item that doesn't affect the liquidity
18 position of the Postal Service which is currently --
19 I'm sorry. I'm trying to get this to go off.

20 CHAIRMAN GOLDWAY: It seems better now,
21 whatever you've done to your BlackBerry. It is better
22 now.

23 THE WITNESS: If we were to exclude that
24 adjustment for workers' compensation or the
25 revaluation of liability for workers' compensation the

1 third quarter results are in line with our expectation
2 for the full year, and in effect they help to affirm
3 the projection that we have for the full year loss in
4 2011.

5 BY MR. KOETTING:

6 Q Mr. Masse, with the exception of the effect
7 of the Quarter 3 actuals as you've just described, if
8 you were to present your statement orally today would
9 it be the same as the statement that you submitted on
10 July 6 and as revised on August 6?

11 A Yes, it would.

12 Q And on page 14 of your statement, is it
13 correct that there are a list of folders related to
14 your statement?

15 A Yes.

16 Q And I believe there are six folders?

17 A Yes.

18 Q And is it your intent to sponsor those
19 folders, as well as this statement?

20 A Yes.

21 MR. KOETTING: With that, Madam Chairman,
22 the Postal Service would request that the statement of
23 Stephen J. Masse on behalf of the United States Postal
24 Service be admitted into the record.

25 CHAIRMAN GOLDWAY: Thank you. The corrected

1 statement of Stephen J. Masse is received into
2 evidence, as well as his associated library
3 references. However, as is our practice, it will not
4 be transcribed.

5 (The document referred to,
6 previously identified as
7 Exhibit No. 1, was received
8 in evidence.)

9 CHAIRMAN GOLDWAY: Mr. Masse has been
10 identified as the Postal Service representative
11 prepared to attest to the accuracy of answers to
12 certain presiding officer information requests and, if
13 necessary, to respond to questions about those
14 answers.

15 (The document referred to was
16 marked for identification as
17 Exhibit No. 2.)

18 CHAIRMAN GOLDWAY: A packet has been
19 prepared that includes Mr. Masse's answers. Do you
20 have those, Mr. Masse?

21 THE WITNESS: Yes, I do.

22 CHAIRMAN GOLDWAY: Mr. Masse, can you affirm
23 that the answers contained in that packet are accurate
24 to the best of your knowledge?

25 THE WITNESS: Yes.

1 CHAIRMAN GOLDWAY: Counsel, will you please
2 provide the reporter two copies of the answers of Mr.
3 Masse to the presiding officer information requests?
4 Those answers are received into evidence and are to be
5 transcribed.

6 (The document referred to,
7 previously identified as
8 Exhibit No. 2, was received
9 in evidence.)

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DOCKET NO. R2010-4
STEPHEN MASSE RESPONSES TO
PRESIDING OFFICER'S INFORMATION REQUESTS

<u>POIR</u>	<u>Question</u>
POIR No. 1	3(c), 4-5, 11, 13-16
POIR No. 2	15
POIR No. 4	2-4, 10

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3. Please refer to Library Reference USPS-R2010-4/1, Excel file Inbound FCMI Worksheets R2010-4.xls, and worksheet tab Inbound FCMI Rates, which references the following terminal dues rates:

Base Terminal Dues in SDRs - UPU			
(Inbound First-Class Mail International/Surface and Air Letters)			
	CY	CY	Percent
	2010	2011	Change
Per Item	0.171	0.169	-1.17%
Per Kilogram	1.731	1.709	-1.27%

The Postal Service cites UPU Circular 155 (July 6, 2009) and UPU Circular 142 (July 5, 2010) for these CY 2010 and CY 2011 inbound terminal dues "base" rates for target system countries, respectively.

a. For CY 2010 and CY 2011, please explain why the Postal Service only used the UPU inbound terminal dues "base" rates for target system countries, rather than the CY 2010 and CY 2011 "provisional" terminal dues rates referenced in the circulars of 0.174 SDR per item and 1.760 SDR per kilogram, and 0.173 SDR per item and 1.747 SDR per kilogram, respectively, that include the quality of service link.

b. For CY 2010 and CY 2011, please explain why the Postal Service only used the UPU inbound terminal dues rates paid by target system countries rather than calculating a weighted average rate reflecting the terminal dues rates paid by countries in the target system that include the quality of service link and the CY 2010 and CY 2011 terminal dues rates paid by countries in the transition system of 0.155 SDR per item and 1.562 SDR per kilogram and 0.159 SDR per item and 1.610 SDR per kilogram, respectively.

c. For FY 2011, please provide the estimated volumes and revenues for inbound letter post from Canada. Please show all calculations used to derive the estimated volumes and revenues in electronic form.

RESPONSE:

a.-b. Answered by Dr. Kiefer.

c) See USPS-R2010-4/NP6 Nonpublic Materials Filed in Response to POIR No. 1, Q. 3, filed under seal. The estimates of FY2011 revenue, pieces and weight filed in the nonpublic version of this response were

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developed using the "rollforward"¹ factors applied to the market dominant classes of mail at issue in this docket. It is important to keep in mind that the Postal Service is not proposing to change First Class Mail International Inbound rates for southbound traffic from Canada in this docket. In this response, inbound letter post from Canada was treated identically to all other countries in the global benchmarking to the revenue forecast, without the benefit of any unique sources of data that may otherwise be used when considering Canada-specific flows. Estimates of future volumes and revenues that would be used to evaluate rates for inbound international mail in the context of Type 2 NSA would accordingly be expected to differ from the estimates presented in this response.

¹ More precisely, FY2009 shares by products and countries are used to disaggregate the total amounts of inbound revenue and implicitly volume and weight, by accounting for rate increases, for general international categories (in this case FCMI Inbound) to more detailed products and countries.

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4. Please refer to the Statement of Stephen J. Masse on Behalf of the United States Postal Service, Attachments 9-12, which provide the contribution by class of mail for FY 2010, FY 2011 Before Rates, FY 2011 After Rates (January 2, 2011 Implementation), and FY 2011 After Rates-Full Year (October 1, 2010 Implementation). Also, refer to Library Reference USPS-R2010-4/NP1, Product Cost and Contribution Estimation Model (Non-Public Version). Attachments 9-12 summarize contribution for all international mail and services on one line. These attachments are also shown in Library Reference USPS-R2010-4/NP1.

a. For FY 2010, FY 2011 Before Rates, FY 2011 After Rates (January 2, 2011 Implementation), and FY 2011 After Rates-Full Year (October 1, 2010 Implementation), please provide the Postal Service's estimates of Revenue, Volume, Attributable Cost, Volume Variable Cost, Product Specific Cost, Revenue per piece, Attributable Cost per piece, Contribution per piece, and Cost Coverage in the same format as shown in Attachments 9-12 for each international mail product and service for which the Postal Service developed revenue and volume estimates in Library Reference USPS-R2010-4/NP3, Revenue and Volume Forecast Materials (Non-Public Version). Please provide in electronic form the requested attachments and all source files used to develop the figures contained therein.

b. For Inbound International Ancillary Services, please separately provide the Postal Service's estimates of Revenue, Volume, Attributable Cost, Volume Variable Cost, Product Specific Cost, Revenue per piece, Attributable Cost per piece, Contribution per piece, and Cost Coverage in the same format as shown in Attachments 9-12 for the Inbound Registered Mail service.

RESPONSE:

a) See USPS-R2010-4/NP5 Nonpublic Materials Filed in Response to POIR No. 1, Q. 4, filed under seal. The requested International product detail has been supplied by a newly commissioned modeling system for disaggregating International cost, revenue and volume results to individual products. This system is still, however, under development and may be refined in the future. The operation of the "International Product Cost and Contribution Estimation Model" essentially involves running sequential ICRA's each with their own inputs relevant to a specific year (e.g., volumes and revenues, settlement rates,

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exchange rates, etc.). Thus, all of the detail from an ICRA is available for each year (with the exception of data for specific NSAs due to the need to streamline the costing process, since NSAs unit costs are not well-defined due to the variety of products in the NSA category). The process starts with the ICRA for FY2009 and uses the revenue and volume forecast to drive what the ICRA nomenclature calls the "booked" version of the ICRA forward in time. Essentially, the booked version uses cost accounts and general revenue categories to tie to the CRA/RPW system consistent with Commission practice (as opposed to the former "imputed" version which generally reflects much more revenue from foreign origin mail -- this is primarily an accounting issue which as we understand is being addressed to bring the two concepts into alignment).

In the future FY versions that have been prepared, revenues and volumes begin with FY2009 shares by country for each class of mail (e.g., Air Letter-post), and then those shares are applied to revenue from the relevant forecast (BR or AR). Volumes and weights are scaled in a similar manner and the resulting costs are driven by country-specific settlement rates entered into the model (i.e., UPU settlement rates, bilateral rates for Canada Post, etc.).

The system is highly similar to the ICRA proper, and the documentation of the ICRA (with the exception of specific numbers relating to FY 2009 data) will apply here. A brief overview of how the modules interact with the Library Reference USPS-R2010-4/NP1, Product Cost and Contribution Estimation Model (Non-Public Version) that provides aggregate International results only and the formal forecasts for broad International categories appears in the nonpublic

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annex. This document also gives an overview of the "folder" structure of the new non-public library reference to support these estimates.

b) The nonpublic version of the response to subpart (a) to this question includes the Inbound Registered breakout, together with the other usual and customary Special Services reported in the Domestic Processing Model (DPM) component of the CRA and incorporated into the ICRA. In the absence of disaggregated costing data for Inbound International Ancillary services, however, the Postal Service is unable to model these ancillary services, with the exception of Foreign Origin Registry. Costs for other Inbound International Ancillary Services are not available in either the CRA or ICRA, and are accordingly not estimated by the International Product Cost and Contribution Estimation Model (IPCCEM), which depends on those systems.

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5. Please refer to the Statement of Stephen J. Masse on Behalf of the United States Postal Service, Attachments 9-12, which provide the contribution by class of mail for FY 2010, FY 2011 Before Rates, FY 2011 After Rates (January 2, 2011 Implementation), and FY 2011 After Rates-Full Year (October 1, 2010 Implementation). Also, refer to Library References USPS-R2010-4/NP1, Product Cost and Contribution Estimation Model (Non-Public Version), and R2010-4/NP3, Revenue and Volume Forecast Materials (Non-Public Version). Attachments 9-12 are shown in Library Reference USPS-R2010-4/NP1, Excel files RFLiteReport2009-2011BR.R2010-4 Exigent.xls, RFLiteReport2009-2011AR.R2010-4 Exigent (January 2, 2011 Implementation).xls, and RFLiteReport2009-2011AR.R2010-4 Exigent (October 1, 2010 Implementation).xls. The Revenue and Volume figures in Attachments 9-12, and the above referenced Excel files are often different from, and are not linked to, the Excel files Before-Rates V&R Forecast Nonpublic.xls, After-Rates Jan11 V&R Forecast Nonpublic.xls, and After-Rates Oct 10 V&R Forecast Nonpublic.xls, in Library Reference R2010-4/NP3, Revenue and Volume Forecast Materials (Non-Public Version). Please reconcile the revenue and volume figures in Attachment 9-12, and Library References R2010-4/NP1 and R2010-4/NP3, and provide electronic links between the files wherever possible.

RESPONSE:

The revenue and volumes in Attachments 9-12 have been reconciled with the revenue and volumes forecast materials in the R2010-4/NP3 folder. The following table summarizes the differences. Most of the differences were due to linking errors in the RevenueSummary Excel files. The RevenueSummary files bridge the revenue and volume materials to the PCCE Model.

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POIR, Question 5: Revenue and Volume Reconciliation

Revenue			Before Rates	Jan 2, 2011	Oct 1, 2010
(Data in millions)	2009	2010	2011BR	2011AR	2011AR
Original filing	\$ 67,979	\$ 67,032	\$ 67,676	\$ 69,656	\$ 70,307
Fees					
1st Class	\$ -	\$ (14)	\$ (20)	\$ (15)	\$ (13)
Standard	\$ -	\$ (6)	\$ 2	\$ 5	\$ 6
Periodicals	\$ -	\$ (1)	\$ (2)	\$ (1)	\$ (1)
Packages	\$ -	\$ (1)	\$ -	\$ -	\$ -
NSA Adjust					
Standard Letters	\$ -	\$ 1	\$ -	\$ -	\$ -
Standard Flats	\$ -		\$ 1	\$ 1	\$ 1
Services					
Other Ancillary				\$ (1)	\$ (1)
Caller Service	\$ -	\$ 1	\$ 1	\$ 4	\$ 5
Money Orders				\$ (1)	\$ (1)
Other	\$ -	\$ 13	\$ 13	\$ 13	\$ 13
Net Change	\$ -	\$ (7)	\$ (5)	\$ 5	\$ 9
POIR adjusted total	\$ 67,979	\$ 67,025	\$ 67,671	\$ 69,661	\$ 70,316
Volume			Before Rates	Jan 2, 2011	Oct 1, 2010
(Data in millions)	2009	2010	2011BR	2011AR	2011AR
Original filing	177,054	169,276	174,316	172,988	172,264
NSA Adjust					
Standard Letters		2			
Standard Flats			2	2	2
Domestic Competitive Mail	(1)	(1)	(1)	(1)	(1)
International Mail & Services	5	5	5	5	5
Other		(1)			
Net Change	4	5	6	6	6
POIR adjusted total	177,058	169,281	174,322	172,994	172,270

These differences have since been corrected in an updated run of the PCCE Model in USPS-R2010-4/NP4. Please see the RFLiteReports in the OutputReports folder for each model run in USPS-R2010-4/NP4, as well as the V&R Forecasts in the Supporting Information folder. Also, please see the POIR.1.Q5.Attachments A-F in USPS-R2010-4/NP4 for more details.

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Similar public versions of that information can be found in the zip file
(POIR.1.Q.5.zip) attached to this answer electronically.

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11. Please refer to Attachments 9-12 to the Statement of Stephen J. Masse on Behalf of the United States Postal Service, which estimate the contribution for each mail class for FY 2010, FY 2011 Before Rates, FY 2011 After Rates (January 2, 2011 Implementation), and FY 2011 After Rates (October 1, 2010 Implementation). Attachments 9-12 do not estimate contribution for the following two special service products: (1) Address Management Services, and (2) Confirm Service. Please separately provide the estimates of contribution (revenue and attributable cost) for Address Management Services (formerly Address List Services) and Confirm Service in the same manner as Attachments 9-12.

RESPONSE:

Address Management Services

In the FY 2009 Annual Compliance Determination (ACD), the Commission stated that:

On January 13, 2010, Order No. 391 renamed Address List Services as Address Management Services *The Commission expects the Postal Service to develop a cost methodology and submit the methodology prior to filing the 2010 ACR.*

ACD at 106. The Postal Service has not yet developed or submitted this cost methodology, and does not yet have a cost estimate for the new Address Management Services product. Therefore, the Postal Service does not have an estimate of contribution for Address Management Services.

Confirm

The Postal Service provided actual Confirm costs and revenues for FY09. The Postal Service, however, currently has no firm basis to project either costs or revenues for this product. To gain some possible insight into the effect of the proposed price increase on the contribution of Confirm, however, the Postal Service offers the following. If one starts with the revenues for Confirm from the Special Services worksheets (which differ from the FY09 revenues because they

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reflect two quarters of FY09 and the first two quarters of FY10), and assumes no change in the amount of service demanded, one would estimate no change in revenue in the full year FY10, or in FY11 before rates. Therefore, for purposes of this exercise, we assume FY10 (and FY11BR) revenue of \$2,514,200. If we then multiply this amount by the percentage increase proposed, we get FY11 After rates revenue of \$2,843,570. On the cost side, we start with the FY09 Confirm Attributable costs of \$2,951 million. The costs for Confirm tend to be dominated by Product Specific costs, and thus there really is no good basis to draw inferences from other costs. Nonetheless, if one wanted to use the same rate of inflation implicit in the exhibits attached to the Statement of Stephen Masse for Total Domestic Market Dominant Special Services, one could inflate FY09 costs by 0.4 percent to derive FY10 costs, and by 3.5 percent to derive FY11 costs. This simplistic exercise would suggest FY10 Confirm costs of \$2.963 million, and FY11 costs of \$3.055 million. Comparing these costs with the revenues discussed above suggests FY10 contribution of negative \$0.449 million, FY11BR contribution of negative \$0.541 million, and FY11AR contribution of negative \$0.211 million. This type of analysis, of course, includes the counterintuitive assumption of no decrease in demand despite an increase in price. Overall, though, this exercise suggests that, if one assumes no material change in Confirm costs (beyond rather minimal inflation similar to that projected for other Special Services), the before-rates contribution would be negative, and the after-rates contribution would still be negative, but less than half of the contribution loss from the before-rates scenario. Most importantly, however, this exercise

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cannot provide any firm information, because it will ultimately be the level of Product Specific costs in any given year which will have the most significant impact on the performance of this product.

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13. In Library Reference USPS-LR-R2010-4/6, the file RFIInput.XLS for the October 1 and the January 2 After Rates roll forward, the ServiceWide Costs' effect for component 211 does not use a separate roll forward distribution key to allocate an FY 2010 \$295 million increase in costs for component 211. However, for the FY 2010 Before Rates roll forward, the file RFIInput.XLS indicates that the ServiceWide cost change uses component 1439, the fixed cost key, as a distribution key for the \$295 million ServiceWide cost change. Please explain this discrepancy in the allocation of the ServiceWide cost change for component 211 between the Before Rates scenario and the October 1 and January 2 implementation scenarios.

RESPONSE:

The method used in the FY 2010 Before Rates RFIInputTables.XLS is the correct method for handling the \$295 million ServiceWide cost change by using component 1439, a fixed cost key. The RFIInput.Tables.XLS files for the October 1 and the January 2 After Rates ServiceWide Costs' effects for component 211 have been updated in the USPS-R2010-4/NP4 folder. The results of that change are reflected in the response to question 16 of this Information Request.

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14. In Library Reference USPS-LR-R2010-4/6, file FY 2010.Irpt.XLS there are several discrepancies in regard to the square footage, rental value, and capital factors used to develop distribution keys for several PESSA related costs. The following questions relate to these discrepancies.

- a. In the "I" report for FY 2010 at worksheet 98.5, a factor appears for component 1002. However, component 1002 is labeled as "not used." In the same table, there is no factor for "OCR and BCS on OCRs." Please explain and correct, if necessary, worksheet 98.5 to reflect the correct factors.
- b. As described in subpart a., above, worksheet 98.6 appears to have the same problem in component 1102. Please explain and correct, if necessary, worksheet 98.6 to reflect the correct factors.
- c. In worksheet 98.7, there is no capital factor reflected for component 1225, labeled as POS One. Please provide the factor that should be reflected for this component and correct, if necessary, worksheet 98.7 to reflect the correct factors.

RESPONSE:

- a.-c. The factors in "FacilSpace_Equip.XLS" were mistakenly applied to FY 2010. Instead, the factors from FY 2009, as developed in Docket No. ACR 2009, USPS-FY09-8, should be used for FY 2010. This is consistent with the past omnibus rate case approach of using base year factors in the non-test year interim years. Using the FY 2009 factors addresses the discrepancies that are raised by this question. The effects of fixing this error are addressed in the response to question 16 of this Information Request. Fixing this error has a minor impact on FY2010 attributable costs, and has no impact on the FY 2011 attributable costs.

The materials provided in response to question 15 of this Information Request show that for FY 2011, all of the OCRs are projected to be removed, which is why there is a zero factors for 1003 and 1103 for

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FY 2011. In addition, by FY 2011, the POS One equipment is fully depreciated, so component 1225 is zero for FY2011.

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15. Please provide the source worksheets, in electronic format, that develop the FY 2010 and FY 2011 square foot, rental value, and capital factors found in file "FacilSpace_Equip.XLS."

RESPONSE:

Attached are two Excel files (POIR.1.Q.15.Attach.A.xls and POIR.1.Q.15.Attach.B.xls) which contain the source worksheets for the factors contained in the file "FacilSpace_Equip.XLS." As indicated in the response to question 14, the factors contained in "FacilSpace_Equip.XLS" only apply to FY 2011. The factors for FY 2010 are the same as those for FY 2009, and the source files would be those from Docket No. ACR 2009, USPS-FY09-8.

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16. If there are any changes as a result of answers to questions 1-15 that impact any other files or worksheets within the roll forward, please correct all files or workpapers that rely on the factors that have been corrected.

RESPONSE:

Revised PCCE Model runs for Before Rates, October 1 After Rates and the January 2 After Rates have been provided in USPS-R2010-4/NP4. The net effects of re-running the models for the Volume and Revenue differences in relation to question 5, the correction of ServiceWide effects in question 13, and the correction of PESSA cost for FY 2010 in question 14 are as follows:

POIR, Question 5: Revenue and Volume Reconciliation

Revenue			Before Rates	Jan 2, 2011	Oct 1, 2010
(Data in millions)	2009	2010	2011BR	2011AR	2011AR
Original filing	\$ 67,979	\$ 67,032	\$ 67,676	\$ 69,656	\$ 70,307
Fees					
1st Class	\$ -	\$ (14)	\$ (20)	\$ (15)	\$ (13)
Standard	\$ -	\$ (6)	\$ 2	\$ 5	\$ 6
Periodicals	\$ -	\$ (1)	\$ (2)	\$ (1)	\$ (1)
Packages	\$ -	\$ (1)	\$ -	\$ -	\$ -
NSA Adjust					
Standard Letters	\$ -	\$ 1	\$ -	\$ -	\$ -
Standard Flats	\$ -		\$ 1	\$ 1	\$ 1
Services					
Other Ancillary				\$ (1)	\$ (1)
Caller Service	\$ -	\$ 1	\$ 1	\$ 4	\$ 5
Money Orders				\$ (1)	\$ (1)
Other	\$ -	\$ 13	\$ 13	\$ 13	\$ 13
Net Change	\$ -	\$ (7)	\$ (5)	\$ 5	\$ 9
POIR adjusted total	\$ 67,979	\$ 67,025	\$ 67,671	\$ 69,661	\$ 70,316
Volume			Before Rates	Jan 2, 2011	Oct 1, 2010
(Data in millions)	2009	2010	2011BR	2011AR	2011AR
Original filing	177,054	169,276	174,316	172,988	172,264
NSA Adjust					

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Standard Letters		2			
Standard Flats			2	2	2
Domestic Competitive Mail	(1)	(1)	(1)	(1)	(1)
International Mail & Services	5	5	5	5	5
Other		(1)			
Net Change	4	5	6	6	6
POIR adjusted total	177,058	169,281	174,322	172,994	172,270

Total Cost		Before Rates	Jan 2, 2011	Oct 1, 2010
(Dollars in 000)	2010	2011BR	2011AR	2011AR
Original Filing Totals	\$73,623,712	\$74,804,829	\$74,523,870	\$74,388,525
POIR Revised Totals	\$73,623,429	\$74,805,347	\$74,524,417	\$74,388,705
Net Change	\$ (283)	\$ 518	\$ 548	\$ 180

Please see the POIR.1.Q5.Attachment A, B, C, D, E & F in the USPS-R2010-4/NP4 for more details on the impact, as well as the zip file (POIR.1.Q.5.zip) attached electronically to the response to Question 5 of this Information Request.

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15. Please refer to the FY 2009 ACD, Table VII-20 at 103, which shows a FY 2009 negative contribution for Registered Mail of \$679,702. Also, please refer to the Statement of Stephen J. Masse, Attachment 10, which shows a FY 2011 before-rates contribution for Registered Mail as \$6,058,375. Please explain the significant increase in contribution from FY 2009 to FY 2011 Before Rates. See the table below.

Comparison of Registered Mail's Contribution FY 2009 versus FY 2011 Before Rates			
	FY 2009	FY 2011	
	Contribution	Before Rates Contribution	Contribution Improvement
	[1]	[2]	[3] = [2]-[1]
Domestic Registered Mail	-\$679,702	\$6,058,375	\$6,738,077
Sources:			
	[1] FY 2009 ACD, Table VII-20 at 103		
	[2] R2010-4, Masse's Statement, Attachment 10		

RESPONSE:

The change in contribution for Registered Mail is due to an increase in unit revenue, along with a decrease in unit cost. Unit revenue increased from \$15.68 in FY 2009 to \$16.30 in FY 2011. Conversely, unit cost decreased from \$15.90 in FY 2009 to \$14.03 in FY 2011.

The decrease in cost is largely due to expected changes in mail volume and to cost/productivity goal reductions. Registered Mail has \$3.3 million in volume-related workload reductions in FY 2010 and a \$2.4 million in volume-related workload reductions in FY 2011. The Postal Service is scheduled to have net cost/productivity goal reductions of \$1.5 billion in FY 2010 and \$0.8 billion in FY

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2011. Of this, Registered Mail is scheduled to have a \$4.6 million in cost/productivity reduction in FY 2010 and a \$1.2 million in cost/productivity reduction in FY 2011. Function-related cost/productivity goal reductions are distributed in the same proportion as the related direct labor. Those that are associated with a program receive the program-related distribution. Please see the following table for a summary of the Registered Mail cost changes.

Description	Cost (\$,000)	Source
ACD 2009 Cost	\$ 50,586	
Mail Volume Change	\$ (3,322)	FY2010BR.CSChgRpt.Exigent_BR.xls
Productivity Goals	\$ (4,555)	FY2010BR.CSChgRpt.Exigent_BR.xls
All Other	\$ (917)	
2010 Cost	\$ 41,792	FY2010BR.CRpt.xls
Mail Volume Change	\$ (2,422)	FY2011BR.CSChgRpt.Exigent_BR.xls
Productivity Goals	\$ (1,206)	FY2011BR.CSChgRpt.Exigent_BR.xls
All Other	\$ (694)	
2011 Cost	\$ 37,470	FY2011BR.CRpt.xls

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2. In USPS LR-R2010-4/6, the file RFInputTable.xls lists the values for the cost effects used in the PCCEM model. In that file there are five different cost reductions for component 165, Segment 15 Rents, which are distributed to products using two different distribution keys. Component 1467 is used for one cost reduction and component 1452 for the four other cost reductions. The effect of using these distribution keys is to allocate cost reductions to zero balances in component 165, resulting in negative balances in the component before distribution of rental costs in the FY 2010BR "B" report. Component 165 generally has zero variable costs in the short run and the distribution of rental costs in this component is handled within the development of the "B" report, the distribution of PESSA costs. The result of the "B" report distribution is reflected in the FY 2010 "C" report, but the results of the cost reductions distribution to products are not reflected in the distribution of costs in the "C" report. Should the distribution key components 1467 and 1452 be used to distribute the cost reductions for component 165, Segment 15 Rents, or should the cost reductions affect only the other costs and total costs of component 165? If the use of components 1467 and 1452 is correct, please explain how the cost reduction distribution to products is reflected in the FY 2010BR "C" report.

RESPONSE:

The distribution key used for cost reductions in component 165 is immaterial because only total costs will ultimately be impacted. As the question states, the component will be distributed again in the "B" report.

The distribution for component 165 in the "B" report is based on the rental value distribution key, which is developed in the Factor report. For FY 2010 the rental factors used to develop the rental value distribution key were the same as FY 2009, while in FY 2011 new factors were developed. Therefore the cost reduction distribution to products for this component is better represented in the FY 2011BR "C" report.

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3. Please refer to the FY 2009 Cost and Revenue Analysis reports (posted at www.usps.com/financials), Attachments 9-12 of the Masse Statement, and PRC Order No. 191, at 43.

- a. Please confirm that the Postal Service increased Standard Mail Not FlatMachinables (NFM)/Parcels rates by an average of 16.4 percent in May 2009. If not confirmed, please explain.
- b. Please confirm that the FY 2010 Standard Mail NFM/Parcel revenue per piece (94.5 cents) presented in Attachment 9 of the Masse Statement is 1.5 percent higher than FY 2009 Standard Mail NFM/Parcel revenue per piece (93.1 cents). If not confirmed, please provide correct figures.
- c. Please explain why the Standard Mail NFM/Parcel average revenue per piece is forecasted to grow by 1.5 percent in FY 2010 despite the significant May 2009 price increase. In particular, please address whether the mail mix (e.g., percentage destination entered) implicit in the FY 2010 revenue forecast is a lower-revenue, lower-cost mail mix than the FY 2009 Standard Mail NFM/Parcel mail mix.
- d. Please confirm that neither the forecasted FY 2010 nor the forecasted FY 2011 Standard Mail NFM/Parcel costs presented in Attachments 9 through 12 include any adjustments to reflect differences in mail mix between the forecasted years and FY 2009. If not confirmed, please identify and explain all adjustments.

RESPONSE:

- a. Confirmed that, using a fixed weight index approach for cap compliance calculations that employed FY08 billing determinants, the measure of the price increase implemented in May of 2009 for NFM/Parcels was 16.4 percent. See page 14 of the Notice of Price Adjustment in Docket No. R2009-2 (Feb. 10, 2009). Using FY09 billing determinants instead of FY08 billing determinants, however, would suggest that the May 2009 price increase for NFM/Parcels was only about 3 percent, rather than 16 percent.
- b. Confirmed.
- c. It is clear that the mail mix implicit in the FY10 revenue forecast is different from the FY08 mail mix which was employed in Docket No. R2009-2 for cap

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compliance purposes. In the 2009 price change, the Postal Service forced migrations by eliminating some price cells. So the shift to lower revenue per piece represents, in part, the elimination of some higher priced options.

Migrations from these May 2009 classification changes, as well as from the May 2009 changes in the relative prices between the remaining rate categories, would have started in the second half of FY09, and therefore would have had an effect on FY09 unit revenues, with the effect intensified in FY10. Note, however, that the FY10 forecasted revenues included in the Masse exhibits use a base period that differs from FY09 by only one quarter. The forecasting base period drops Q1 of FY09, and adds Q1 of FY10. In any event, as indicated in the response to part a. of this question, using the FY09 billing determinants to evaluate the May 2009 price changes explains why the forecasted revenue increase in FY10 is much less than one might imagine when focusing on the results using FY08 billing determinants.

d. Confirmed.

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4. Please refer to the FY 2008 and FY 2009 Cost and Revenue Analysis reports, Cost Segments and Component reports, and Revenue, Pieces, and Weight reports (posted on www.usps.com/financials).

a. Please confirm that the unit cost of Standard Mail NFM/Parcels increased by 11.6 percent from FY 2008 to FY 2009. If confirmed, please explain why Standard Mail NFM/Parcel unit costs increased by such a large amount between FY 2008 and FY 2009. If not confirmed, please provide the correct figure.

b. Please confirm the following FY 2009 (vs. FY 2008) cost segment-specific percentage changes in Standard Mail NFM/Parcel unit costs and explain why Standard Mail NFM/Parcel unit costs in each listed cost segment increased so rapidly from FY 2008 to FY 2009. If not confirmed, please provide the correct figure.

- i. C/S 3 Clerks and Mailhandlers (CAG A-J) – 11.6%
- ii. C/S 6 City Carriers Office Activity – 36.5%
- iii. C/S 7 City Carriers Street Activity – 24.5%
- iv. C/S 8 Vehicle Service Drivers – 72.2%

RESPONSE:

a. Confirmed. The unit costs for Standard Mail NFM/Parcels rose 13 cents from \$1.11 in FY 2008 to \$1.24 in FY 2009, an 11.6 percent increase. The increase is driven by the increases in cost segments 3, and 6 to 8 as discussed below in part b, which accounts for nearly 10 cents of the increase in unit costs. These same factors, as discussed below, also led to increases in cost segments 2 (Supervisors and Technicians), 11 (Custodial and Maintenance Services), 15 (Building Occupancy) and 18 (for Service-Wide Benefits). There was a decline in cost segment 14 (Purchased Transportation) as well. A common thread of the explanations in part b, is the shift in mail mix toward a higher share of parcels vs. NFMs. In addition, many postal products had significant increases in these same cost segments for FY 2009.

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b. i. Confirmed. Cost segment 3 costs rose 11.6 percent, going from 41.5 cents in FY 2008 to 46.3 cents in FY 2009, an increase of 4.8 cents. The entire increase was in mail processing, cost segment 3.1, a 12.3 percent increase. Several factors are relevant. First, clerk and mail handler cost per work hour rose by about 7 percent. Second, the share of NFMs declined in FY 2009, likely raising unit processing costs. RPW data show the FY 2008 share was 28.1 percent and in FY 2009 it was only 20.9 percent. Finally, variance could also be part of the increase, as there was a decline in cost segment 3 unit costs from FY 2007 to FY 2008 as large as the increase between FY 2008 and FY 2009. These factors outweighed the increase in dropshipping for this product in FY 2009 as compared to FY 2008.

ii. Confirmed. Standard Parcels/NFM unit costs for city carriers in-office activities increased approximately 1.8 cents in FY09 (from 4.7 cents in FY08 to 6.5 cents in FY09). Standard Parcels/NFMs are often cased by city carriers after they have cased their other mail, made up of non-DPS letters and flats. Two mail-mix changes for Standard Parcels/NFMs occurred in FY09, both of which resulted in an increase in C/S6 unit costs.

First, the City Carrier Cost System (CCCS) shows that NFM volume dropped approximately 26 percent while Standard Parcel volume decreased by two percent. This means that the proportion of Standard Parcels rose in FY2009. NFM pieces because of their small size and uniform dimension (rectangular) can be cased by the carrier quickly and efficiently. Standard Parcels, conversely, may require the carrier additional time to put them in the case. An increase in

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the proportion of Standard Parcels thus leads to higher unit casing costs for the aggregate product.

Second, a higher percentage of Standard Parcels in FY09 were irregular in shape (source billing determinants – 51 percent irregular in FY09 and 47 percent in FY08). This also increases the unit casing time relative to regular shaped Standard Parcels and results in an increase in C/S6 unit costs. These two factors largely explain the CS/6 unit cost increase for Standard Parcels/NFMs in FY09.

Moreover, it is quite possible that the sharp decline in volume was accompanied by a decline in casing productivity. Such a productivity decline would lead to higher unit costs.

iii. Confirmed. Standard Parcels/NFM unit costs for city carrier street activities increased approximately 2.4 cents in FY09 (from 9.9 cents in FY08 to 12.3 cents in FY09). Two factors largely explain the increase in unit costs in FY09. First there was a methodology change that introduced a new and current distribution key for special purpose route carriers. The dated distribution key that was previously used was replaced with a current one obtained through CCCS-SPR (City Carrier Cost System – Special Purpose Route). Second an environment with declining volumes and a stable number of delivery points reduces the number of pieces per delivery point which, in turn reduces, carrier street time productivity. This fall in productivity resulted in an average unit cost increase of sixteen percent for all products in CS/7 in FY09.

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The Service's introduction of a new distribution key for mail delivered by special purpose route carriers¹ was expected to cause about a one cent unit cost change, based upon FY08 data. This anticipated increase represents about forty percent of the actual increase. After accounting for this methodology change, the Standard Parcels/NFM unit cost change for city carrier street activities was approximately the same as the average change in unit costs for all products (sixteen percent) in C/S7.² This unit cost change in FY09 was largely a function of working in an environment in which there was declining volume and constant delivery points.

iv. Confirmed. Standard Parcels/NFM unit costs for Vehicle Service Drivers increased 0.6 cent in FY09 (1.4 cents in FY09 and 0.8 cent in FY08). CS/8 costs encompass less than 1.2 percent of the total unit cost for Standard Parcels/NFMs (\$1.24 unit cost in FY09). Two factors largely explain the increase in unit costs in FY09, 1) a methodology change in surface densities and 2) statistical variance in the distribution factor used to assign relevant costs.

The Service's proposal of a methodology change³ which introduced new surface densities was expected to result in a 0.3 cent unit cost increase, based on FY08 data. This accounts for approximately 50 percent of 0.6 unit cost change. The remaining 0.3 cent increase in unit costs is likely

¹ Filed July 28, 2009 in Docket No. RM2009-10, Proposal Eight – accepted by the Commission in Order No. 339, dated November 13, 2009.

² In other words, approximately 10 points of the 24.5 percentage point increase were due to the methodology change and the other 14.5 points were due to the effects of the decline in volume.

³ Filed October 6, 2009 in Docket No. RM2009-10, Proposal Twenty, accepted by the Commission in Order No. 393, dated January 14, 2010.

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accounted for by statistical variation from the estimate used to assign the relevant costs. The estimate comes from sampled data collected as part of the Transportation Cost System (TRACS). The distribution factor derived from Intra-SCF transportation data is used to assign relevant VSD costs. Standard Parcels/NFMs have an approximate coefficient of variation (CVs) of 14 percent⁴. The point estimate and CV result in a 95 percent confidence interval with a lower bound cost of \$6.9 million and an upper bound of \$12.2 million.⁵ In terms of unit costs, this translates into a margin of error of 0.4 cent. In sum, the combination of incorporating updated surface densities and statistical variation likely accounted for the 0.6 cent unit cost increase for Standard Parcels/NFMs in CS/8 in FY09.

⁴ TRACS CVs are filed with ACR in USPS-FY09-NP24, dated December 29, 2009

⁵ A 95 percent confidence interval is formed by taking
Annual Estimate – \$9,519 ± (1.96 × 0.14 × \$9,519))

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10. Please: (a) explain how you have modeled the negative volume impact of the Internet and other electronic alternatives in the demand equation for First-Class workshared letters; and (b) describe any differences in modeling the Internet impact on First-Class workshared letters between the July 1, 2010 periodic reports filings (Narrative Explanation of Econometric Demand Equations for Market Dominant Products as of November, 2009) and the Docket No. R2010-4 filing.

RESPONSE:

(a) The negative impact of the Internet and other electronic alternatives on First-Class workshared letters volume in recent years is modeled by including the number of Broadband subscribers in the First-Class workshared letters equation.

Prior to 2002 or so, there was little, if any, apparent Internet diversion of First-Class workshared letters (or, to the extent such diversion existed, its presence was offset by other factors). Over the past decade, electronic diversion of First-Class workshared mail has increased because of the growth in broadband internet access. In addition, it appears that diversion has increased further during the most recent recession, suggesting an interaction between the growth in broadband and the decline in the economy. This is modeled by interacting the coefficient on the Broadband variable with the cumulative negative trend on Employment (EMPL_TN_L). The Broadband variable, as well as the interaction term, is lagged eight quarters (two years) in the First-Class workshared letters equation in recognition of the observed lag between people's acquisition of Internet access and the extent to which they begin to divert mail. Prior to the growth in EMPL_TN_L tied to the 2001 recession, the modeled impact of Broadband usage on First-Class workshared letters volume is set equal to zero here.

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(b) The only differences between the First-Class workshared letters equations filed in Docket No. R2010-4 and those described in the July 1, 2010, periodic reports filing with the Commission is that the former are estimated using one additional quarter of data (2010PQ1, which ran from October 1, 2009 through December 31, 2009) and the elimination of a dummy variable equal to one in quarters during which Federal general elections occur.

1 CHAIRMAN GOLDWAY: We are now ready for
2 questions from the Commission. I'd like to begin with
3 the third quarter results --

4 THE WITNESS: Yes.

5 CHAIRMAN GOLDWAY: -- which were mentioned a
6 moment or two ago. We have now gotten the more
7 detailed breakdown of the USPS financial information
8 reports for June 30, and the Commissioners all have
9 copies of them so we will probably be asking for some
10 information based on those.

11 I haven't checked with counsel on this, but
12 should I give the court reporter a copy of this as
13 well? Okay. We'll give the court reporter a copy of
14 this as well for the record.

15 (The document referred to was
16 marked for identification and
17 received in evidence.)

18 CHAIRMAN GOLDWAY: I guess I'll begin by
19 asking. It appears that volume has been greater than
20 planned consistently for the first nine months of the
21 year, some months more than others, but even in this
22 last quarter volume was greater.

23 THE WITNESS: Yes.

24 CHAIRMAN GOLDWAY: I wanted to confirm that
25 this does not include any of the summer sale. Is that

1 correct?

2 THE WITNESS: Well, the summer sale is just
3 beginning so that wouldn't really --

4 CHAIRMAN GOLDWAY: It just began on
5 July 1 --

6 THE WITNESS: Yes.

7 CHAIRMAN GOLDWAY: -- so this wouldn't
8 include any effects of possible volume growth --

9 THE WITNESS: No.

10 CHAIRMAN GOLDWAY: -- from the summer sale?

11 THE WITNESS: No.

12 CHAIRMAN GOLDWAY: Okay.

13 THE WITNESS: The majority of the volume
14 improvement that we experienced was really in the
15 first quarter of the fiscal year. The economic
16 recovery fortunately began a bit earlier than we had
17 previously assumed when we drew up the plan for the
18 year.

19 Unfortunately it's kind of flattened out and
20 has dropped off in the most recent months, but the
21 first quarter of our fiscal year, the fourth calendar
22 quarter, we did see an increase in volume during our
23 heaviest season.

24 So we've enjoyed that benefit, if you will,
25 and carried it forward throughout the nine months for

1 the three quarters that we have completed.

2 CHAIRMAN GOLDWAY: And it looks like total
3 work hours are somewhat higher than planned --

4 THE WITNESS: Yes, and that's --

5 CHAIRMAN GOLDWAY: -- and that that related
6 to the higher volume.

7 THE WITNESS: Yes. If you look at the Year
8 To Date column, the actual versus planned for total
9 work hours, we are about 11 million hours ahead of or
10 overplanned, and that's partly a result of the
11 additional volume.

12 We're some three billion pieces of mail
13 ahead for the year to date for the nine months, but we
14 also have versus fly have been able to save 63 million
15 hours, which is a substantial savings for the year.
16 At some \$40 an hour, that's worth in excess of \$2.5
17 billion.

18 CHAIRMAN GOLDWAY: Are there any
19 measurements in this report that would indicate the
20 introduction of the FSS machine?

21 THE WITNESS: There are some benefits that
22 are occurring with regard to FSS. We have 12 of the
23 machines operating in I believe five locations. Our
24 plan is for the remainder of this year and into 2011
25 to roll out 100 of those machines in I believe it's

1 approximately 47 locations.

2 So the effects, if any, are not very
3 significant at this stage as we haven't deployed all
4 the equipment yet and we're still working on the
5 equipment and fine tuning it.

6 CHAIRMAN GOLDWAY: So in your estimate for
7 future savings --

8 THE WITNESS: Yes.

9 CHAIRMAN GOLDWAY: -- for next year and
10 beyond how much are you estimating the FSS is going to
11 save?

12 THE WITNESS: We've included the benefits,
13 if you will, of FSS in our forecast for 2011 and
14 future years. The exact figure I don't have.

15 CHAIRMAN GOLDWAY: But is that included --

16 THE WITNESS: But it's part of the
17 \$1 billion of savings that you will see if we look at
18 the roll forwards that are included in the attachment.

19 CHAIRMAN GOLDWAY: But you can't tell me how
20 much of that \$1 billion?

21 THE WITNESS: Exactly what it is? No. I
22 don't recall the specific number.

23 COMMISSIONER LANGLEY: Madam Chairman, will
24 tomorrow's witness be able to provide that
25 information?

1 CHAIRMAN GOLDWAY: Postal counsel, do you
2 think we can get more specifics from tomorrow's
3 witness on the subject of savings?

4 MR. KOETTING: Madam Chairman, I believe
5 that information has been available for the record.

6 CHAIRMAN GOLDWAY: Forgive me if I don't
7 recall it.

8 MR. KOETTING: Specifically, the Postal
9 Service filed a response to an informal question at a
10 technical conference on August 2nd, 2010, we filed the
11 response of the United States Postal Service to an
12 informal question regarding cost reduction programs
13 proposed at the technical conference on July 27, 2010.

14 Attached to that response electronically was
15 an Excel spreadsheet that gave detail on all the cost
16 reduction programs, including the FSS program. I
17 believe that information is all included in that file
18 attached to that.

19 CHAIRMAN GOLDWAY: And are you able by
20 looking at that Excel to tell me what the estimate is
21 for savings for next year?

22 MR. KOETTING: I'm sorry. All I have is a
23 hard copy of the pleading. The Excel is an electronic
24 file that --

25 CHAIRMAN GOLDWAY: You don't have it.

1 MR. KOETTING: I don't. It may be
2 incompatible or not. Mr. Rubin is looking.

3 CHAIRMAN GOLDWAY: We'll try and get it and
4 perhaps ask a question for the next witness from it.

5 And then I will simply ask you the same
6 question that I asked Mr. Corbett yesterday --

7 THE WITNESS: Yes.

8 CHAIRMAN GOLDWAY: -- and that is the Postal
9 Service has presented in its Envisioning the Future
10 10-Year Forecast seven items in its plan that it hopes
11 to pursue. Of those seven, which do you think is the
12 most important to the future financial viability of
13 the Postal Service?

14 THE WITNESS: All seven of those items are
15 important to the future of the Postal Service, and
16 what we planned for is a 10 year timeframe. Some of
17 those items have more significant value in the
18 short-term, especially as we face a condition of
19 insolvency just 13 months away, and others will
20 provide value on an annual basis for many, many years
21 to come, so there is a significant cumulative effect
22 of those kind of initiatives.

23 In the near term, the initiative that can
24 have the most effect on our ability to avoid
25 insolvency are those related to the funding or the

1 prefunding of retiree health benefits.

2 The \$5.5 billion that's due at the end of
3 this year and a similar payment due at the end of the
4 next fiscal year and then rolling until 2016 are very
5 significant in the grand scheme of things, and we need
6 a level of assistance with that, as I said, in order
7 to avoid insolvency in 13 months' time.

8 CHAIRMAN GOLDWAY: In the near term --

9 THE WITNESS: Yes.

10 CHAIRMAN GOLDWAY: -- how does this request
11 for a rate increase compare to in the near term for
12 relief from the health care retiree benefits fund?

13 THE WITNESS: In the near term, in the
14 fourth quarter of our fiscal year, the price increase
15 has no effect, but some level of assistance from
16 Congress on retiree health benefits could have a very,
17 very significant effect on our ability to remain
18 liquid.

19 The exigent price increase would begin to
20 provide benefit to us starting in January of 2011, our
21 second fiscal quarter and, as outlined in my
22 statement, would provide about \$2 billion of both
23 contribution and cash towards our rather ugly
24 financial position. So it can assist with our
25 liquidity problems that come to a head in September of

1 2011, but that alone is not enough to solve the short
2 term insolvency problem of the Postal Service.

3 The proposal to move delivery from six days
4 to five days, if it were approved today by everyone,
5 is something that would take at least six months to
6 put into effect, and there would be a ramp up period.
7 We believe that once it's fully implemented the
8 savings would be \$3 billion a year, but even if we
9 were to put that in place right now we would see very
10 little of that in fiscal year '11.

11 But over time, at \$3 billion a year and
12 growing with time that can be worth \$20 to \$30
13 billion, the same as the exigent price increase, which
14 on a full-year basis has a benefit to the Postal
15 Service of some \$3 billion. Again, over a 10 year
16 timeframe \$3 billion adds up to \$30 billion plus
17 interest savings.

18 So we have to balance out all of those seven
19 initiatives and consider the ability to, if you will,
20 live to fight another day, which is the 13 month
21 problem that we're facing, with how do we restore the
22 overall financial health of the Postal Service.

23 Our March 2 management plan, which doesn't
24 include any of these fundamental changes, but did
25 include price increases based upon CPI in accordance

1 with PAEA, you may recall, has us losing over the next
2 10 years \$115 billion. Of that, about \$20 billion is
3 interest. So \$115 billion over 10 years is about \$11
4 billion a year on average of losses. Take out the
5 interest of \$2 billion, so on operations we're losing
6 about \$9 billion a year on average.

7 Completely removing retiree health --

8 COMMISSIONER ACTON: I'm sorry, Mr. Masse.

9 THE WITNESS: I'm sorry.

10 COMMISSIONER ACTON: What about was
11 interest?

12 THE WITNESS: About \$20 billion --

13 COMMISSIONER ACTON: \$20 billion.

14 THE WITNESS: -- over the 10 years.

15 COMMISSIONER ACTON: Thank you.

16 THE WITNESS: Yes. So back to my math.

17 \$11 billion a year total losses less an average of
18 \$2 billion of year of interest is \$9 billion of annual
19 operating loss. If you completely remove retiree
20 health benefits prefunding, the math is \$5.5 billion.
21 They'll lose \$3.5 billion a year.

22 And add to that the fact that we run out of
23 borrowing in 2011. We hit our \$50 billion limit. The
24 interest, Commissioner Acton, assumed that someone
25 would loan us up to \$115 billion to keep the operation

1 running, which is why it adds up to some nearly \$20
2 billion of interest.

3 So the seven initiatives were seeking to
4 solve the short-term hurdle, the significant hurdle of
5 insolvency in 13 months, as well as address the
6 long-term picture, and that's why we've described it
7 as a balanced approach where there is no one silver
8 bullet.

9 There's no one solution that can solve it
10 all, but rather a variety of items that to a degree
11 share the burden amongst our stakeholders so that no
12 one stakeholder is being asked to completely solve the
13 problems of the Postal Service and to do it over that
14 extended time period.

15 CHAIRMAN GOLDWAY: So the plan on March 2
16 included a presumption of rate increases only
17 following the current laws --

18 THE WITNESS: Yes.

19 CHAIRMAN GOLDWAY: -- based on the rate of
20 inflation? And what did you estimate the rate of
21 inflation would be in that plan?

22 THE WITNESS: I believe it was about 1.5
23 percent a year on average or 1.6 percent or something
24 in that range.

25 CHAIRMAN GOLDWAY: So when you were

1 considering this proposal --

2 THE WITNESS: Yes.

3 CHAIRMAN GOLDWAY: -- because this is an
4 exceptional and an extraordinary case, a one time, did
5 you consider what you would need to completely address
6 the emergency that you faced, the short-term
7 emergency, which is what one would normally presume
8 this request would be for?

9 THE WITNESS: We did some analysis around
10 what would a sort of a -- I don't remember if it was a
11 one year or two year's worth of rate increases need to
12 be to completely address the whole \$115 billion gap.

13 As I recall, it was somewhere in the 25
14 percent range, so we would need to increase our prices
15 for the one to two years I think by as much as 25
16 percent if that were the only initiative or the only
17 lever, if you will, that was being pulled to help fill
18 that \$115 billion profit and cash gap.

19 CHAIRMAN GOLDWAY: You weren't here, I
20 understand. When did you begin with the Postal
21 Service?

22 THE WITNESS: I started in May of last year,
23 so I've been with the Postal Service about 15 months
24 now.

25 CHAIRMAN GOLDWAY: The Postal Service was

1 experiencing a significant volume drop in 2008, fiscal
2 year 2008.

3 THE WITNESS: Yes.

4 CHAIRMAN GOLDWAY: In fact, the worst was in
5 2008. It was not quite as back in 2009. Is that
6 correct?

7 THE WITNESS: No. I believe the worst, and
8 in my statement --

9 CHAIRMAN GOLDWAY: The calendar and the
10 fiscal year are sometimes confusing.

11 THE WITNESS: Right. We were down 12.7
12 percent in volume terms in 2009, 4.5 percent in 2008.

13 CHAIRMAN GOLDWAY: Okay. Were you involved
14 in any discussions about pursuing a rate increase last
15 year?

16 THE WITNESS: Yes. That was considered, an
17 exigent price increase, and the Postmaster General
18 announced towards the end of last calendar year -- I
19 can't remember exactly when it was -- that the choice
20 had been made to not put into place a price increase
21 either at that time or throughout calendar year 2010
22 because the belief then was that we did not want to
23 overburden our customers who were in the throes of the
24 effects of a terrible recession.

25 CHAIRMAN GOLDWAY: But did you consider what

1 the long-term effect would be to Postal Service
2 revenues by delaying a request for a rate increase?

3 THE WITNESS: Well, we understood at that
4 time also that a price increase would not be the
5 overall best solution or would not be the silver
6 bullet again to solve the financial problems of the
7 Postal Service and we began the work of developing
8 the March 2 plan in the fourth calendar quarter and
9 certainly into the first calendar quarter of this year
10 when we looked at the effects.

11 And I think what was most interesting was
12 the long-term projection of mail volume. When I
13 joined the Postal Service last summer, the belief was
14 that the volume or most of the volume would return.
15 What we have seen is that first class mail volume
16 continues to decline and our forecasts, which were
17 developed with the Boston Consulting Group, indicate
18 that first class mail volumes over the next 10 years
19 will decline at about 4 percent a year.

20 Standard mail volume has begun to improve,
21 especially in the last few months, but it is not
22 anywhere near the level that we saw 10 years ago.

23 CHAIRMAN GOLDWAY: Is the improvement better
24 than your forecast?

25 THE WITNESS: No.

1 CHAIRMAN GOLDWAY: It appears to be for
2 the --

3 THE WITNESS: We're doing fairly well versus
4 the forecast, but over time again it's expected to be
5 fairly flat with really a small growth in standard
6 mail over the 10 years averaging about 2 percent, but
7 the contribution, the dollars, if you will, have
8 always been in the first class product, not in the
9 standard mail product.

10 So the belief, as I said, this time last
11 year that much of the volume would return has now been
12 proven by actual results, if you will, for this year,
13 and our forecasting out for the next 10 years says
14 this is probably not going to be the case, which is
15 why we rolled out our plan on March 2, which included
16 the seven initiatives, one of which was related to
17 pricing.

18 CHAIRMAN GOLDWAY: I think I'll defer to
19 other Commissioners at the moment. Commissioner
20 Blair?

21 COMMISSIONER BLAIR: I appreciate that line
22 of questioning, Madam Chair, and I'd like to kind of
23 continue that.

24 Mr. Masse, it says in your biographical
25 sketch that you're responsible for all forward looking

1 financial information.

2 THE WITNESS: That is correct.

3 COMMISSIONER BLAIR: And you also say on
4 page 1 of your testimony that the purpose of your
5 statements includes an explanation of why price
6 increase is based on movements in inflation as
7 measured by the CPI-U will not provide sufficient
8 additional revenue to make an adequate contribution to
9 help solve the financial crisis faced by the Postal
10 Service.

11 THE WITNESS: Right.

12 COMMISSIONER BLAIR: Do you stand by that
13 statement?

14 THE WITNESS: Yes.

15 COMMISSIONER BLAIR: In Quarter 3, the
16 Postal Service showed a little bit better results than
17 it had in the previous quarters. Is that a correct
18 statement?

19 It seemed that there were some bright spots
20 that weren't there the previous year or even in the
21 previous months particularly with standard mail.

22 THE WITNESS: Actually, the first quarter of
23 the year was the bright spot.

24 COMMISSIONER BLAIR: But mail volume --

25 THE WITNESS: Our volume levels were above

1 our plan.

2 COMMISSIONER BLAIR: But the decline, the
3 rapid decline, seems to be on the uptick. The decline
4 is not as steep as it was a year ago.

5 THE WITNESS: Do you mean versus the prior
6 year?

7 COMMISSIONER BLAIR: Yes.

8 THE WITNESS: Okay. It has flattened out.
9 Again, yes, if you were to look at Mr. Corbett's
10 presentation that was done yesterday the volume
11 decline versus the previous year was down 1.7 percent
12 for the third quarter, whereas for the year-to-date
13 total volume is down 4.9 percent.

14 COMMISSIONER BLAIR: And I think in reply to
15 the Chairman when she asked why didn't you file last
16 year you answered that it would not have been -- I
17 don't want to put words. I'd like to hear your words
18 as to why the Postal Service chose not to file an
19 exigent case last year.

20 THE WITNESS: Well, it was, as I mentioned,
21 and unfortunately I don't remember the words of the
22 Postmaster General, but his statement was that we
23 didn't feel that it was the best thing to do at the
24 time given the very harsh economic climate that the
25 country was enduring, including the effects thereof on

1 our customers.

2 COMMISSIONER BLAIR: Well, I'm hearing from
3 news reports today that the growth outlook from the
4 Federal Reserve is saying that we may be going through
5 a double dip or that the growth seems to be stalling.

6 THE WITNESS: Yes.

7 COMMISSIONER BLAIR: Do you think your
8 customers are in a better position now than they were
9 last year to afford a 5.2 percent increase?

10 THE WITNESS: I think they've had some
11 benefits of the economic recovery, which, as I said,
12 began to occur a bit earlier than was assumed,
13 especially in our first fiscal quarter, but the fourth
14 quarter, fourth calendar quarter, of 2009.

15 There was also an improvement in the early
16 months of again calendar year '11, and it's just been
17 in the last few months that we've seen the stalling,
18 if you will, of the economic improvement. But, yes,
19 we've had the same sort of information presented to us
20 by the economists that we consulted.

21 COMMISSIONER BLAIR: This rate increase
22 won't go into effect until January, so you're hoping
23 that in January the economy will have emerged from
24 this stall and it'll be more robust?

25 THE WITNESS: Yes, we would hope. The

1 projections for 2011, again which are included in my
2 statement on Table 4 on page 7, show that there is
3 hope for the economy, both growth in GDP, growth in
4 employment for 2011, which is a different position
5 than for 2010, and growth in investment.

6 COMMISSIONER BLAIR: The reason I'm asking
7 this is looking back at past global insight
8 projections, and at my request I asked staff to look
9 at what was done in 2007 and 2008.

10 THE WITNESS: Right.

11 COMMISSIONER BLAIR: Much of the economic
12 situation that we find ourselves in today,
13 particularly the subprime debacle --

14 THE WITNESS: Right.

15 COMMISSIONER BLAIR: -- wasn't predicted.

16 THE WITNESS: Right. Everyone missed it.

17 COMMISSIONER BLAIR: Right. And I'm just
18 thinking if we once again find -- and projections are
19 never perfect and they're not expected to be. I mean,
20 that's what they are. They're projections.

21 THE WITNESS: Right.

22 COMMISSIONER BLAIR: I'm wondering what the
23 Postal Service will do should we find ourselves in a
24 double dip recession at a time that these increases
25 are going into effect. Don't you think they'll put

1 your customers in a worse position than they are now?

2 THE WITNESS: It very well could. What we
3 are attempting to do is with our seven point plan
4 provide a balanced solution to our financial problem.

5 Unfortunately, that means, as I said
6 earlier, sharing the burden, sharing the pain. We
7 aren't trying to balance the books of the Postal
8 Service completely on the back of our customers, but
9 rather have it spread, if you will, amongst a number
10 of areas.

11 I would also note that it's been estimated
12 that the cost, the average cost to an individual
13 household, of our price increase is estimated to be
14 about 15 cents a month, so from the perspective of the
15 public the cost is negligible when you consider that a
16 couple of years ago gasoline prices were rising by 15
17 cents a gallon every few weeks. So at 15 cents a
18 month it's not a terrible burden on individual
19 households.

20 COMMISSIONER BLAIR: Well, I understand. I
21 understand that perspective. I just would point out
22 that you're referring to the single piece first class
23 mail and households utilized. That's been in decline
24 for at least 10 years.

25 THE WITNESS: Oh, yes. Certainly.

1 COMMISSIONER BLAIR: And so price increases
2 and really the revenue it generates for the Postal
3 Service is not a segment that the Postal Service is --

4 THE WITNESS: Right.

5 COMMISSIONER BLAIR: -- really depending on.
6 It's your business customers.

7 THE WITNESS: Right. Well, and also -- I'm
8 sorry. I would ask that you bear in mind that our
9 price increase that would be effective in January
10 would be the first increase since May of 2009, so if
11 you were to look at it on an annual basis the price
12 increase is really 3.3 percent rather than 5.6 percent
13 so an average --

14 COMMISSIONER BLAIR: But inflation --

15 THE WITNESS: -- over nearly two years.

16 COMMISSIONER BLAIR: If you take it against
17 inflation, it certainly seems divorced from where
18 that --

19 THE WITNESS: Yes, unfortunately.

20 COMMISSIONER BLAIR: -- inflationary trend
21 has been.

22 THE WITNESS: Unfortunately it is.

23 COMMISSIONER BLAIR: And that's how the
24 price cap regime is set up. Yesterday I asked Mr.
25 Corbett basically if the price cap regime is dead. I

1 think I caught him a little bit off guard with the
2 question, and I'd like to know.

3 Do you see the Postal Service operating in
4 the future under this price cap regime? Is it a
5 viable pricing or ratemaking structure for the Postal
6 Service over the next five to 10 years?

7 THE WITNESS: I believe that only time will
8 tell and it depends on the contributions that we're
9 able to achieve from all of our stakeholders to
10 restore the financial fitness of the Postal Service.

11 Again, I hate to keep coming back to it, but
12 the U.S. Postal Service will be unable to pay its
13 bills, will be insolvent, in 13 months, and that to me
14 is a very extraordinary situation and requires some
15 emergency measures.

16 Predicting into the future the levels of
17 postal increases is obviously extremely difficult, but
18 again we hope to share the burden, as painful as it
19 is, amongst all of our stakeholders, but we do need
20 some very significant assistance in order to keep the
21 institution running.

22 COMMISSIONER BLAIR: And looking forward, on
23 pages 5 and 6 of your statement my inference of what
24 you were saying is that the Postal Service cannot
25 successful operate during an economic downturn,

1 whether those downturns are severe or moderate. Is
2 that a correct inference that I'm reading from your
3 testimony?

4 THE WITNESS: I think that some of the
5 points to bear in mind are that with the change in the
6 law that affectively impacted us in 2007, we have been
7 asked to fund substantial amounts of cash into the
8 Retiree Health Benefits Program. No other government
9 agency has been asked to do that, and we've
10 contributed some \$30 billion over the past three
11 years.

12 Unfortunately, that's also at a time when
13 our mail volumes, which is directly tied to our
14 revenue, has fallen substantially, mostly as a result
15 of the economic crisis and recession that our country
16 has faced. Combining those factors has left us in a
17 position where we will -- again, where we will run out
18 of cash in a few months time.

19 COMMISSIONER BLAIR: Right, but is it fair
20 to anticipate an exigency case every time the economy
21 declines over the next few years then?

22 THE WITNESS: No, I don't think so,
23 especially if we are able to achieve the contribution
24 from stakeholders that would provide us with a degree
25 of financial cushion in the event there are movements

1 in the economy.

2 COMMISSIONER BLAIR: But even with this
3 increase you are still facing solvency issues at the
4 end of 2011, aren't you?

5 THE WITNESS: Yes. As I said --

6 COMMISSIONER BLAIR: If the economy's growth
7 stalls in the future --

8 THE WITNESS: Yes.

9 COMMISSIONER BLAIR: -- are we going to be
10 back in this room again in 12 months or 18 months?

11 THE WITNESS: Only time will tell. In the
12 ideal world, we would be able to see the benefits of
13 the \$65 billion overpayment on our CSRS, and that
14 could be used to fully fund our retiree health
15 benefits, and that could result then in the repeal of
16 the requirements of funds \$5.5 billion a year for
17 retiree health benefits. That would, as I mentioned
18 earlier, have the most significant near-term effect on
19 our financial positions and would certainly improve
20 everything greatly.

21 COMMISSIONER BLAIR: If you get those
22 benefits, are you withdrawing the exigency case or do
23 you still need the exigency case on top of that?

24 THE WITNESS: As I mentioned earlier, that's
25 not enough. You know, losing \$11 billion a year or 9

1 billion, excluding interest, say 5.5 billion, we're
2 still losing 3.5, so some of the other initiatives are
3 still going to be required over the long haul.

4 CHAIRMAN GOLDWAY: But let's be clear, we're
5 talking about a liquidity crisis here. That's why we
6 have this exigent rate case in front of us, and what
7 would solve it is relief of something like you had
8 last year from the government. If you got that, would
9 you still be out of money in September 30, 2011? If
10 you got on September 30th of this year, you got \$4
11 billion --

12 THE WITNESS: Yes.

13 CHAIRMAN GOLDWAY: -- would you be out of
14 money, would you be out of cash on September 30, 2011?

15 THE WITNESS: No.

16 CHAIRMAN GOLDWAY: And if you got the relief
17 that you asked for of 5.5 billion this year and/or
18 next year, would that avoid the liquidity crisis?

19 THE WITNESS: Over time, no.

20 CHAIRMAN GOLDWAY: But in the short run.

21 THE WITNESS: It depends how you define
22 short run. 2011?

23 CHAIRMAN GOLDWAY: Well, September 2011 or
24 if you got ongoing it would continue for how many more
25 years before you would --

1 THE WITNESS: And that's exactly the point.

2 CHAIRMAN GOLDWAY: Yes.

3 THE WITNESS: Correct. If we were to be
4 resolved, if you will, of the \$5.5 billion payment,
5 and that only --

6 CHAIRMAN GOLDWAY: We can only do cash
7 estimates month by month for you in this fiscal year
8 2011, but you can apparently do more, so when do you
9 think?

10 THE WITNESS: No, that's my point. If we
11 were to have deferrals or waiving, if you will, of the
12 \$5.5 billion free funding, and only that, we would
13 still run out of cash in 2015.

14 CHAIRMAN GOLDWAY: 2015.

15 THE WITNESS: So assuming that price
16 increases are based solely on CPI through that time.

17 CHAIRMAN GOLDWAY: Right.

18 THE WITNESS: So as I mentioned earlier,
19 that one item is not enough to solve the financial
20 problems of the Postal Service over the 10-year
21 planning.

22 COMMISSIONER BLAIR: What I'm hearing from
23 you, Mr. Massey, is that at the rate -- the rate
24 change mechanisms that we have in place being based --
25 rate increase being based on CPI, which is, frankly, a

1 very generous cap in a regulatory regime like we
2 have --

3 THE WITNESS: Right.

4 CHAIRMAN GOLDWAY: -- is going to prevent
5 deficiencies by the fact that the Postal Service
6 reform is going through, said it could operate within
7 the CPI cap, and that there have been some fundamental
8 changes taking place in that you're -- are you urging
9 Congress to go in and change the ratemaking process in
10 order to provide more income?

11 Or I see that this case is kind of tapering
12 over. We have a much more fundamental problem, and
13 I'm just trying to get a sense of what the Postal
14 Service -- I know that the March 2nd report provided a
15 blueprint for you.

16 THE WITNESS: Yes.

17 COMMISSIONER BLAIR: But it sounds that
18 these liquidity problems are going to be a year-to-
19 year crisis and clinging from one crisis to the next,
20 and I'm trying to get a sense of what is extraordinary
21 and exceptional, and was it extraordinary and
22 exceptional this year, or is this a continuing
23 ordinary and exceptional circumstance over the next
24 five years that we're going to be seeing rate
25 increases over and above inflation in the Postal

1 Service?

2 THE WITNESS: As I said earlier, only time
3 will tell and it will be dependent on the levels of
4 contributions that we are able to achieve with the
5 other stakeholders.

6 CHAIRMAN GOLDWAY: Okay. So we've
7 established that if we got the 5.5 --

8 THE WITNESS: Right.

9 CHAIRMAN GOLDWAY: -- which everyone in the
10 community is working hard to do, you would avoid this
11 liquidity crisis until the end of 2015?

12 THE WITNESS: I don't have the details of it
13 but it would be some time in 2015, yes.

14 CHAIRMAN GOLDWAY: Do you have an estimate
15 of what your liquidity crisis problems would be if you
16 had this 5.6 percent increase and the prefunding of
17 the Retiree Health Care Retirement Fund waived?

18 THE WITNESS: That would get us probably
19 until about 2017.

20 CHAIRMAN GOLDWAY: Okay. So the additional
21 5.5 gets you two extra years --

22 THE WITNESS: Yes.

23 CHAIRMAN GOLDWAY: -- you would say?

24 THE WITNESS: Yes.

25 CHAIRMAN GOLDWAY: But after the fact.

1 THE WITNESS: But assuming there are no
2 other changes with regard to things like five-day
3 delivery or anything like that.

4 CHAIRMAN GOLDWAY: Right. Okay. I think
5 we're trying to get a sense of the feel of the problem
6 and what the appropriate action to take is at this
7 time, and this discussion is helpful even if it
8 doesn't give the answer.

9 I know Commissioner Langley said she wanted
10 to follow up with something.

11 COMMISSIONER LANGLEY: Thank you very much.
12 I have a couple of areas that I would like to follow
13 up on. I think Commissioner Blair appropriately
14 stated the swinging economy that we are experiencing
15 right now. One expert even said that it's either
16 we're in the middle of the problems or we're falling
17 off a cliff.

18 THE WITNESS: Right.

19 COMMISSIONER LANGLEY: So the strength of
20 the economic recovery, I think, has a lot to do with
21 the Postal Service's recovery as well, and one area
22 that is of interest to me is Commission regulations on
23 exigent rate increases. It requires the Postal
24 Service to discuss whether and when the increase might
25 be rescinded, and I know the Postal Service in

1 response to this said that it had little expectations
2 of, you know, rescinding other than over time the CPI
3 cap is going to catch up with what you need.

4 THE WITNESS: Correct.

5 COMMISSIONER LANGLEY: Is it correct then to
6 assume that these rates are going to stay in effect --
7 if the Commission approves the exigent rates -- stay
8 in effect until the next rate increase?

9 THE WITNESS: Yes, I believe that would be
10 reasonable assumption at this time.

11 COMMISSIONER LANGLEY: And then if that's
12 the case, has the Postal Service got an estimate as to
13 when they might need the next rate increase?

14 THE WITNESS: Unfortunately, as I mentioned
15 earlier, that all depends on the level of contribution
16 that we are able to achieve on the other areas of our
17 plan. The most significant of which in the short term
18 is related to the Retiree Health Benefit Fund.

19 COMMISSIONER LANGLEY: Given that Congress
20 seems to be indicating a willingness, at least this
21 year, to again defer, but because the Postal Service
22 has been involved in forecasting for a number of
23 scenarios I would assume there is some scenario out
24 there as well looking at all the variables to at least
25 have an estimate as to what it might do in the future

1 if X, Y and Z happens, and you have all your
2 forecasts, you know, where you're going to move to
3 raise rates again.

4 THE WITNESS: No, we have not really spent
5 much time looking at the potential for the next rate
6 increase, if you will, because it will be very highly
7 dependent on, as I said, the contributions from all of
8 the other areas, and it's not that we are trying to
9 achieve a certain number in any area, but we're
10 trying -- again, it's a balance approach to resolving
11 the financial difficulties of the Postal Service, and
12 it will be dependent on obviously what happens in the
13 economy and what we can achieve in the whole fleet of
14 areas, and how quickly these things can be resolved
15 given our problems, significant problems.

16 COMMISSIONER LANGLEY: All right, then --

17 THE WITNESS: Extraordinary.

18 COMMISSIONER LANGLEY: No, I understand
19 that, but given that the exigent rate increase is
20 based on, and the Postal Service calls it dramatic
21 rapid unprecedented decline in mail volume.

22 THE WITNESS: Yes.

23 COMMISSIONER LANGLEY: Do you believe that
24 the decrease in volume after an exigent rate increase
25 goes into effect -- are the volume forecasts correct?

1 THE WITNESS: We believe they are, and my
2 statement includes the effect on volumes both with and
3 without the exigent price increase. Sample one, for
4 example, shows the before rate in 2011 position of
5 174.3 billion pieces. After rates for 2011, 173, and
6 a full-year basis is 172. So our forecasts -- our
7 belief is that on an annual basis this price increase
8 would result in a loss of 2 billion pieces of mail.
9 But overall drives a higher revenue and contribution
10 number.

11 COMMISSIONER LANGLEY: My concern is that
12 the extraordinary and exceptional atmosphere in which
13 the Postal Service finds itself in is -- I'm just not
14 quite confident that the volume forecast debates on,
15 you know, really the historical data is going to yield
16 the expected outcome, and Dr. Keefer in his testimony
17 mentions that current econometric estimates of price
18 elasticity may not adequate predict such tipping point
19 in movements, and he was referring to large mailers
20 who may decide to leave the system, I believe.

21 THE WITNESS: But that was one of the
22 reasons that we asked the Boston Consulting Group to
23 long-term forecasts with us, and they didn't rely on
24 an econometric estimate, but rather their forecasting
25 was based on direct discussions with our customers, to

1 ask them what their plans were over the long term.

2 CHAIRMAN GOLDWAY: Did Boston Consulting
3 Group ask them what their response would be to a 5.6
4 percent increase?

5 THE WITNESS: I don't believe they asked
6 that specific question, but as I recall they did
7 discuss price increases with customers, and --

8 CHAIRMAN GOLDWAY: Did you get any
9 information, this is to follow up on Commissioner
10 Langley, did you get any information from Boston
11 Consulting Group that would indicate that the
12 elasticity formulas that are now in place that you're
13 using for this rate case request --

14 THE WITNESS: Right.

15 CHAIRMAN GOLDWAY: -- are accurate or
16 inaccurate, outdated, reliable?

17 THE WITNESS: I don't recall that was asked
18 in great detail with Boston Consulting, but I think
19 one thing to bear in mind is that if we look at the
20 last two price increases, which as I recall were
21 around 4 percent, or somewhere around 3 percent and 4
22 percent, we did not see massive losses of volume with
23 those, and again, unfortunately, it's historical, but
24 going back in time from what I'm told, this is
25 obviously before I joined the Postal Service, when

1 there were double digit price increases the volume did
2 not drop.

3 COMMISSIONER LANGLEY: But this is a
4 different time.

5 THE WITNESS: But you are right. Exactly.
6 I agree completely.

7 COMMISSIONER LANGLEY: Yes, it's a different
8 time, and the Postal Service is asking the Commission
9 to consider the economic environment in which the
10 Postal Service is operating today.

11 THE WITNESS: Yes.

12 COMMISSIONER LANGLEY: And looking back at
13 past rate increases is historical. It's nothing more
14 than historical.

15 THE WITNESS: Right.

16 COMMISSIONER LANGLEY: You know, what type
17 of forecasting is needed now? I mean, again, the
18 Federal Reserve yesterday acted to keep interest rates
19 near zero.

20 THE WITNESS: Yes.

21 COMMISSIONER LANGLEY: Assume we're not
22 progressing on the economic front as everything would
23 hope.

24 THE WITNESS: Right, and we made those kinds
25 of assumptions, you know, in our forecasts.

1 COMMISSIONER LANGLEY: So that was all
2 factored in?

3 THE WITNESS: Well, it has weakened in the
4 near term, but we have always projected a long, drawn
5 out recovery from this -- I guess it's not a passive
6 session -- and the fact that it would be the so-called
7 jobless recovery with very small order of -- it would
8 take a long time for employment levels to return.

9 COMMISSIONER LANGLEY: But this is impacting
10 the housing market now again.

11 THE WITNESS: Yes, and the housing market
12 is --

13 COMMISSIONER LANGLEY: The housing market --

14 THE WITNESS: That's statistics which go
15 into economics.

16 COMMISSIONER LANGLEY: So the long-term
17 decline in employment and inability of people to get
18 jobs --

19 THE WITNESS: Yes.

20 COMMISSIONER LANGLEY: -- is going to impact
21 a number of the mailing sectors, and if the economy
22 continues to just thump along --

23 THE WITNESS: Right.

24 COMMISSIONER LANGLEY: -- the financial
25 institutions are going to have to retrench. I mean

1 there is going to be a retrenchment of the economy, or
2 economic activity at some point in order to --

3 THE WITNESS: Well, I don't know if anyone
4 has did a --

5 COMMISSIONER LANGLEY: No one is predicting.

6 THE WITNESS: -- retrenchments or the
7 terrible double dip, but instead what I have heard is
8 that it's a slowing of the recovery.

9 COMMISSIONER LANGLEY: I guess my primary
10 question is the Postal Service is taking all of this
11 into consideration when it's coming up with what
12 appears to be not a huge decline in volume, and one
13 that would recover.

14 THE WITNESS: Yes.

15 COMMISSIONER LANGLEY: Thank you. I have
16 one final question. You know, you indicated that the
17 Postal Service had developed its multi-prong approach
18 to long-term solvency in the fourth quarter of last
19 year, the first quarter of this year.

20 I am curious how an exigent price increase
21 which many believe should be a response to something
22 rather immediate, you know, Senator Colins has
23 mentioned in her filing with the Postal Service that
24 it be something like an anthrax attack, or a bio
25 terrorist attack, How do you respond to the opponents

1 of this exigent price increase that it is exigent when
2 it's part of a seven-prong approach to long-term
3 solvency?

4 THE WITNESS: Right. I think Mr. Corbett
5 talked at length yesterday about the extraordinary,
6 certainly a significant departure from the ordinary,
7 the extraordinary volume, decline in mail volume that
8 we saw essentially in 2009, mostly attributable again
9 to the 2006, and I would certainly agree that that was
10 an extraordinary event for the Postal Service.

11 But what I believe the real extraordinary
12 event is, and I would ask you to keep that in mind
13 going further, the extraordinary event is the
14 insolvency in 13 months. It's the inability of an
15 institution like the U.S. Postal Service to pay its
16 bills when due 13 months from now. That's really the
17 extraordinary event as I see it.

18 Senator Colins talked about, you know, the
19 exigent provisions only being used in cases of anthrax
20 and the like. But if we look back in history for our
21 fiscal year 2002, when we experienced the effect of
22 September 11th, anthrax, and then a recession as well,
23 that sort of trisecta, our volume only went down 3 or
24 3 percent. Last year our volume declined by 12.7
25 percent.

1 So one could argue that that our recently,
2 our hopefully recently ended recession had a more
3 extraordinary impact on mail volumes than the combined
4 effects of 9/11, anthrax, and a recession at the time.

5 COMMISSIONER LANGLEY: Thank you for your
6 straightforward answers.

7 THE WITNESS: Sure.

8 CHAIRMAN GOLDWAY: My fellow Commissioners
9 on my left, any questions?

10 COMMISSIONER ACTON: Thank you, Madam
11 Chairman. Welcome, Mr. Massey

12 THE WITNESS: Thank you.

13 COMMISSIONER ACTON: I think when we focused
14 on this question about the double-dip recession and
15 the possibility of all of that we were just trying to
16 understand if indeed the Postal Service was filing an
17 exigent rate care because of extraordinary
18 circumstances or whether this was part of what you're
19 doing to address a long-term trend, and in some ways
20 it's both.

21 As I have said, in the near term we have
22 insolvency, but over time with a decline in use of
23 mail, which we predicted along with the Boston
24 Consulting Group, where our mail volume will go down
25 over the next 10 years by an average of about 2

1 percent a year, that's reflecting the change in the
2 way that Americans especially communicate; away from
3 hard copies, and more and more to electronic means.
4 Has the Postal Service managers thought about whether
5 or not there would be a need for another exigent rate
6 case?

7 THE WITNESS: I don't believe, I haven't
8 been involved in discussions about a second exigent
9 rate case. I don't believe that others have as well.
10 Our hope is that this is one element of the balance
11 approach of the spoke of the seven prongs that we can
12 move forward with and that we will have sufficient
13 contributions from the other six prongs, if you will,
14 so that it will help to right the ship.

15 COMMISSIONER ACTON: Yesterday Mr. Corbett
16 indicated that, I believe he indicated, he threatened
17 if I'm not mistaken, that there wasn't really a
18 revenue target, that you set on a percentage increase
19 in terms of this rate filing.

20 THE WITNESS: Yes. I was not involved in
21 the details as to how the percentages were developed
22 but as the Postmaster General said on March 2nd, the
23 Postal Service planned to and we believe now has
24 proposed a moderate price increase.

25 COMMISSIONER ACTON: So you're not familiar

1 with the factor that drove that decision?

2 THE WITNESS: The individual pricing
3 elements?

4 COMMISSIONER ACTON: No, I'll get to that.
5 I want to know when management had this discussion
6 about setting this percentile for the exigency rate
7 increase request, what sort of issues were on the
8 table?

9 THE WITNESS: Well, one issue was the
10 ability to generate cash.

11 COMMISSIONER ACTON: Yes.

12 THE WITNESS: And generate cash quickly, but
13 also to try to change prices in a way that would not
14 drive away massive amounts of mail; would not try to
15 balance the books of the Postal Service on our
16 customers; and so on.

17 COMMISSIONER ACTON: Okay.

18 THE WITNESS: But we were not -- we did not
19 seek a specific number in terms of revenue or
20 contribution from the outset but rather tried to
21 adjust the pricing -- and Mr. Keefer can discuss that
22 in more detail tomorrow -- adjust the pricing by
23 looking at the individual products.

24 COMMISSIONER ACTON: So would it be fair to
25 characterize your thoughts and management's thought

1 that these rates are what the market will bear?

2 THE WITNESS: Perhaps, but obviously the
3 market, our customers, the mailers, don't want to see
4 a price increase.

5 COMMISSIONER ACTON: Obviously. And can you
6 describe the methodology that you used for volume
7 forecasting for this case?

8 THE WITNESS: For volume forecasting?

9 COMMISSIONER ACTON: Yes.

10 THE WITNESS: We used our econometric models
11 to forecast the volumes for 2011 with the impacts of
12 the price increase in January and in September to
13 derive the values for after rates forecast. All that
14 is included in my statement.

15 COMMISSIONER ACTON: And the volume
16 forecasting that you referenced earlier this morning
17 from Boston Consulting Group --

18 THE WITNESS: Yes.

19 COMMISSIONER ACTON: -- that's a different
20 approach?

21 THE WITNESS: Yes.

22 COMMISSIONER ACTON: It's not used in this
23 proposal, is it?

24 THE WITNESS: No, it was not but the results
25 of our volume forecasting are similar to what Boston

1 Consulting Group and McKenzie supplied for 2011.

2 COMMISSIONER ACTON: You used the McKenzie
3 and the Boston Consulting Group in another docket in
4 the proposal for the elimination of Saturday delivery?

5 THE WITNESS: I believe so, yes.

6 COMMISSIONER ACTON: Why the change in
7 methodology? Why in one instance and not in the
8 other?

9 THE WITNESS: Well, the both derived, as I
10 said, similar results. We believe it would be most
11 efficient, especially for the Commission, if we were
12 able to present reports and analysis in formats that
13 the Commission and staff were familiar with as similar
14 to those that were used in previous rate cases. So,
15 we tried to do things -- do the analysis, do the
16 calculations, if you will, in a way that would
17 facilitate the speed with which this case could be
18 considered.

19 COMMISSIONER ACTON: Okay. You're a
20 certified public accountant, aren't you?

21 THE WITNESS: Yes, I am.

22 COMMISSIONER ACTON: Member of the American
23 Institute of CPAs?

24 THE WITNESS: I am.

25 COMMISSIONER ACTON: Are you familiar with

Heritage Reporting Corporation
(202) 628-4888

1 this report, the Siegel findings?

2 THE WITNESS: Yes, I am.

3 COMMISSIONER ACTON: Will you offer an
4 impression of your -- what's your thoughts?

5 THE WITNESS: I think it's a good report and
6 it comes to very good conclusions. I believe that the
7 valuation of potential liabilities in question and the
8 sharing of the future liability for employees that
9 work for the old Post Office Department and then
10 subsequently worked for the Postal Service should take
11 into account the future pay increases that went into
12 place which is a finding that Siegel came up with as
13 well. It is consistent with current
14 accounting and actuarial rules.

15 COMMISSIONER ACTON: You did read it. Here
16 is my concern about this particular scenario, and I
17 talked with Mr. Corbett about this yesterday. I think
18 some of us in the community believe that there need to
19 be some changes made, some legislative changes that
20 will help express some of the findings that are shown
21 in this report.

22 THE WITNESS: Yes.

23 COMMISSIONER ACTON: You know reality, and
24 one factor in this big debate is that will granting an
25 exigency rate case sort of just delay some of the

1 legislative issues that need to be accomplished.

2 THE WITNESS: No, I don't think so, and
3 again if we go back to my example of an average loss
4 of \$11 billion a year, 9 billion without interest, \$3
5 billion contributions from the exigent rate case --
6 well, actually less than three because the 11 billion
7 loss had built into it already increase at the CPI
8 level.

9 But ignoring that difference, losing 9
10 million or a billion a year, add back three, probably
11 less, more like two, still losing 7 billion a year,
12 we're still --

13 COMMISSIONER ACTON: Okay.

14 THE WITNESS: Once again, the exigent rate
15 case is not a silver bullet with all the financial
16 problems of the Postal Service.

17 COMMISSIONER ACTON: These are interrelated
18 factors that leverage one another is sort of my view.

19 THE WITNESS: Yes, they do because it all
20 comes down to these area cash position of the Postal
21 Service when all is said and done.

22 COMMISSIONER ACTON: I know, you know, a lot
23 of the situation that the Postal Service finds itself
24 in isn't necessarily of the Postal Service's making,
25 and I don't think it's any secret that I will enjoy

1 that the Postal Service's door will be open for these
2 sorts of discussions. It doesn't mean that I will
3 advocate for them but it's important that we know what
4 you have got to say. Postal is in our name. You guys
5 are at the epicenter.

6 THE WITNESS: Yes.

7 COMMISSIONER ACTON: But I worry about the
8 mailers having paid some of these costs already, and
9 it's not necessarily that the bills haven't been paid,
10 it's just not accounted for properly. So to have to
11 ask for a rate increase to apply more funds towards,
12 you know, whatever the type of shared goals are is
13 difficult to come to terms with.

14 THE WITNESS: Let me address that. As I
15 mentioned earlier, in the perfect world the 55
16 billion, 50 to 55 billion that Siegel has identified,
17 which was overpayment of CSRS obligations, which as
18 you mentioned yesterday in your discussion with Mr.
19 Corbett, and I believe we're alluding to today, is
20 something that ratepayers have paid for in the past
21 since 1971.

22 If that overpayment, that 55 billion were
23 transferred to the underfunded retiree health benefits
24 obligation, which at the end of 2009 just happened to
25 be underfunded by, I think, 52 or 53 billion dollars,

1 that would top that up completely, and would eliminate
2 the need for the \$5.5 billion of prefunding that we
3 currently are required to make.

4 But once again, if we take that 5.5 billion
5 out of the 9 billion a year of operating losses,
6 unfortunately we're still losing 3.5 billion. So
7 that's taking the money that ratepayers have already
8 paid, using it to satisfy another obligation, another
9 financial problem of the Postal Service, but
10 unfortunately still is not enough to solve the
11 financial problems of -- the overall financial
12 problems of the Postal Service.

13 CHAIRMAN GOLDWAY: Could you, just for the
14 record, provide us -- assuming that the Congress does
15 provide relief for the 5.5 billion in a similar
16 fashion that they did in 2009, or this ideal program,
17 could you give us cash flows for 2010 and '11, perhaps
18 even '12, to show us what the effect would be of the 4
19 billion, 5 billion, and with or without a rate
20 increase?

21 THE WITNESS: We could do some of that --

22 CHAIRMAN GOLDWAY: Could you do that?

23 THE WITNESS: -- quickly if you would like.

24 CHAIRMAN GOLDWAY: We have the three years
25 of cash flows, 2010, '11 and 12.

1 THE WITNESS: If we look at Table 5 of my
2 statement.

3 CHAIRMAN GOLDWAY: Yes.

4 THE WITNESS: And the right-hand column is
5 our cash shortfall, and this is all for 2011, and the
6 before rates line is as if there is no price increase,
7 we will be short cash of \$4.4 billion. That assumes
8 that we pay the full \$5.5 billion claim. After rate
9 has this \$2 billion benefit that we talked about for
10 the exigent pricing for the nine months of 2011, and
11 the full years is a 12-month impact.

12 But if we look at those first two lines, and
13 this is the cash position at the end of fiscal year
14 '11, if we were to get \$4 billion of assistance from
15 Congress for 2010, that 4.4 billion shortfall before
16 rates, no price change, would be about \$400 million.

17 If we were to get another \$4 billion at the
18 end of fiscal year '11 in terms of assistance or
19 relief, it would flip to a positive number of about
20 \$3.6 billion.

21 CHAIRMAN GOLDWAY: And can you give us 2012?

22 THE WITNESS: I don't have all the
23 information here to do it.

24 CHAIRMAN GOLDWAY: Could you provide that
25 for us in writing?

1 THE WITNESS: Yes.

2 COMMISSIONER ACTON: I have one last
3 question, Madam Chairman.

4 THE WITNESS: I can do it. The 2012 in
5 writing. I'm sorry.

6 COMMISSIONER ACTON: I realize that you were
7 not at the Postal Service when the reform was enacted
8 in 2006. For the provision therein that you may be
9 familiar with where the Postal Service had one last
10 opportunity to craft a rate case, set the rates up to
11 they be appropriate going forward under reform.

12 THE WITNESS: I'm not familiar with that.

13 COMMISSIONER ACTON: Thanks for your
14 testimony today. Appreciate it.

15 THE WITNESS: Okay.

16 VICE CHAIRMAN HAMMOND: Thank you, Madam
17 Chairman. I think you taking us directly down this
18 line of questioning and the details that you and
19 Commissioner Blair and all of my colleagues, I don't
20 know exactly any way to ask the question any
21 differently, it would be redundant. So I will not ask
22 any questions at this time. Thank you.

23 CHAIRMAN GOLDWAY: I'd like to go through
24 some of the questions that were asked by some of the
25 participants in this hearing. The Public

1 Representative would like us to confirm that the \$2
2 billion that will be generated in additional revenue
3 is simply going to be applied to the general operating
4 budget?

5 THE WITNESS: Yes.

6 CHAIRMAN GOLDWAY: So there are no specific
7 plans for that \$2 billion?

8 THE WITNESS: No.

9 CHAIRMAN GOLDWAY: Okay. Valpak would like
10 to know if you could describe any major revenue
11 generating initiatives that the Postal Service is
12 contemplating. We're talking here about losses and
13 declining revenues for mail volumes. Are there any
14 major revenue generating initiatives that the Postal
15 Service is contemplating?

16 THE WITNESS: Well over the last year or so
17 and extending into the future some of the revenue
18 initiatives that we are pursuing include things like
19 the last mile package service, partial collect, new
20 stamp products including a rubber stamp for the
21 holidays which our customers have been very interested
22 in. We hope to expand direct mail, advertising mail,
23 with small and medium businesses, make the processes
24 for them to be able to use that medium much simpler
25 and easier to use, which obviously would benefit us

1 and our mail volumes. The flat rate boxes have been
2 very attractive products and has contributed well to
3 us. We are doing and have done incremental volume
4 promotions, such as the summer sale, which kicked off
5 and we hope to get as much as a billion pieces of
6 incremental mail from that.

7 CHAIRMAN GOLDWAY: There seems to be concern
8 whether the volume results in actual revenue increases
9 so far in the previous sales. Do you have revenue
10 generating estimates for some of these projects you're
11 listing?

12 THE WITNESS: Well let's just consider that
13 one at a billion pieces. On average standard mail
14 generates about 20 cents of revenue. So that's worth
15 about \$200 million of revenue from that one
16 initiative. All those things that have been mentioned
17 are the reply rides free initiative with reply
18 envelopes riding free, more work around post office
19 boxes which are especially a cash cow, and we have a
20 number of those that are vacant, get people interested
21 in them and using them more.

22 We've sent out and are still test marketing
23 what we call the sample co-op boxes which have, you
24 know, six to ten different sample items in one box, so
25 a number of companies can send out this sample

1 together in what's hoped to be a more efficient
2 package that also would probably have more impact this
3 year. So we're doing a number of things along those
4 lines. But is there anything there that would
5 significantly move the needle, that is going to have a
6 huge contribution towards our insolvency problem 13
7 months away? No. They're all steps in the right
8 direction and they will make contributions towards the
9 overall position, but again there's not a --

10 CHAIRMAN GOLDWAY: What do you estimate the
11 total revenue of these efforts to be?

12 THE WITNESS: Of all of these? You know, as
13 we talked about the incremental volume promotion for
14 standard mail is worth about \$200 million. So the
15 whole package combined, \$2, \$3, \$400 million.

16 CHAIRMAN GOLDWAY: So when we're talking
17 about a business model of revenues that cover costs,
18 you haven't come up with a product or an opportunity
19 for increased revenue that's going to address the long
20 term business model problem you have?

21 THE WITNESS: We haven't found a silver
22 bullet that will solve all the problems. We continue
23 to chip away at it by looking at new products and
24 actually are sponsoring later today and then again in
25 a month or so an innovation forum with some of our

1 customers, see what ideas they might have about
2 products that the Postal Service could offer them
3 within the limitations of what we're allowed to offer
4 as products, but products that they would see as
5 attractive to the marketplace.

6 So we are continuing to search and are
7 asking for help from whatever sources there may be to
8 try to find attractive and innovative new products
9 that we're able to offer. But with the effects of
10 electronic diversion and communications moving to
11 electronic medium, it's certainly difficult. My kids
12 don't use the mail. They don't even use the
13 telephone. They do all of their communication with
14 their phones.

15 CHAIRMAN GOLDWAY: So and can you describe
16 any additional cost cutting initiatives that the
17 Postal Service is contemplating pursuing?

18 THE WITNESS: We're continuing our
19 automation efforts for mail processing, we're doing
20 plant consolidations, delivery route optimizations,
21 the Mirap and Jrap programs that you're probably
22 familiar with. We rolled out our ABC program which is
23 trying to increase the efficiencies of our surface
24 transportation and distribution networks. The main
25 area that we continue to target, and it affects all of

1 these kinds of cost savings, are reductions in work
2 hours and reductions in the size of the workforce. As
3 I mentioned earlier we've taken out 63 million hours
4 of work hours in the nine months that ended in June as
5 compared to the previous year. We'll continue to
6 target that. Labor is 80 percent of our cost --

7 CHAIRMAN GOLDWAY: The original plan had
8 called for 83 million work hours.

9 THE WITNESS: Actually 90 to 93 million work
10 hours. We've had to back down from that a bit because
11 of the increases in volume. We've done 63 million for
12 nine months. We hope that for the full year to still
13 be at a level close to 80.

14 CHAIRMAN GOLDWAY: Do you think you're still
15 on track for that?

16 THE WITNESS: Yes.

17 CHAIRMAN GOLDWAY: And while we're at the
18 work hours savings, the Greeting Cards Association
19 have some specific questions about work hours. They
20 wanted to know whether on page 4 of your statement
21 when you note that during Fiscal Year 2008 there was a
22 reduction of 21,500 career employees in response to
23 significant mail volume losses, of that 21,500 how
24 many career employees left because of VIRA and how
25 many left because of attrition?

1 THE WITNESS: Virtually all of them left as
2 a result of attrition, in most cases related to
3 retirement. And some of those retirements may have
4 been stimulated if you will by the VIRAs, which is
5 just --

6 CHAIRMAN GOLDWAY: You don't know what
7 percentage was the VIRA?

8 THE WITNESS: But the specific numbers I
9 don't have, and I mean if it's critical, you know, if
10 it's --

11 CHAIRMAN GOLDWAY: Can you provide them for
12 us? And for 2009 as well?

13 THE WITNESS: Yes. Yeah, in 2009 we had
14 about 40,000 career employees.

15 COMMISSIONER BLAIR: Are there any plans to
16 offer voluntary and separation payments, buyouts, to
17 employees over the next few years as part of your cost
18 reduction measures? Is that on the table?

19 THE WITNESS: We don't. It's always under
20 consideration but we don't have specific plans around
21 that at the current time.

22 COMMISSIONER ACTON: You haven't budgeted
23 for it?

24 THE WITNESS: No, not specifically.

25 CHAIRMAN GOLDWAY: The Greeting Cards

1 Association also has a specific question about the
2 fixed cost and labor costs of the delivery network.
3 How much of the fixed cost in the delivery network are
4 labor costs versus non-labor costs?

5 THE WITNESS: I don't have that. We would
6 have to research that. But a big portion I suspect is
7 labor cost for the close to 200,000 city carriers we
8 have and 60,000 some rural carriers.

9 CHAIRMAN GOLDWAY: And do you know what the
10 cost savings was as a result of the memorandum of
11 understanding with the National Association of Letter
12 Carriers to reduce routes?

13 THE WITNESS: The specifics we would have to
14 research, but as I recall the initial memorandum we
15 were able to reduce I think it was about 12,000, or
16 eliminate if you will, 12,000 routes. But I would
17 have to go back and we would have to do some
18 calculations --

19 CHAIRMAN GOLDWAY: Well for the benefit of
20 the record then could you give us your understanding
21 of what the fixed costs are in the delivery network?

22 THE WITNESS: Okay, we'll just put that on
23 the list.

24 CHAIRMAN GOLDWAY: And non-fixed, and how
25 much are non-labor -- how much in the fixed cost are

1 labor and how much are non-labor, and how much savings
2 there was in the restructuring of the city delivery
3 routes, how much you're expecting to have additional
4 savings in restructuring there.

5 THE WITNESS: Right.

6 CHAIRMAN GOLDWAY: And to what extent you
7 can separate out within that restructuring route
8 process what was labor and what was non-labor.

9 THE WITNESS: Okay.

10 CHAIRMAN GOLDWAY: And then I'll --

11 THE WITNESS: Are these best accomplished
12 via another --

13 CHAIRMAN GOLDWAY: A written --

14 THE WITNESS: POIR?

15 CHAIRMAN GOLDWAY: Well this substitutes for
16 a POIR.

17 THE WITNESS: Okay.

18 CHAIRMAN GOLDWAY: This is asking you to do
19 it.

20 THE WITNESS: You guys are writing all this
21 down I hope, right, okay.

22 CHAIRMAN GOLDWAY: So you'll do it. And
23 then I cut you off. Are there other additional cost
24 savings initiatives that you wanted to list?

25 THE WITNESS: I think we touched on the big,

1 obviously most significant is work hours savings and
2 the area that we have tried for. We are also
3 experiencing or we're seeing high levels of success
4 with our digital or alternative retail channels,
5 continuing use and improvement of USPS.com, our online
6 capabilities, contract postal units, the kiosks,
7 stamps on consignment, selling stamps through our
8 retail partners, all of those efforts which are
9 significantly less expensive than the brick and mortar
10 post offices, but those efforts, you know, continue to
11 show improvements and growth.

12 CHAIRMAN GOLDWAY: There's another question
13 here from Valpak. If you refer to attachments 11 and
14 12 of your statement, do all of the market dominant
15 products shown include the full effect of all lags in
16 own price elasticity as developed in Library Reference
17 USPS-R-2010-4/8?

18 THE WITNESS: Yes they do.

19 MR. KOETTING: Madam Chairman, there was,
20 that has been addressed at two of the telephone
21 conferences and then we filed a written response on
22 that which is already available.

23 CHAIRMAN GOLDWAY: Okay, well my staff asked
24 to consider that, so we're doing that. With regard to
25 the flat strategy document that you filed, which

1 addresses a number of possible cost reduction
2 initiatives, some of which are indicated as having an
3 effect on Fiscal Year 2011, are any of the cost
4 initiatives discussed in the flat strategy documents
5 not included in the cost forecast for 2011?

6 THE WITNESS: Any of them not included? No,
7 I don't believe any have been left out.

8 CHAIRMAN GOLDWAY: So what cost reduction
9 initiatives are included in the cost forecast for
10 2011?

11 THE WITNESS: I think the effects of FSS,
12 and more details I think we could probably get from
13 Mr. Neery when he speaks on flat strategy.

14 CHAIRMAN GOLDWAY: Okay, so --

15 THE WITNESS: But we could look into it as
16 well.

17 CHAIRMAN GOLDWAY: If I understand this
18 right, in the cost roll forward work papers for flat,
19 cost reductions for 2010 would be approximately \$51
20 million, \$76,000 in cost savings and \$25,000 in
21 additional cost. So one can assume that that savings
22 -- this is, do you have this? This is cost roll
23 forward work papers, USPS-R-2010-4-6?

24 THE WITNESS: I don't believe I have that
25 here with me, and I think it would be best if --

1 CHAIRMAN GOLDWAY: So it looks like there's
2 \$51 million in 2010 and \$250 million in 2011, is that?

3 THE WITNESS: I'd prefer to let my staff
4 address those kinds of details.

5 CHAIRMAN GOLDWAY: Okay, so just for the
6 record so I understand it, since I'm not all that good
7 on these records, could you simply indicate to me what
8 are the cost savings for the flat strategy that have
9 been included in 2010 and 2011?

10 THE WITNESS: The details of the cost?

11 CHAIRMAN GOLDWAY: Yes, what the cost
12 savings will be for those two years.

13 THE WITNESS: We would have to, I'd have to
14 consult with my staff and come back with it.

15 MR. KOETTING: Madam Chairman, relating to
16 that type of a question, earlier you asked about the
17 flat sequencing program, and we did find that in the -
18 -

19 CHAIRMAN GOLDWAY: Right, yes, so that's
20 what I'm referring to but I still don't quite
21 understand it clearly, and it would be simpler for me
22 to just know exactly what the bottom line deduction
23 you're planning to use for the flat sequence is. I
24 think, you know, in our annual compliance
25 determination the Commission points out that there's a

1 -- oh, it went off.

2 In our annual compliance determination the
3 Commission points out that there is \$6 to \$700 million
4 worth of costs in the periodicals and flat that the
5 Postal Service has to absorb above the prices that
6 they charge for those products. So when we're looking
7 at significant structural changes, it's really
8 important to see whether we can solve that problem
9 through cost savings. One of the questions that was
10 asked by the Periodical and Catalogue Mailers was they
11 wanted you to know that during the period during 1999
12 and 2009 the unit cost of mail processing and delivery
13 for standard mail flats almost doubled while the
14 consumer price index for the same period increased 29
15 percent.

16 And during that time the deployment of the
17 AFSM 100 was completed and the amount of work sharing
18 standard mail flats increased. So that assuming those
19 assumptions were true, the question is what was the
20 reason for the increase in standard mail flats cost
21 from '99 to 2009? And that's the question that hangs
22 over the concern we have about the flat sequencing
23 savings that is presented in proposal for 2010 and
24 '11. Do you have an answer as to why you think the
25 numbers for savings in flat sequencing are going to be

1 more reliable this time than they have been in the
2 past?

3 THE WITNESS: I'd have to consult with my
4 staff and review it in more detail, I don't have that
5 information.

6 CHAIRMAN GOLDWAY: Another question from the
7 Affordable Mail Alliance is, how much does the Postal
8 Service expect to save from the recently announced
9 hiring freeze?

10 THE WITNESS: The savings there are built
11 into our forecast for 2011. We in effect had a hiring
12 freeze at least at headquarters since last summer, so
13 the impact will not be massive comparing '11 to 2010,
14 but those, that's just one of many cost saving
15 initiatives that we've had in place and continue to
16 keep in place as we've struggled through this --

17 CHAIRMAN GOLDWAY: You don't have a number
18 though for what that is?

19 THE WITNESS: A specific number no I don't.

20 CHAIRMAN GOLDWAY: Can you get it for us?

21 THE WITNESS: Sure, we can do an estimate of
22 it, yes.

23 CHAIRMAN GOLDWAY: Could you provide it for
24 us?

25 THE WITNESS: Sure.

1 CHAIRMAN GOLDWAY: Thank you. And then I
2 have one last question, are there other questions?
3 One of the things that has come to my attention when
4 I've spoken to people who are in the private sector is
5 that the \$15 billion borrowing cap is really very low
6 in relationship to the assets of the Postal Service.
7 You do have a cash flow problem but you're sitting on
8 a fully funded pension system of, a maybe overfunded
9 pension system, a healthcare retiree benefit fund
10 which is bigger than most private companies have.

11 THE WITNESS: Yes.

12 CHAIRMAN GOLDWAY: As well as fully paid for
13 assets around the country with very little mortgage
14 payment et cetera et cetera et cetera.

15 THE WITNESS: Yes.

16 CHAIRMAN GOLDWAY: So you've come from the
17 private sector, what is your opinion on whether the
18 borrowing limit that's been established by the
19 Congress is reasonable?

20 THE WITNESS: Obviously with a government
21 entity there is no contributing capital, we don't have
22 the ability to sell shares to the public to raise
23 money as do private companies. Our ability to borrow
24 and the borrowing that we have been provided, the
25 borrowing capacity we have been provided in the past,

1 from my understanding was mostly to see us through
2 short term difficulties, cases where there were
3 declines in volume or something of that nature, and
4 was never intended to form capital base for the Postal
5 Service, as most, as I said, government entities or
6 agencies don't have a capital base that they have to
7 draw upon.

8 The Postal Service is designed and being
9 asked to run much like a private business, private
10 enterprise, where it's able to generate profits and
11 cash flow that cover all of its costs, which is
12 certainly the appropriate thing to do. If you were to
13 consider an increase in the borrowing capacity beyond
14 the \$15 billion, that certainly could help with the
15 short term cash effects, although there's also the \$3
16 billion cap in any one year.

17 But really all that's doing is deferring the
18 problem again out into the future, the underlying big
19 picture problems of the Postal Service and its
20 financial difficulties, and it really is just in some
21 ways promoting deficit spending, as it would be called
22 in government circles. So we don't believe that
23 changing the borrowing limit, increasing the borrowing
24 limit is the best solution to the problems of the
25 Postal Service because all it will do is really push

1 off into the future the issue.

2 Now you do mention that we are for our two
3 pension plans, CSRS and FERS, on a combined basis
4 we've funded about 99 percent of the liabilities, or
5 at least that was the position at the end of 2009.
6 That's certainly a better position than most private
7 companies that are usually in the sort of 90s percent
8 kind of range, and private companies also do not
9 necessarily fund retiree health benefits in terms of
10 setting aside money now to pay them in the future.

11 But again it's a very different environment,
12 and here from what I believe is the reason these
13 things have been funded and the reasons that the
14 funding is being pursued, which is very different from
15 the rest of the U.S. government, is so that in the
16 future the taxpayers of America aren't burdened with
17 these pension and retiree health benefit costs of the
18 Postal Service, of government workers, to avoid
19 creating bigger problems for the Federal government in
20 terms of deficit out into the future. So that's why
21 we're asked to fully fund all of those kind of
22 retirement programs.

23 VICE CHAIRMAN HAMMOND: Madam Chairman,
24 could I follow up just in, just quickly.

25 CHAIRMAN GOLDWAY: Sure, absolutely.

1 VICE CHAIRMAN HAMMOND: So what you're
2 saying is, keeping at the \$15 billion worth of total
3 debt helps force efficiencies on the Postal Service.
4 So if you were given billions more and the authority
5 to go into debt that would relieve burdens for you but
6 just be putting off things that you should actually
7 face right now, is that what you're saying?

8 THE WITNESS: No, I don't think it has
9 anything to do with efficiencies, Commissioner
10 Hammond, but rather the fundamental problems that
11 again we've outlined in our seven-point plan that need
12 to be addressed to improve the Postal Service. We
13 continue and have worked tirelessly in the past to
14 constantly improve the efficiency of our operation.

15 But unfortunately we're burdened with things
16 like this funding of retiree health benefits and the
17 potential overpayment on CSRS pension liabilities from
18 years ago, and our ability to withstand a, shall we
19 say, extraordinary decline in mail volume that
20 occurred over the course of just over a year is very
21 difficult when we have no real capital base or
22 financial cushion if you will to fall back on as that
23 cushion has been stretched to the limit mostly as a
24 result of funding retiree health benefits.

25 VICE CHAIRMAN HAMMOND: So then with regard

1 to this debt maximum that you have, if you get your
2 prefunding relief and if you get some acknowledgment
3 and possible relief from the overpayment that we all
4 agree you have been paying for the old post office
5 employees, the post office department employees, the
6 Siegel report and all that --

7 THE WITNESS: Yes.

8 VICE CHAIRMAN HAMMOND: And I don't want to
9 get back into the long yesterday discussion of how
10 many billions and billions that I think that comes up
11 to and I don't see what extra you would need if you
12 get that relief. But that if you get that, you're not
13 going to be bumping up against your debt limit. I
14 mean you've talked about being insolvent in 13 months,
15 but if you get that you're not going to be insolvent
16 in 13 months, are you?

17 THE WITNESS: If we were to get the benefit
18 of \$4 billion of relief this year, no, we will be able
19 to pay our bills through September of 2011, but we
20 will begin to run out of cash then in Fiscal Year '12.

21 VICE CHAIRMAN HAMMOND: Okay.

22 CHAIRMAN GOLDWAY: But if you got an
23 additional relief in the end of 2011 then you said
24 you'd go to at least 2015.

25 THE WITNESS: Right, exactly. But as I said

1 it doesn't, if we were to get relief on that \$4 or
2 \$5.5 billion a year, so that's five and a half from
3 the losses of, from \$9 billion including interest,
4 we're still losing \$3.5 billion, we're still running a
5 deficit year to year, cash flow negative.

6 VICE CHAIRMAN HAMMOND: \$3.5 billion still
7 negative if you don't have the prefunding burden,
8 that's all you're talking about, just the prefunding
9 burden?

10 THE WITNESS: Yes.

11 VICE CHAIRMAN HAMMOND: If the issue of
12 overpayment into the CSRS by the Postal Service is
13 also taken care of?

14 THE WITNESS: Well but recall that
15 overpayment into the CSRS, that \$55 million, in my
16 happy world is being transferred to the underfunded
17 RHB, and that's what's allowing us to not have to make
18 the \$5.5 billion payment.

19 CHAIRMAN GOLDWAY: I think Commissioner
20 Hammond is saying perhaps the requirement to prefund
21 the healthcare retirement benefit fund, certainly at
22 the rapid rate at which it's required under the
23 current law, could be changed as well.

24 THE WITNESS: Yes it could.

25 CHAIRMAN GOLDWAY: Which could free up more

1 of the money.

2 THE WITNESS: Right, whereas --

3 CHAIRMAN GOLDWAY: My point being that
4 Postal Service is sitting on potentially a lot of cash
5 if it were freed up in the right way.

6 THE WITNESS: \$55 billion is a lot of cash.

7 VICE CHAIRMAN HAMMOND: Yes, yes, and --

8 THE WITNESS: If we were to get some
9 relaxation of the prefunding, yes. Unfortunately
10 we're not, people aren't biting our hand off, should
11 we say, in Congress to make those offers to us because
12 it's a lot of money.

13 VICE CHAIRMAN HAMMOND: But if you get at
14 least some of that if not all of that, and you might,
15 you're still going to lose money?

16 THE WITNESS: Yes.

17 VICE CHAIRMAN HAMMOND: But of course the
18 issue before us is not whether the Postal Service is
19 losing money, we realize the Postal Service is losing
20 money. The issue before us is whether that has caused
21 an exigency, extraordinary circumstances et cetera.
22 So, you know, yes you may be losing money but it's up
23 to us to decide the exigency situation.

24 THE WITNESS: Right.

25 VICE CHAIRMAN HAMMOND: Right.

1 THE WITNESS: But the loss that we've
2 incurred to date and the losses forecasted for the
3 future, even if you remove the funding of retiree
4 health benefits, if, and that's a very big if, we'll
5 still run out of cash. We still will face insolvency,
6 it's just by removing the \$5.5 billion a year we push
7 it out farther into the future. You can't lose \$3.5
8 billion a year and expect to be able to pay your bills
9 going forward.

10 VICE CHAIRMAN HAMMOND: Okay.

11 THE WITNESS: And an expansion of our
12 borrowing capacity would solve that in the short term,
13 but that's just creating deficit spending and pushing
14 out into the future the real problem that should be
15 addressed.

16 CHAIRMAN GOLDWAY: I think the other concern
17 we have is that at least as we understood the
18 provision in the law the exigency was something that
19 was an emergency and that the decision to do it would
20 solve the problem. And what we're hearing is that the
21 problem is not solved in the short run or the long run
22 by a 5 percent rate increase, that there are in
23 addition to this great deal of cash that's sitting
24 around that's a structural issue that should be freed
25 up to be used in other ways, there are some structural

1 problems in terms of products that do not, whose
2 prices do not cover their costs.

3 THE WITNESS: Right.

4 CHAIRMAN GOLDWAY: There are problems that I
5 see in terms of lack of innovation of new products and
6 new strategies. I heard it again from MTAC members
7 yesterday that you're having an innovation meeting
8 now, what about the six months of innovation talks we
9 had last year? And I see the opportunities that I
10 believe were offered to you in the PAEA with regard to
11 the competitive field not being taken advantage of in
12 nearly the way or the capacity that was envisioned or
13 that seems possible given what the success of your
14 competitors at the moment.

15 THE WITNESS: Well a lot of this recent
16 success of Federal Express and UPS is in international
17 markets, that's where they've seen their highest
18 levels of growth.

19 CHAIRMAN GOLDWAY: You have some
20 international contacts as well.

21 THE WITNESS: Yes, but they're actually
22 running businesses in foreign countries, shipping and
23 receiving. You know, we're just, we're part of a
24 network to move mail between countries, but they're
25 initiating and receiving mail. But their growth

1 recently has mostly been the growth of their
2 international operations. Yes we do handle
3 international mail, but not to the extent that Federal
4 Express and UPS does.

5 CHAIRMAN GOLDWAY: Well I think that's an
6 opportunity that needs a great deal more effort.
7 Unfortunately we're not going to solve the Postal
8 Service's problems in this forum, it takes all of the
9 mailers and the operators together to work out the
10 nuts and bolts. We try to provide some leadership and
11 hopefully in this forum have asked some useful
12 questions for you as well as for us in our
13 deliberations, but I think if --

14 COMMISSIONER BLAIR: A couple more.

15 CHAIRMAN GOLDWAY: Okay, we'll keep going.

16 COMMISSIONER BLAIR: Thank you, Madam
17 Chairman.

18 CHAIRMAN GOLDWAY: Commissioner Blair.

19 COMMISSIONER BLAIR: What I thought I heard
20 you say, and correct me if I'm wrong, that should
21 Congress accept the conclusions of the Siegel report
22 and you would have access to that \$55 billion, it
23 would not be used so much for operations as it would
24 be used to offset the \$5.5 billion payment you now
25 make and it would go in -- is that correct, that it

1 would affect your yearly \$5.5 billion payment?

2 THE WITNESS: We haven't necessarily, we
3 haven't explored all of the options to that, but we
4 believe it is unlikely that the Treasury or the Office
5 of Personnel Management is going to send us a check
6 for \$55 billion that we can put into our operating
7 fund.

8 COMMISSIONER BLAIR: But the end game is
9 getting rid of that \$5.5 billion payment?

10 THE WITNESS: Yes.

11 COMMISSIONER BLAIR: Okay.

12 THE WITNESS: We think what's the most
13 likely outcome is if that is identified as
14 overfunding, then under the rules surrounding RHB and
15 CSRS today that overfunding could then be transferred
16 to the RHB, which is under the law today in I believe
17 2015 is the current provision.

18 COMMISSIONER BLAIR: Okay. Had you --

19 THE WITNESS: That would put RHB as it
20 stands today in a fully funded position and there
21 would no longer be a need to do the \$5.5 billion.

22 COMMISSIONER BLAIR: Right.

23 THE WITNESS: But that would also require
24 change to the law, change to PAEA to specifically
25 remove those sections that say, you will pay \$5.5

1 billion --

2 COMMISSIONER BLAIR: That's fine. I wanted
3 to understand what the end game was. But would you
4 say that over the last, since enactment of the PAEA
5 having that burden, has that forced efficiencies on
6 the Postal Service that you otherwise wouldn't have
7 had to engage in?

8 THE WITNESS: No I don't think so, I don't
9 think the burden --

10 COMMISSIONER BLAIR: Has the cap to debt
11 forced efficiencies on the Postal Service?

12 THE WITNESS: I think the Postal Service,
13 and one thing that I have been very impressed with in
14 my short tenure there is the passion with which the
15 people work, and it's obvious that their number one
16 objective is increasing efficiencies while at the same
17 time improving service. So I think that's part of --

18 COMMISSIONER BLAIR: But you don't think the
19 rate making structure or the financial burden has had
20 any impact --

21 THE WITNESS: I'm sure it has --

22 COMMISSIONER BLAIR: I'm sorry. It hasn't
23 been a driver in reducing what the Postal Service has
24 said, what, it reduced \$6.5, \$7 billion last year?

25 THE WITNESS: We've always tried to cover

1 our costs, and certainly adding the \$5.5 billion to
2 the cost is a big challenge to try to cover. And I'm
3 sure that when that was first done and as it evolved
4 since then that that has been a major driver. But
5 it's not as if, we need \$5.5 billion to fund the RHB,
6 is posted on a notice board throughout the plants or
7 anything. It's the overall effort to constantly
8 improve and make the operations more efficient while
9 at the same time maintaining and improving service is
10 the underlying factors that go to it. But it
11 obviously will create pressure to try to cover the
12 whole costs of the Postal Service.

13 CHAIRMAN GOLDWAY: Their \$6.5 or \$7 billion
14 reduction in cost is unprecedented though for the
15 Postal Service.

16 THE WITNESS: Yes.

17 CHAIRMAN GOLDWAY: And I think Commissioner
18 Blair is saying that the pressures of having to pay
19 into the RHB --

20 THE WITNESS: Yes.

21 CHAIRMAN GOLDWAY: Was certainly a driver.

22 THE WITNESS: That does enter into it, yes.
23 But as I said, even before that was put into place the
24 Postal Service was seeking to achieve efficiencies and
25 has set goals of \$1 billion a year of efficiencies.

1 CHAIRMAN GOLDWAY: Yes, I mean it did pay
2 off all their debts in early 2000, and --

3 COMMISSIONER BLAIR: And that was due to the
4 fact that their CSRS obligations were reduced
5 accordingly.

6 CHAIRMAN GOLDWAY: Well and they did seem to
7 be having surpluses for several years --

8 THE WITNESS: Right.

9 CHAIRMAN GOLDWAY: Which then got put into
10 an escrow. So I think they thought in the enactment
11 of PAEA that they would have to, they could make \$3
12 billion fairly easily and the two extra billion would
13 be a stretch but they could do it at the time.

14 COMMISSIONER BLAIR: I think it's, at the
15 time I think --

16 CHAIRMAN GOLDWAY: And I think the volume
17 decline could have made that --

18 THE WITNESS: That has significantly hurt
19 us.

20 COMMISSIONER BLAIR: But what I was trying
21 to get to --

22 CHAIRMAN GOLDWAY: Much more difficult, but
23 there are these structural problems as well.

24 COMMISSIONER BLAIR: The cap was intended to
25 drive those efficiencies.

1 THE WITNESS: Yes. And all of those factors

2 --

3 COMMISSIONER BLAIR: And while this isn't a
4 question for you, it's just that between your
5 testimony today and Mr. Corbett's, I'm troubled by
6 what I'm inferring from this is that the value of the
7 cap system isn't appreciated by the Postal Service and
8 that we're going to be back in proceedings like this
9 and that even though an exigent rate increase may go
10 into effect, the exigency was claimed in 2008 and 2009
11 but it's being used to fund cash flow problems in 2011
12 and that we're going, we're bouncing back and forth on
13 a path that doesn't seem to provide a long term
14 solution to the Postal Service's fundamental problems,
15 and I'm concerned that this may add to the problem
16 rather than subtract from it.

17 THE WITNESS: The fundamental problem I
18 think in part stems from the volume decline that, we
19 will never get back to the volume levels that we saw a
20 few years ago, you know, 200 billion pieces of mail on
21 an equal basis, because the way that people
22 communicate has changed so significantly. But certain
23 changes were made to the business model, you know, in
24 2005 2006 time frame when we were at our peak, if you
25 will, and unfortunately the belief then was that

1 volume would stay high and volume would continue to
2 increase. But that's proven to be a bad assumption,
3 and hence is the reason that we need to reconsider the
4 overall business model. And, you know, that's the
5 reason, the underlying basis for the seven-point,
6 pronged plan that we've rolled out.

7 COMMISSIONER BLAIR: Well you've been quite
8 patient and willing in your willingness to answer our
9 questions, and sometimes repetitively in asking
10 different ways.

11 THE WITNESS: Right.

12 COMMISSIONER BLAIR: It's much appreciated.

13 THE WITNESS: I hope I also haven't answered
14 with the same, 13 months away the terrible things et
15 cetera, but that's what worries me the most is our
16 ability to have enough cash to satisfy our obligations
17 in September of next year.

18 COMMISSIONER BLAIR: Thank you.

19 CHAIRMAN GOLDWAY: Thank you. Commissioner
20 Langley, if you have another question?

21 COMMISSIONER LANGLEY: Thank you, and I also
22 appreciate as I said your straightforward responses.
23 I think it's important for the Postal Service to have
24 individuals such as yourself who can bring commercial
25 experience to the government. I have two questions on

1 the impact of electronic diversion, which in my mind
2 would divert the flow of this particular discussion.
3 So if possible I would like to have them answered in
4 the information request. I think it would be valuable
5 to have the information, but I don't want to take away
6 from the discussion at hand.

7 THE WITNESS: Okay.

8 CHAIRMAN GOLDWAY: I've indicated that we'll
9 be submitted additional POIRs so just, you know, give
10 us the questions and we'll.

11 COMMISSIONER LANGLEY: Oh, thank you. Thank
12 you again for your testimony and responses.

13 CHAIRMAN GOLDWAY: Okay, one more question
14 from Commissioner Acton?

15 COMMISSIONER ACTON: One question, Mr.
16 Masse. Thank you, Madam Chairman. You referenced a
17 moment ago and you've spoken a couple of times here
18 about the 13-month threshold.

19 THE WITNESS: Right.

20 COMMISSIONER ACTON: Has the Postal Service
21 management modeled responses to what they'll do if
22 that scenario develops?

23 THE WITNESS: If the scenario develops?

24 COMMISSIONER ACTON: Yes.

25 THE WITNESS: The discussion has been what

1 payments would we not make, and as we did this time a
2 year ago we had discussions both in Congress and the
3 Administration of, if we don't have the money to make
4 the retiree health benefit's \$5.5 billion payment, we
5 can't pay it, we can't pay something that we don't
6 physically have the money for. And so far the
7 responses that we've had from both Congress and the
8 Administration are positive, they understand the
9 position and the situation, they have mentioned that,
10 well this is unprecedented that an agency hasn't paid
11 another agency as required by law, but they certainly
12 understand the situation.

13 COMMISSIONER ACTON: Thank you, Mr. Masse.

14 THE WITNESS: Okay.

15 CHAIRMAN GOLDWAY: Well, as I was saying I
16 think we've raised a lot of questions and you've been
17 very helpful and I think we've had a constructive
18 discussion about the issues that the Postal Service
19 faces. The answers are not clear to us yet but we
20 appreciate that we've had the opportunity to talk to
21 you and we thank you for participating. And we will
22 take the information you've given to us under
23 advisement and review the written information that
24 we've requested from you. And we'll proceed tomorrow
25 with hearing from some of your colleagues. So with

1 that I will adjourn this meeting and excuse you, and
2 thank you for your participation here today.

3 THE WITNESS: Thank you, my pleasure. I
4 hope it helps.

5 CHAIRMAN GOLDWAY: I'll see many of you here
6 tomorrow morning at 9:30. Thank you.

7 (Whereupon, the hearing in the above-
8 entitled matter was adjourned, to reconvene at 9:30
9 a.m. on Thursday, August 12, 2010.)

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REPORTER'S CERTIFICATE

DOCKET NO.: R 2010-4
CASE TITLE: Rate Adjustment Due to Extraordinary or
Exceptional Circumstances
HEARING DATE: 8/11/10
LOCATION: WDC

I hereby certify that the proceedings and evidence are contained fully and accurately on the tapes and notes or digital recording reported by me at the hearing in the above case before Postal Regulatory Commission

Date: 8/11/10



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