Postal Regulatory Commission
Submitted 8/18/2010 4:23:33 PM
Filing ID: 69805
Accepted 8/18/2010

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

RATE ADJUSTMENT DUE TO EXTRAORDINARY OR EXCEPTIONAL CIRCUMSTANCES

Docket No. R2010-4

RESPONSES OF THE UNITED STATES POSTAL SERVICE TO QUESTIONS FROM THE BENCH AT THE HEARING FOR MR. MASSE (August 18, 2010)

The United States Postal Service hereby provides its response to the oral question posed from the bench at the August 11 hearing on the statement of Mr. Masse. The relevant portion of the transcript is quoted, and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorney:

Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260–1137
(202) 268-2992, FAX: -5402
August 18, 2010

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

TR. 2/174, 227-28. A discussion on page 174 of FSS led to the following statement by Mr. Masse: “We’ve included the benefits, if you will, of FSS in our forecast for 2011…. The exact figure I don’t have….But it’s part of the $1 billion of savings.” Chairman Goldway asked: “But you can’t tell me how much of that $1 billion?” Later, on pages 227-28, Mr. Masse indicated that he would have to consult with staff regarding the FSS savings in 2010 and 2011.

RESPONSE:

As counsel noted at the hearing, a response to a question at the Technical Conference (July 27, 2010) was filed August 3, 2010, attached to which was an Excel file (3rd.TC.Cost.Redctn.Attach.xls) that included the cost savings incorporated into the FY2011 financial projections in this case. Regarding FSS, for FY2010, the net savings are $43 million, which is the net of cells AT26 and AT27 in the FY2010 Cost Reduction tab and the FY2010 Other Programs tab. For FY2011, the net savings are $242 million, which is the net of cells AT24 and AT27 in the FY2011 Cost Reduction tab and the FY2011 Other Programs tab.

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

TR. 2/215. Could you, just for the record, provide us -- assuming that the Congress does provide relief for the 5.5 billion in a similar fashion that they did in 2009, or this ideal program, could you give us cash flows for 2010 and ‘11, perhaps even ‘12, to show us what the effect would be of the 4 billion, 5 billion, and with or without a rate increase?

RESPONSE:

Attached to this response electronically is an Excel file (Tr.2.215.Cash.Flow.xls) providing the cash balances at the end of 2010, 2011, and 2012 if we had a $4B RHB pre-payment deferral in each year. Please note that for 2011 and 2012, we are estimating the cash balances for two scenarios: 1) With no exigent price increase and 2) With exigent price increase.

Under the assumptions stated as notes in the spreadsheet, the results can be summarized as follows.

$4B Pre-payment deferral in Sept 2010:
According to the projections filed with the Request, we expect to have a cash balance of $1.3B on Sep 30, 2010. If we got the $4B RHB pre-payment deferral in Sept 2010, we would end FY 2010 with a cash balance of $5.3 B. The 2010 $4B RHB deferral, however, would not be enough to alleviate our liquidity problems. In 2011 we would have a cash shortfall of $(400M) if we do not have an exigent price increase. We would have $1.8B left in cash if we do. In 2012 we estimate significant cash shortfalls under both scenarios.

$4B Pre-payment deferral in Sept 2011:
With an additional $4B RHB pre-funding deferral in Sep 2011, we would have sufficient cash during 2011 under both scenarios. However, we would struggle in 2012. In the scenario with no price increase, we would have a cash shortfall of $(4.8B) in 2012. If we got the exigent price increase, we would end 2012 with a cash balance of only $600M

$4B Pre-payment deferral in Sept 2012:
An additional $4B RHB pre-payment deferral at the end of 2012 would help us end 2012 with about $4.6B in cash, if we got approval for the exigent price increase. If we did not get approval, we would be short in cash by almost $(1B).

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

TR. 2/222. You note that during Fiscal Year 2008 there was a reduction of 21,500 career employees in response to significant mail volume losses, of that 21,500 how many career employees left because of VERA and how many left because of attrition? Can you provide them for us? …And for 2009 as well?

RESPONSE:

The 21,500 figure cited is the *net* reduction in career employees, which is the result of total separations offset by new hires. The requested breakout of separation data is provided below.

	FY 2008	FY 2009	FY 2010 YTD** 8/11/2010
Retired VERA	197	13,290	4,588
Retired Other	22,984	22,166	27,487
Other Separation	10,698	7,010	10,342
Total Separations	33,879	42,466	42,417

** The FY 2010 YTD includes 19,828 who took the Early Out Incentive as of 12/31/2009, which include Retirements & Resignations. (Another 1,048 recipients of the Early Out Incentive are reflected in the FY 2009 separations.) Some who took the Early Out Incentive could be reflected in the Retired VERA row, some could be reflected in the Retired Other row (if, for example, they were already eligible to retire and thus did not need to use the VERA option), and some could be reflected in the Other Separations row. In other words, while there is overlap between the VERA and the Early Out Incentive, the two are distinct.

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

TR. 2/224. How much of the fixed cost in the delivery network are labor costs versus non-labor costs? Well for the benefit of the record then could you give us your understanding of what the fixed costs are in the delivery network? And non-fixed, and how much are non-labor -- how much in the fixed cost are labor and how much are non-labor, and how much savings there was in the restructuring of the city delivery routes, how much you're expecting to have additional savings in restructuring there. And to what extent you can separate out within that restructuring route process what was labor and what was non-labor.

RESPONSE:

Nature of Delivery Costs

The "fixity" of the delivery network being discussed here is captured by the institutional costs of carrier delivery. These are the delivery costs that do not vary at the margin as volume changes, and they include both labor and non-labor costs. The institutional cost of delivery can be estimated by identifying the institutional components all of the cost components in the CRA model that contain carrier delivery-related costs. These components include not only the direct labor costs of carrier delivery, but also the indirect costs such as supervision, vehicle, and fuel costs.

While this calculation can provide guidance about the overall size of carrier delivery institutional costs, however, it should only be viewed as an estimate, not a final number. That is because the methodology for finding carrier-related institutional costs in the indirect components has not been reviewed or finalized. For purposes of responding to this question, the Postal Service's "piggyback" model has been extended to institutional cost to provide the estimate of total institutional costs, but the logical and economic basis for "institutional cost piggybacks" has not been developed and reviewed. With this caveat in mind, the following table provides an estimate of the overall institutional cost in the carrier delivery network.

FY2009 Carrier Delivery Costs

	City Carriers	Rural Carriers	Total
Attributable Cost	$10,760,675	$2,990,740	$13,751,415
Institutional Cost	$10,610,191	$4,872,352	$15,482,543

(Thousands of dollars)

The basic approach to estimating the portion of carrier delivery institutional cost made up of non-labor costs starts by reviewing all of the cost components associated with city and rural carriers, and then identifying those components that are non-labor expenses. A list of the non-labor components is provided below. The following table presents the breakout of labor and non-labor costs for both attributable costs and institutional costs.

FY2009 Carrier Delivery Labor and Non-labor Costs

City Carrier

	Attributable Cost	Proportion	Institutional Cost	Proportion
Labor	$ 10,147,038	94.3%	$ 9,844,928	92.8%
Non-Labor	$ 613,637	5.7%	$ 765,263	7.2%
Total	$ 10,760,675	100.0%	$ 10,610,191	100.0%

(Thousands of dollars)

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

Rural Carrier

	Attributable Cost	Proportion	Institutional Cost	Proportion
Labor	$ 2,805,482	93.8%	$ 4,174,120	85.7%
Non-Labor	$ 185,258	6.2%	$ 698,232	14.3%
Total	$ 2,990,740	100.0%	$ 4,872,352	100.0%

(Thousands of dollars)

City Carrier Non-Labor Components

Description	**Component No.**	**Subsegment**
Contract Cleaners	81	11.1.2
MVS Sup & Mat City Delivery Activity	92	12.2.1.1
MVS Sup & Mat City Delivery Network Travel	95	12.2.1.2
MVS Sup & Mat City Delivery Special Purpose Routes	549	12.2.1.3
MVS Vehicle Hire City Delivery Office	100	12.3.1.1
MVS Vehicle Hire City Delivery Activity	101	12.3.1.2
MVS Vehicle Hire City Delivery Network Travel	104	12.3.1.3
Carfare City Delivery Office	127	13.2.1.1.1
Carfare City Delivery Activity	128	13.2.1.1.2
Carfare City Delivery Office	127	13.2.1.1.1
Carfare City Delivery Activity	128	13.2.1.1.2
Carfare City Delivery Network Travel	131	13.2.1.1.3
Driveout City Delivery Office	136	13.2.2.1
Driveout City Delivery Activity	137	13.2.2.2
Driveout City Delivery Network Travel	140	13.2.2.3
Rents	165	15.1.1
Fuel	166	15.2.1
Utilities	167	15.2.2
Custodial and Building	176	16.3.1
Miscellaneous Postal Supplies & Services	177	16.3.4.6
Equipment	184	16.3.2
Equipment Depreciation	232	20.1
Veh Depr. City Delivery Delivery Activities	222	20.2.1.1
Veh Depr. City Delivery Network Travel	225	20.2.1.2
Depreciation - Building	236	20.3.1
Depreciation - Leasehold	237	20.3.2
Interest Land / Building Veh & Equip	587	20.5.1

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

Rural Carrier Non-Labor Components

Description	**Component No.**	**Subsegment**
Contract Cleaners	81	11.1.2
MVS Sup & Mat City Rural Delivery	556	12.2.3
Rents	165	15.1.1
Fuel	166	15.2.1
Utilities	167	15.2.2
Custodial and Building	176	16.3.1
Miscellaneous Postal Supplies & Services	177	16.3.4.6
Equipment Maintenance Allowance	73	10.3
Equipment	184	16.3.2
Equipment Depreciation	232	20.1
Vehicle Depreciation - Rural Delivery	582	20.2.3
Depreciation - Building	236	20.3.1
Depreciation - Leasehold	237	20.3.2
Interest Land / Building Veh & Equip	587	20.5.1

Restructuring

During the first two Memorandum Of Understanding's (MOU's), the Postal Service has shown a net reduction in city delivery routes of over 11,000, or a base hour reduction of the equivalent of 12,473 routes, saving over $1.24 Billion in the City Delivery operation in just over a year and a half. The new Joint Alternate Route Adjustment Process (JARAP) MOU is a continuation of the previous two MOU's. As of this date, there has been a reduction of just over 1,100 city delivery routes due to JARAP. We are still in the middle of the current process.

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

TR. 2/228. [F]or the record….could you simply indicate what the cost savings are for the flat strategy that have been included in 2010 and 2011?

RESPONSE:

As indicated in the previous response in this set to the question posed at Tr. 2/174, 227-28, the FSS net costs savings are $43 million in FY10 and $242 in FY11. Two other initiatives relating to flats also show savings in the Excel file (3rd.TC.Cost.Redctn.Attach.xls) submitted on August 3, 2010 in response to the technical conference inquiry. Those savings and other costs can be found in the AT column of rows 23 and 25 in the FY2010 and FY2011 Cost Reduction tabs and the FY2010 and the FY2011 Other Programs tabs. For FY2010, the net savings from these two rows are approximately $10 million, and for FY2011, the net savings are approximately $2.5 million. In total therefore, across all five rows (23-27), including FSS, the FY2010 net savings are approximately $53 million, and the FY2011 net savings are approximately $244 million.

Those figures are specifically included in our financial projections in this case. Further, there are $1.7 billion (net of the trend adjustment) and $0.5 billion in “Breakthrough Productivity” cost reductions for 2010 and 2011. These figures are targets for cost reductions that are not specifically included in the initiatives that <u>are</u> specifically identified in the cost projection workpapers. Any concepts in the Flats Strategy document (or other cost reduction efforts, for that matter) that are not explicitly identified in the financial projections can be considered part of this “Breakthrough Productivity”.

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

TR. 2/229. One of the questions that was asked by the Periodical and Catalog Mailers was they wanted you to know that during the period during 1999 and 2009 the unit cost of mail processing and delivery for standard mail flats almost doubled while the consumer price index for the same period increased 29 percent. (Another question asked why unit costs of Periodicals increased by more than double the rate of inflation between FY1996 and FY2009 despite deployment of AFSM 100s and increased worksharing.)

Do you have an answer as to why you think the numbers for savings in flat sequencing are going to be more reliable this time than they have been in the past…(e.g., AFSM 100)?

RESPONSE:

In comparing 2009 costs to 1999, it is important to recognize that even though all the costs are based on Commission methodology, there have been changes in methodology and mail characteristics over time that affect the costs. Obviously, a more thorough analysis could illuminate possible reasons for the changes is the measured costs, and the responses to Questions 9 and 10 of POIR No. 5 (due on August 25, 2010) may provide an opportunity for further analysis. For instance, the extraordinary volume declines experienced between FY 2007 and FY 2009 affected unit costs, and a disproportionate share of the increase occurred during this period. During FY 2007 to FY 2009, total mail volume declined about 17 percent. There was an even larger decline in total flats volume of nearly 23 percent; and the decline in non-carrier route presort flats volume was 33 percent. This led to excess capacity in delivery costs and in plant and equipment costs, as indicated in the Summer Sale 2009 filing. Going forward, as excess capacity is eliminated, there should be some offsetting reductions.

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

Looking at the period FY1999 to FY2007 allows us to consider cost trends in the absence of large and sudden volume shifts. Mail processing unit costs over that period rose 45.3 percent, going from 12.79 cents in FY 1999 to 18.58 cents in FY 2007. Within this change, though, clerk and mail handler labor costs for Standard Flats have risen at less than the growth in cost per workhour, 34.2 percent vs. 38.2 percent respectively. However, the indirect costs – particularly for equipment depreciation, maintenance and supplies have risen much faster, rising 67.5 percent on a unit cost basis. Delivery unit costs grew faster than wages. In the case of the rise in carrier street time, which has grown faster than the rise in the cost per workhour, one factor is that the street variability changed from approximately 29 percent to 37 percent with the adoption of the 2002 City Carrier Street Time Study (adopted as part Docket No. R2005-1).

In any event, there are many factors that affect the cost measurements, and it is not necessarily possible to pinpoint the exact causes of changes over time. Nevertheless, it is important to understand the changes in costs. Obviously, as discussed above, the swift volume reduction plays a role in the unit cost change. To the extent there are further explanations to offer, they will be discussed in the response to POIR No. 5, Questions 9 and 10.

Regarding flat sequencing, the Postal Service is determined to make the most of the new FSS technology in the face of unprecedented changes in volume.

RESPONSE OF THE UNITED STATES POSTAL SERVICE TO ORAL REQUEST AT THE HEARING ON AUGUST 11, 2010

TR. 2/230. How much does the Postal Service expect to save from the recently announced hiring freeze?

RESPONSE:

In 2011, we expect 4,500 of the non-bargaining employees affected by the freeze to attrite. This would result in maximum "annualized" savings of $470M. Assuming attrition occurs evenly throughout the year, we expect 2011 savings of roughly $230M. It is not possible, however, to determine specifically how much of this savings is exclusively attributable to the most recent freeze, as opposed to previous similar actions, which would already have covered many of the same employees, as Mr. Masse suggested at this page of the transcript.

.

CERTIFICATE OF SERVICE

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

Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260–1137
(202) 268-2992, FAX: -5402
August 18, 2010