Postal Regulatory Commission
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POSTAL REGULATORY COMMISSION

Annual Report to the President and Congress

FISCAL YEAR 2016

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COVER PHOTO BY M DOGAN

Acronyms

ACD	*Annual Compliance Determination*
ACR	*Annual Compliance Report*
C.F.R.	Code of Federal Regulations
CAG	Cost Ascertainment Group
CPI	consumer price index
DSCF	destination sectional center facility
FSS	Flats Sequencing System
FY	Fiscal Year
GEPS	Global Expedited Package Service
IMb	Intelligent Mail barcode
IBRS	International Business Reply Service
IOCS	In-Office Cost System
NPR	non-published rates
MCS	*Mail Classification Schedule*
NOI	Notice of Inquiry
NSA	negotiated service agreement
PAEA	Postal Accountability and Enhancement Act
RHBF	Postal Service Retirement Health Benefits Fund
RRM	Return Receipt for Merchandise
RTM	Round-Trip Mailer
TACS	Time and Attendance Collection System
U.S.C.	United States Code
UPU	Universal Postal Union
USO	Universal Service Obligation

PRC | Mission, Vision, and Guiding Principles

PHOTO BY SEAN PAVONE

Mission Statement

Ensure transparency and accountability of the United States Postal Service and foster a vital and efficient universal mail system.

Vision Statement

To be an independent regulator respected for effectively engaging postal stakeholders to promote a robust universal mail system through objective, accurate, and timely regulatory analyses and decisions.

We will look to achieve our vision by:

- Taking a multi-disciplinary and integrated approach to work
- Monitoring the environment and anticipating changes to enhance agility
- Utilizing rigorous evaluative methods
- Optimizing stakeholder engagement through an appropriate and clearly-defined public involvement process
- Developing staff expertise to ensure that the Commission is a center for excellence in postal regulatory matters
- Ensuring that the Commission is an employer of choice
- Ensuring efficient stewardship of resources

Guiding Principles

The Commission is committed to and operates by the principles of:

Openness

- Public participation

Integrity

- Fairness and impartiality
- Timely and rigorous analysis

Merit

- Commitment to excellence
- Collegiality and multi-disciplinary approaches

Adaptability

- Proactive response to the rapidly changing postal environment

Potomac River with Lincoln Memorial, Washington Monument, and Arlington Memorial Bridge.

Interior of the Library of Congress in Washington, DC.

PHOTO BY KAMIRA

Chairman's Letter

JANUARY 2017

On behalf of the Postal Regulatory Commission, I am pleased to present our *Annual Report to the President and Congress.* This report details the key activities over the past year in the Commission's area of regulatory oversight and includes information required under the Postal Accountability and Enhancement Act of 2006 (PAEA) on the operations of the Commission, including the extent to which regulations are achieving the objectives outlined in the PAEA.

As mandated by the statute, the Commission also recently issued a report discussing how well the PAEA is operating and making recommendations for legislation or other measures necessary to improve the effectiveness and efficiency of the Nation's postal laws. The Commission's report stressed the need to address the volatile financial condition of the Postal Service.

In the coming year, the Commission will focus a significant portion of its resources and expertise to conducting a comprehensive evaluation of the current system for regulating rates and classes for Market Dominant products. The PAEA mandates this important review and requires the Commission to determine whether the law's objectives are being achieved. If the Commission finds that the objectives are not being met, it has the authority to either propose rules that modify the system or adopt an alternative system to achieve the objectives.

Recognizing the effect the outcome of the review may have on the Postal Service's stressed financial condition, the Commission has set an aggressive agenda to complete its review in the most efficient and effective manner possible without compromising the integrity of the process or the outcome. The Commission will work diligently to complete this duty in conjunction with its other responsibilities of reviewing and approving Postal Service rates, adjudicating formal and informal complaints, examining proposals for new products and services, and ensuring the Postal Service complies with Title 39.

During my time as agency head, the Commission has become even more efficient and effective in carrying out its mission as measured by budget savings and timeliness of work. The Commission has achieved improvements in its employees' satisfaction and engagement, as evidenced by the Federal Employee Viewpoint Survey results. The Commission has become a more frequently sought resource for postal expertise, particularly to the Congress. I hope to build upon these accomplishments to achieve further improvements in staff achievement, the timeliness and quality of work products, and the efficiency and effectiveness of agency operations.

On behalf of my fellow Commissioners and the entire hard working agency staff, I extend a welcome to the new Congress and Administration. I look forward to a productive dialogue on how to ensure the integrity of a universal mail system for years to come.

With best wishes, I am

Sincerely yours,

Robert G. Taub
CHAIRMAN

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CHAPTER I | Fiscal Year 2016 in Review

PHOTOS BY ORHAN CAM

The Postal Regulatory Commission (Commission) achieved the following significant accomplishments in Fiscal Year (FY) 2016 that support its mission to ensure transparency and accountability of Postal Service operations and foster a vital and efficient universal mail system.

Top left: US Capitol Building
Top right: Thomas Jefferson Memorial

1. The Commission published four major reports in FY 2016:
   - The *Annual Report to the President and Congress* (*Annual Report*) described the Commission's accomplishments and activities as the regulator of the U.S. Postal Service.
   - The *Annual Compliance Determination* (ACD) reviewed the Postal Service's compliance with pricing and service standards.
   - The *Analysis of Postal Service Financial Results and 10-K Statement for Fiscal Year 2015* provided an in-depth analysis of the Postal Service's financial condition.
   - The *Review of Postal Service FY 2015 Performance Report and FY 2016 Performance Plan* evaluated whether the Postal Service met its performance goals as required under 39 U.S.C., § 3653(d).
   - In early FY 2017, the Commission also issued the *Section 701 Report Analysis of the Postal Accountability and Enhancement Act of 2006*, recommending to the President and Congress legislation and other ways to improve the effectiveness and efficiency of the United States postal laws.

2. The Commission presided over several rate and classification cases in FY 2016. It:
   - Reviewed and approved two proposals to adjust Market Dominant prices.
     - Approved five temporary promotional discount proposals related to First-Class Mail and Standard Mail.
     - Approved six First-Class Mail and Standard Mail promotional discount proposals to be offered during calendar year 2017, and increased prices to correct an anomaly within First-Class Mail Parcels.
   - Approved the Postal Service's planned removal of the exigent surcharge.
   - Announced a standard for determining whether a mail preparation change has rate effects that impact the price cap. A Postal Service petition for reconsideration and clarification of the application of the standard is currently pending before the U. S. Court of Appeals for the District of Columbia Circuit.
   - Reviewed and approved the Global eCommerce Marketplace (GeM) market test and the extension of the Customized Delivery market test.
   - Approved a Postal Service request to remove Global Direct Contracts from the Competitive product list.

3. The Commission issued several orders approving classification changes. It:
   - Approved material Mail Classification Schedule (MCS) changes related to Priority Mail International Flat Rate Envelopes and Small Flat Rate Boxes.
   - Issued two orders approving minor classification changes to the Country Price Lists for International Mail in Part D of the MCS.

4. The Commission considered issues related to service performance measurement and reporting in two key dockets. The Commission:
   - Hosted two off-the-record technical conferences to discuss the Postal Service's statistical design plan for internal service performance measurement. This case remains open pending the Postal Service's filing of more information.
   - Issued a final order enhancing the reporting requirement of service performance measurement data that requires the Postal Service to regularly provide descriptions of current methodologies used to verify accuracy, reliability, and representativeness of data for each measurement system.

5. The Commission conducted several rulemakings related to rate and costing issues.
   - Currently pending before the Commission are proposed rules for regulating mail preparation changes that affect the price cap.
   - The Commission also considered 16 petitions proposing to change various accepted analytical principles. Proposals were submitted by the United Parcel Service (UPS), the Postal Service, and other interested parties.

6. The Commission considered several postal rate adjustment and MCS requests by the Postal Service for domestic and international Competitive products.

7. The Commission approved 281 Negotiated Service Agreements (NSAs) for Competitive products (186 domestic, 95 international).

8. The Commission reviewed and approved the Postal Service's calculation of FY 2015 assumed Federal income tax on Competitive products.

9. Several public inquiry dockets were initiated by the Commission to solicit comments on the development of the Section 701 Report, Scope of Public Service or Activity Cost Reporting, Commission Jurisdiction Over Post Office Closings and Consolidations, and Service Performance.

10. The Commission finalized three rulemakings that updated its rules of practice and procedures. The Commission:
    - Revised and reorganized rules concerning ex parte communications
    - Considered amendments to publishing rules concerning the Market Dominant and Competitive product lists
    - Reviewed and adopted rules proposing to replace existing regulations governing product lists and the MCS

11. In other proceedings, the Commission:
    - Adjudicated two post office closing appeals.
    - Reviewed and dismissed a complaint alleging violations of postal regulations and policies by the Postal Service.
    - Issued an order that resolved issues on remand related to the Exigent price adjustment.
    - Denied a Postal Service request to add Round-Trip Mailer to the Competitive product list.
    - Dismissed a complaint by the American Postal Workers Union (APWU) alleging that the Postal Service failed to adhere to the service standards established as a result of the Mail Processing Network Rationalization initiative. APWU filed a petition for review before the U.S. Court of Appeals for the District of Columbia (D.C. Circuit) which was recently denied.
    - Dismissed a complaint concerning the sale and closure of the Atlantic Street Station post office in Stamford, Connecticut.
    - Issued an order resolving issues on remand concerning a Postal Service request to remove Return Receipt for Merchandise Service from the list of Special Services in the MCS.

12. With respect to international postal policy responsibilities, the Commission:
    - Continued its active role in the Universal Postal Union (UPU) Letters and Parcels Remuneration Groups on international letter mail and parcel delivery rates by chairing the UPU Regulatory Issues Project Group on behalf of the U.S. government
    - Continued collaboration on international postal issues with other government agencies such as the Department of State through its Federal Advisory Committee on International Postal and Delivery Services
    - Adopted final rules describing general procedures related to the Commission's views on proposals submitted for consideration at UPU Congresses that could affect a Market Dominant rate or classification
    - Provided views to the Secretary of State on whether certain proposals for the 26th Congress of the UPU are consistent with the standards and criteria for modern rate regulation established by the Commission under 39 U.S.C. § 3622

13. Other activities performed by the Commission include:
    - Testimony before the U.S. Senate Committee on Homeland Security and Governmental Affairs and the U.S. House Oversight and Government Reform Committee
    - The development of the Commission's five-year *Strategic Plan* for fiscal years 2017-2022
    - The processing of more than 5,500 inquiries, questions, suggestions, and comments from the general public which primarily involved undelivered, delayed, misdelivered, and missing mail
    - Further website enhancements addressing navigation and 508 compliance

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CHAPTER II | About the Commission

PHOTO BY PRC STAFFER MAX SCHNIDMAN

Pictured left to right: Commissioner Mark Acton, Chairman Robert Taub, Vice Chairman Nanci Langley, Commissioner Tony Hammond

The Commission is an independent agency that has exercised regulatory oversight over the Postal Service since its creation by the Postal Reorganization Act of 1970, with expanded responsibilities under the Postal Accountability and Enhancement Act of 2006. The Commission is composed of five commissioners, each of whom is appointed by the President, by and with the advice and consent of the Senate, for a term of six years. A commissioner may continue to serve after the expiration of his or her term until a successor is confirmed, except that a commissioner may not continue to serve for more than 1 year after the date on which his or her term would have otherwise expired. Not more than 3 of the commissioners may be adherents of the same political party.

Commission Leadership

Robert G. Taub | CHAIRMAN

Mr. Taub was designated Chairman upon his reappointment as a commissioner on December 12, 2016, for a second term, following his nomination by President Barack Obama and confirmation by the United States Senate. At the time of his designation and reappointment, he had been serving as acting chairman since December 4, 2014. He was originally sworn in as a commissioner in October 2011 following his nomination and Senate confirmation. The Commission elected him vice chairman for the calendar year 2013. His more than 30 years of previous public service include special assistant to Secretary of the Army John McHugh; chief of staff to U.S. Representative John McHugh (R-NY); 12 years in senior positions on the House of Representative's Committee on Oversight and Government Reform, including staff director of its former Postal Service Subcommittee; senior policy analyst with the U.S. Government Accountability Office; and staff member for three members of Congress, a member of the British Parliament, and state and county officials in upstate New York. He was awarded the Army's Decoration for Distinguished Civilian Service, and is a Fellow of the National Academy of Public Administration.

Nanci E. Langley | VICE CHAIRMAN

Ms. Langley was reappointed as a commissioner on December 10, 2014. Her term expires November 22, 2018. She was first appointed as a commissioner on June 6, 2008; that term expired on November 22, 2013. She also served as the Commission's vice chairman from October 2008 to October 2009, January to December 2012, and January to December 2016. Her previous positions include director of the Office of Public Affairs and Government Relations at the Commission; 17 years as a senior adviser to Senator Daniel K. Akaka (D-HI), including 9 years as a deputy staff director on the U.S. Senate Committee on Homeland Security and Governmental Affairs Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia; and communications director to former U.S. Senator Spark M. Matsunaga (D-HI). She was elected as a fellow of the National Academy of Public Administration in 2009.

Mark Acton | COMMISSIONER

Mr. Acton was appointed as a commissioner on August 3, 2006; his term expired on October 14, 2016. He served as Commission vice chairman from 2007 to 2008, 2011 to 2012, and 2014 to 2015, and as special assistant to former Postal Rate Commission Chairman George Omas. His other positions have included staff director of the Republican National Committee Counsel's Office; deputy to the chairman of the 2004 Republican National Convention; special assistant to the Republican National Committee chief counsel and Counsel's Office government relations officer and redistricting coordinator; executive director, Republican National Convention, Committee on Permanent Organization, and deputy executive director, Committee on Rules; and executive director of the Republican National Committee Redistricting Task Force.

Tony Hammond | COMMISSIONER

Mr. Hammond was reappointed as a commissioner on December 10, 2014, and has been elected to three separate terms as vice chairman during his tenure. His term expires October 14, 2018. Commissioner Hammond served on the Postal Regulatory Commission and its predecessor agency, the Postal Rate Commission, from 2002 to 2011, as an appointee of President George W. Bush, and was reappointed by President Barack Obama for an additional term from 2012 to 2013. Before joining the Commission, Mr. Hammond was the owner and managing member of T. Hammond Company, LLC; senior consultant to Forbes 2000, Incorporated; senior vice president of FL&S, a direct marketing firm; director of campaign operations for the Republican National Committee; executive director and finance director of the Missouri Republican Party; and served 10 years on the staff of former U.S. Representative Gene Taylor (R-MO).

Staff and Office Structure

Commission staff has expertise in law, economics, finance, statistics, and cost accounting.

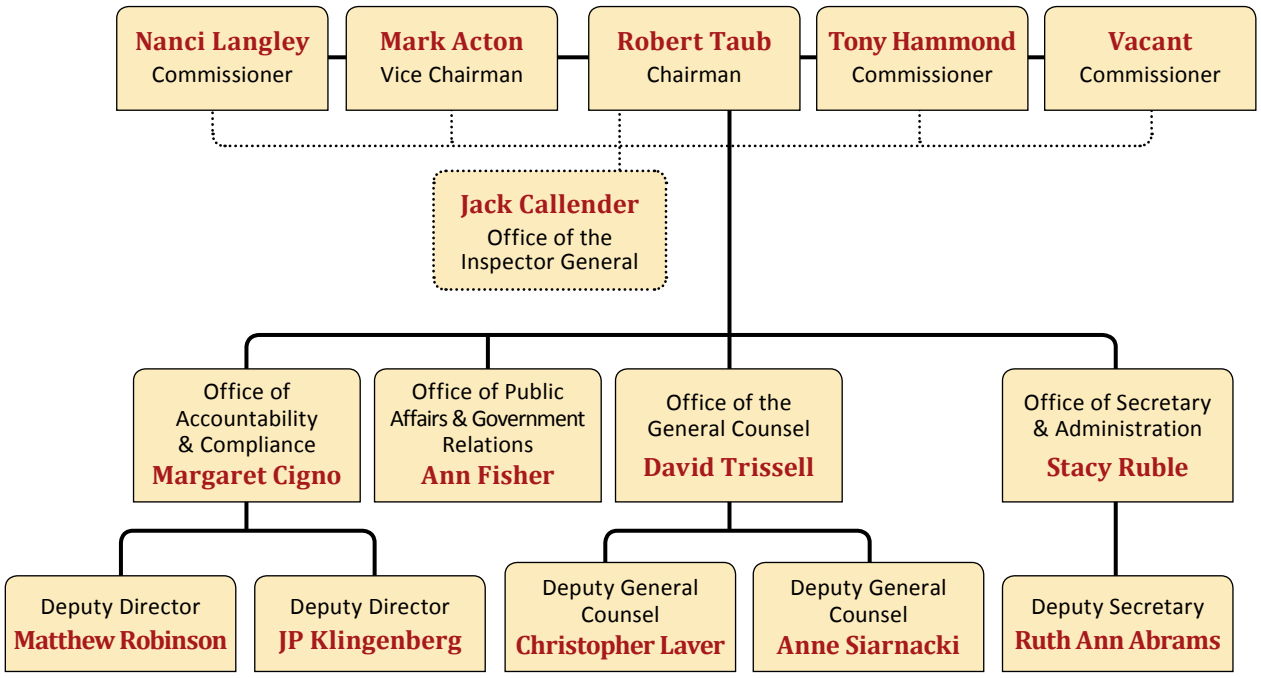
The Commission is organized into four operating offices:

- **Accountability and Compliance.** The Office of Accountability and Compliance is responsible for technical analysis and formulating policy recommendations for the Commission on domestic and international matters.
- **General Counsel.** The Office of the General Counsel ensures the Commission fulfills its statutory and regulatory obligations by providing legal guidance on matters involving the Commission's responsibilities.
- **Public Affairs and Government Relations.** The Office of Public Affairs and Government Relations facilitates prompt and responsive communications with the public, Congress, Federal agencies, the Postal Service, and media.
- **Secretary and Administration.** The Office of Secretary and Administration records the Commission's official actions; manages the Commission's records, human resources, budget and accounting, and information technology; and provides other support services.

The Commission maintains an independent Office of the Inspector General. It conducts, supervises, and coordinates audits and investigations relating to Commission programs and operations, and identifies and reports fraud and abuse in these programs and operations.

Figure II-1 displays the Commission's current organizational structure.

Figure II-1: Commission's Current Organizational Structure



Commission *Strategic Plan*

In FY 2016, the Commission developed its 2017–2022 *Strategic Plan* following a vigorous and inclusive process which incorporated input from all Commission employees. The *Plan* outlines the agency's vision to promote a robust universal mail system through objective, accurate, and timely regulatory analyses and decisions.

Over the next 5 years, the Commission will focus its activities on the following four strategic goals:

Goal 1: Deliver accurate and objective analyses and decisions to ensure transparency and accountability of the Postal Service.

Goal 2: Actively engage with Congress and stakeholders in support of a dynamic postal system.

Goal 3: Provide an optimal internal infrastructure to support management of priorities, workload, and emerging requirements.

Goal 4: Recruit, develop, and retain a diverse, high-performing workforce.

The Commission's *Strategic Plan* can be viewed or downloaded at **www.prc.gov.**

PHOTO BY PRC STAFFER MAX SCHNIDMAN

PRC Public Meeting

Office of Public Affairs and Government Relations

The Commission's Office of Public Affairs and Government Relations is the primary office providing assistance to the general public. It supports public outreach and education, responds to inquiries and informal complaints, engages with the media, and liaises with Congress, presidential administrations, the Postal Service, and other government agencies. It informs and advises commissioners and Commission staff on legislative issues and policies related to the Commission and the Postal Service, and coordinates the preparation of congressional testimony and responses to congressional inquiries concerning Commission policies and activities.

Another of its critical functions is to respond to inquiries, informal complaints, questions, suggestions, and comments from the public, business owners, government bodies, and other stakeholders.

Senate Briefings and Congressional Testimony

On January 21, 2016, Acting Chairman Robert Taub testified on behalf of the Commission at a hearing held by the U.S. Senate Committee on Homeland Security and Governmental Affairs. The hearing was entitled, "Laying out the Reality of the U.S. Postal Service." The purpose of the hearing, according to Committee Chairman Ron Johnson, was to develop a better understanding of the financial realities facing the U.S. Postal Service. Commission rules require that Postal Service financial reports be filed with the Commission on a monthly, quarterly and annual basis. The Commission analyzes these reports and for the third year in a row, issued a *Financial Analysis* report to provide greater clarity and transparency of the Postal Service's financial data. Acting Chairman Taub's statement focused upon the findings contained within the Commission's *Financial Analysis* report for FY 2014. His testimony also covered some preliminary observations based on the Commission's review of FY 2015 data. At the Committee's request, Acting Chairman Taub also discussed the continuing decline in total mail volume, personnel related costs, and the impact of legislative and regulatory requirements upon the U.S. Postal Service.

On May 11, 2016, Acting Chairman Taub testified on behalf of the Commission at a hearing held by the U.S. House Oversight and Government Reform Committee. The hearing was entitled, "Reforming the Postal Service: Finding a Viable Solution." Acting Chairman Taub highlighted the Commission's observations and conclusions from its FY 2015 *Financial Analysis* report, making clear the Postal Service faces significant financial obstacles. Aside from the financial pressure of generating sufficient funds to remain solvent, he noted that the Postal Service is also responsible for funding $4 billion in universal service obligations (as calculated annually by the Commission). At the Committee's request, Acting ChairmanTaub briefly touched upon the Commission's statutorily required December 2016 rate review.

Consumer Relations — Comments and Inquiries

INQUIRIES BY SOURCE

During FY 2016, the Office of Public Affairs and Government Relations received 5,572 inquiries, informal complaints, questions, suggestions, and comments. Approximately 82 percent of consumer inquiries were submitted online through "Contact PRC" on the Commission website. Of the remaining inquiries, 13 percent were submitted by phone and 4 percent by mail. Table II-1 shows the number of inquiries from Postal Service stakeholders for FY 2011 to FY 2016.

Table II-1: Inquiries Submitted to the Office of Public Affairs and Government Relations

Source/Stakeholder	Fiscal Year					
	2016	2015	2014	2013	2012	2011
Consumer	5201	7,783	8,919	4,058	5,227	4,663
Business Owner	287	468	482	224	67	81
Postal Employee	46	77	151	92	250	427
Federal/State/Local Government	20	39	47	72	214	223
Mailer	3	16	21	16	18	53
Media	15	14	54	48	94	132
Postal Organization	0	5	3	6	6	69
TOTAL	5,572	8,402	9,677	4,516	5,876	5,648

Order No. 195 directs the Postal Service to respond to rate and service inquiries forwarded to its Office of the Consumer Advocate within 45 days. In FY 2016, the Commission forwarded 462 such inquiries. The order also requires the Postal Service to file a monthly report summarizing the general nature of these inquiries. The reports are available on the Commission's website.

INQUIRIES BY LOCATION

The Postal Service's geographic landscape is divided into seven Area offices. In FY 2016, the number of comments and inquiries received was consistent with previous years. Table II-2 shows the FY 2016 breakdown by Area office, top issues reported, and the total number received.

Table II-2: Comments and Inquiries by Area Office

Area Office	Top Issues					FY 2016
	Delayed	Missing	Misdelivered	Undelivered	Rudeness	
Southern Area	215	185	129	134	28	1,056
Capital Metro	133	142	94	93	18	820
Western Area	137	139	83	84	14	751
Northeast Area	131	105	102	175	32	858
Pacific Area	82	70	57	66	6	462
Eastern Area	91	58	67	54	19	518
Great Lakes	10	3	6	9	0	498

INQUIRIES BY ISSUE

As in past years, the predominant types of inquiries the Commission received from business owners were undelivered mail (mail not being delivered), delayed mail (mail not being picked up by the carrier, or being delivered late in the day or after close of business), misdelivered mail (mail being delivered to the wrong address), and the carrier not attempting to deliver packages.

Service continues to be the highest inquiry category. The Commission received 4,721 inquiries regarding delivery service. There were 311 service-related inquiries regarding the carrier not making an initial attempt to deliver a package; 838 reports of mail being misdelivered or delivered to nearby addresses; 738 reports of undelivered mail or mail not being delivered to residences; 972 reports of mail and packages delayed or missing in the mail; and 197 reports of mail not being forwarded. There were 255 inquiries regarding employee behavior, including 139 reports of rudeness by Postal Service employees. Table II-3 shows inquiries categorized by top 10 issues for FY 2016.

Table II-3: Comments and Inquiries by Issue

Issue	2016	2015	2014	2013	2012	2011	2010
Delayed Mail	972	1,590	1,513	469	94	89	39
Misdelivered Mail	838	1,151	1,192	393	76	51	52
Undelivered Mail	738	1,127	1,651	520	137	107	71
Missing Mail	646	843	1,023	601	211	159	129
Return to Sender	234	321	410	139	64	47	22
Change of Address	197	296	334	180	54	20	6
Mail Damage	167	288	345	149	30	37	24
Rudeness	139	278	378	207	43	21	22
Hold Mail	78	139	110	45	13	14	6
Post Office Box	68	65	113	81	55	16	21

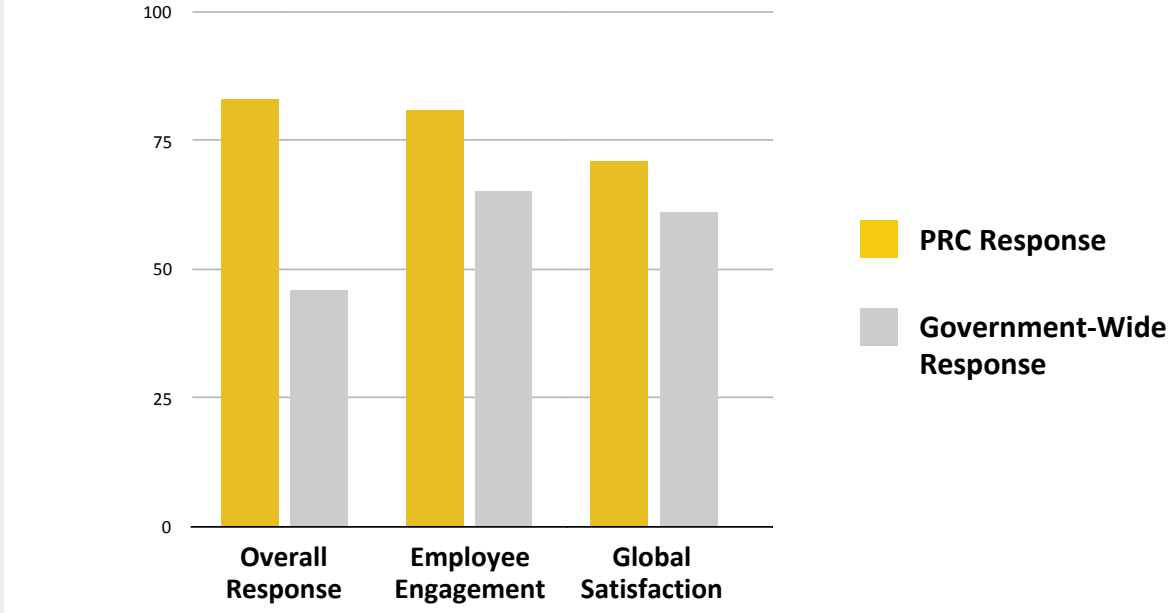
Office of the Secretary and Administration

The Office of the Secretary and Administration (OSA) provides management and staff support to the Commission's operational offices (including the Office of the Inspector General), the Commission's *Strategic Plan,* and various initiatives of the Executive Branch. OSA ensures that the Commission has the physical, financial, technological, and human capital infrastructure needed to accomplish its mission. Responsibilities include financial management, records management, administrative and organizational support, human resources management and workforce planning, and information technology support.

Employee Engagement and Training

The Commission is committed to enhancing a system that fosters recruitment, development, and retention of a talented, skilled, diverse, and adaptable workforce as part of its Human Capital Plan within the 2012–2016 *Strategic Plan*. In FY 2016, the Commission participated in the annual Federal Employee Viewpoint Survey (FEVS). The Commission's response rate of 83 percent was significantly higher than the government-wide rate of 46 percent. Figure II-2 shows an overview of the Commission's ratings on the Office of Personnel Management (OPM) indices when compared with the Federal government as a whole.

Figure II-2: Overview of FY 2016 FEVS Results



OPM has aggregated the results of the FEVS into two indices. "Employee Engagement" ranks employees' perceptions on the leadership within their agency, their supervisors, and the overall work experience. "Global Satisfaction" measures employees' satisfaction about four aspects related to work: job, pay, organization, and whether they would recommend their organization as a good place to work. Compared to responses with Federal employees government-wide, Commission staff had a higher degree of satisfaction with their work and office environment: an 81 percent rating in "Employee Engagement" versus the government-wide rating of 65 percent, and a 71 percent rating in "Global Satisfaction" versus the government-wide rate of 61 percent. The Commission is committed to developing actionable plans based on the confidential feedback received from employees through this survey as part of the Commission's new 2017–2022 *Strategic Plan.*

Commission leadership's investment in its employees remains a top priority. In FY 2016, the Commission offered training and professional development opportunities designed to increase employee knowledge, engagement, and retention. The Commission also ensured that employees were in compliance with mandatory training requirements in all areas including cybersecurity, the Hatch Act, ethics, and records management. All employees participated in the training program; 46 percent of employees chose to participate in off-site training, and the remainder attended in-house professional development and other Commission-provided training sessions.

This year, the Commission revised and expanded its policy on the Flexible Work Program, which includes alternate work schedules (AWS) and telework opportunities. Employee participation in the AWS program remained static at 41 percent, and the number of employees teleworking on an ongoing basis increased to 44 percent. In 2016, the Commission offered extended telework to eligible employees, and 9 percent of the workforce used this increased flexibility to telework more than three days per week. Telework is an integral part of the Commission's continuity of operations plan, particularly situational or ad-hoc telework, to ensure the Commission's continued operations during government closure or delay situations (including inclement weather or events that deter or delay regular commuting into downtown Washington). During FY 2016, 70 percent of Commission staff participated in such situational telework, up from 62 percent last year.

Equal Employment Opportunity and Diversity

In FY 2016, the Commission continued its commitment to equal employment opportunity (EEO) in its initiatives to recruit, develop, and retain a skilled, high-achieving, and diverse workforce. Women and minorities accounted for 63 percent and 32 percent of the workforce, respectively. Women filled 40 percent of the Commission's executive positions; minorities filled 10 percent. During FY 2016, the Commission had no formal EEO complaints filed.

The Commission provides internship opportunities to aid in the recruitment and development of professionals with diverse backgrounds. The Commission will continue to monitor and offer opportunities to increase diversity, including the use of formal recruitment channels such as local universities, veterans' groups, and comparable organizations and groups that target under-represented populations.

Over the fiscal year, the Commission revised and updated its workplace harassment policy and provided EEO and Notification and Federal Employee Antidiscrimination and Retaliation Act (NoFEAR Act) training for all employees, supervisors, and managers.

Transparency and Open Government

The Commission is committed to transparency, accountability, and open government. In compliance with the Freedom of Information Act (FOIA), the Commission completed all FY 2016 FOIA requests within statutory time limits. The Commission received a favorable review in the Department of Justice's FY 2016 *Assessment of Agency Progress.* The Commission also began a comprehensive review and revision of its FOIA regulations in line with the FOIA Improvement Act of 2016.

The Commission continued to provide live audio webcasts of hearings, technical conferences, and public meetings, and expanded these capabilities to provide for video recordings and webcasting of public meetings and technical conferences. Recordings of the webcasts are available on the Commission's website, **www.prc.gov.**

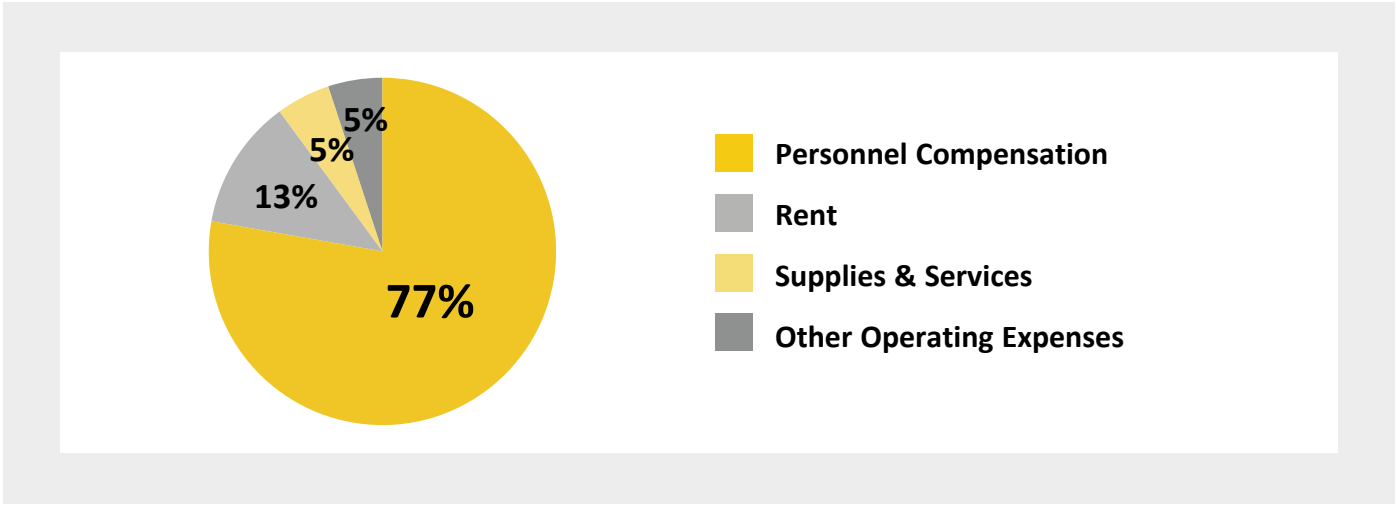
Budget and Finance

The Commission's Total Obligation Authority for FY 2016 was $15,200,000. These funds were used to maintain staffing levels of 72 full-time employees and for operating expenses. Salaries and benefits accounted for $10,846,504 (77%) of the Commission expenditures, the remaining $4,353,496 was allocated for operating expenses.

Figure II-3 displays the Commission's actual expenditures for FY 2016: "Rent" goes toward the agency's commercial office and storage space, and "Other Operating Expenses" includes information technology, training, supplies, printing, and consulting services. The Commission is also implementing a revised budget formulation and forecasting process to further enhance budget development. The Commission also successfully partnered with women and minority-owned businesses for a total of 49 percent of all Commission contracts.

In response to the 2009 presidential memorandum regarding government contracting, and in line with Executive Order 13576, "Delivering an Efficient, Effective, and Accountable Government" (2011), the Commission is in the process of updating our procurement policy and process. The new policy is centered on strengthening the Commission's commitment to best value and promoting a fair and equitable procurement opportunity for all vendors.

Figure II-3: FY 2016 Actual Expenditures



Information Technology (IT)

In FY 2016, the Commission invested significantly in its IT infrastructure. Investments included continued improvements to the Commission website, ensuring a user-friendly and Section 508 compliant interface. The Commission's IT team upgraded security and infrastructure to improve the overall integrity of the Commission's network and to comply with new and on-going initiatives related to network security. The IT team worked closely with the Records Management team on developing projects to comply with records management directives and Commission policy. These improvements continue to build on the Commission's commitment to openness and transparency.

Records Management

In FY 2016, the records management team continued its work in compliance with the directive from the Office of Management and Budget (OMB) and the National Archives and Records Administration (NARA) on managing government records. The Commission updated its records management policy and began work on an electronic records management system. The records management team worked closely with IT to issue an update on email records use and retention. The Commission continues to move forward with initiatives designed to meet the deadlines outlined in the OMB/NARA directive. The Commission received positive ratings from NARA for proceeding with and expanding its records management program.

CHAPTER III | Effectiveness of Commission Rules in Achieving PAEA Objectives

PHOTO BY M DOGAN

The Commission is required by 39 U.S.C. § 3651 to submit an annual report to the President and the Congress that includes an analysis of the extent to which regulations are achieving the objectives under section 3622 of Title 39 of the U.S. Code. In FY 2017, the Commission will review the current system of ratemaking that was developed pursuant to section 3622 to determine if it is achieving the objectives established by Congress.[1] If the Commission determines that the system is not achieving the objectives, taking into account the factors, the Commission may, by regulation, make modifications or adopt an alternative system as necessary to achieve the objectives. Id. Consequently, the Commission anticipates that future Annual Reports will provide in-depth analysis of how well the system in place upon completion of the review is achieving the objectives.

Old Post Office building with Benjamin Franklin Statue in Washington, DC.

[1] 39 U.S.C. 3622(d)(3).

The objectives applicable to Market Dominant products are listed in 39 U.S.C. § 3622(b):

1. Maximize incentives to reduce costs and increase efficiency.
2. Create predictability and stability in rates.
3. Maintain high-quality service standards established under 39 U.S.C. § 3691.
4. Allow the Postal Service pricing flexibility.
5. Assure adequate revenues, including retained earnings, to maintain financial stability.
6. Reduce the administrative burden and increase the transparency of the ratemaking process.
7. Enhance mail security and deter terrorism.
8. Establish and maintain a just and reasonable schedule for rates and classifications; however, this objective does not prohibit the Postal Service from making changes of unequal magnitude within, between, or among classes of mail.
9. Allocate the total institutional costs of the Postal Service appropriately between Market Dominant and Competitive products.

Section 3622(b) establishes a tension between the restrictions of an inflation-based price cap on Market Dominant price increases and the objective that the Postal Service must assure adequate revenues and retained earnings to maintain financial stability. Furthermore, although the PAEA provides incentives via the price cap to reduce costs and increase efficiency, it also imposes personnel-related expenses requiring the Postal Service to pre-fund future healthcare costs for its retirees.

The Commission's rules for applying the price cap and the application of those rules help to achieve several objectives of the PAEA. For example, enforcing the limitation that price increases for each class of mail do not exceed inflation incentivizes the Postal Service to reduce costs and increase efficiency (objective 1). The Commission applies the price cap at the class level, which allows the Postal Service pricing flexibility (objective 4) because there are few restrictions on the prices the Postal Service sets within each class. In FY 2016, the Commission approved promotional rates for certain Market Dominant products, which furthered objectives 1 and 4.

The Commission's review of Postal Service requests to add products or NSAs to the Market Dominant or Competitive product lists helps maintain a just and reasonable schedule for rates and classifications (objective 8).

Each year, the Commission analyzes the Postal Service's rates and service performance and reports its findings in the *Annual Compliance Determination* (ACD). The Commission's rules for reviewing potential changes to the methods underlying the development of data the Postal Service reports help promote accuracy and reliability. Accurate, reliable cost estimates are essential to appropriately allocate the Postal Service's total institutional costs between Market Dominant and Competitive products (objective 9).

In FY 2016, the Commission continued its practice of analyzing the Postal Service's financial results and performance goals in expanded reports separate from the ACD. This helps increase the transparency of the ratemaking process (part of objective 6). The Commission's analysis of the Postal Service's financial results evaluates the Postal Service's financial stability, which promotes objective 5.

In FY 2016, the Commission reviewed the Postal Service's service performance and related reporting requirements. It also considered the Postal Service's proposal to replace an existing external service performance measurement system with an internal system. These analyses help maintain high-quality service standards (objective 3).

The Commission did not develop any rules or review any cases with a direct effect on mail security or terrorism (objective 7) in FY 2016. The requirements applicable to Competitive products are contained in 39 U.S.C. § 3633(a):

1. Prohibit Market Dominant products from subsidizing Competitive products.
2. Ensure each Competitive product covers its attributable costs.
3. Ensure all Competitive products collectively cover what the Commission determines to be an appropriate share of the Postal Service's institutional costs.

The Commission evaluated Competitive products for compliance with these requirements during FY 2016. First, in the FY 2015 ACD, the Commission reviewed Competitive products to determine whether any rates or fees in effect during FY 2015 were not in compliance with 39 U.S.C. § 3633(a). Second, the Commission analyzed changes in rates of general applicability for Competitive products as well as NSAs proposed by the Postal Service. Third, the Commission evaluated proposed changes to the Postal Service's costing methodologies.

The following sections describe the Commission's major orders, reports, and proceedings during FY 2016.

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A fleet of United States Postal Service mail delivery vehicles in Franklin Park, Illinois.

Annual Reports

Annual Compliance Determination

The ACD is an important tool for enhancing transparency and determining whether the Postal Service complies with statutory pricing and service requirements. Under the PAEA and Commission regulations, the Postal Service has 90 days after the fiscal year ends to prepare and submit its *Annual Compliance Report* (ACR) to the Commission. The ACR analyzes costs, revenues, rates, and quality of service for Market Dominant and Competitive products. 39 U.S.C. § 3652(a). After receiving the ACR, the Commission then has 90 days to solicit comments from the public and determine (1) whether rates or fees in effect during the fiscal year complied with applicable provisions and (2) whether the Postal Service met its service standards in effect during the fiscal year. Id. § 3653(a) and (b). The Commission publishes its analysis of the ACR in the ACD.

On March 28, 2016, the Commission issued the FY 2015 ACD and made several principal findings and directives.[2] First, when reviewing Market Dominant products for compliance with statutory pricing policies, the Commission found that 24 workshare discounts did not comply with 39 U.S.C. § 3622(e), which prohibits workshare discounts from exceeding avoided costs except under specific circumstances. The Commission directed the Postal Service to either align workshare discounts with avoided costs during the next Market Dominant price adjustment or specify an applicable statutory exception.

Second, the Commission found that for the Periodicals class, the Postal Service failed to meaningfully address the FY 2014 ACD directives to report on the cost and contribution impact of worksharing incentives offered for 5-Digit and Carrier Route presortation and progress in improving pricing efficiency. The Commission directed the Postal Service to provide further information within 120 days after the FY 2015 ACD was issued.

Third, the Commission identified seven Market Dominant products that did not generate sufficient revenues to cover their attributable costs: Periodicals In-County, Periodicals Outside County, Standard Mail Flats, Standard Parcels, Media Mail/Library Mail, Inbound Letter Post, and Stamp Fulfillment Services. The Commission directed the Postal Service to take appropriate action for some products.

[2] Docket No. ACR2015, *Annual Compliance Determination,* March 28, 2016 (FY 2015 ACD).

Fourth, the Commission found that six Competitive products did not cover their attributable costs as required by 39 U.S.C. § 3633(a)(2). The Commission directed the Postal Service to take corrective action for each product found out of compliance. Such corrective action was directed to the specific circumstances surrounding the non-compliance and included amending or terminating contracts, reporting on the status of contracts or negotiations, and identifying obstacles to exiting or renegotiating international agreements.

Fifth, the Commission found that most products failed to meet their service performance targets for FY 2015. It also found that the Postal Service's plans to improve service performance results were inadequate to address service performance issues. The Commission directed the Postal Service to file additional service performance information within 120 days after the FY 2015 ACD was issued.

Sixth, the Commission discussed the recent dramatic decline of service performance for First-Class Mail Single-Piece Letters/Postcards with a 3-5-Day service standard. As a result, the Commission determined that First-Class Mail Single-Piece Letters/Postcards were not in compliance. It directed the Postal Service to improve service for this product in FY 2016 and provide a detailed, comprehensive plan for improving service performance. It required the Postal Service to explain in the FY 2016 ACR specific efforts to improve service performance for this product. It directed the Postal Service to provide certain information disaggregated by district level and service standard.

Seventh, the Commission discussed the Postal Service's long term difficulties processing and delivering flats in a timely and cost effective manner. It found that due to the lack of comprehensive data, the Postal Service cannot measure the impact or success of initiatives designed to improve flats cost and service issues. Consequently, the Commission directed the Postal Service to submit a report on flats issues and provide further information regarding options for improving cost and service efficiency. This report was required to quantify the main drivers of significant and ongoing service failures and cost shortfalls and include a plan to address each of the main drivers.

Analysis of Performance Goals

Each year, the Commission must evaluate whether the Postal Service met the performance goals established in its *Annual Performance Report* and *Performance Plan.* 39 U.S.C. § 3653(d). The Commission may also provide the Postal Service recommendations related to protecting or promoting public policy objectives in Title 39. *Id.*

On May 4, 2016, the Commission issued its Analysis of the Postal Service's FY 2015 Annual Performance Report and FY 2016 Performance Plan.[3] The Commission provided an in-depth analysis of the Postal Service's four performance goals: Deliver High-Quality Services, Provide Excellent Customer Experiences, Ensure a Safe Workplace and Engaged Workforce, and Sustain Controllable Income.

The Commission found that the FY 2015 *Annual Performance Report* and FY 2016 *Performance Plan* complied with most statutory requirements. Also, the Commission found that in FY 2015, the Postal Service partially met the Sustain Controllable Income performance goal, but did not meet the other three goals. For each performance goal, the Commission provided recommendations to help the Postal Service meet the goal and better assess its performance in future years.

[3] Docket No. ACR2015, *Analysis of the Postal Service's FY 2015 Annual Performance Report and FY 2016 Performance Plan,* May 4, 2016.

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Financial Analysis Report

On March 29, 2016, the Commission issued its *Financial Analysis of United States Postal Service Financial Results and 10-K Statement for FY 2015.*[4] In this report, the Commission evaluated the Postal Service's financial status; analyzed volume, revenue, and cost trends for each mail class; and reviewed the Postal Service's sustainability, liquidity, and solvency.

The Commission acknowledged the Postal Service's significant efforts to reduce operating expenses and improve efficiency to better align expenses with mail volumes. The Commission found that in FY 2015, the Postal Service generated an annual net operating income of $1.2 billion due to the Market Dominant exigent rate surcharge and increases in Competitive product volume and revenue. However, it stated that operating expenses also grew during FY 2015, resulting in increased work hours and career employees.

The Commission found that the Postal Service's liquidity continued to improve compared to FY 2013. Despite this improvement, the Commission observed that the Postal Service faces significant financial challenges such as the statutorily-required payments to the Retiree Health Benefits Fund.

[4] Docket No. ACR2015, *Financial Analysis of United States Postal Service Financial Results and 10-K Statement Fiscal Year 2015,* March 29, 2016 (Financial Analysis).

Rate and Classification Cases of Note

In FY 2016, there were several important rate and classification cases before the Commission.

Market Dominant Price Adjustments

The Commission approved two Postal Service proposals to adjust Market Dominant prices. First, on November 16, 2015, the Postal Service sought approval of five temporary promotional discounts to be offered during FY 2016.[5] These promotions applied to First-Class Mail and Standard Mail products. After considering comments received, the Commission found that these temporary promotional discounts were consistent with 39 U.S.C. § 3622(d) and could take effect as planned.[6]

Second, on May 16, 2016, the Postal Service sought approval of six First-Class Mail and Standard Mail promotional discounts to be offered during calendar year 2017.[7] The Postal Service also asked to increase prices to correct an anomaly within First-Class Mail Parcels. Id. at 1. After considering comments received, the Commission concluded that the proposed price adjustments were consistent with the price cap under 39 U.S.C. § 3622(d), the reduced rates requirements under 39 U.S.C. § 3626, and the annual limitation calculated under 39 C.F.R. § 3010.21.[8]

Removal of Exigent Surcharge

In FY 2014, the Commission granted the Postal Service's request for an exigent price adjustment under 39 U.S.C. § 3622(d)(1)(E).[9] In FY 2015, the Commission authorized the Postal Service to collect a total of $3.957 billion in after-rates contribution by imposing an exigent surcharge on existing Market Dominant rates.[10]

To monitor and prevent over-collection, the Commission directed the Postal Service to provide notice of its intent to remove the exigent rate surcharge 45 days before reaching the surcharge revenue limitation.[11] On February 25, 2016, the Postal Service filed notice that it intended to remove the exigent surcharge on April 10, 2016.[12]

The Commission established a 20 day public comment period and ordered the Postal Service to continue to file bi-weekly estimates of surcharge revenue.[13] On March 29, 2016, the Commission approved the Postal Service's planned removal of the exigent surcharge.[14]

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5 Docket No. R2016-2, United States Postal Service Notice of Market-Dominant Price Adjustment, November 16, 2015.
6 Docket No. R2016-2, Order No. 2861, Order on Price Adjustments for Market Dominant Products and Related Mail Classification Changes, December 10, 2015, at 7.
7 Docket No. R2016-5, United States Postal Service Notice of Market-Dominant Price Adjustment, May 16, 2016.
8 Docket No. R2016-5, Order No. 3373, Order on Price Adjustments for Market Dominant Products, June 16, 2016, at 1.
9 Docket No. R2013-11, Order Granting Exigent Price Increase, December 24, 2013 (Order No. 1926).
10 Docket No. R2013-11R, Order Resolving Issues on Remand, July 29, 2015 (Order No. 2623); *see also* Order No. 1926; *Alliance of Nonprofit Mailers* v. *Postal Regulatory Commission,* 790 F.3d 186 (D.C. Cir. June 5, 2015). These orders and the court's decision are discussed in more detail in Chapter V, infra.
11 Order No. 2623 at 62; see Docket No. R2013-11, Order No. 2319, Order on Exigent Surcharge Removal, January 12, 2015.
12 Docket No. R2013-11, Notice of the United States Postal Service of Removal of the Exigent Surcharge, February 25, 2016.
13 Docket No. R2013-11, Order No. 3103, Notice and Order on Removal of Exigent Surcharge, February 26, 2016.
14 Docket No. R2013-11, Order No. 3186, Order on Removal of the Exigent Surcharge and Related Changes to the Mail Classification Schedule, March 29, 2016.

IMb Remand

In FY 2008, the Postal Service introduced Intelligent Mail barcoding (IMb) as a requirement for automation rates at two different discount and service levels: basic and full service.

In FY 2013, the Postal Service announced plans to require certain mailpieces to bear Full Service IMbs to qualify for an automation discount (pieces with Basic IMbs would pay a higher non-automation rate).[15] In the Postal Service's September 26, 2013 notice of planned price adjustments for Market Dominant products, the Postal Service did not alter the price cap calculation to account for the Full Service IMb requirement for any Market Dominant class except Package Services.[16] The Commission subsequently found that the Full Service IMb requirement constituted a classification change with rate implications, concluding that the Postal Service's implementation of the Full Service IMb requirement simultaneously with its planned rate adjustment would violate the price cap.[17] The Postal Service deferred implementation of the Full Service IMb requirement and appealed the Commission's order to the D.C. Circuit.[18]

In FY 2015, the D.C. Circuit affirmed the Commission's authority to regulate mail preparation changes, but remanded the decision for the Commission to enunciate a standard for when a mail preparation change would have a rate effect with price cap implications and then reconsider its decision in light of that standard.[19]

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On January 22, 2016, in Order No. 3047, the Commission, following an opportunity for public comment, announced a standard for determining whether a mail preparation change has rate effects that impact the price cap.[20] Under that standard, a mail preparation change has rate effects when the change results in either the deletion or the redefinition of a rate cell. *Id.* at 20. The Commission also established Docket No. RM2016-6 to consider proposed procedural rules relating to this standard.[21]

On February 22, 2016, the Postal Service moved for reconsideration and clarification of the application of the standard set forth in Order No. 3047.[22] On July 20, 2016, the Commission issued an order resolving the Motion for Reconsideration and maintaining its holding set forth in Order No. 3047.[23]

On August 11, 2016, the Postal Service appealed Order No. 3047 and the Commission's order resolving the Motion for Reconsideration to the D.C. Circuit.[24] The petition is currently pending before the court.

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[15] Implementation of Full-Service Intelligent Mail Requirements for Automation Prices, 78 Fed. Reg. 23137 (Apr. 18, 2013).
[16] Docket No. R2013-10, United States Postal Service Notice of Market-Dominant Price Adjustment, September 26, 2013.
[17] Docket No. R2013-10, Order on Price Adjustments for Market Dominant Products and Related Mail Classification Changes, November 21, 2013, at 2, 13-14, 36 (Order No. 1890).
[18] Docket No. R2013-10, Response of the United States Postal Service to Order No. 1890, November 29, 2013, at 2; *United States Postal Service* v. *Postal Regulatory Commission,* No. 13-1308 (D.C. Cir. filed Dec. 20, 2013).
[19] *United States Postal Service* v. *Postal Regulatory Commission,* 785 F.3d 740, 754-56 (D.C. Cir. 2015).
[20] Docket No. R2013-10R, Order Resolving Issues on Remand, January 22, 2016 (Order No. 3047).
[21] Docket No. RM2016-6, Notice of Proposed Rulemaking on Motions Concerning Mail Preparation Changes, January 22, 2016 (Order No. 3048).
[22] Docket No. R2013-10R, Motion for Reconsideration of Order No. 3047, February 22, 2016 (Motion for Reconsideration).
[23] Docket No. R2013-10R, Order No. 3441, Order Resolving Motion for Reconsideration of Commission Order No. 3047, July 20, 2016.
[24] *United States Postal Service v. Postal Regulatory Commission,* No. 16-1284 (D.C. Cir. filed Aug. 11, 2016).

Market Tests

The Postal Service may conduct market tests of experimental products under 39 U.S.C. § 3641. During FY 2016, the Commission authorized one new market test and an extension of an existing market test.

On May 25, 2016, the Commission approved the Postal Service's request to conduct the Global eCommerce Marketplace (GeM) Merchant market test.[25] Customers mailing items to foreign countries must pay duties and taxes to the foreign country's customs agency when the item arrives. Order No. 3319 at 2. GeM Merchant allows participating domestic online merchants to offer their international customers the ability to estimate and prepay these duties and taxes when purchasing the item. *Id.* The Postal Service will offer GeM Merchant to a limited number of merchants through NSAs. *Id.* The Commission found that the GeM Merchant market test met applicable statutory and regulatory requirements and authorized the market test to proceed for 2 years. *Id.* at 26.

Under the Customized Delivery market test, the Postal Service delivers groceries and other prepackaged goods to customers.[26] The market test was scheduled to expire on October 31, 2016. Order No. 3543 at 2. On September 28, 2016, the Commission authorized the extension of the Customized Delivery market test for an additional 12 months. *Id.* at 15. The Commission directed the Postal Service to continue providing advance notice at least 10 days before expanding the market test into other geographic areas. *Id.* at 11. It also updated the data collection plan for the market test. *Id.* at 12-13.

Product List and Mail Classification Schedule Changes

The Postal Service may request that the Commission add, remove, or transfer products from the Market Dominant and Competitive product lists. 39 U.S.C. § 3642; 39 C.F.R. part 3020, subpart B. On October 28, 2015, the Commission approved the Postal Service's request to remove Global Direct Contracts from the Competitive product list.[27]

The Commission's rules also enable the Postal Service to make material changes or minor corrections to the MCS by filing notice with the Commission. 39 C.F.R. part 3020, subpart E. During FY 2016, the Commission issued several orders approving MCS changes. First, the Commission approved material MCS changes related to Priority Mail International Flat Rate Envelopes and Small Flat Rate Boxes.[28] Second, the Commission issued two orders approving minor classification changes to the Country Price Lists for International Mail in Part D of the MCS.[29]

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[25] Docket MT2016-1, Order Authorizing Market Test of Global eCommerce Marketplace (GeM) Merchant, May 25, 2016 (Order No. 3319).
[26] Docket MT2014-1, Order Authorizing Extension of Customized Delivery Market Test and Updating Data Collection Plan, September 28, 2016, at 2 (Order No. 3543).
[27] Docket No. MC2016-7, Order No. 2788, Order Approving Removal of Global Direct Contracts from the Competitive Product List, October 28, 2015. Requests to add new Competitive NSAs are discussed in the "Competitive Products" section below.
[28] Docket No. MC2016-118, Order No. 3250, Order Approving Changes to the Mail Classification Schedule Related to Priority Mail International Flat Rate Envelopes and Priority Mail International Small Flat Rate Boxes, April 19, 2016.
[29] Docket No. MC2016-10, Order No. 3458, Order Approving Minor Classification Changes, November 9, 2015; Docket No. MC2016-172, Order No. 2808, Order Approving Minor Classification Change, August 8, 2016.

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Service Performance Measurement and Reporting

There were two key dockets, in addition to the ACD, in FY 2016 where the Commission considered issues related to service performance measurement and reporting.

Proposed Service Performance Measurement System

Service performance must be measured by an objective external performance measurement system unless the Commission approves the use of an internal or a hybrid measurement system. 39 U.S.C. § 3691(b)(2). In FY 2016, the Commission continued discussions with the Postal Service in Docket No. PI2015-1 regarding its proposal to develop a new internal service performance measurement system for several Market Dominant products, including products within First-Class Mail, Standard Mail, Periodicals, and Package Services.

The Commission hosted two off-the-record technical conferences in FY 2016. First, on October 28, 2015, the Commission hosted a technical conference to discuss the Postal Service's statistical design plan for internal service performance measurement.[30] Second, on August 26, 2016, the Commission hosted a technical conference where Postal Service officials discussed the implications of the FY 2016 Quarters 2 and 3 service performance results that were produced by the proposed measurement system.[31] This docket remains open pending the Postal Service's filing of further information, including two more quarters of service performance results produced by the proposed measurement system.

[30] Docket No. PI2015-1, Order No. 2733, Order Scheduling Technical Conference Concerning the Statistical Design Plan, September 28, 2015.
[31] Docket No. PI2015-1, Order No. 3459, Order Scheduling Technical Conference to Review Internal Service Performance Data, August 11, 2016.

Enhancing Service Performance Reporting Requirements

On September 30, 2015, the Government Accountability Office published a report recommending that the Commission hold a public proceeding to address how the Postal Service may improve the quality and completeness of its service performance data.[32] Accordingly, Docket No. PI2016-1 was established to invite public comments on potential issues related to the quality and completeness of service performance data measured by the Postal Service.[33] The GAO also recommended that the Commission provide service performance data and analyses in a more readily available format. *Id.* at 26, 31. In response, the Commission updated its website to allow instantaneous access to service performance related reports and dockets under the tab "Reports/Data Service Reports."

On August 26, 2016, the Commission issued a final order that enhanced reporting of service performance measurement data by requiring the Postal Service to regularly provide descriptions

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of the current methodologies used to verify the accuracy, reliability, and representativeness of data for each service performance measurement system.[34] The Commission also required the Postal Service to provide regular, detailed information concerning mailpieces included and excluded from measurement and explain why mailpieces are excluded from measurement. Order No. 3490 at 2.

Rulemakings

In FY 2016, the Commission conducted several rulemakings addressing rate and costing issues.

Mail Preparation Changes and the Price Cap

On January 22, 2016, the Commission initiated Docket No. RM2016-6 to consider proposed rules for regulating mail preparation changes that affect the price cap. See Order No. 3048. The proposed rules' primary purpose is to ensure that the Postal Service properly accounts for the rate effects of mail preparation changes under 39 C.F.R. § 3010.23(d)(2) in accordance with the Commission's standard articulated in Order No. 3047.[35]

The proposed rules are intended to standardize the procedure and timeframe for interested parties to file motions with the Commission when they contend that a mail preparation change affects compliance with the price cap. *Id.* at 2.

The Commission received five sets of comments. This rulemaking is currently pending before the Commission.

[32] United States Government Accountability Office, *U.S. Postal Service: Actions Needed to Make Delivery Performance Information More Complete, Useful, and Transparent,* GAO-15-756, at 22 (September 2015).
[33] Docket No. PI2016-1, Order No. 2791, Notice Establishing Docket Concerning Service Performance Measurement Data, October 29, 2015.
[34] Docket No. PI2016-1, Order Enhancing Service Performance Reporting Requirements and Closing Docket, August 26, 2016, at 1-2 (Order No. 3490).
[35] *Id.* at 1-2. Order No. 3047 is discussed in the "IMb Remand" section above.

Proposals to Change Analytical Principles

The Commission's rules allow any interested person, including the Postal Service and public representative, to petition the Commission to initiate proceedings to consider proposals to change accepted analytical principles. 39 C.F.R. § 3050.11(a). These proceedings are intended to improve the quality, accuracy, or completeness of data or data analysis in the Postal Service's annual periodic reports to the Commission. *Id.*

During FY 2016, the Commission considered 16 petitions proposing to change various accepted analytical principles. Several of these proposals are discussed below.

On October 8, 2015, United Parcel Service (UPS) submitted three proposals asking the Commission to consider changes in cost attribution concerning inframarginal costs, "hidden" variable costs, and the minimum contribution of Competitive products to institutional costs. These proposals are discussed in detail in the "UPS Proposals One, Two, and Three" section on the following page.

The Commission also considered several proposals filed by the Postal Service. The Postal Service filed two proposals relating to city carrier costing. First, the Postal Service asked the Commission to consider Proposal Nine, which sought to utilize the Time and Attendance Collection System to decompose city carrier accrued costs into office costs (cost segment 6) and street costs (cost segment 7), replacing the current methodology that uses the In-Office Cost System.[36] The Commission rejected Proposal Nine on September 22, 2016, because of insufficient documentation that conflicts with other information on record and contains unexplained procedures.[37]

Second, the Postal Service asked the Commission to consider Proposal Thirteen, which proposed an update to the city carrier street time model used to determine the attributable street time costs of city carriers.[38] The Commission issued an order approving the Postal Service's proposal on October 29, 2015.[39]

On November 24, 2015, the Commission approved a proposal to combine Cost Segments 3 and 4, the costs for Post Office Clerks in Cost Ascertainment Groups (CAG) A-J and K-L.[40] In doing so, however, the Commission also directed the Postal Service to report the costs for CAGs K-L separately in order to estimate accurately the costs of the universal service obligation. Order No. 2837 at 11.

On August 22, 2016, the Postal Service filed a proposal to develop an econometric model to determine the relationship between transportation capacity and mail volume, which was previously assumed to be 100 percent proportional.[41] This relationship is used in developing the attributable costs for purchased highway transportation. This proposal is currently pending before the Commission.

The Commission approved several other proposals it found would improve the quality, accuracy, and completeness of financial data or data analysis. The proposals included initiatives to update and improve data sources for existing cost and revenue systems that either streamline data production or improve data quality. For example, the Commission approved an econometric model for determining the cost variability of call centers, once sufficient data are available for a robust estimation.[42]

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[36] Docket No. RM2015-2, Petition of the United States Postal Service for the Initiation of a Proceeding to Consider Proposed Changes in Analytical Principles (Proposal Nine), October 31, 2014.
[37] Docket No. RM2015-2, Order No. 3526, Order Denying Changes in Analytical Principles Used in Periodic Reporting (Proposal Nine), September 22, 2016
[38] Docket No. RM2015-7, Petition of the United States Postal Service for the Initiation of a Proceeding to Consider Proposed Change in Analytical Principles (Proposal Thirteen), December 11, 2014.
[39] Docket No. RM2015-7, Order No. 2792, Order Approving Analytical Principles Used in Periodic Reporting (Proposal Thirteen), October 29, 2015.
[40] Docket No. RM2015-19, Order Approving Analytical Principles Used in Periodic Reporting (Proposal Ten), November 24, 2015 (Order No. 2837).
[41] Docket No. RM2016-12, Petition of the United States Postal Service for the Initiation of a Proceeding to Consider Proposed Changes in Analytical Principles (Proposal Four), August 22, 2016.
[42] Docket No. RM2015-5, Order No. 2826, Final Order on Analytical Principles Used in Periodic Reporting (Proposal Twelve), November 19, 2015.

UPS Proposals One, Two, and Three

On October 8, 2015, UPS submitted three proposals asking the Commission to consider changes in cost attribution concerning inframarginal costs, "hidden" variable costs, and the minimum contribution of Competitive products to institutional costs.[43]

Proposal One recommended that the Postal Service calculate and attribute inframarginal costs to individual products. Proposal Two recommended that the Commission include "hidden" variable costs when calculating attributable costs. Proposal Three recommended that the Commission increase the minimum contribution required from Competitive products under 39 U.S.C. § 3633(a)(3) from 5.5 percent to 24.6 percent.

On September 9, 2016, the Commission issued its order on these proposals.[44] Proposals One and Two were not adopted because they failed to demonstrate that inframarginal costs and "hidden" variable costs can be attributed to products through "reliably identified causal relationships." Order No. 3506 at 2-3. The Commission declined to consider Proposal Three because it is required under 39 U.S.C. § 3633(b) to review the Competitive products' appropriate share requirement every 5 years. *Id.* at 124. The Commission stated it will conduct this review as required by section 3633(b). *Id.* In early FY 2017, UPS petitioned the D.C. Circuit for review of the Commission's order.[45] The appeal is currently pending before the court.

While not adopting the UPS proposals, the Commission found it appropriate to change the Postal Service's costing methodology to better reflect general economic costing principles. Order No. 3506 at 123. Specifically, the Commission redefined attributable costs to mean the incremental costs of a product or service. *Id.* at 123-24. The Commission initiated a rulemaking to consider conforming changes to its rules that define or describe attributable costs.[46] In FY 2017, the Commission issued a final order making these changes.[47]

Price Elasticities and Internet Diversion

In response to a petition filed by interested persons, the Commission explored possible improvements to the Postal Service's econometric demand model and associated factors relating to price elasticity estimates and internet diversion in Docket No. RM2014-5.[48] The Commission held a technical conference, issued a notice of inquiry, and considered comments received.[49]

On February 26, 2016, the Commission issued a final order closing this docket.[50] The Commission stated that while the commenters' observations and comments were helpful, they did not provide analytical approaches that could be directly incorporated into a postal demand model. Order No. 3100 at 8-9. The Commission also noted that the Postal Service had already implemented a number of changes to its demand and forecasting methodology. *Id.* at 10. For these reasons, the Commission declined to issue a notice of proposed rulemaking based on these proceedings. *Id.* at 9, 12. The Commission requested that the Postal Service annually apprise the Commission of its progress to more accurately model the impact of diversion on mail volumes. *Id.* at 12.

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[43] Docket No. RM2016-2, Petition of United Parcel Service, Inc. for the Initiation of Proceedings to Make Changes to Postal Service Costing Methodologies, October 8, 2015 (Petition). Proposals One, Two, and Three are attached to the Petition.

[44] Docket No. RM2016-2, Order Concerning United Parcel Service, Inc.'s Proposed Changes to Postal Service Costing Methodologies (UPS Proposals One, Two, and Three), September 9, 2016, at 2, 4 (Order No. 3506).

[45] *United Parcel Service, Inc. v. Postal Regulatory Commission,* No. 16-1354 (D.C. Cir. filed October 7, 2016).

[46] *Id.* at 124; see Docket No. RM2016-13, Order No. 3507, Notice of Proposed Rulemaking on Changes Concerning Attributable Costing, September 9, 2016.

[47] Docket No. RM2016-3, Order No. 3641, Order Adopting Final Rules on Changes Concerning Attributable Costing, December 1, 2016.

[48] Docket No. RM2014-5, Petition to Improve Econometric Demand Equations for Market-Dominant Products and Related Estimates of Price Elasticities and Internet Diversion, May 2, 2014.

[49] Docket No. RM2014-5, Order No. 2117, Notice and Order Scheduling Technical Conference, July 9, 2014; Docket No. RM2014-5, Notice of Inquiry No. 1, June 12, 2015.

[50] Docket No. RM2014-5, Order Closing Docket, February 26, 2016, at 2-3 (Order No. 3100).

Competitive Products

The Commission reviews Competitive product rates to ensure compliance with three statutory requirements:

1. *39 U.S.C. § 3633(a)(1).* Competitive products must not be cross-subsidized by Market Dominant products. The Commission uses incremental costs to test whether Competitive products are being cross-subsidized; there is no cross-subsidy where the Commission finds that Competitive product revenues as a whole are equal to or exceed total incremental costs.

2. *39 U.S.C. § 3633(a)(2).* Each Competitive product must cover its attributable costs. In the ACD and in response to a Postal Service notice of change in Competitive product prices, the Commission reviews whether revenues for each Competitive product exceed its attributable costs to determine compliance with this objective.

3. *39 U.S.C. § 3633(a)(3).* This requires Competitive products to collectively cover an appropriate share of institutional costs. A Commission review determined that the contribution from Competitive products as a whole must be at least 5.5 percent of the Postal Service's total institutional costs.[51]

Within the constraints of these statutory criteria, Commission rules provide flexibility to the Postal Service to set prices for Competitive products.[52] For Competitive products featuring "rates of general applicability" (*i.e.,* products available to the general mailing public), the Commission completes its review within 30 days. For Competitive products featuring "rates not of general applicability" (*i.e.,* products with rates offered only to specific mailers), the Commission completes its review within 15 days.

Changes in Rates of General Applicability

On October 16, 2015, the Postal Service filed notice of changes in rates of general applicability for several domestic and international Competitive products.[53] The Postal Service also proposed related changes to the MCS. The Commission found that the new rates for Competitive products and related classification changes complied with 39 U.S.C. § 3633(a).[54]

The Postal Service also proposed a change in rates for Inbound Parcel Post (at UPU rates).[55] Under UPU regulations, the Postal Service and other designated postal operators may qualify for semi-annual increases to their "base" rates for inbound air parcels if they provide certain value-added services. These price increases are applied to the base rates effective January 1 and July 1 of each year. The Commission issued an order acknowledging revised rates for this product.[56]

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[51] Docket No. RM2012-3, Order No. 1449, Order Reviewing Competitive Products' Appropriate Share Contribution to Institutional Costs, August 23, 2012.
[52] *See* 39 C.F.R. part 3015.
[53] Docket No. CP2016-9, Notice of the United States Postal Service of Changes in Rates of General Applicability for Competitive Products Established in Governors' Decision No. 15-1, October 16, 2015.
[54] Docket No. CP2016-9, Order No. 2814, Order Approving Changes in Rates of General Applicability for Competitive Products, November 13, 2015, at 8-9.
[55] Docket No. CP2016-207, Notice of the United States Postal Service of Filing Changes in Rates Not of General Applicability for Inbound Parcel Post (at UPU Rates) and Application for Non-Public Treatment, June 14, 2016.
[56] Docket No. CP2016-207, Order No. 3404, Order Acknowledging Changes in Rates For Inbound Parcel Post (At UPU Rates), June 30, 2016.

Changes in Rates Not of General Applicability: NSAs

During FY 2016, the Commission approved new Competitive NSAs in 281 docketed proceedings. Table III-1 shows these NSAs, as well as those the Commission approved during each of the prior 6 fiscal years.[57] These NSAs required prior Commission approval for compliance with the statutory criteria.[58]

Table III-1: Competitive NSAs Approved by the Commission

Competitive NSAs	FY 2016	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011	FY 2010
Domestic	186	81	40	52	32	13	13
International	95	58	36	29	22	48	111
Total	281	139	76	81	54	61	124

The Commission completed its review of each Competitive NSA within an average of 13 days. Of the NSAs approved in FY 2016, 186 involved domestic shipping services, including Priority Mail Express, Priority Mail, Parcel Select, Parcel Return Service, and First-Class Package Service. The Commission determined that the negotiated rates for each NSA request complied with 39 U.S.C. § 3633(a).

The remaining 95 were Competitive international NSAs. The Commission reviewed the Postal Service's requests concerning the following products in FY 2016:

Inbound services:

- International Business Reply Service Competitive Contracts 3
- Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1

Outbound services:

- Global Expedited Package Services (GEPS) 3
- GEPS 5
- GEPS 6
- GEPS 7
- Global Plus 1C
- Global Plus 1D
- Global Plus 2C
- Global Plus 3
- Global Reseller Expedited Package (GREP) Contracts 2
- GREP Contracts 3
- GREP Contracts 4
- Priority Mail International Regional Rate Boxes Contract 1

In addition, non-published rates (NPR) products authorize the Postal Service to enter into contracts featuring negotiated rates without prior Commission approval. Such NPR contracts must comply with Commission classification and regulatory requirements, including pre-approved pricing formulas, minimum cost coverage, and documentation. The absence of pre-implementation review streamlines the approval process, providing the Postal Service with additional flexibility. The Commission has approved 14 NPR products since their inception in FY 2011. *See* Table III-2 on following page.

[57] Specifically, Table III-1 shows approved NSAs that were filed as new products to be added to the MCS and/or functionally equivalent to a baseline agreement in a previously approved MCS product.

[58] Since the enactment of the PAEA, the Commission has approved all requested Competitive NSAs filed by the Postal Service.

- GEPS – NPR 1
- GEPS – NPR 2
- GEPS – NPR 3
- GEPS – NPR 4
- GEPS – NPR 5
- GEPS – NPR 6
- GEPS – NPR 7
- GEPS – NPR 8
- GEPS – NPR 9
- GEPS – NPR 10
- International Merchandise Return Service Agreements with Foreign Postal Operators (IMRS-FPO) 1
- IMRS-FPO 2
- Priority Mail – NPR
- Priority Mail International Regional Rate Boxes – NPR

Table III-2 also shows the number of NPR contracts included in these NPR products.[59] The Priority Mail – NPR product is the only Competitive domestic NPR product currently in effect; the other 13 are Competitive international NPR products.

Table III-2: NPR Contracts Implemented by the Postal Service by Product

NPR Products	Number of Contracts						
	FY 2016	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011	Total
GEPS–NPR 1–10	243	91	124	129	141	168	896
IMRS-FPO 1 and 2	0	0	N/A	N/A	N/A	N/A	0
Priority Mail–NPR	0	0	1	2	3	3	9
Priority Mail International Regional Rate Boxes–NPR	0	0	0	0	N/A	N/A	0
Total	243	91	125	131	144	171	905

Review of Calculation of Assumed Federal Income Tax on Competitive Products

To further enhance transparency, the Commission established a proceeding to review the Postal Service's calculation of the FY 2014 assumed Federal income tax on Competitive products. Before FY 2014, the Commission had included this review as part of the ACD. On January 20, 2016, the Commission established Docket No. T2016-1 to separately review the calculations of the FY 2015 assumed Federal income tax on Competitive products and supporting documentation, appointed a Public Representative, and invited comments from interested parties.[60] On March 30, 2016, the Commission approved the Postal Service's calculation of the FY 2015 assumed Federal income tax on Competitive products.[61]

[59] For display purposes, Table III-2 lists all 10 GEPS—NPR products and both IMRS-FPO products as single line items.
[60] Docket No. T2016-1, Order No. 3038, Notice and Order Concerning the Review of the Calculation of the Assumed Federal Income Tax on Competitive Products, January 20, 2016.
[61] Docket No. T2016-1, Order No. 3196, Order Approving the Calculation of the FY 2015 Assumed Federal Income Tax on Competitive Products, March 30, 2016.

PHOTO PROVIDED BY THE USPS

CHAPTER IV | Universal Service Obligation and Postal Monopoly

PHOTO PROVIDED BY THE USPS

Background

In this chapter, the Commission provides its annual estimates of the cost of the Universal Service Obligation (USO) and the value of the postal monopoly. In its *Report on Universal Postal Service and the Postal Monopoly,* the Commission stated that the overarching USO of the Postal Service is set forth in 39 U.S.C. § 101(a), which states that the Postal Service must "provide postal services to bind the Nation together through the personal, educational, literary, and business correspondence of the people. It shall provide prompt, reliable, and efficient services to patrons in all areas and shall render postal services to all communities." The USO has seven principal attributes: geographic scope, product range, access, delivery, pricing, service quality, and an enforcement mechanism.[62]

The postal monopoly is the Postal Service's exclusive right to carry and deliver certain types of mail and deposit mail into mailboxes.[63] Unlike the cost of the USO (USO Cost), the Commission is not required to estimate the value of the postal monopoly. Nevertheless, the Commission provides estimates for both the USO Cost and the value of the postal monopoly to present a balanced perspective.

In 2008, the Commission estimated the USO Cost and the value of the postal monopoly in the USO Report. The Commission updates these estimates each year in the *Annual Report.*

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[62] Postal Regulatory Commission, *Report on Universal Postal Service and the Postal Monopoly,* December 19, 2008, at 18 (USO Report).
[63] *Id.* at 10 n.1.

Estimated USO Cost

The PAEA requires the Commission to estimate the costs incurred by the Postal Service in providing three types of public services or activities:

- Postal services to areas of the nation the Postal Service would not otherwise serve
- Free or reduced rates for postal services as required by Title 39
- Other public services or activities the Postal Service would not otherwise provide but for legal requirements

39 U.S.C. § 3651(b)(1)

The USO Cost is the total costs incurred by the Postal Service in providing these three types of public services or activities. Table IV-1 illustrates the estimated USO Cost for the last 5 fiscal years, FY 2011 to FY 2015.

Table IV-1: Estimated USO Cost ($ Billions)

	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
Postal Services to Areas of the Nation the Postal Service Would Not Otherwise Serve*	0.35	0.51	0.61	0.77	0.83
Estimated Revenue Not Received	1.63	1.62	1.65	1.64	1.94
Other Public Services or Activities	2.26	2.21	2.39	2.43	2.49
TOTAL*	4.24	4.34	4.65	4.84	5.26

* FY 2011 through FY 2014 figures differ from past *Annual Reports* because the Commission recalculated the costs of maintaining small post offices. See "Maintaining Small Post Offices" section below.

In this chapter, the Commission provides estimates of the costs incurred by the Postal Service in providing the public services or activities under section 3651(b)(1), describes related statutory requirements, and explains the methodologies used to estimate these costs.[64] The Commission also estimates the value of the postal monopoly.

[64] *See* 39 U.S.C. § 3651(b)(2).

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Postal Services to Areas of the Nation the Postal Service Would Not Otherwise Serve

The Commission must estimate the costs incurred by the Postal Service in providing postal services to areas of the Nation where, in the judgment of the Postal Regulatory Commission, the Postal Service either would not provide services at all or would not provide such services in accordance with the requirements of this title if the Postal Service were not required to provide prompt, reliable, and efficient services to patrons in all areas and all communities, including as required under the first sentence of [39 U.S.C.] section 101(b)[.][65]

The Commission determines these costs by combining the estimated costs of maintaining small post offices, the Alaska Air Subsidy, and Group E Post Office Boxes. Table IV-2 compares the costs of each one from FY 2011 to FY 2015.

Table IV-2: Estimated Costs of Providing Postal Services to Areas of the Nation the Postal Service Would Not Otherwise Serve ($ Millions)

	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
Maintaining Small Post Offices*	209	366	468	610	673
Alaska Air Subsidy	107	112	114	122	123
Group E Post Office Boxes	33	33	31	34	36
TOTAL*	349	511	613	766	832

* FY 2011 through FY 2014 figures differ from past *Annual Reports* because the Commission recalculated the costs of maintaining small post offices. See "Maintaining Small Post Offices" section below.

As shown in Table IV-2, the estimated cost of providing postal services to areas of the nation the Postal Service would not otherwise serve declined at an accelerated pace between FY 2011 and FY 2015. This decline was due primarily to the large reductions in the cost of maintaining small post offices as described on the following page.

[65] *Id.* § 3651(b)(1)(A). 39 U.S.C. § 101(b) requires the Postal Service to "provide a maximum degree of effective and regular postal services to rural areas, communities, and small towns where post offices are not self-sustaining." *Id.* § 101(b).

MAINTAINING SMALL POST OFFICES

The Postal Service maintains small post offices, which are generally located in rural or remote areas, as part of its duty "to establish and maintain postal facilities of such character and in such locations, that postal patrons throughout the Nation will, consistent with reasonable economies of postal operations, have ready access to essential postal services."[66] The Postal Service uses CAG classifications A to L to categorize post offices based on amount of revenue generated. Order No. 2837 at 1 n.2. Small post offices are those that fall within CAG K and L classifications; they have higher unit transaction costs than larger post offices and lower levels of annual revenue.[67]

The Commission determines the cost of maintaining small post offices by estimating the amount the Postal Service would save if rural carriers on the street provided the same services as those provided at small post offices, as well as the amount of revenue lost from existing CAG K and L Post Office Boxes. The Commission uses the Rural Mail Count to estimate the cost of rural carriers providing retail services and for new delivery service to those who would no longer have a CAG K and L Post Office Box.[68]

On November 24, 2015, the Commission approved a Postal Service proposal to change an accepted analytical principle by combining Cost Segments 3 and 4, the costs for post office clerks in CAGs A to L. Order No. 2837 at 12. The Postal Service submitted this proposal to account for recent changes in the staffing of small post offices resulting largely from the Postal Service's implementation of the Post Office Structure Plan (POStPlan) and a related arbitration ruling. *Id.* at 2, 11.

STILLWATER, MN/USA PHOTO BY KEN WOLTER

Table IV-2 lists the estimated costs of maintaining small post offices from FY 2011 to FY 2015 using a modified methodology. The modifications are an effort to incorporate all of the categories of employees who perform functions that were previously performed primarily by postmasters, and to accurately identify those costs associated with this element of the USO Cost.

Table IV-3 disaggregates the cost by component and illustrates the recent large shifts between these components. It also illustrates changes in employee categories staffing CAG K and L post offices. Postmaster salary costs (along with overhead and other personnel and non-personnel related costs) have dropped sharply since FY 2013, while the costs of other employees assuming postmaster duties have had corresponding increases. Postmaster direct and indirect costs decreased from $659 million in FY 2011 to $26 million in FY 2015. Conversely, in FY 2013 and FY 2014, CAG L leave replacement costs were more than double typical fiscal year annual costs. Also, CAG K clerk costs increased significantly in FY 2015.

[66] 39 U.S.C. § 403(b)(3).
[67] USO Report, Appendix F, Section 3 (Robert H. Cohen and Charles McBride, "Estimates of the Current Costs of the USO in the U.S." at 26).
[68] The Rural Mail Count classifies all remunerable activities of rural carriers as either post office or street activities. However, some post office activities can occur on the street. For example, even though it occurs on the street, parcel acceptance is considered a post office activity because it can substitute for a customer sending a parcel at a post office window.

Table IV-3: Estimated Cost Savings from Closing CAG K and L Post Offices
Derivation of Updated Costs of Maintaining Small Post Offices ($ Millions)

Selected CAG K and L Post Offices Annual Operating Costs	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
CAG K and L Postmasters[a]	26	228	332	587	659
CAG L Leave Replacements	102	216	219	105	96
CAG K Clerks	176	13	6	5	4
Total Potential Operating Costs Saved (If CAG K and L Post Offices Closed)	304	457	558	698	759

Annual Estimated Cost Saving Adjustments (If CAG K and L Post Offices Closed)	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
Rural Carrier Now Provides Retail Services Costs[b]	17	16	16	16	17
Rural Carrier Now Provides Delivery Service (CAG K and L Post Office Boxes No Longer Available)[c]	42	41	41	40	40
CAG K and L Post Office Boxes Revenue Foregone[d]	36	33	33	32	30
Total Annual Cost Savings Adjustment	96	91	89	88	87

Updated Costs of Maintaining Small Post Offices	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
(Potential Operating Costs Saved Less Cost Savings Adjustments)	209	366	468	610	673

Note: The sum of individual row components may not equal totals due to rounding

[a] Consistent with the USO Report, previous *Annual Reports* used CAG K and L postmaster salary costs (along with overhead and other personnel and non-personnel related costs) to represent the total potential operating costs saved if CAG K and L post offices closed. Postmaster costs at CAG K and L post offices were derived by using the postmaster salary costs from the Postmaster Position Schedule CAG group proportions to distribute total postmaster (less CAG L leave replacements) costs to the CAG K and L group. However, due to recent staffing changes at small post offices, the costs of maintaining small post offices shown in Table IV-2 were recalculated to also include the CAG L leave replacement (postmaster relief employees) and CAG K clerk costs in addition to the postmasters costs in the potential operating costs saved total. The costs of maintaining small post offices in the FY 2012 and FY 2013 Annual Reports inadvertently listed the unadjusted total potential CAG K and L postmaster operating costs saved.

[b] The annual number of CAG K and L retail transactions was approximated using the most currently available data: the FY 2010 retail transactions per revenue dollar and the FY 2013 POStPlan revenues in Docket No. N2012-1. The annual number of CAG K and L retail transactions was approximated to be about 142 million and was used in this calculation for the fiscal years shown in the table.

[c] FY 2010 CAG K and L Post Office Box volumes were used to estimate the number of new delivery points (for those CAG K and L Post Office Boxes no longer available).

[d] The FY 2010 CAG K and L Post Office Box volumes were used with the respective current fiscal year Post Office Box unit revenue (billing determinants) to estimate fiscal year CAG K and L Post Office Boxes revenue foregone.

Sources:

Postmaster Position Schedule CAG Group Proportions: Library Reference 32 in Docket Nos. ACR2011, ACR2012, ACR2013, ACR2014, and ACR2015 (CRA "B" Workpapers, "I-Forms" workbook, "I-CS01.0.2" tab).

Postmasters, CAG L Leave Replacement and Clerks CAG K costs: Library Reference 5 in Docket Nos. ACR2011, ACR2012, ACR2013, ACR2014, and ACR2015 (Cost Segments and Components Reconciliation to Financial Statement and Account Reallocation, "seg 1" and "seg 4" tabs in workbook).

Rural Mail Count: Library Reference 40 in Docket Nos. ACR2011, ACR2012, ACR2013, ACR2014, and ACR2015.

ALASKA AIR SUBSIDY

Alaska Bypass Service allows mailers to ship goods such as food and other cargo on pallets directly to rural customers in Alaska. Commercial airline carriers deliver goods on pallets to hub airports in either Anchorage or Fairbanks. Smaller airline companies or independent pilots then break down these pallets and deliver the goods to remote communities accessible only by air, which are commonly called bush sites. The shipped goods "bypass" the Postal Service's network.

With Alaska Bypass Service, the Postal Service pays for the cost of air transportation from hub airports to bush sites. The Alaska Air Subsidy is the difference between this cost of air transportation from hub airports to bush sites and the average cost of ground transportation if it were available. The Commission previously concluded that the Alaska Air Subsidy is part of the USO.[69] The Alaska Air Subsidy has declined since FY 2011 from $123 million to $107 million in FY 2015.

GROUP E POST OFFICE BOXES

Group E Post Office Boxes are provided free of charge to postal customers who do not receive mail delivery.[70] The Postal Service provides this service to address potential discrimination issues arising from instances where customers do not receive carrier delivery. In FY 2011, the Commission approved treating the cost of providing Group E Post Office Boxes as an institutional cost to more equitably distribute the USO Cost. The Commission also concluded that this treatment was analogous to, and consistent with, the treatment of the Alaska Air Subsidy.[71] Consequently, the Commission approved including the cost of Group E Post Office Boxes, which are primarily facility-related, in estimating the USO Cost. In FY 2015, Group E Post Office Boxes cost $33 million.

Free or Reduced Rates

The Commission must estimate the costs incurred by the Postal Service in providing "free or reduced rates for postal services as required by [Title 39.]"[72] The Commission estimates the costs of providing free or reduced rates for postal services by combining preferred rate discounts net of costs and the negative contribution of Periodicals (Periodicals Losses). Table IV-4 shows the estimated revenue not received as a result of preferred rate discounts and Periodicals Losses between FY 2011 to FY 2015.

Table IV-4: Estimated Revenue Not Received ($ Millions)

	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
Preferred Rate Discounts Net of Costs	1,116	1,114	1,130	974	1,329
Periodicals Losses	512	509	521	670	609
TOTAL	1,628	1,623	1,651	1,644	1,938

[69] USO Report at 139.
[70] Docket No. RM2011-9, Order No. 744, Order Concerning Analytical Principles Used in Periodic Reporting (Proposal One), June 9, 2011, at 2.
[71] *Id.* at 4.
[72] 39 U.S.C. § 3651(b)(1)(B). The Postal Service provides free postage for blind and disabled persons and for overseas voting. *Id.* §§ 3403, 3406. The Postal Service receives appropriated funds reimbursing it for providing free postage. *Id.* § 2401(c). For this reason, the cost of providing free postage is not included in the USO Cost.

PREFERRED RATE DISCOUNTS NET OF COSTS

39 U.S.C. § 3626 requires the Postal Service to provide reduced rates for preferred rate categories in Standard Mail, Periodicals, and Library Mail. FY 2015 ACD at 41. The Commission determines estimated revenue not received by quantifying the difference in revenue between mail that is statutorily required to receive a discount and the revenue the Postal Service would have received if those mail pieces were not discounted. In that case, rates for these mail pieces would be higher, resulting in a loss of volume and, consequently, lower costs.

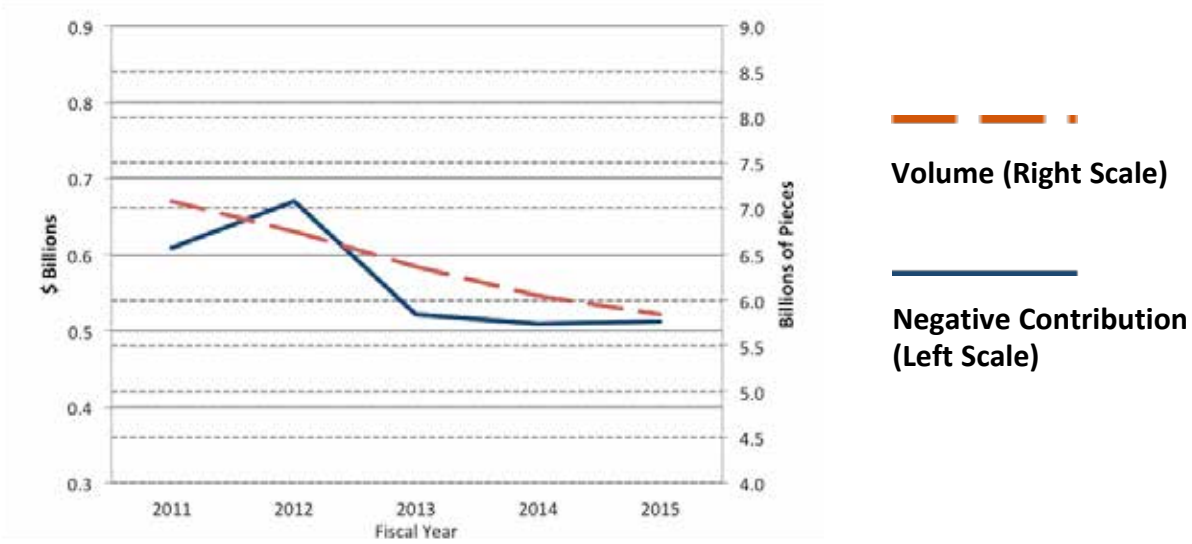
PERIODICALS LOSSES

The PAEA's price cap does not allow the Postal Service to fully recover Periodicals Losses through rate increases.[73] It is assumed that, if not for the price cap, the Postal Service would raise Periodicals rates to the level necessary to cover attributable costs. Accordingly, the Commission considers these losses to be part of the USO Cost. Periodicals Losses are the annual amount by which Periodicals attributable cost exceeds revenue.

Table IV-4 illustrates that although there was some variation year-to-year, overall Periodicals Losses declined. During the 5-year period shown, FY 2012 had the largest overall loss at $670 million, while in FY 2015, the overall loss increased slightly to $512 million over the FY 2014 loss of $509 million.

Figure IV-1 shows the trend of Periodicals Losses and volumes from FY 2011 to FY 2015. The largest loss in FY 2012 was due to the largest increase in attributable cost per piece for the period and a slight decrease in revenue per piece between FY 2011 and FY 2012.[74] In FY 2015, a slight increase in revenue per piece was not sufficient to offset the increase in cost per piece. Consequently, contribution per piece decreased, resulting in a slight increase in Periodicals Losses between FY 2014 and FY 2015.[75]

Figure IV-1: Periodicals Losses of Contribution and Volumes



[73] These losses were initially called "Losses on Market Dominant Products" in past *Annual Reports.* The Commission later clarified that the USO Cost only includes Periodicals Losses. Postal Regulatory Commission, *Annual Report to the President and Congress Fiscal Year 2012,* January 3, 2013, at 37 n.3. Losses on other unprofitable Market Dominant products are not included because those products are in classes that were profitable overall. USO Report at 134.

[74] *See* FY 2014 ACD at 34.

[75] *See* FY 2015 ACD at 43.

Other Public Services or Activities

The Commission must estimate the costs incurred by the Postal Service in providing "other public services or activities which, in the judgment of the Postal Regulatory Commission, would not otherwise have been provided by the Postal Service but for the requirements of law."[76] Currently, these costs include the costs of providing Six-Day Delivery and uniform rates for First-Class Mail and Media Mail/Library Mail. Table IV-5 shows the costs of providing these public services or activities from FY 2011 to FY 2015.

Table IV-5: Other Public Services or Activities the Postal Service Would Not Provide But for Legal Requirements ($ Millions)

Public Service or Activity	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
Six-Day Delivery	2,074	2,080	2,212	2,240	2,250
Uniform First-Class Mail Rates	86	93	109	117	122
Uniform Media Mail/Library Mail Rates	101	37	70	71	115
TOTAL	2,261	2,210	2,391	2,428	2,487

SIX-DAY DELIVERY

Since 1984, appropriations bills have included a provision requiring the Postal Service to continue providing Six-Day Delivery.[77] The cost of providing Six-Day Delivery is measured as the estimated savings the Postal Service would achieve by providing residential delivery service 5 days a week instead of 6 days a week. Table IV-5 shows the cost of Six-Day Delivery from FY 2011 to FY 2015. The cost of Six-Day Delivery declined from $2.25 billion in FY 2011 to $2.07 billion in FY 2015.

For FY 2008 and FY 2009, the Commission estimated the cost of providing Six-Day Delivery based on the methodology described in the USO Report. For FY 2010 to FY 2015, the Commission updated its methodology to reflect its findings in its Advisory Opinion on Elimination of Saturday Delivery.[78] The update included additional components, such as the costs of mail processing and transportation; improvements in calculating average wage rates and overhead costs; and more disaggregated methods of estimating mail processing, transportation, and delivery costs.

[76] 39 U.S.C. § 3651(b)(1)(C).
[77] *See, e.g.,* Consolidated Appropriations Act, 2016, Pub L. No. 114-113, 129 Stat. 2242, 2464 (2015) ("6-day delivery and rural delivery of mail shall continue at not less than the 1983 level").
[78] Docket No. N2010-1, Advisory Opinion on Elimination of Saturday Delivery, March 24, 2011.

UNIFORM RATES

Rates for First-Class Mail must be uniform throughout the United States.[79] To determine the cost of uniform First-Class Mail rates, the Commission estimates the increased contribution that the Postal Service would earn if dropship discounts were allowed for workshared First-Class Mail. Table IV-5 shows the cost of uniform First-Class Mail rates. In FY 2015, the cost of uniform First-Class Mail rates declined from $93 million in FY 2014 to $86 million in FY 2015.

Media Mail/Library Mail rates must be uniform for mail of the same weight and must not vary with the distance transported.[80] The Commission estimates the cost of the distance component by assuming that without this requirement, Media Mail/Library Mail would provide the unit contribution of Bound Printed Matter, a proxy that does not have this restriction. The Commission estimates the additional unit contribution by determining the difference between the unit contributions of Bound Printed Matter and Media Mail/Library Mail. Media Mail/Library Mail total volumes are then multiplied by the estimated additional unit contribution to produce an estimate of the total additional contribution if Media Mail/Library Mail rates were not uniform.

In FY 2015, the estimated cost of providing uniform Media Mail/Library Mail rates was $101 million. The substantial increase in cost between FY 2014 and FY 2015 is due primarily to the large decrease in the unit contribution of Media Mail/Library Mail.[81]

OTHER PUBLIC SERVICES OR ACTIVITIES

On November 17, 2015, the Commission issued an order interpreting "other public services or activities" under 39 U.S.C. § 3651(b)(1)(C).[82] The Commission interpreted "public services or activities" to comprise statutorily-required offerings and actions by the Postal Service that are "public facing." They must also relate to the USO and be similar in type to the services or activities enumerated under 39 U.S.C. §§ 3651(b)(1)(A) and (B). The Postal Service must have an active role in offering, supplying, or performing "public services or activities."

For each public service or public activity, the Commission must determine whether a hypothetical profit-maximizing Postal Service would provide it absent statutory requirements. If a hypothetical profit-maximizing Postal Service would not provide a public service or activity absent statutory requirements, the Commission would report the full cost of the public service or activity in the *Annual Report.* If it were determined that a hypothetical profit-maximizing Postal Service would provide all of a public service or activity absent statutory requirements, the cost would not be reported. If it were determined that a hypothetical profit-maximizing Postal Service would provide only part of a public service or activity absent statutory requirements, the Commission would conduct a separate cost analysis to determine how much of the cost of the public service or activity should be reported.

The Commission stated it would apply the interpretation set forth in its order if it determines that the costs of other public services or activities should be included in the *Annual Report.* The Commission has determined that no new public services or activities should be added at this time.

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[79] 39 U.S.C. § 404(c).

[80] *Id.* § 3683.

[81] The large decrease in the unit contribution of Media Mail/Library Mail was due to the 26 percent increase in the unit attributable cost for Media Mail/Library Mail in FY 2015. *See* Financial Analysis of the United States Postal Service Financial Results and 10-K Statement, March 29, 2016, at 67-68.

[82] Docket No. PI2014-1, Order No. 2820, Order Interpreting 39 U.S.C. § 3651(b)(1)(C), November 17, 2015.

Value of the Postal Monopoly

The postal monopoly is the Postal Service's exclusive right to carry and deliver certain types of mail and deposit mail into mailboxes. The mailbox monopoly is the Postal Service's exclusive right to deliver to and collect from mailboxes.[83] The letter monopoly is the Postal Service's exclusive right to carry and deliver most addressed, paper-based correspondence.[84]

The value of the postal monopoly is an estimate of the profit that the Postal Service would lose if both the mailbox and letter monopolies were lifted, and the Postal Service were subject to competition for mail currently covered by the postal monopoly.

Table IV-6 shows the values of the postal and mailbox monopolies from FY 2011 to FY 2015.[85] The increase in the estimated value of the postal monopoly from FY 2013 to FY 2015 is largely due to increases in the percentage of mail that is considered contestable.[86] The value of the mailbox monopoly is estimated based on contestable mail volumes in Periodicals, Standard Mail ECR, and Parcel Select. Changes in the volume of contestable mail affect the number of profitable routes the competitor could deliver to and the amount of contribution the Postal Service would lose if the competitor captured the contestable mail on those routes.

Table IV-6: Values of the Postal and Mailbox Monopolies ($ Billions)

	FY 2015	FY 2014	FY 2013	FY 2012	FY 2011
Postal Monopoly	**5.45**	**4.61**	**3.93**	**3.28**	**3.34**
Mailbox Monopoly	**1.03**	**0.77**	**0.81**	**0.70**	**0.91**

The Commission used the model described in the USO Report to update current estimates.[87] The model assumes that the competitor will "win" or "skim" all of the contestable mail on a route if the revenue it would earn from these mail volumes is greater than the fixed and attributable costs related to the volumes. The model also assumes the competitor would deliver only local and regional mail to focus on the most profitable delivery routes and avoid the need for significant capital to establish a processing and transportation network.

Even with the postal monopoly, competitors still deliver material (*e.g.,* newspapers' weekly advertising supplements) that might otherwise be sent via the Postal Service. If the mailbox monopoly alone were lifted, competitors could deliver and deposit into mailboxes products that fall outside of the letter monopoly, such as Periodicals, unaddressed saturation mail, catalogs over 24 pages, and letters over 12.5 ounces. The letter monopoly prevents competitors from delivering certain mail that is directed to a specific person or address, such

[83] 18 U.S.C. § 1725.
[84] The letter monopoly is codified in the Private Express Statutes. *See* 18 U.S.C. §§ 1693–1699 and 39 U.S.C. §§ 601–606.
[85] Subtracting the value of the mailbox monopoly from the value of the postal monopoly does not yield the value of the letter monopoly because there is an overlap in the contestable mail and a different frequency of delivery by the competitor. A separate estimate of the value of the letter monopoly alone (retaining the mailbox monopoly) is not provided. Without access to mailboxes, it is unlikely that the competitor could successfully capture mail directed to a specific person or address because those mail pieces are delivered to and collected from mailboxes.
[86] Contestable mail is mail that is dropshipped to the processing facility or delivery unit closest to its destination. The competitor would need to perform little or no mail processing to prepare it for delivery.
[87] *See* USO Report at 143-52.

as First-Class Presorted Letters/Postcards and Standard Mail Letters. If the letter monopoly were also lifted, this restriction would not apply.

The key variables for estimating the values of the postal and mailbox monopolies are the competitor's delivery frequency, the cost of entry to the competitor, the rates charged by the competitor, and the volume of the contestable mail. The model assumes that the competitor is 10 percent more efficient than the Postal Service, but needs to offer a 10 percent discount to entice customers to switch from the Postal Service. Because this discount offsets the competitor's efficiency advantage, reducing delivery frequency is the only way for the competitor to lower delivery costs below that of the Postal Service.[88]

The model currently evaluates the competitor's entry for each route regardless of the extent of route clustering. Focusing on routes in the same cluster or area would reduce the competitor's fixed costs.[89] Also, because the model assumes that the competitor does not incur mail processing costs, values of the postal and mailbox monopolies do not reflect the cost of sorting to carrier routes, which is necessary to deliver mail presorted to the 5-digit ZIP Code. The model also does not account for mailers' switching costs or brand loyalty.[90] In addition, bulk parcels, which are Competitive products, are considered contestable mail.

[88] The current model assumes the competitor will deliver mail 3 days a week under the postal monopoly and 1 day a week under the mailbox monopoly.

[89] The Commission would need route-level geographic-specific data to account for clustering. Further improvements could be made by assuming the competitor would design routes to more efficiently deliver the contestable mail. However, this would require information about volume delivered to each stop that is not currently available.

[90] Although the model assumes a 10 percent discount would be necessary to entice customers to switch, brand loyalty, inertia, the need to prove quality, and other factors affect the pace at which customers would switch from the Postal Service to a competitor. The model assumes a competitor would capture 100 percent of the contestable mail on routes that are skimmed. See USO Report at 149. However, some customers may not switch to a competitor even if a discount were offered.

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CHAPTER V | Other Proceedings and Actions

PHOTO BY JOE RAVI

United States Supreme Court.

In addition to dockets that directly relate to various objectives, the Commission initiates orders and performs work on other matters. These matters include rules, regulations, and procedures on rates, mail classifications, service standards, public inquiries, rulemakings, formal complaints, and post office closing appeals.

In FY 2016, the Commission:

- Conducted five public inquiry dockets to seek public input on important issues
- Initiated three rulemaking dockets to clarify its regulations and procedures
- Adjudicated two post office closing appeals and one formal complaint
- Assisted the Department of Justice with the defense of Commission orders appealed to the D.C. Circuit
- Provided views to the United States Department of State (State Department) on international postal policy issues

Public Inquiries

Section 701 Report

Section 701 of the PAEA requires the Commission to submit a report to the President and Congress at least every 5 years (Section 701 Report). In this report, the Commission must describe how PAEA amendments are operating and recommend legislation or other measures to improve the effectiveness or efficiency of postal laws.[91]

The Commission issued its first Section 701 Report in FY 2011.[92] On April 14, 2016, the Commission established Docket No. PI2016-3 to obtain public comment on its second Section 701 Report.[93] After considering comments received, in FY 2017, the Commission issued its second Section 701 Report.[94] It is available on the Commission's website at **www.prc.gov.**

Scope of Public Service or Activity Cost Reporting

In the *Annual Report,* the Commission must include, among other things, an estimate of the Postal Service's costs incurred in providing "other public services or activities which, in the judgment of the Postal Regulatory Commission, would not otherwise have been provided by the Postal Service but for the requirements of law." 39 U.S.C. § 3651(b)(1)(C). As described in detail in Chapter IV, the Commission issued an order interpreting this statutory provision on November 17, 2015. *See* Order No. 2820.

Jurisdiction over Post Office Closings and Consolidations

The Commission is authorized to review appeals of Postal Service decisions to "close or consolidate any post office." 39 U.S.C. § 404(d)(5). On December 10, 2015, the Commission established a proceeding to solicit comments on issues related to the Commission's jurisdiction under section 404(d).[95] The Commission considered the comments received and stated that they will be helpful when deciding future cases and preparing the second Section 701 Report. The Commission concluded that no further action was necessary and closed the docket.[96]

Service Performance

The Commission considered issues related to service performance measurement and reporting in two public inquiry dockets. First, in Docket No. PI2015-1, the Commission continued discussions with the Postal Service regarding its proposal to develop a new internal service performance measurement system for several Market Dominant products. Second, in Docket No. PI2016-1, the Commission issued a final order enhancing the Postal Service's reporting of service performance measurement data. These dockets are discussed in detail in Chapter III.

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91 Pub L. 109-435, 120 Stat. 3198 (2006), section 701(a).
92 Postal Regulatory Commission, *Section 701 Report, Analysis of the Postal Accountability and Enhancement Act of 2006,* September 22, 2011.
93 Docket No. PI2016-3, Order No. 3238, Notice and Order Seeking Comments on Report to the President and Congress Pursuant to Section 701 of the Postal Accountability and Enhancement Act, April 14, 2016.
94 Postal Regulatory Commission*, Section 701 Analysis of the Postal Accountability and Enhancement Act of 2006,* November 14, 2016.
95 Docket No. PI2016-2, Order No. 2862, Notice and Order Seeking Comments on Commission Jurisdiction Over Postal Service Determinations to Close or Consolidate Post Offices, December 10, 2015.
96 Docket No. PI2016-2, Order No. 3456, Order Concluding Proceeding, August 8, 2016.

PHOTO BY EDDTORO

A postal carrier delivering mail in the Bronx, New York.

Rulemakings on Commission Procedures

Ex Parte Rules

On January 8, 2016, the Commission initiated a rulemaking to revise and reorganize its rules concerning ex parte communications.[97] These rules apply to all verbal, written, and electronic interactions between Commission decision-making personnel and the Postal Service or public stakeholders in matters before the Commission. The Commission provided several reasons for revising the existing rules, such as removing redundant regulations, clarifying who qualifies as Commission "decision-making personnel," removing references to rate and classification cases that the PAEA eliminated, and providing guidance on ex parte communications outside of nature of service cases, post office closings appeals, and complaints.

After considering comments received, the Commission issued an order adopting final rules for ex parte communications on June 22, 2016.[98] The final rules contained requirements for all proceedings before the Commission with specific exceptions. They set forth a permit-but-disclose approach to ex parte communications and clarified when penalties for violating ex parte communication rules apply.

[97] Docket No. RM2016-4, Order No. 3005, Notice of Proposed Rulemaking Regarding Ex Parte Communications, January 8, 2016.
[98] Docket No. RM2016-4, Order No. 3379, Order Adopting Final Rules for Ex Parte Communications, June 22, 2016.

Amendments to Commission Publishing Rules

On January 20, 2016, the Commission initiated a rulemaking to consider amendments to the Commission's rules concerning the Market Dominant and Competitive product lists.[99] The proposed amendments were designed to reduce duplicative efforts and streamline the process for reviewing Postal Service requests filed under 39 C.F.R. part 3020.[100]

After considering comments received, the Commission determined to make no changes to the rules at this time.[101] The Commission expects the Postal Service to file hundreds of requests annually. The Commission will continue to explore ways to improve efficiency without sacrificing transparency or accountability. For example, Commission startup and Federal Register notices now combine all Postal Service NSA requests and notices filed on a given day.

Product Lists and Mail Classification Schedule

On April 6, 2016, the Commission initiated a rulemaking proposing to replace existing regulations governing product lists and the MCS.[102] On June 8, 2016, after considering comments received, the Commission adopted the proposed rules as final rules with one minor clarification.[103] The final rules codify the current practice of publishing the MCS on the Commission's website, noticing changes to the product lists in the Federal Register, and publishing product lists in the *Code of Federal Regulations*.

PHOTO BY ANDREY POPOV

[99] Docket No. RM2016-5, Order No. 3039, Notice of Proposed Rulemaking Regarding Minor Amendments to Commission Rules Regarding Proposed Modifications to the Mail Classification Schedule, January 20, 2016.
[100] The Postal Service is statutorily required to independently notice its requests to change the product lists in the *Federal Register*. *See* 39 U.S.C. § 3642(d)(1).
[101] Docket No. RM2016-5, Order No. 3356, Order Closing Docket, June 7, 2016.
[102] Docket No. RM2016-8, Notice of Proposed Rulemaking Concerning Product Lists and the Mail Classification Schedule, April 6, 2016 (Order No. 3213).
[103] Docket No. RM2016-8, Order No. 3360, Final Rule Concerning Product Lists and the Mail Classification Schedule, June 8, 2016. The final rules clarified that the Commission will update the MCS in accordance with its regulations.

PHOTO PROVIDED BY THE USPS

Post Office Closing Appeals

The Commission adjudicated two post office closing appeals in FY 2016. First, the Commission dismissed an appeal of the Westbrookville, New York post office closing.[104] The Commission considered the appeal moot because the Postal Service executed a permanent contract with a new supplier to provide continued postal services to the community.

Second, the City of Winchester, Illinois appealed the Postal Service's decision to temporarily suspend operations at the Winchester post office. A few days later, the City of Winchester moved to dismiss the appeal because the Postal Service executed a lease for the post office, permitting it to remain open. For this reason, the Commission dismissed the appeal as moot.[105]

Goodman Complaint

In FY 2015, James and Rosalyn Goodman filed a complaint alleging that the Postal Service violated postal regulations and policies and other federal laws by suspending delivery to Rosalyn Goodman's residence.[106] On July 15, 2015, the Commission found that the Postal Service's regulations were reasonable and dismissed the complaint.[107]

On October 16, 2015, Goodman moved to vacate the Commission's order dismissing the complaint,[108] which the Postal Service answered.[109] The Commission denied the motion to vacate because no new arguments of fact or law were presented.[110]

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[104] Docket No. A2016-1, Order No. 3364, Order Dismissing Appeal, June 14, 2016.
[105] Docket No. A2016-2, Order No. 3357, Order Granting Motion to Dismiss, June 7, 2016.
[106] Docket No. C2015-2, First Amended Complaint of James D. Goodman and Rosalyn Goodman Regarding Failure and Refusal to Deliver Mail by the US Postal Service to 1600 Entre Colinas Place, Pomona California, April 23, 2015.
[107] Docket No. C2015-2, Order No. 2585, Order Granting Motion to Dismiss, July 15, 2015.
[108] Docket No. C2015-2, Motion to Vacate Order Granting Motion to Dismiss and Other Relief, October 16, 2015.
[109] Docket No. C2015-2, United States Postal Service Answer in Opposition to Complainants' Motion to Vacate Order Granting Motion to Dismiss and Other Relief, October 23, 2015.
[110] Docket No. C2015-2, Order No. 2850, Order Denying Motion to Vacate Order Granting Motion to Dismiss and Other Relief, December 4, 2015.

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District of Columbia Court of Appeals building with Abraham Lincoln statue.

Court Appeals

The following cases were before the D.C. Circuit during FY 2016.

Remand of Exigent Price Adjustment

In FY 2014, the Commission granted the Postal Service's request for an exigent price adjustment under 39 U.S.C. § 3622(d)(1)(E). Order No. 1926 at 193. The Commission found that the Postal Service was entitled to collect $2.766 billion in 2014 after-rates contribution as a result of losses it incurred due to the Great Recession. *Id.* at 106. The Postal Service petitioned the D.C. Circuit for review of the Commission's order.[111] The court largely affirmed the Commission's order, but vacated the Commission's method for counting mail volume losses due to the Great Recession. 790 F.3d at 196. It remanded the case to the Commission for further proceedings. *Id.* at 197.

Responding to the court's decision, the Commission initiated Docket No. R2013-11R to establish procedures on remand and solicit comments.[112] On June 29, 2015, after considering comments received, the Commission issued Order No. 2623 that resolved issues on remand. The Commission accepted the Postal Service's methodology for counting mail volume losses due to the Great Recession. Order No. 2623 at 41-46. It found that the Postal Service was entitled to recover $1.191 billion in additional contribution. *Id.* at 62.

The Postal Service petitioned the D.C. Circuit for review of Order No. 2623.[113] The court held oral argument on September 20, 2016. On November 15, 2016, the court issued its decision dismissing the Postal Service's appeal for lack of jurisdiction.[114]

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[111] *United States Postal Service v. Postal Regulatory Commission,* No. 14-1010 (D.C. Cir. filed Jan. 23, 2014).
[112] Docket No. R2013-11R, Order No. 2540, Notice and Order Establishing Procedures on Remand and Suspending the 45-Day Notice Requirement for Removing the Exigent Surcharge, June 12, 2015.
[113] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1297 (D.C. Cir. filed Aug. 28, 2015).
[114] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1297, 2016 WL 6694950 (D.C. Cir. Nov. 15, 2016).

Round-Trip Mailer

In FY 2013, the Postal Service filed a request to add a new product, Round-Trip Mailer (RTM), to the Competitive product list.[115] The proposed RTM featured equal prices for letter-shaped and flat-shaped round-trip DVD mail. The Postal Service intended for the RTM to replace existing Market Dominant product offerings for round-trip DVD mail.

On December 23, 2014, the Commission issued an order denying the request because the Postal Service failed to demonstrate that RTM met the requirements for inclusion on the Competitive product list under 39 U.S.C. § 3642(b).[116] The Commission found that the Postal Service failed to provide sufficient evidence to demonstrate that it did not exercise "sufficient market power" to "effectively set the price of [the Round-Trip Mailer] substantially above costs, raise prices significantly, decrease quality, or decrease output, without risk of losing a significant level of business to other firms offering similar products." Order No. 2306 at 2-3. The Commission denied the request without prejudice to the filing of a new, adequately supported request. *Id.* at 3.

On January 21, 2015, the Postal Service petitioned the D.C. Circuit to review the Commission's order.[117] On March 22, 2016, the D.C. Circuit denied the petition for review.[118] The court affirmed the Commission's decision as "more than just reasonable; its decision seems rather compelling." *Id.* at 886. The court also identified flaws with the Postal Service's arguments. For example, the court noted that the Postal Service failed to show that it lacked market power in the DVD-by-mail distribution market. *Id.* at 886-87.

Complaint of the American Postal Workers Union

In FY 2013, the American Postal Workers Union (APWU) filed a complaint alleging that the Postal Service failed to adhere to the service standards established as a result of the Mail Processing Network Rationalization initiative.[119] The Commission granted the Postal Service's motion to dismiss the APWU complaint.[120]

Subsequently, APWU filed a motion for reconsideration, which the Commission granted, vacating its previous order dismissing the complaint.[121] The Commission, however, found that service standards outlined in 39 C.F.R. § 121.1 represent expectations that cannot be violated *per se.* Rather, the Commission assesses service performance by determining whether the Postal Service met its performance goals. The Commission stated that it already evaluated the Postal Service's compliance with its service standards and directed the Postal Service to take remedial action. For these reasons, the Commission dismissed the complaint.

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[115] Docket No. C2009-1R, Request of the United States Postal Service Under Section 3642 to Create Round-Trip Mailer Product, July 26, 2013.
[116] Docket Nos. MC2013-57 and CP2013-75, Order Denying Request, December 23, 2014 (Order No. 2306).
[117] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1018 (D.C. Cir. filed Jan. 21, 2015).
[118] *United States Postal Service v. Postal Regulatory Commission,* 816 F.3d 883 (D.C. Cir. 2016).
[119] Docket No. C2013-10, Complaint of American Postal Workers Union, AFL-CIO Regarding Violations of 39 U.S.C. 3661 and 3691, September 5, 2013. *See also* Docket No. C2013-10, Amended Complaint of American Postal Workers Union, AFL-CIO Regarding Violations of 39 U.S.C. § 3691 and 39 C.F.R. § 121.1, December 13, 2013.
[120] Docket No. C2013-10, Order No. 2000, Order Dismissing Complaint, February 27, 2014.
[121] Docket No. C2013-10, Order No. 2512, Order Granting Motion for Reconsideration and Granting Motion to Dismiss, May 27, 2015.

On May 29, 2015, APWU filed a petition for review before the D.C. Circuit.[122] In FY 2017, the court denied the petition for review.[123] The court found that the Commission's method for evaluating when service standards have been violated was reasonable. It also found the Commission's interpretation that service standards should be measured with separately defined performance goals was reasonable and entitled to deference. The court stated that the Commission logically construed APWU's amended complaint and that dismissing the complaint was not arbitrary or capricious.

First-Class Mail Parcels Transfer

On November 14, 2014, the Postal Service filed a request with the Commission to transfer the First-Class Mail Parcels product from the Market Dominant product list to the Competitive product list (merging the new offering into the existing First-Class Package Service product).[124]

For a Market Dominant product to be transferred to the Competitive product list, the Postal Service must demonstrate compliance with 39 U.S.C. § 3642(b), which includes criteria relevant to market power, the postal monopoly, and other additional considerations. The Commission found that the Postal Service did not provide sufficient evidence to demonstrate that it lacks market power and denied the Postal Service's request.[125]

On September 22, 2015, the Postal Service filed a petition for review before the D.C. Circuit.[126] In FY 2017, the court granted the petition for review, stating that the Commission did not adequately distinguish the First-Class Mail Parcels transfer case from previous parcel transfer cases.[127] It remanded the case to the Commission for further proceedings and the case is currently pending before the Commission.

Complaint of the Center for Art and Mindfulness

In FY 2015, the Center for Art and Mindfulness, Inc. and Norton Hazel (Complainants) filed a complaint concerning the sale and closure of the Atlantic Street Station post office in Stamford, Connecticut.[128] The Postal Service filed a motion to dismiss,[129] which the Commission granted on March 4, 2015. On April 1, 2015,[130] Complainants filed a motion for reconsideration of the Commission's order.[131] On April 23, 2015, the Commission denied the motion for reconsideration.[132]

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[122] *American Postal Workers Union, AFL-CIO v. Postal Regulatory Commission,* No 15-1156 (D.C. Cir. filed May 29, 2015).
[123] *American Postal Workers Union, AFL-CIO v. Postal Regulatory Commission,* No. 15-1156, 2016 WL 6956668 (D.C. Cir. Nov. 29, 2016).
[124] Docket No. MC2015-7, Request of the United States Postal Service to Transfer First-Class Mail Parcels to the Competitive Product List, November 14, 2014.
[125] Docket No. MC2015-7, Order No. 2686, Order Denying Transfer of First-Class Mail Parcels to the Competitive Product Category, August 26, 2015.
[126] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1338 (D.C. Cir. filed Sept. 22, 2015).
[127] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1338, 2016 WL ^ (D.C. Cir. December 6, 2016).
[128] Docket No. C2015-1, Complaint of Center for Art and Mindfulness, Inc. and Norton Hazel, December 29, 2014.
[129] Docket No. C2015-1, United States Postal Service Motion to Dismiss the Complaint of the Center for Art and Mindfulness, Inc. and Norton Hazel, January 20, 2015.
[130] Docket No. C2015-1, Order No. 2377, Order Granting Motion to Dismiss, March 4, 2015.
[131] Docket No. C2015-1, Brief in Support of Motion for Reconsideration of Commission Order of Center for Art and Mindfulness, Inc. and Norton Hazel, April 1, 2015.
[132] Docket No. C2015-1, Order No. 2460, Order Denying Reconsideration of Commission Order No. 2377, April 23, 2015.

On April 3, 2015, Complainants appealed the Commission's order dismissing their complaint to the D.C. Circuit.[133] The Commission moved to dismiss the petition on the grounds that the order appealed by Complainants was not a final order subject to judicial review. On January 4, 2016, the court granted the motion to dismiss.[134] On February 2, 2016, Complainants filed a petition for rehearing,[135] which the court denied on March 3, 2016.[136]

Removal of Return Receipt for Merchandise Service

On January 15, 2015, the Commission issued an order conditionally approving the Postal Service's request to remove Return Receipt for Merchandise Service from the list of Special Services in the MCS.[137] The Postal Service subsequently notified the Commission that it decided to indefinitely defer removing this Special Service from the MCS.[138]

On February 18, 2015, the Postal Service appealed the Commission's order to the D.C. Circuit.[139] On June 5, 2015, the Postal Service and the Commission filed a joint motion to return the case to the Commission for further proceedings in light of a decision from a separate panel of the court.[140] The court granted the motion on June 15, 2015, and remanded the matter to the Commission.[141] In FY 2017, the Commission issued a final order resolving issues on remand.[142]

Pending Court Appeals

The following appeals are pending before the D.C. Circuit:

- IMb Remand[143]
- UPS Proposals One, Two, and Three[144]
- Complaint of Ramon Lopez[145]
- Complaint of Frederick Foster[146]

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[133] *Center for Art and Mindfulness v. Postal Regulatory Commission,* No 15-1079 (D.C. Cir. filed Apr. 3, 2015).
[134] *Center for Art and Mindfulness v. Postal Regulatory Commission,* No. 15-1079 (D.C. Cir. filed Jan. 4, 2016).
[135] *Center for Art and Mindfulness v. Postal Regulatory Commission,* No. 15-1079 (D.C. Cir. filed Feb. 2, 2016).
[136] *Center for Art and Mindfulness v. Postal Regulatory Commission,* No. 15-1079 (D.C. Cir. filed Mar. 3, 2016).
[137] Docket No. MC2015-8, Order No. 2322, Order Conditionally Approving Removal of Return Receipt for Merchandise Service from Mail Classification Schedule, January 15, 2015.
[138] Docket No. MC2015-8, Response of the United States Postal Service to Order No. 2322, January 28, 2015.
[139] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1037 (D.C. Cir. filed Feb. 18, 2015).
[140] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1037 (D.C. Cir. filed Jun. 5, 2015).
[141] *United States Postal Service v. Postal Regulatory Commission,* No. 15-1037 (D.C. Cir. filed Jun. 15, 2015).
[142] Docket No. MC2015-8R, Order No. 3597, Order Resolving Issues on Remand, October 31, 2016.
[143] *United States Postal Service v. Postal Regulatory Commission,* No. 16-1284 (D.C. Cir. filed Aug. 11, 2016). This case is discussed in Chapter III, supra.
[144] *United Parcel Service, Inc. v. Postal Regulatory Commission,* No. 16-1354 (D.C. Cir. filed October 7, 2016). This case is discussed in Chapter III, supra.
[145] *Ramon Lopez v. Postal Regulatory Commission,* No. 12-1341 (D.C. Cir. filed Aug. 3, 2012).
[146] *Frederick Foster v. Postal Regulatory Commission,* No. 15-1339 (D.C. Cir. filed Sep. 23, 2015).

Commission's Role in International Postal Policy

The Secretary of State is responsible for formulating, coordinating, and overseeing international postal policy, including concluding postal treaties such as those involving the UPU. 39 U.S.C. § 407. Headquartered in Bern, Switzerland, the UPU is an international treaty organization tasked with facilitating high-quality universal mail service at affordable rates. Although the State Department has primary authority over international postal policy, it requests the Commission's views on whether any treaty, convention, or amendment that establishes a Market Dominant rate or classification is consistent with the PAEA's modern system of ratemaking for Market Dominant products. *Id.* § 407(c)(1). The State Department ensures that relevant United States positions in the UPU are consistent with the Commission's views unless there is a foreign policy or national security concern. *Id.* § 407(c)(2).

In FY 2016, the Commission chaired the Regulatory Issues Project Group and continued its active role in the UPU Letters and Parcels Remuneration Groups on international letter mail and parcel delivery rates, as well as in several other UPU project groups. Also, the Commission continued its role as an active member of the State Department's Federal Advisory Committee on International and Postal Delivery Services.

On December 30, 2015, the Commission adopted final rules describing general procedures related to the Commission's views on proposals submitted for consideration at UPU Congresses that could affect a Market Dominant rate or classification.[147] The purpose of the new rules was to facilitate public participation in, and promote the transparency of, the development of Commission views.

Under the new rules, the Commission will establish a docket for each UPU Congress. The Commission will seek comments on "the general principles that should guide the Commission's development of views on relevant proposals, in a general way, and on specific relevant proposals, if the Commission is able to make these available." 39 C.F.R. 3017.3(a). Comment deadlines will be established on a case-by-case basis to ensure the Commission's views are submitted to the Secretary of State in a timely manner.

The Commission applied these rules for the first time when the Secretary of State requested the Commission's views on proposals for the 26th UPU Congress. Specifically, the Secretary of State asked the Commission whether these proposals were consistent with the standards and criteria for modern rate regulation established by the Commission under 39 U.S.C. § 3622.[148] The Commission established Docket No. IM2016-1 to solicit comments.[149] The Commission received comments from 19 interested individuals and parties representing a broad array of postal stakeholders.

After considering comments received, the Commission provided its views to the Secretary of State on August 31, 2016, and supplemental views on September 19, 2016. Consistent with the Commission's new rules, these views were posted on the Commission's website in Docket No. IM2016-1.[150]

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147 Docket No. RM2015-14, Order No. 2960, Order Adopting Final Rules on Procedures Related to Commission Views, December 30, 2015.

148 *See* Letter from Nerissa J. Cook, Deputy Assistant Secretary, U.S. Department of State, Bureau of International Organization Affairs, on behalf of the Secretary of State, April 1, 2016. See also Letter from Acting Chairman Robert G. Taub, on behalf of the Commission, April 14, 2016.

149 Docket No. IM2016-1, Order No. 3253, Notice and Order Establishing Section 407 Proceeding, April 20, 2016.

150 Docket No. IM2016-1, Notice of Posting of Views, October 7, 2016.

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