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U.S. POSTAL REGULATORY COMMISSION

ANNUAL COMPLIANCE DETERMINATION REPORT

Fiscal Year 2011

March 28, 2012

Letter From the Chairman

Ruth Y. Goldway
Chairman

On behalf of the Postal Regulatory Commission, I am pleased to present this Annual Compliance Determination reviewing the performance of the U.S. Postal Service for Fiscal Year 2011. This annual review is required by the Postal Accountability and Enhancement Act (PAEA) and primarily focuses on financial transparency and compliance with pricing and service performance standards.

The Postal Service is continuing to experience severe financial losses. In FY 2011, the Postal Service lost $5.1 billion, and had Congress not deferred a statutorily required $5.5 billion payment into the Retiree Health Benefit Fund (RHBF), the loss would have totaled $10.6 billion. There is little reason to believe the Postal Service situation will improve in the near future. Mail volume continues to decline. More importantly, the Postal Service now faces a cash flow crisis related to the overly ambitious RHBF prefunding requirement. In FY 2012, the Postal Service is obligated to pay both the $5.5 billion deferred from 2011 as well as $5.5 billion due in FY 2012. It is unlikely to be able to do so.

Based on our review of information provided by the Postal Service, the Commission has determined the Postal Service to be largely in compliance with postal policies and the pricing requirements of the PAEA. Significant problems, however, remain. Ten Market Dominant products' prices did not raise revenue sufficient to cover even their attributable costs, creating losses of $1.6 billion. Two were particularly problematic. Standard Mail Flats generated revenues $643 million less than its attributable costs, yet the Postal Service has repeatedly failed to utilize existing pricing options to address this growing Standard Mail intra-class subsidy.

The other major problem area was Periodicals, a class with revenues $609 million below attributable costs. At the end of FY 2011, the Commission and the Postal Service jointly issued the "Periodicals Mail Study," a report to Congress under Section 708 of the PAEA which examined, in part, how cost coverage for Periodicals might be improved. The Postal Service has indicated it is proceeding with operational changes recommended in the Report yet this year's losses were greater than last year's losses.

The Commission commends and continues to support the Postal Service's efforts to innovate. In FY 2011, the Commission approved several pricing incentives designed to increase the value of the mail and slow the diversion of mail to electronic channels. The Commission also authorized several Postal Service market tests and the first market dominant Negotiated Service Agreement (NSA) since passage of the PAEA. The Postal Service continued to pursue competitive NSAs, agreeing to 67 in FY 2011.

In FY 2011, in response to the Postal Service's significant increase in post office closings, 103 communities appealed the planned closing of their local post office to the Commission. These appeals demonstrate the value and relevance of local post offices to the communities they serve. The Commission plays an important role in allowing the public a forum to voice their concerns. However, only nine of these appeals were remanded for further review.

Congress and the Administration are considering legislative action to address the Postal Service's structural problems. At the end of FY 2011, the Commission released its first five-year review of the PAEA, reporting on the operation of that statute and making recommendations for statutory changes that would benefit the Postal Service. The Commission suggested, for example, that Congress adjust the RHBF payment schedule to help address the Postal Service's current liquidity challenge and clarify of the scope of appellate review for Postal Service determinations to close Postal Service operated retail facilities. We hope this Annual Compliance Determination helps to further inform Congress' consideration.

I wish to thank Vice Chairman Nanci Langley and Commissioners Mark Acton and Robert Taub for their valuable work and contributions to this report. On behalf of my fellow Commissioners, I also want to recognize the Commission staff's outstanding efforts and dedication to our work.

Ruth Y. Goldway

Ruth Y. Goldway

Chairman

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Chapter I

Executive Summary

This report reviews the Postal Service's performance in Fiscal Year 2011, fulfilling the Commission's responsibility to produce an annual assessment of Postal Service rates and service. 39 U.S.C. 3653. It is based on information the Postal Service is required to provide within 90 days after the close of that fiscal year and on comments subsequently received from the public.

Principal Findings — Financial

In FY 2011, the Postal Service's financial condition continued to deteriorate. At the end of FY 2012, it will not have sufficient cash to meet its Retiree Health Benefits Fund (RHBF) obligation. Even without this obligation, the Postal Service soon may be unable to meet payroll or pay its other bills.

The Postal Service's cumulative loss over the last 5 years amounts to $25.3 billion. The Postal Service lost $5.1 billion in FY 2011, but the loss would have been $10.6 billion had Congress not deferred the RHBF payment at the end of FY 2011. The primary reason for the losses is the overly optimistic RHBF pre-funding requirement. If there had been no prefunding requirement, the cumulative 5-year loss would have been reduced to $4.4 billion. The prefunding obligation is also the primary reason the Postal Service has had to use almost all of its statutory authority to borrow funds.

Since the passage of the Postal Accountability and Enhancement Act (PAEA), volume has declined in all classes of mail, especially First-Class Mail, the Postal Service's most profitable product. The combination of the price cap and the continuing decline of First-Class Mail prevents the Postal Service from generating sufficient funds from mail users to cover its institutional costs. First-Class Mail declined by 5 billion pieces in FY 2011 resulting in the Postal Service losing $1.0 billion in contribution to institutional costs. Had First-Class Mail remained at its 2006 volume level, the Postal Service would have generated an additional $5.2 billion in contribution in FY 2011 which exceeds the $5.1 billion loss noted above.

Principal Findings — Pricing

The rates and fees for Standard Mail Flats remain out of compliance as its losses grew from $577 million in FY 2010 to $643 million in FY 2011. The Commission orders no new remedial action pending resolution of an ongoing judicial review of this matter.

Ten market dominant products failed to generate revenues sufficient to cover attributable costs, losing in the aggregate $1.6 billion, including:

- $609 million from Periodicals,
- $643 million from Standard Mail Flats, and
- $112 million from Standard Mail Parcels/Not-Flat Machinables (NFMs);

For Periodicals, the Postal Service should continue to pursue opportunities identified by the Periodicals Study to reduce the costs of handling flats.

For Standard Parcels/NFMs, the Postal Service should continue to use its pricing flexibility to give this mail above average price increases.

The evaluation of cost coverage and contribution is important because it demonstrates that the losses from market dominant products contributed substantially to the Postal Service's $5.1 billion loss in FY 2011. This indicates that the Postal Service has not been able to use its pricing flexibility to cover costs nor to maximize profit.

Of the 35 workshare discounts that exceeded avoided cost in FY 2011,16 did not satisfy 3622(e)(2) and, except for one discount discussed in Chapter VII, the Postal Service is directed to align these discounts with avoided cost in the next market dominant price adjustment.

Competitive products, as a whole, have generated a profit, making a positive contribution to institutional cost, amounting to 7.8 percent, which exceeded the required 5.5 percent share; however, two international competitive products and one competitive special services product failed to cover attributable cost and thus did not comply with section 3633(a)(2). The Postal Service is ordered to take steps to remediate the problem.

Principal Findings — Service Performance

The Commission must determine, for the year covered by the ACD, "whether any service standards in effect during such year were not met." 39 U.S.C. 3653(b)(2). This fulfills part of the required transparency and accountability of the PAEA. Moreover, maintaining or increasing service performance will help the Postal Service retain users of the mail. In some cases, particularly Package Services, improving service performance may result in volume growth.

The Postal Service is demonstrating success in meeting its service standard goals in the areas of single-piece First-Class Mail and Special Services. However, the Postal Service did not meet its delivery service standard target for the majority of market dominant products in FY 2011. Overall, the Commission regards low performance results for speed of delivery as an important issue the Postal Service must resolve and the Commission will closely monitor the reporting results in FY 2012. The Commission expects that in FY 2012, service performance results will be closer to established targets.

Significant issues continue to hinder the Intelligent Mail barcode system from fulfilling its potential as a useful component of service performance measurement. Despite the requirement that it report service performance for market dominant products in FY 2011, results for many products were only

available for one quarter. If continued progress is not evident, the Commission will review its decision to allow the use of the hybrid system for service performance measurement.

Principal Findings — Filing Requirements

Contrary to the Commission's rules, which require that the Postal Service's Annual Compliance Report be submitted based on existing, approved costing methodologies, the Postal Service filed certain attributable costs and cost avoidance estimates based on proposed methodological changes still pending before the Commission. These filings were made less than a month before the Annual Compliance Report.

FY 2011's Annual Compliance Report and Annual Performance Plan and descriptions of strategic initiatives did not contain information similar to the level of detail provided in FY 2010. Future Annual Compliance reports must adhere to the Commission's rules as specified in 39 CFR part 3050.

The Postal Service's flexibility under the PAEA includes deciding when to implement rate changes. However the FY 2011 schedule necessarily required reliance on data over one year old. Use of more current data would allow for more cost-based rates and, in all likelihood, minimize the need for remedial action by the Commission.


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Chapter II

Background

Introduction

Statutory context. Ongoing, systematic reporting and assessment of the financial and operational performance of the United States Postal Service are mandated by two provisions of the Postal Accountability and Enhancement Act (PAEA). Pub L. 109-435, 120 Stat. 3198 (2006). The first provision, 39 U.S.C. 3652, requires the Postal Service to file certain annual reports with the Commission, including an Annual Compliance Report (ACR). *See* 39 U.S.C. 3652(a) and (g). The second provision, 39 U.S.C. 3653, provides for the Commission's review of these annual reports, including an Annual Compliance Determination (ACD) regarding the compliance or non-compliance of various rates and service standards.[1] Together, these provisions establish the ACD and the ACR as integrated mechanisms for achieving the PAEA's objectives of providing ongoing accountability, transparency, and oversight.

Timeline and review of report. The Postal Service is required to file the ACR no later than 90 days after the end of each fiscal year, which ends September 30. The Commission is required to complete the ACD within 90 days after receiving the ACR. The Postal Service filed the 2011 ACR on December 29, 2011. Thus, the Commission must issue the ACD no later than March 28, 2012.

Focus of the ACR. In accordance with section 3652, the ACR must provide analyses of costs, revenues, rates, and quality of service sufficient to demonstrate that during the reporting year all products complied with all applicable requirements of title 39. Additionally, for market dominant products, the ACR must report product information, mail volumes, and measures of quality of service, including the speed of delivery, reliability, and the degree of customer satisfaction. For market dominant products with workshare discounts, the ACR must report the per-item cost avoided by the Postal Service by virtue of such discount, the percentage of such per-

[1] Common abbreviations and acronyms are identified in Appendix C.

item cost avoided that the per-item workshare discount represents, and the per-item contribution to institutional costs. 39 U.S.C. 3652(a) and (b).

Other reports. In conjunction with its filing of the ACR, the Postal Service must also file its most recent comprehensive statement on postal operations, its performance plan, and program performance reports. 39 U.S.C. 3652(g).

Commission responsibilities. Under section 3653, the Commission's corresponding responsibilities include providing an opportunity for comment on the Postal Service's submission, making a written determination as to whether any rates or fees were not in compliance with applicable provisions of chapter 36 of title 39 or related regulations, and whether any service standards were not met. If no instance of non-compliance is found, the determination is written accordingly. 39 U.S.C. 3653 (a), (b). If a determination of non-compliance is made, the Commission is directed to take such action as it deems appropriate. The Commission is also required to evaluate annually whether the Postal Service has met the goals established under sections 2803 and 2804, and may make recommendations to the Postal Service related to the protection or promotion of public policy objectives of title 39. 39 U.S.C. 3653(d).

Procedural History

On December 29, 2011, the Postal Service filed its 2011 ACR, covering the period from October 1, 2010 through September 30, 2011. In accordance with section 3652(g), the Postal Service concurrently filed its 2011 Comprehensive Statement on Postal Operations.[2] The Comprehensive Statement included the Postal Service's 2011 Annual Performance Report and 2012 Performance Plan required by the Government Performance and Results Act, P.L. 103-62.

The ACR includes an extensive narrative discussion and a substantial amount of detailed public and non-public information contained in library references. The library references include the Cost and Revenue Analysis, the International Cost and Revenue Analysis, cost models supporting workshare discount analysis, and billing determinant information. Library Reference USPS-FY11-9 serves as a road map that summarizes other materials in the submission. It also includes a section on methodology changes and a section in response to Commission rule 3050.12 regarding data obsolescence.

The Postal Service also filed its annual report to the Secretary of the Treasury regarding the competitive products fund, as required by section 2011(i) of title 39, as part of library reference USPS-FY10-39 in conjunction with the other Competitive Products Fund materials required to comply with 39 CFR 3060.20 through 3060.23.

On January 3, 2012, the Commission issued an order providing notice of the Postal Service's filing, establishing Docket No. ACR 2011 as a formal docket to consider the filing, appointing a Public Representative to represent the interests of the general public, and providing an opportunity for public comment.[3] It established February 3, 2012, as the deadline for comments and February 17, 2012, as the deadline for reply comments.

Methodology changes. The Postal Service reports that the scope of new methodologies has been minimized

[2] 2011 Comprehensive Statement on Postal Operations, December 29, 2011 (Comprehensive Statement). This document was filed as Library Reference USPS FY11-17.

[3] *See* Notice of Postal Service's Filing of Annual Compliance Report and Request for Public Comments, January 3, 2012 (Order No. 1095); *see also* 77 FR 1521 (January 10, 2012).

because it has generally replicated the methodologies most recently used by the Commission. It indicates, however, that several methodological changes are reflected in the ACR. It identifies and discusses these changes in a separate section of the road map document and in the prefaces to the appended materials. Additionally, the Postal Service filed proposals to change analytical principles since the filing of the 2010 ACR. It summarizes 12 proposals and proposed changes that were pending resolution as of the date of the filing, which have been incorporated into the 2011 ACR. Five proposals (Proposals 16 through 20) are still pending before the Commission, having been submitted shortly before the 2011 ACR on November 30, 2011.

Product analysis. The Postal Service provides a detailed analysis of each market dominant product, including domestic negotiated service agreements entered into during FY 2011. It also presents information on workshare discounts responsive to 39 U.S.C. 3652(b). The Postal Service presents a product-by-product analysis of competitive products and discusses available FY 2011 data regarding conformity with 39 U.S.C. 3633. Further, the Postal Service provides information on the five market tests conducted during FY 2011, and on nonpostal services. The Postal Service explains that the Commission linked reporting on nonpostal services to approval of classification in Docket No. MC2010-24, a docket that was still pending at the close of FY 2011. As a result, the Postal Service has provided information on two market dominant nonpostal services.

Confidentiality. In FY 2009, the Commission adopted rules governing the treatment of commercially sensitive information.[4] These rules require the Postal Service to apply for non-public treatment when it considers information required in periodic reports to be commercially sensitive. Its application must specify reasons for concluding the particular information is commercially sensitive and in need of non-public treatment, and describe with particularity the nature of the competitive harm that public disclosure is likely to cause. Accordingly, the Postal Service accompanied its 2011 ACR with an application for non-public treatment of certain competitive product information, including its supporting rationale.

Requests for additional information. On January 19, 2012, Chairman's Information Request (CHIR) No. 1 was issued, directing the Postal Service to provide additional information to clarify estimates in the ACR. Three additional CHIRs were issued during the course of this proceeding. The Postal Service has responded to all information requests. In addition, the Postal Service subsequently filed supplemental information to support its responses. The Commission appreciates the Postal Service's responsiveness to the information requests.

4 *See* Docket No., RM2008-1, Final Rule Establishing Appropriate Confidentiality Procedures, June 19, 2009 (Order No. 225).


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Chapter III

Legal Issues

Introduction

Commenters raise several legal issues related to the 2011 ACR. Of particular concern are (1) Standard Mail Flats remain out of compliance with title 39, and (2) the Periodicals Class products' compliance with title 39 notwithstanding the failure of those products to cover costs. Another, more theoretical issue is whether workshare discount passthroughs of less than 100 percent of avoided costs satisfy section 3622(a).[1] Finally, in response to comments, the Commission discusses the impact that the Postal Service's recent revision to the Schedule for Regular and Predictable Rate Changes may have on the data utilized during the ACD.

Standard Mail Flats

Background. On March 29, 2011, the Commission issued its FY 2010 ACD. The Commission concluded that because of the Postal Service's failure to address the increasing cost contribution shortfall of the Standard Mail Flats product (then 81.6 percent), the prices in effect in FY 2010 for that product amounted to an unfair and inequitable apportionment of costs in violation of 39 U.S.C. 101(d). 2010 ACD at 106. Pursuant to the authority granted to it by 39 U.S.C. 3653(c), the Commission directed the Postal Service to increase the cost coverage of the Standard Mail Flats product through a combination of above-average price adjustments and cost reductions until such time that revenue for the product exceeds attributable costs. *Id.* The Commission further directed the Postal Service to present a schedule of future above-CPI price increases for the Standard

[1] Two commenters assert that the Postal Service, by setting workshare discounts at a rate less than avoided costs, engages in a form of exclusionary pricing. According to these commenters, such discounts do not satisfy the directive that the Commission establish "a modern system for regulating rates and classes for market-dominant products." Panzar Comments at 15; Pitney Bowes Comments at 6. They ask that the Commission revise the rate regulations to require that workshare discounts be set at 100 percent of avoided cost. Regardless of the policy or legal merits of this proposal, neither commenter suggests that the Postal Service was out of compliance in FY 2011 because of workshare discounts. *See also* Chapter VII.

Mail Flats product within 90 days of the issuance of the FY 2010 ACD, with the schedule to be updated with each subsequent market dominant price adjustment and ACR. Finally, in order to provide increased transparency concerning the steps that the Postal Service is taking to eliminate the intra-class subsidy with respect to Standard Mail Flats, the Commission ordered the Postal Service to provide certain additional information in subsequent ACRs and notices of market dominant price adjustments until the revenue for the product exceeds attributable costs. *Id.* at 107.

D.C. Circuit litigation. On April 27, 2011, the Postal Service filed a petition with the United States Court of Appeals for the District of Columbia Circuit (D.C. Circuit) seeking review of the FY 2010 ACD relating to the Commission's determination of non-compliance for the Standard Mail Flats product. In its Petition, the Postal Service argued, among other things, that the PAEA requires the Standard Mail class to cover costs, not the Standard Mail Flats product[2] within that class, and that the finding of non-compliance exceeded the Commission's authority in ACD proceedings. *Id.* at 7-8.; *see also 2011 ACR at 28.*

On May 17, 2011, the Postal Service moved to have the Commission stay that portion of the ACD requiring it to present a schedule of above-CPI price increases for Standard Mail Flats within 90 days. On May 27, 2011, the Commission granted this request and instituted a stay that will remain in effect until 30 days following resolution of the Petition.[3] Oral argument in the case was held on February 7, 2012. The outcome of the case is pending before the Court.

FY 2011 Compliance. Pursuant to 39 U.S.C. 3652(a)(1), the Postal Service is required to "demonstrate that all products during such year complied with all applicable requirements of [title 39]." The Postal Service notes that it increased prices for the Standard Mail Flats product by 0.835 percent in FY 2011 and argues that this "moderate increase" was made in an effort to "gradually move Standard Mail Flats towards 100 percent cost coverage without placing an undue burden on the already fragile catalog mailing industry, which depends heavily on Standard Mail Flats." 2011 ACR at 28-29. The cost coverage for the Standard Mail Flats product, however, has decreased from 81.6 percent in FY 2010 to 79.4 percent in FY 2011. The Postal Service concedes that pricing and efficiency measures need to be taken to move this product toward covering its costs and making an appropriate contribution toward institutional costs. *Id.* at 28.

Standard Mail, as a class, covers attributable costs and makes a substantial contribution to institutional costs. However, the 2011 ACR results show that the Standard Mail Flats product does not cover costs, and therefore does not make a contribution to institutional costs. *Id.*

Beginning as early as the FY 2008 ACD and reiterated in subsequent proceedings, the Commission has recognized some mailers' concern that the Standard Mail Flats product does not cover costs and, as a consequence, imposes a disproportionate institutional cost burden on other Standard Mail

2 United States Postal Service v. Postal Regulatory Commission, No. 11-1117 (D.C. Cir. 2011), (April 27, 2011) at i (Petition).

3 Docket No. ACR2010, Order Granting Stay, May 27, 2011, at 3 (Order No. 739).

products, particularly the Standard Mail Letters and Carrier Route products.[4] Since FY 2008 that burden has worsened. The Standard Mail Flats product's contribution per piece, which was negative 2.2 cents in FY 2008, has expanded to negative 9.5 cents in FY 2011. In contrast, the Standard Mail Letters product's contribution per piece was positive 8.9 cents in FY 2011. An alternate way of viewing the increasing intra-class burden that the Standard Mail Flats product is imposing on the Standard Mail Letters and Carrier Route products is to compare the difference in unit contribution. In FY 2008, the difference in unit contribution between Standard Mail Flats and Standard Mail Letters was 11.2 cents. In FY 2011, the difference in unit contribution was 18.4 cents. Similarly, in FY 2008, the difference in unit contribution between Standard Mail Flats and Standard Mail Carrier Route was 9.9 cents. In FY 2011, the difference in unit contribution was 15.8 cents. Despite the Commission's repeated suggestions that Standard Mail Flats be priced above cost,[5] the Postal Service had persisted in proposing below-average price increases for this product. However, its recent FY 2012 price increase of 2.209 percent is minimally higher than the average Standard Mail price increase of 2.133 percent.

Parties' comments. Five commenters address the Postal Service's Standard Mail Flats pricing strategy. L.L.Bean challenges the Postal Service's proffered reason for continuing the below-cost pricing strategy – concerns about placing an "undue burden" on the "fragile catalog mailing industry." *See* 2011 ACR at 29. L.L.Bean references a recent survey conducted by the American Catalog Mailers Association (ACMA) that found that only one-third of catalogs are mailed as Standard Mail Flats whereas two-thirds of catalogs are mailed as Carrier Route, a Standard Mail product that generates a positive contribution to institutional costs. L.L.Bean Comments at 1-2. L.L.Bean requests that the Commission issue a noncompliance determination for the Standard Mail Flats product in the 2011 ACD. *Id.* at 3.

Claiming that previous efforts to control the costs of the Standard Mail Flats product have largely failed, Valpak argues that the Postal Service should be required to increase cost coverage by implementing consecutive above-average price increases. Valpak Comments at 58. Valpak suggests that if the D.C. Circuit Court affirms the Commission's authority to make a finding of noncompliance and issue remedial orders, the Commission should direct that substantial price increases be made for Standard Mail Flats to ensure that the product makes a positive contribution to institutional costs in 3 years time. *Id.* at 60.

Noting the burden that cross-subsidization of the Standard Mail Flats product imposes on users of the Standard Mail Letters product, the National Postal Policy Council (NPPC) requests that the Commission remediate the cross-subsidization of Standard Mail products in a manner that reduces the burden on Standard Mail Letter mailers while accounting for the possible consequences that abrupt reductions in Standard Mail Flats volumes may cause. NPPC Comments at 2.

The Public Representative recognizes that the Postal Service did implement an above-average price increase of 2.209 percent for Standard Mail Flats in

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4 *See* 2008 ACD at 61; *see also* 2009 ACD at 86; 2010 ACD at 103; Docket No. R2009-2, Order No. 191 at 52-53, and Docket No. R2010-2, Order No. 675 at 31.

5 *See, e.g.*, Order No. 191, at 53; 2010 ACD at 103-104, 107; 2009 ACD at 86-87.

January 2012. However, the Public Representative notes that the Postal Service failed to provide the information that the Commission, in its FY 2010 ACD, ordered it to present concerning the elimination of the intra-class cross-subsidy.[6] The Public Representative urges the Commission to request that the Postal Service submit a plan to bring the Standard Mail Flats product back into compliance. Public Representative Comments at 18-19. Valpak concurs with this request. Valpak Reply Comments at 26.

In contrast to the other commenters, the American Catalog Mailers Association (ACMA) challenges the premise that the Standard Mail Flats product is suitable for a cross-subsidy test. According to the ACMA, three products within the Standard Mail class – Standard Mail Flats, Carrier Route, and High-Density & Saturation Flats and Parcels – are each composed of nonhomogeneous agglomerations of commercial and nonprofit items. ACMA Comments at 25-27.

In their reply comments, both Valpak and L.L.Bean urge the Commission to make a formal finding of non-compliance. Valpak asserts that if the Commission does not make a finding of non-compliance, it could render the pending D.C. Circuit Court proceedings moot. Valpak Reply Comments at 20. Valpak also notes that under section 3653(e), a failure by the Commission to render a determination of non-compliance will create a rebuttable presumption that the rates for the Standard Mail Flats product were in compliance in FY 2011, thereby prejudicing the position of any putative mailer that might file a complaint with the Commission pursuant to section 3662. L.L.Bean echoes these two concerns. L.L.Bean Reply Comments at 3.

The factual predicates that prompted the Commission to conclude in the FY 2010 ACD that the Standard Mail Flats product was not in compliance with title 39, and which prompted the Commission to order remedial measures, remained during FY 2011. The Commission accordingly finds that the Standard Mail Flats product remained out of compliance.

Shortly after the close of FY 2011, the Postal Service filed notice with the Commission announcing, among other things, a planned increase in Standard Mail Flats rates of 2.209 percent, only 0.076 percent above the class average, 2.133 percent. Ordinarily, the Commission would consider the Postal Service's subsequent filing. Given the pendency of the appeal before the D.C. Circuit, however, the Commission will hold action in this area in abeyance pending receipt of the Court's decision. Following that, the Commission will take action as appropriate.

Periodicals

The Postal Service reports that in FY 2011 Periodicals continued not to cover attributable costs. In FY 2011, the cost coverage of the Periodicals class declined slightly, to 74.9 percent from 75.5 percent in FY 2010. 2011 ACR at 32. Both products that comprise the Periodicals class – Within County and Outside County – have reported cost coverage shortfalls of similar ratio. Thus, a rebalancing pricing strategy which keeps the overall price cap intact at the class level, is not feasible. The Postal Service reports that if it increased Periodicals prices to cover

[6] Specifically, the Commission ordered the Postal Service to provide, in the ACR: (1) a description of all operational changes designed to reduce Standard Mail Flats costs that were made in the previous year and an estimate of the financial effects of such changes, (2) a description of all costing methodology or measurement improvements made in the previous year and an estimate of the financial effects of such changes, and (3) a statement summarizing the historical and current year subsidy of the Standard Mail Flats product. *See* 2010 ACD at 107.

attributable costs, the resulting prices would drive many publishers out of the print business altogether. *Id.* at 33. It indicates, however, that it is continuing to pursue operational efficiencies and opportunities to fine-tune prices in an effort to improve the cost contribution of Periodicals. *Id.* at 33-34.

Valpak contends that the cost reductions that the Postal Service hopes to achieve cannot possibly resolve the cost coverage gap for Periodicals. Valpak Comments at 70. It contends that a non-compliance determination for this class is warranted on the basis of the repeated cost coverage shortfalls, which it asserts violate section 101(d), and many of the statutory objectives and factors listed in section 3622. *Id.* at 72-78. Valpak therefore asks the Commission to make a non-compliance determination and either order a price adjustment above the cap, or order that the Periodicals products be discontinued and replaced with a discount. *Id.* at 80-81.

Time Inc. (Time) comments that it expects to see improvements in the cost coverage for Periodicals as the Postal Service implements various operational efficiencies. Specifically, Time is hopeful that eliminating Hot 2-C Processing, advancing the Critical Entry Time for Periodicals, and implementing the FSS and Network Consolidation will lead to cost reductions. Time Comments, Attachment A at 1-3.

As discussed in Chapter VII, the Commission concludes that the rates for Periodicals do not satisfy section 3622(c)(2), but it does not find the FY 2011 Periodicals rates to be out of compliance with the applicable statutory provisions or the regulations promulgated thereunder. As the Commission explained in the FY 2010 ACD, a finding that a product fails to satisfy a provision of title 39 does not compel a finding of non-compliance. In making a compliance determination, the Commission must take into account numerous and sometimes conflicting considerations. For example, the Commission must take into account the effect that rate increases will have upon the general public, business mail users, and enterprises in the private sector of the economy engaged in the delivery of mail matter other than letters. 39 U.S.C. 3622(c)(3). The Commission must also take into account "the educational, cultural, scientific, and informational value to the recipient of mail matter." 39 U.S.C. 3622(c)(12).

Periodicals and Standard Flats face distinguishable circumstances. Periodicals had cost coverage shortfalls in the years prior to the passage of the PAEA. Moreover, unlike Standard Mail, Periodicals as a class fails to cover costs, thus foreclosing a rebalancing pricing strategy. While this is a concern, there is no suggestion that the Postal Service has ignored its pricing flexibility under the PAEA with respect to the Periodicals products. In addition, management has not yet fully brought to bear efficiency enhancements, network adjustments, and related changes which could alter the attributable cost picture for Periodicals. The Commission finds it appropriate to allow more time for these measures to be implemented. The Commission takes seriously the concerns that price increases on Periodicals may, as a consequence, drive periodical publishers out of the print business. Nonetheless, the persistent negative contribution from Periodicals cannot endure indefinitely. *See* Postal Service Reply Comments at 7. For the reasons stated above, the Commission is persuaded that affording the Postal Service an opportunity to realize new efficiencies is the appropriate course.

Timing of Market Dominant Price Adjustments and the ACR

Under Commission regulations implementing the PAEA, the Postal Service is required to maintain on file with the Commission a Schedule for Regular and Predictable Rate Changes (Schedule). 39 CFR 3010.7(a). The Postal Service is required to file a revised schedule when it deems it appropriate to change the Schedule. 39 CFR 3010.7(e). To date, the Postal Service has established or updated the Schedule on three occasions – February 11, 2008, January 13, 2011, and October 18, 2011 – with the proposed rate changes taking effect approximately three months later.[7] In the notice accompanying its most recent market dominant price adjustment, the Postal Service indicated that it intends to implement price adjustments in January of each year.

By statute, the Postal Service is required to file its ACR no later than 90 days after the end of each fiscal year (*i.e.*, December 29). 39 U.S.C. 3652(a). The Commission is then required to issue its ACD within 90 days after receiving the ACR. 39 U.S.C. 3653(b). The Postal Service filed the 2011 ACR on December 29, 2011. Thus, the Commission must issue the ACD no later than March 28, 2012.

Two commenters — Valpak and the Public Representative — submitted comments regarding when the Postal Service should implement price changes in light of the statutory timing requirements of the ACD process. Valpak identifies two problems with the Postal Service's proposed market dominant price adjustment annual implementation time frame. First, implementing price changes in the midst of a fiscal year creates technical challenges in completing the ACR because there are two sets of rates in effect during the fiscal year that is being reviewed for compliance. Second, implementing price adjustments in January creates a long delay between the Commission's ACD, which provides guidance to the Postal Service on pricing, and the implementation of rate adjustments. Valpak Comments at 18. The Public Representative notes that by not implementing price adjustments until January, the Postal Service will deprive itself of the opportunity to promptly make improvements to problematic rates and discounts that it identifies as part of the ACR process in December. PR Comments at 25-26.

Valpak recommends that the Postal Service provide notice of price adjustments 2 to 3 months after the Commission issues the ACD with the price adjustments to take effect at the start of each fiscal year (*i.e.*, October 1). The Public Representative recommends that the Postal Service file its notice of market dominant price adjustment after it files the ACR with the Commission.

The Postal Service indicates that it is sympathetic to the commenters' concerns. It notes that ideally it would implement price changes after the ACD is issued (typically late March) or at the start of the fiscal year (October 1). However, with respect to Valpak's suggestion that the price adjustment be implemented on October 1, the Postal Service indicates that it cannot accommodate a start-of-the-fiscal year schedule because it cannot review the results from a fiscal year until after the fiscal year closes. Postal Service Reply Comments at 8. The Postal Service concedes that it could delay the implementation of

[7] *See* United States Postal Service Notice of Market-Dominant Price Adjustment, February 11, 2008; United States Postal Service Notice of Market-Dominant Price Adjustment, January 13, 2011; United States Postal Service Notice of Market-Dominant Price Adjustment, October 18, 2011.

price adjustments until after the completion of the ACD process. However, it argues that to do so would undermine its statutory pricing flexibility. The Postal Service contends that it is best suited to balance these conflicting considerations and determine when during the year it will implement price adjustments. *Id.* at 9.

The Postal Service has pricing flexibility under the PAEA, including deciding when to implement rate changes. However, rate adjustment notices filed in October, November, or December necessarily require reliance on data that may be more than one year old.[8] This most recent schedule delays, and to some extent frustrates, the goals of transparency and accountability central to the PAEA. Use of more current cost data would be beneficial by allowing for more cost-based rates, fostering stable and predictable rates and, in all likelihood, minimizing the need for remedial action by the Commission.

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8 *See* Section 701 Report, Analysis of the Postal Accountability and Enhancement Act of 2006, September 22, 2011; *see also* Docket No. R2012-3, Order on Adjustments for Market Dominant Products and Related Mail Classification Changes, November 22, 2011 (Order No. 987).


U.S. POST OFFICE

Chapter IV

Postal Service Financial Condition

Introduction

The Postal Service's basic function is to "provide postal services to bind the Nation together through the personal, educational, literary, and business correspondence of the people." 39 U.S.C. 101(a). The Commission developed a modern ratemaking system as required by the PAEA which, among other things, "assures adequate revenues, including retained earnings, to maintain financial stability." Despite this objective, the Postal Service's ability to continue to meet its service obligation is in serious jeopardy, in part, due to its inability to generate sufficient revenues to meet all of its financial obligations.

Since the passage of the PAEA, volume has declined in all classes of mail, especially First-Class Mail—the Postal Service's most profitable product. In addition, mandated payments into the Retiree Health Benefits Fund have seriously eroded the Postal Service's ability to fulfill the mandates of title 39. This chapter provides an overview of the Postal Services finances. It includes a discussion of the liquidity problems that the Postal Service has experienced over the past 3 years, the problem of declining volumes and revenues, legislative reform, and the Retiree Health Benefits Fund. It also discusses class/product volume, revenue and cost data, as well as overall work hours, and productivity.

Overview

FY 2011 marked the fifth consecutive year of financial losses for the Postal Service. The net loss of $5.1 billion in FY 2011 would have been significantly higher if the payment of $5.5 billion for the Retiree Health Benefits Fund had not been deferred by Congress.[1] The largest net loss in Postal Service history occurred in

[1] Congress has actually deferred the retiree health benefits payment several times through continuing resolutions, first deferring the payment to October 4, 2011 (P.L. 112-33), then deferring the payment further to November 18, 2011 (P.L. 112-36), and finally deferring the payment to August 1, 2012 (P.L. 112-74, Consolidated Appropriations Act).

FY 2010 when losses amounted to $8.5 billion. Since FY 2007, the Postal Service has lost $25.3 billion. These losses have created a situation where there may not be enough cash or borrowing authority available to finance postal operations beyond the summer of 2012. As shown in Table IV–1 below, the continued losses have seriously eroded the retained earnings and increased the total debt of the Postal Service. Total debt now stands at $13 billion as of the end of FY 2011, only $2 billion less than the statutory limit of $15 billion.

Continuing Liquidity Issues

Liquidity, or the availability of cash through operating revenues and debt, is the most important requirement for any business organization. Without the ability to generate sufficient cash from business operations, or to access sufficient debt capacity to invest in the business, an organization cannot continue to operate. The Postal Service's ability to generate cash from operations has been severely hampered due to the continuing decline in mail volumes, especially First-Class Mail, which provides the highest contribution to institutional costs. The significant payments to the Retiree Health Benefits Fund, inflation-based caps on prices for most products the Postal Service offers, and the increasing cost of maintaining a growing network of delivery points have also restricted the Postal Service's ability to generate sufficient cash from operations. Over the last 5 years, the Postal Service has relied on debt and Congressional intervention[2] to continue to provide service to the American public as required under title 39. The acquisition of debt was primarily to make the statutorily required payments to pre-fund retiree health benefits, which in turn denies the Postal Services the ability to invest in capital improvements, technology, or other means of enhancing operations.

In each ACD since FY 2008, the Commission has raised the issue of declining Postal Service liquidity. In the FY 2008 ACD, the Commission detailed the cash flows of the Postal Service and noted that the

> *…significant declines in revenues and the inability of the Postal Service to reduce costs fast enough could significantly increase the [expected] net loss for FY 2009 to as much as*

[2] The deferrals of the FY 2011 payment noted above and the deferral of $4 billion of the scheduled $5.4 billion due on September 30, 2009. P.L. 111-68, Continuing Appropriations Resolution, 2010.

Table IV–1—Financial Position of USPS FY 2006–2011 ($ in Millions)

	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
Net Income (Loss) before RHB and Workers Comp Adj.	$900	$3,216	$3,211	$(1,051)	$(505)	$(2825)
Payments to Retiree Health Benefits Fund	-	8,358	5,600	1,400	5,500	–
Workers Comp Liability Adj.	-	—	417	1,343	2,500	2,242
Net Financial Loss	900	(5,142)	(2,806)	(3,794)	(8,505)	(5,067)
Retained Earnings	6,276	1,134	(1,672)	(5,466)	(13,971)	(19,038)
Total Debt	**2,100**	**4,200**	**7,200**	**10,200**	**12,000**	**13,000**

Source: USPS Financial Statements, FY 2006–2011

> *$6.5 billion. The ability to finance a net loss of this magnitude would be problematic at best, as the Postal Service is currently limited in ways in which it can raise cash fast enough to cover this estimated loss. If current conditions continue there is a very real possibility that the Postal Service will not be able to pay some of the large year-end payments for the retiree health benefits fund and workers compensation.*[3]

Subsequently, in the FY 2009 ACD, the Commission noted that the Postal Service was on a financial path that would put its section 101 mandates at risk and that the Postal Service should utilize its flexibility and authority under current law to address its financial instability.[4] The Commission continued to express concern regarding the continuing financial losses and the liquidity of the Postal Service in the FY 2010 ACD. There it noted that while the Postal Service had made some strides in reducing costs and was able to meet all of its financial obligations during that year. Nevertheless, the Commission noted that conditions which existed in prior years remained, and were still creating an adverse affect on Postal Service finances and the ability to generate sufficient cash to meet all its financial obligations.

In this ACR, Valpak comments that the aggressive pre-funding requirement for retiree health benefits has put an unbearable strain on Postal Service finances. Valpak Comments at 3. Valpak also notes that without the pre-funding requirement, the net operating losses over the past 5 years would have been just slightly more than $4 billion rather than over $25 billion. Valpak states that the pre-funding requirement alone has driven the Postal Service to the brink of insolvency. *Id.* at 5-7. The Public Representative comments that unless the Postal Service is able to maintain sufficient liquidity, it will be unable to provide universal service, and that its ability to provide effective and regular postal services will be in jeopardy. PR Comments at 3. The Public Representative also notes that until the Congress acts to alleviate the burden of pre-funding retiree health benefits, the financial stress of the Postal Service will continue unabated. *Id.* at 5.

Declining Volumes and Revenues

In general, the public reports filed by the Postal Service which include volumes and revenues usually contain data from the current year and the prior year for comparison purposes. The previous year's data are sometimes revised to reflect corrections resulting from audits and reviews. Data are also restated due to methodological changes implemented by the Postal Service in the reporting year. These methodological changes are implemented for the current year's data, and the prior year's data is restated in order to facilitate comparative analysis.

For the purposes of this chapter, the comparisons of volumes and revenues are based on the data reported in the FY 2011 Revenue, Pieces, and Weight Reports (RPW) and the Postal Service's Form 10-K filing. The comparative figures in those reports reflect methodological changes from the previous year's reporting that were approved by the Commission subsequent to the issuance of the FY 2010 ACD. The Postal Service notified the Commission of the changes to the comparative data upon the filing of the FY 2011 RPW reports.[5] This

3 Postal Regulatory Commission FY 2008 Annual Compliance Determination at 24-25.

4 Postal Regulatory Commission FY 2009 Annual Compliance Determination at 22.

5 Transmittal letter from Daniel J. Foucheaux, Jr. to Commission Secretary Shoshana M. Grove accompanying filing of Quarters 1 through 3 FY 2011 RPW reports, November 25, 2011.

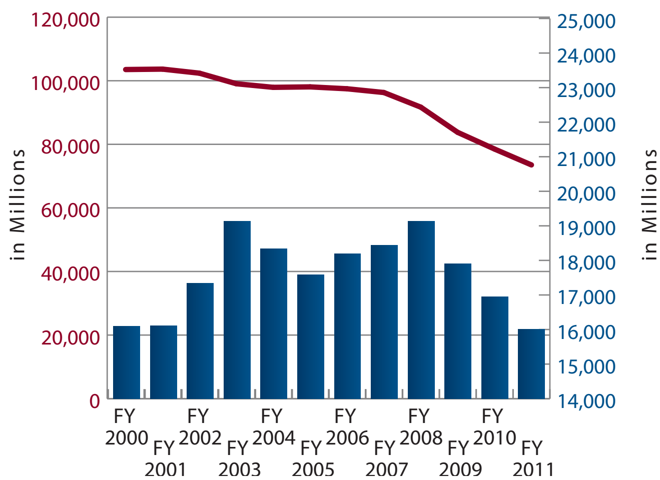
presents a problem for year-to-year comparisons because the revised FY 2010 RPW figures are not reflected in the FY 2010 ACD. For longer run comparisons like the data presented in the mail volume section, the revised RPW figures are appropriate because the Postal Service's historic RPW data reflect revisions based on corrections to audited figures. Thus, for consistency, trend analyses should be based on the historic data with revisions. However, for the year-to-year ACD comparisons, the Commission cannot restate the figures in the previous ACD to reflect after-the fact Postal Service revisions. Therefore, in subsequent chapters, current year volume and revenues by product are compared to the data as reported in the FY 2010 ACD. This maintains consistency among ACDs.

In FY 2011, mail volumes and revenues for First-Class Mail and Periodicals continued to decline although at a slower pace than in the previous 3 years. As shown in Table IV–2, First-Class Mail declined by 5 billion pieces. Single-Piece volumes were down 10.5 percent, a little over 3 billion pieces, or more than half of the total First-Class volume loss. First-Class presort declined 3.7 percent, or about 1.7 billion pieces.

Mail volume increased for Standard Mail, Package Services, and competitive products. Standard Mail volumes increased 2.2 billion pieces, or 2.6 percent, and market-dominant Package Service volumes were 2.8 percent higher than last year. Competitive products, which include Priority Mail and Parcel Select, increased 6.1 percent over last year.

As shown in Figure IV–1, the volume loss in First-Class Mail decreased contribution to institutional costs by $1 billion.[6] The increase in Standard Mail volume only added $150 million toward the contribution to institutional costs, not enough to make up for the loss from First-Class Mail.[7] It takes approximately three pieces of Standard Mail to replace the contribution per piece from First-Class Mail. Thus, to cover the lost contribution from the First-Class volume decline, Standard Mail would have had to increase by more than 15 billion pieces, or 18 percent.

Figure IV–1 — First Class Volumes and Contributions to Institutional Costs FY 2000 – 2011



As First-Class volume continues to erode, the Postal Service's ability to cover its institutional cost also erodes. The Postal Service has focused on reductions of service in several initiatives outlined in its five-year plan to reduce its annual deficits. These include the reduction of delivery days from the current 6 to 5, and the elimination of overnight service standards for First-Class Single-Piece Mail and Periodicals in conjunction with the downsizing of its mail processing network. The Postal Service also proposes to close post offices and other retail facilities in an effort to lower costs.

6 Multiple 5 billion pieces by $0.216 (the average contribution per piece for First-Class Mail).

7 Multiply 2.2 billion pieces by $0.068 (the average contribution per piece for Standard Mail).

Table IV–2—Mail Volumes ($ in Millions)

	FY 2011	FY 2010	Increase or (Decrease)	% Change
First-Class	73,521	78,514	-4,994	-6.4%
Periodicals	7,077	7,269	-193	-2.7%
Standard Mail	84,692	82,525	2,167	2.6%
Package Services	675	657	18	2.8%
Other	496	506	-10	-1.9%
Total Mailing Services	166,461	169,471	-3,010	-1.8%
Total Shipping Services	1,473	1,389	85	6.1%
Total Mail	167,934	170,860	-2,925	-1.7%

Source: USPS FY 2011 Form 10-K at 18

Table IV–3—Mail Revenues ($ in Millions)

	FY 2011	FY 2010	Increase or (Decrease)	% Change
First-Class	32,178	34,152	-1,974	-5.8%
Periodicals	1,821	1,879	-58	-3.1%
Standard Mail	17,826	17,331	495	2.9%
Package Services	1,606	1,544	62	4.0%
Other	3,285	3,681	-395	-10.7%
Total Mailing Services	56,717	58,587	-1,870	-3.2%
Total Shipping Services	8,994	8,464	531	6.3%
Total Mail	65,711	67,051	-1,340	-2.0%

Source: USPS FY 2010 Form 10-K at 19

Table IV–3 shows mail revenues by class. The decline in First-Class volume led to reductions in revenues for the year. Total First-Class revenue dropped almost $2 billion from the previous year which was slightly offset by revenue increases in Standard Mail, Package Services, and competitive products. Because these increases were not enough to offset the significant reductions in First-Class revenues, total revenues were $1.3 billion less than last year.

As shown in Table IV–4, total expenses for FY 2011 were 6.3 percent less than last year primarily due to the deferment of the $5.5 billion payment to the Retiree Health Benefits Fund into FY 2012. Total compensation costs declined $858 million from last year due to the Postal Service's continuing efforts to reduce work hours. Some of these savings were offset by increases in Federal Employee Retirement System (FERS) retirement costs, as calculated by the Office of

Table IV–4—Total Expenses–FY 2011 ($ in Millions)

	FY 2011	FY 2010	Change in Amount	Percent Change
Compensation & Benefits	$48,312	$49,036	$(725)	-1.5%
Retiree Health Expenses	2,441	7,747	(5,307)	-68.5%
Workers Compensation	3,672	3,567	105	2.9%
Transportation	6,389	5,878	512	8.7%
Supplies & Services	2,302	2,271	31	1.4%
Depreciation and Amortization	2,313	2,469	(156)	-6.3%
Other Expenses	,203	4,459	744	16.7%
Total Operating Expenses	$70,631	$75,427	$(4,796)	-6.4%
Interest Expense	172	156	17	10.7%
Total Expenses	**$70,803**	**$75,582**	**$(4,779)**	**-6.3%**

Personnel and Management (OPM), and increases in premiums for health benefits for both current employees and retirees. Higher fuel costs drove non-personnel expenses. Transportation costs increased over $500 million and vehicle maintenance costs increased over $150 million. Additionally, the Postal Service charged to expenses $448 million for legal costs and contingent liabilities associated with arbitration awards. This expense is a one-time charge and represents the Postal Service's best estimate of the costs of these rewards.

The Postal Service was only able to meet all of its financial obligations during FY 2011 because of the deferment of the $5.5 billion payment to the Retiree Health Benefits Fund into FY 2012. Without this deferment, the Postal Service would have defaulted on the mandated payment. This one-year deferment is not a solution to the current financial problems facing the Postal Service. The Postal Service's FY 2012 Integrated Financial Plan (IFP) shows an expected net loss of $14.1 billion, of which $11.1 billion is the payment for the deferred FY 2011 Retiree Health Benefit Fund payment of $5.5 billion and the currently scheduled Retiree Health Benefit Fund payment of $5.6 billion due on September 30, 2012. Given its current financial state, the Postal Service will not have sufficient cash to make these payments. The current financing plan in the FY 2012 IFP, including the payments, shows a shortfall of $10.5 billion.

Despite undertaking several initiatives over the past few years to reduce costs, the Postal Service has not been able to offset the reductions in revenues due to rapidly declining volumes, the aggressive payment schedule that applies to its Retiree Health Benefits Fund, and its own limited use of its rate setting flexibility and new revenue opportunities. In FY 2010, the Postal Service developed a 10-year action plan that identified ways to increase revenues and control costs. This has now evolved into a five-year plan, which includes a downsizing of its mail processing network, closing retail post offices, amending service standards, and reducing the number of delivery days from 6 to 5. Under the plan, the Postal Service would leave the Federal Employee Health Benefits program and establish its own health benefits plan. It believes that this would significantly reduce its health care costs, thereby reducing the need to pre-fund retiree health benefits. Overall, the Postal Service estimates that it can reduce its costs by over $20 billion by FY 2015. The Postal Service's recovery plan, however, relies on legislative reform to provide almost half of the projected $20 billion in savings.[8]

Legislative Reform

Both the House of Representatives and the Senate have drafted legislative proposals over the past year which would reform the Postal Service's finances. Two proposals have been passed through their respective oversight committees[9] and are awaiting floor consideration.

The Senate bill, S. 1789, 21st Century Postal Service Act, would allow surplus funds in the FERS annuity fund to be transferred to the Postal Service fund but would restrict their use to incentivizing employees to retire or separate, reduce Postal Service debt, or make the required payments to the Workers Compensation Fund or the Retiree Health Benefits Fund. It would also move the start date for actuarial funding of the retiree health benefits from FY 2017

8 Details of the Postal Service's new business plan can be found on the Postal Service website at http://about.usps.com/news/national-releases/2012/pr12_029.htm.

9 The House Committee on Oversight and Government Reform and the Senate Committee on Homeland Security and Government Affairs.

to FY 2012 and eliminate the scheduled payments due in FY 2011 through FY 2016. The legislation also includes provisions on five-day delivery, retail alternatives, post office and mail processing facility closures. The proposed legislation also would allow the Postal Service to provide non-postal products and services that utilize the processing, transportation, delivery, retail network, or technology infrastructure of the Postal Service after review by the Commission.

The legislation proposed in the House of Representatives, is H.R. 2309, The *Postal Reform Act* of 2011. It also would allow the transfer of surplus funds in the FERS annuity fund to the Postal Service. It establishes two new organizations. One federal oversight entity would be the *Commission on Postal Reorganization* (CPR) which would make recommendations on the structure of the Postal Service's retail, mail processing, and area administration network. The structure of the CPR is based closely on the military Base Realignment and Closure (BRAC) system. The other entity would be established upon the Postal Service's default on any obligation due to the Department of Treasury, including the pre-funding payment to the Retiree Health Benefits Fund. *The Postal Service Financial Responsibility and Management Assistance Authority* (The Authority) would serve as an advisory board to the Board of Governors and senior Postal Service management for the first 2 fiscal years after the default. If the Postal Service's annual deficit is still $2 billion or more after those two advisory years, The Authority would assume power to change the Postal Service's operations and finances.[10] Other important changes proposed in the legislation would allow the Postal Service to declare up to 12 days for non-delivery of mail, increase rates for nonprofit and loss making postal products, and changes arbitration rules that apply to impasses in labor negotiations. The proposed legislation would also allow more flexible service arrangements with state and local governments and allow the Postal Service to sell advertising space at postal facilities and on postal vehicles.

Retiree Health Benefits Fund

One of the primary issues regarding the Postal Service's financial difficulties since the passage of PAEA remains the pre-funding requirements of the Retiree Health Benefits Fund.

In its comments, Valpak has characterized the retiree health benefit pre-funding schedule as "impossible." Valpak Comments at 19. Valpak also advises that a truly viable funding of the retiree health benefits will not occur until the Postal Service is able to generate operating profits sufficient to reduce debt and restore its net worth to the levels before enactment of the PAEA. *Id.* at 21-23. To meet this goal, the Postal Service would have required more than $11 billion in additional revenue in FY 2011. This amount would have allowed the Postal Service to make its payment to the Retiree Health Benefits Fund, cover operating losses, and possibly invest some amount to improve or replace deteriorating assets.

Valpak has also urged the Commission to evaluate the Postal Service's compliance without limiting the review to current law. Valpak says that the Commission should present one or more alternative scenarios assuming small payments to the Retiree Health Benefits Fund or no payments at all. *Id.* at 24.

The Commission has discussed the effects of the pre-funding requirement for retiree health benefits several times over the past 3 years, as well as in

[10] This power currently resides with the Board of Governors.

Congressional testimony. The Commission conducted an analysis of the Retiree Health Benefits Fund valuation and payment requirements in its July 30, 2009 report.[11] In its report, the Commission recommended several revisions to the Office of Personnel Management's (OPM) valuation of the liability and a payment schedule that was less than is currently required. The Commission also extensively discussed the effects of the pre-funding requirement in Order No. 547 denying the Postal Service's request for an exigent rate increase. The effect of the pre-funding requirement on the Postal Service's finances has been highlighted in the last three ACDs, as well as this one. Finally, the Commission, in its report to Congress required by section 701 of the PAEA, discussed the issue extensively and presented optional financing mechanisms for retiree health benefits for Congress to consider.

The PAEA requires that information on the funding status of the retiree health benefit liability be provided every year in the annual Postal Service Form 10-K statement. This information is compiled and reported to the Postal Service by OPM. It shows the obligations, costs, and funding status of the Retiree Health Benefits Fund. As of the end of FY 2011, the total actuarial liability for retiree health benefits was $90.3 billion, a reduction of over $700 million from the total liability at the beginning of the year. Total assets in the Retiree Health Benefits Fund amounted to $44.1 billion, leaving an unfunded liability of $46.2 billion, a reduction of $2.3 billion from the prior year.

Long Term Outlook

The Postal Service has significantly reduced labor costs over the past 4 years through major reductions in work hours and employees. It has also decreased operating costs by renegotiating vendor contracts and restructuring delivery routes. However, these efforts have not been enough to offset the reductions in revenues or finance the needed capital improvements to the universal network.

Legislative mandates to pre-fund large legacy retirement costs have severely eroded the Postal Service's ability to finance its current processing and delivery networks. Continued degradation of volumes and revenues due in large part to diversion to electronic alternatives and a price cap on most Postal Service products have also contributed substantially to the Postal Service's financial problems.

The most immediate need is a change in the pre-funding requirements for retiree health benefits. Dramatically reducing the required pre-funding, or even eliminating it altogether, will not, in and of itself, make the Postal Service financially viable. It will, however, provide time and resources for rational and efficient right-sizing of the processing and transportation networks that are needed to reduce the large fixed costs associated with this network. Additional time and resources are also needed to adjust rates and to encourage innovation and competitive product expansion. Innovative retail options need to be developed to ensure that every American business and household has sufficient access to the products and services provided by the Postal Service at an affordable cost.

Changes to the business model, not just cost reductions, are imperative if the Postal Service is to

[11] The analysis was requested by the House Oversight and Government Reform Subcommittee on the Federal Workforce, the Postal Service, and the District of Columbia.

survive as the largest, most efficient provider of mail services in the world and to ensure that the universal service obligations of the Act are met.

Financial Reporting Requirements

Section 3654 of title 39 requires the Postal Service to file with the Commission certain reports that conform to the Securities and Exchange Commission (SEC) regulations.[12] The reports to be filed with the Commission are the annual Form 10-K, the quarterly Form 10-Q, and Form 8-K.

Form 10-K is an annual report which contains a comprehensive summary of a company's performance, including the audited financial statements. The report also includes information regarding the executive compensation policies of the company, and detailed information on the compensation and benefits packages of all senior executive officers. This report is due to the Commission within 60 days of the end of the reportable fiscal year.

Form 10-Q is a similar report to Form 10-K, but filed on a quarterly basis. Form 10-Q provides quarterly financial reports and a management discussion of the Postal Service's operations and finances, including management's assessment of the outlook for the rest of the year. Form 10-Q is required to be filed with the Commission within 40 days of the end of the fiscal quarter.

Form 8-K is a report that includes major public announcements that could materially affect the financial status of the Postal Service. This would include public releases of financial information within a press release, public speeches, or presentations by operating managers or senior executives to Congress. It would also include any updates of significant events that would affect the financial standing of the Postal Service between filings of Form 10-K and/or Form 10-Q, such as resignations, promotions, or retirements of senior executive officers. Form 8-K must be filed within 3 business days of the occurrence of the reportable event.

The Postal Service filed the required FY 2011 Forms 10-Q in February 2011 (Quarter 1), May 2011 (Quarter 2), and August 2011 (Quarter 3). All filings were within the specified 40-day time frame. Form 10-K for FY 2011 was filed on November 16, 2011.

During FY 2011, the Postal Service filed eight Form 8-K's, notifying the Commission of senior executive personnel changes and publicly reported financial results. All of the filed Form 8-K's were within the three-day time limit.

Summary by Product

Revenue, Profit, and Losses

This section contains a general review of revenues, attributable costs, and volumes at the product level. More detailed discussion is included in Chapter VII on market dominant products and in Chapter VIII on competitive products.

For competitive products, section 3633(a)(2) requires that the revenue for each product cover its attributable cost.

For market dominant products, the PAEA includes 9 objectives and 14 factors which the Postal Service must consider when adjusting market dominant prices. Among these many different considerations are revenue adequacy and the need to generate revenue that covers the direct and indirect cost of each class or type

[12] This requirement is also embodied in the Commission's Rules of Practice and Procedure under section 3050.40.

of service. The PAEA provides the Postal Service with the pricing flexibility to balance these considerations. However, the analysis in this chapter and in Chapter VII suggests that the Postal Service is not taking full advantage of its pricing flexibility to address loss-making products. In FY 2011, 10 market dominant products failed to generate sufficient revenues to cover their direct and indirect costs. The losses for these products amounted to $1.6 billion in total.

The direct and indirect costs of all products and services represent about 60 percent of the total cost of the Postal Service. Pricing market dominant products to cover at least direct and indirect cost should not present an insurmountable hurdle for pricing market dominant products, yet the problem persists as evidenced by the continuing losses. The remainder of this section contains a discussion of product profit and losses, and product volumes.

Table IV–5 shows the volumes, revenues, attributable costs, contributions to institutional costs, and cost coverage for postal products, reflecting the current mail classification.[13] Table B–1 in Appendix B presents the same financial information by subclass, reflecting the mail classification prior to the PAEA, thus allowing the comparison of FY 2011 financial results with the financial results of previous fiscal years.

The RPW system and the billing determinants are the main sources for volumes and revenues in Table IV–5. Report B of the Postal Service's Cost Model is the source for the attributable costs (variable- and product-specific) for domestic mail. The International Cost and Revenue Analysis (ICRA) is the source for the attributable costs for international mail. As in previous years, the volume, revenue, and weight figures that the Postal Service submitted were not internally consistent.[14] The lack of internally consistent figures adds to the difficulty of validating the Postal Service's numbers within the statutory time constraints for issuing the ACD. As in previous compliance determinations, the Commission has used audited revenues and expenses in the analysis of the financial results for postal products and NSAs. Thus, the revenues and expenses used in the Commission's financial analyses are consistent with the Postal Service's audited financial statements.

Profit and Losses by Product

As Table IV–5 shows, Postal Service attributable costs totalled $41.3 billion in FY 2011, or 58.3 percent of its total costs, leaving $29.6 billion of institutional (or overhead) costs to be recovered from product revenue contributions that are greater than their costs. In part, because of mail volume declines and high costs of certain products, the revenue generated from the sale of postal products contributed only $24.4 billion to the recovery of institutional costs, leaving a negative net contribution (a loss) of $5.2 billion. The Postal Service received $95.3 million of Congressional appropriations partially covering legislated mandatory costs and $28.2 million of investment income, leaving the Postal Service with a net loss of $5.1 billion for FY 2011.

In FY 2011, 3 competitive mail products and 10 market dominant products did not generate sufficient revenue to cover their attributable costs. Thus, these

13 For a detailed presentation of the financial performance, see public library reference PRC-ACR2011-LR1 (which covers only market dominant products and NSAs) and non-public library reference PRC-ACR2011-NP-LR1 (which covers market dominant, competitive products, and NSAs).

14 As documented in library reference PRC-ACR2011-NP-LR-1, there are instances in the Postal Service's FY 2011 CRA where volume, revenue, and weight figures do not precisely match the corresponding figures in the relevant source documents, such as the RPW system and the billing determinants.

Table IV–5—FY 2011 Volume , Revenue, Cost and Cost Coverage by Class Current Classification (Products)

	Volume (000)	Revenue ($000)	Attributable Cost ($000)	Contribution to Institutional Cost ($000)	Rev./Pc. (Cents)	Cost/Pc. (Cents)	Contribution to Institutional Cost/Pc. (Cents)	Cost Coverage
Competitive Mail								
Express Mail	40,492	799,500	479,432	320,068	1,974.464	1,184.017	790.447	166.8%
Priority Mail	790,633	5,638,963	4,469,854	1,169,109	713.221	565.351	147.870	126.2%
Parcel Select and Parcel Return Service (PRS)	380,834	718,402	516,545	201,857	188.639	135.635	53.004	139.1%
Competitive International Mail	261,531	1,674,743	1,105,965	568,779	640.362	422.881	217.481	151.4%
Competitive Domestic Services	83,407	146,646	101,732	44,914	175.820	121.971	53.849	144.1%
Competitive International Services	2,021	11,688	6,476	5,212	578.248	320.405	257.844	180.5%
Total Competitive Mail and Services	**1,473,490**	**8,989,942**	**6,680,004**	**2,309,938**	**610.112**	**453.346**	**156.766**	**134.6%**
Market Dominant Mail								
First-Class Mail								
Single-Piece Letters and Cards	25,846,765	11,643,428	7,184,644	4,458,784	45.048	27.797	17.251	162.1%
Presort Letters and Cards	44,494,498	15,564,929	5,183,590	10,381,338	34.982	11.650	23.332	300.3%
Flats	2,230,920	2,819,164	1,946,399	872,764	126.368	87.246	39.121	144.8%
Parcels	637,982	1,286,003	1,168,973	117,030	201.573	183.230	18.344	110.0%
Outbound Single-Piece Mail Intl	310,335	648,080	438,476	209,605	208.832	141.291	67.541	147.8%
Inbound Single-Piece Mail Intl	44	216,756	249,709	(32,953)				86.8%
Standard Mail								
High Density & Saturation Letters	5,653,875	772,149	349,010	423,139	13.657	6.173	7.484	221.2%
High Density & Saturation Flats & Parcels	11,424,568	1,885,335	882,761	1,002,574	16.502	7.727	8.776	213.6%
Carrier Route	9,367,761	2,235,782	1,647,828	587,954	23.867	17.590	6.276	135.7%
Letters	50,719,613	9,777,603	5,288,553	4,489,049	19.278	10.427	8.851	184.9%
Flats	6,791,672	2,499,669	3,142,862	(643,193)	36.805	46.275	(9.470)	79.5%
Not Flat-Machinables and Parcels	733,770	655,613	767,298	(111,685)	89.349	104.569	(15.221)	85.4%
Inbound NSA Mail Intl	712	316	87	229				
Periodicals								
Within County	661,561	69,966	89,250	(19,283)	10.576	13.491	(2.915)	78.4%
Outside County	6,415,178	1,751,169	2,340,774	(589,605)	27.297	36.488	(9.191)	74.8%

Table IV–5—FY 2011 Volume, Revenue, Cost and Cost Coverage by Class Current Classification (Products)—Continued

	Volume (000)	Revenue ($000)	Attributable Cost ($000)	Contribution to Institutional Cost ($000)	Rev./Pc. (Cents)	Cost/Pc. (Cents)	Contribution to Institutional Cost/Pc. (Cents)	Cost Coverage
Package Services								
Single-Piece Parcel Post	70,218	732,901	821,119	(88,217)	1,043.754	1,169.388	(125.634)	89.3%
Inbound Surface Parcel Post (at UPU Rates)	1,017	24,250	10,725	13,525	2,383.777	1,054.290	1,329.487	226.1%
Bound Printed Matter Flats	251,831	205,156	125,417	79,739	81.466	49.802	31.664	163.6%
Bound Printed Matter Parcels	245,282	310,642	314,562	(3,920)	126.647	128.245	(1.598)	98.8%
Media and Library Mail	107,829	332,607	431,068	(98,460)	308.459	399.771	(91.312)	77.2%
Inbound NSA Mail Intl	14	30	2	28				
U.S. Postal Service Mail	434,596							
Free Mail	61,854		51,111	(51,111)		82.631		
Total Market Dominant Mail	166,460,877	53,431,549	32,434,216	20,997,333	32.099	19.485	12.614	164.7%
Market Dominant Services								
Ancillary Services								
Certified Mail	251,222	708,755	599,328	109,428	282.123	238.565	43.558	118.3%
COD	819	6,678	4,373	2,304	814.927	533.710	281.218	152.7%
Insurance	34,573	116,652	103,411	13,241	337.406	299.109	38.297	112.8%
Registered Mail	2,688	45,236	42,809	2,427	1,682.930	1,592.633	90.297	105.7%
Stamped Envelopes		10,650	6,886	3,764				154.7%
Stamped Cards		1,611	820	791				196.5%
Other Ancillary Services	1,698,368	771,746	579,485	192,261				133.2%
Money Orders	115,510	172,696	123,438	49,258	149.508	106.864	42.644	139.9%
Post Office Box Service		801,899	592,763	209,135				135.3%
Caller Service		92,162	27,785	64,377				
Other Special Services		35,541	17,674	17,867				
International Services	1,845	32,707	38,811	(6,104)				84.3%
Other Income		397,737		397,737				
Total Mail and Services	167,934,367	65,615,560	41,251,803	24,363,757	39.072	24.564	14.508	159.1%
Institutional Costs			29,553,781					
Appropriations: Revenue Forgone		95,285						
Investment Income		28,167						
Total Revenues		65,739,012						
Total Costs			70,805,584					
Net Income (Loss)		(5,066,572)						

Source: Library Reference PRC-ACR2011-LR1

products contributed to the Postal Service's annual losses. The negative contribution from the 10 market dominant products amounted to $1.6 billion. Table IV–6 shows the market dominant products that made negative contributions to institutional costs. The negative contribution from the three competitive products totalled only $4.3 million. The competitive products as a group generated a pre-tax net income of $684.3 million and contributed more to institutional costs than the required 5.5 percent. By law, the Postal Service must compute an assumed Federal income tax on its net income from competitive products each year and transfer that amount to the Postal Service Fund. 39 U.S.C. 3634(b).

The negative contributions of (losses from) two of the products, Standard Flats and Outside County Periodicals, amounted to $1.2 billion, or about 77 percent of the total shortfall.

Table IV–6—List of Market Dominant Products and Services with Respective Negative Contribution to Institutional Costs ($ in Millions)

1	First-Class, Inbound International Single-Piece Mail	(33.0)
2	Standard, Flats	(643.2)
3	Standard Not Flat-Machinables and Parcels	(111.7)
4	Periodicals, Within County	(19.3)
5	Periodicals, Outside County	(589.6)
6	Package Services, Single-Piece Parcel Post	(88.2)
7	Package Services, Bound Printed Matter Parcels	(3.9)
8	Package Services, Media and Library Mail	(98.5)
9	Special Services, Stamp Fulfillment Services	(2.1)
10	Special Services, International Ancillary Services	(6.1)
Total		**(1,595.6)**

Source: Library Reference PRC-ACR2010-LR1

Table IV–5 shows that with the exception of Inbound International Single-Piece Mail (Letter Post), all First-Class Mail products covered their respective attributable costs. As in previous years, in FY 2011, First-Class Presort Letters and Cards was the most successful postal product financially. Its volume was the second highest—44.5 billion pieces, or 27 percent of total mail volume. It generated the largest amount of revenue, $15.6 billion, or 24 percent of total revenue. It also made the largest contribution to institutional costs at $10.4 billion, or about 43 percent of the total contribution from all postal products. Its per-piece contribution was 23.3 cents, which is about 2.6 times higher than the per-piece contribution of Standard Letters. Its cost coverage of 300.3 percent was the highest of all products.

As in previous years, Standard Flats, and Standard Not-Flat Machinables/Parcels did not cover their attributable costs in FY 2011. First-Class Flats and Bound Printed Matter (BPM) Flats made positive per-piece contributions of 39.1 cents and 31.7 cents respectively, whereas Standard Flats made a negative per-piece contribution of 9.5 cents. The average revenues for First-Class Flats and BPM Flats were 3.4 and 2.2 times higher, respectively, than Standard Flats.

As in previous years, Periodicals did not cover attributable costs in FY 2011. The cost coverage for Outside County Periodicals declined from 75.5 percent in FY 2010 to 74.8 percent in FY 2011, while the cost coverage for Within County Periodicals showed an improvement from 75.4 percent in FY 2010 to 78.4 percent in FY 2011.

Three of the four domestic Package Service products (Single-Piece Parcel Post, Bound Printed Matter

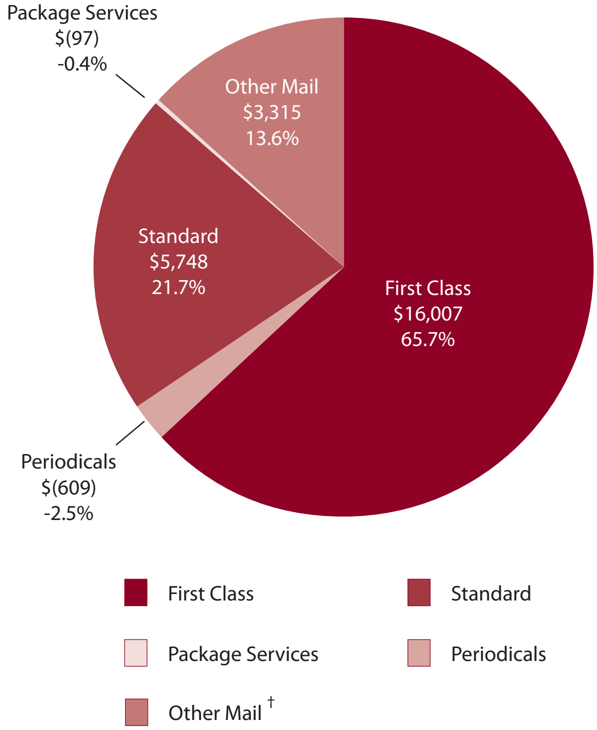
Parcels, and Media and Library Mail) failed to cover their attributable costs.

With the exception of International Ancillary Services, which recorded a cost coverage of 84.3 percent, cost coverage for market dominant Special Services products exceeded 100 percent in FY 2011.

Analysis of Current Problems in Business Model

Many market dominant products that are shrinking realize profits. Conversely, many market dominant products that are growing or stabilized are contributing minimally.

Figure IV–2—FY 2011 Contribution to Institutional (Overhead) Costs by Class (Dollars in Millions)



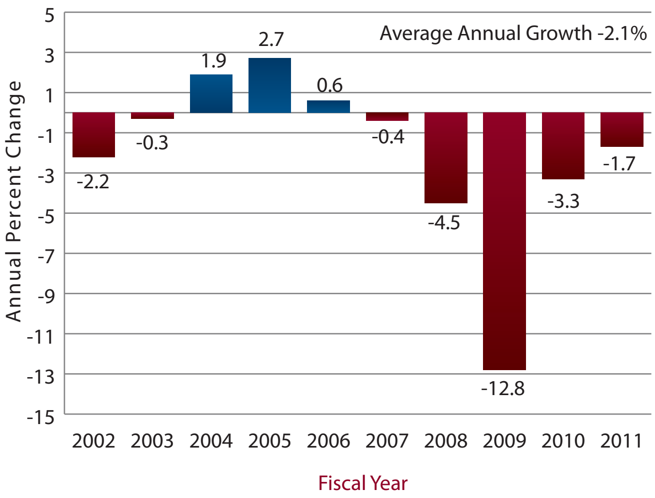
† Includes Express Mail, Priority Mail, Parcel Select, Parcel Return Service, International Competitive Mail, Free Mail, Special Services and Other Income.

The following breakdown of contributions to institutional costs is derived from Table IV–5. In FY 2011, domestic products accounted for 96.9 percent of the total contribution to institutional costs—with 89.8 percent coming from domestic market dominant products and 7.1 percent coming from domestic competitive products. International products accounted for the remaining 3.1 percent of the total contribution to institutional costs—with 0.8 percent coming from international market dominant products and 2.4 percent coming from international competitive products.

Figure IV–2 illustrates the contribution to institutional costs by each mail class. In FY 2011, First-Class Mail contributed $16 billion, or 66 percent, to the Postal Service's institutional costs. First-Class Mail volume, however, appears to be the most susceptible to diversion to electronic services, such as electronic mail, online bill payment and presentment, and online banking. In the past 10 years, First-Class Mail volume decreased by 30.1 billion pieces, or 34.4 percent. This was due, in significant part, to increased adoption of these technologies. In light of its dependency on First-Class Mail, the Postal Service is vulnerable to the continuing volume erosion to electronic services, threatening its financial stability.

Figure IV–2 also shows that Standard Mail accounted for $5.7 billion, or 21.7 percent, of the total contribution to institutional costs in FY 2011. Cost coverage for market dominant Package Services has been below 100 percent in FY 2009 and FY 2010. Periodicals contribution to institutional costs has been negative since FY 1997. Periodicals and market dominant Package Services continued to make negative contributions to institutional costs in FY 2011.

Figure IV–3—Total Mail Volume Annual Growth Rates FY 2002–2011



Mail Volumes Trends

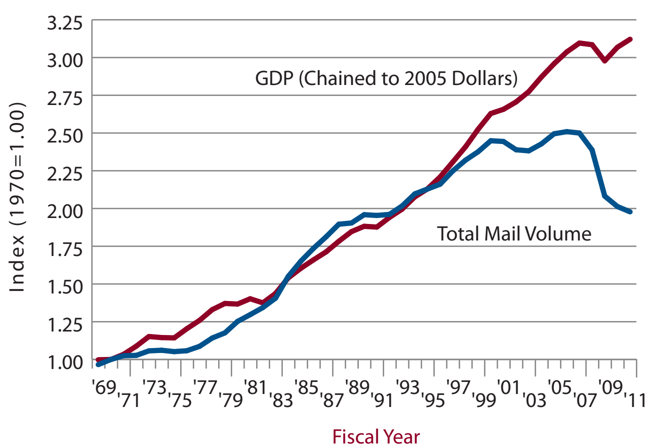
Figure IV–3 shows annual mail volume changes for the past 10 years. While the most recent economic recession ended in June 2009,[15] the effects of the economic slowdown and the rate at which mail is migrating from traditional postal hard copy services to electronic media continue to negatively impact mail volume. Although the rate of volume decline diminished in FY 2011, its downward trend continued with a decrease of 2.9 billion pieces, or 1.7 percent.[16] In the past four years (2008 – 2011), the total volume has declined by 44.3 billion pieces, or about 21 percent.

Over the past decade, the Postal Service has experienced volume reductions in 7 years and volume increases in 3 years. For the decade as a whole, volume declined at an average annual rate of 2.1 percent. In contrast, mail volume grew at an average annual rate of 2.0 percent during the 1970s, 4.9 percent during the 1980s, and 2.2 percent during the 1990s. In FY 2011, mail volume was 167.9 billion pieces, returning to FY 1992 levels.

The volume increases in FYs 2004, 2005, and 2006 coincided with the formation of the "housing bubble," which generated an unusually high demand for mail-based advertising regarding mortgage financing and refinancing, and credit card issuance. Figure IV–4 compares the growth of total mail volume with the growth of the U.S. Gross Domestic Product (GDP) over the past 42 years.

From FY 1970 to FY 2000, the growth of mail volume closely matched the growth of the U.S. economy. During the last 31 years of the 20th century, GDP and mail volume grew at an average annual rate of 3.2 percent and 3.1 percent, respectively. Since FY 2001 however, this close relationship between GDP and mail volume growth has deteriorated. During the first 11 years of the

Figure IV–4—Gross Domestic Product (GDP) and Total Mail Volume Growth FY 1969–2011



15 National Bureau of Economic Research (NBER), Business Cycle Dating Committee, September, 2010.

16 As pointed out earlier, the Postal Service makes revisions to RPW volumes and revenues due to corrections from audits and reviews, as well as due to periodic methodological changes. Volume comparisons in this section are based on revised RPW numbers.

current century, GDP has grown at an average annual rate of 1.6 percent whereas mail volume has declined at an average annual rate of 1.9 percent. This has created a gap of 3.5 percentage points between the average changes in the two measures. Over the past 11 years, GDP has grown at a steady rate, with the exception of a 0.3 percent decline in FY 2008 and a 3.5 percent decline in FY 2009, both due to the economic recession. In contrast, mail volume has stagnated or declined, with the exception of the short period of growth from FY 2004 through FY 2006.

In FY 2011, mail volume declined by 1.7 percent even though GDP grew by 1.7 percent. This created a gap of 3.4 percentage points between the two measures. This recent divergence between the trends in mail volume and GDP is expected to continue in the future. The Postal Service cannot rely on economic recovery to return to profitability. The Postal Service's financial sustainability is at greater risk than in the past and understanding the potential of each mail product to generate additional revenue is more important than ever.

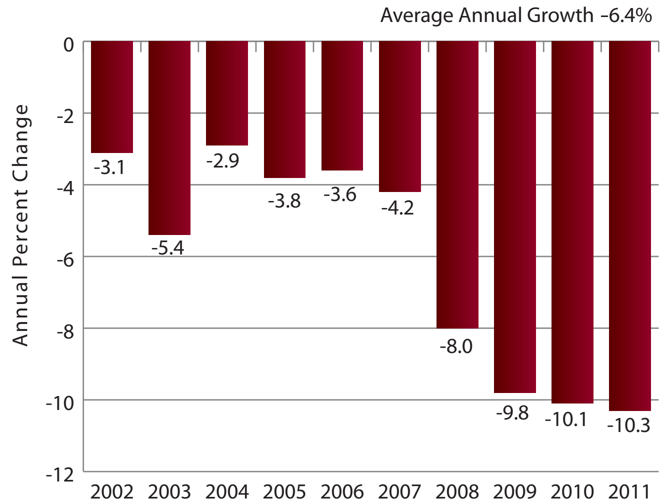
First-Class Mail Single-Piece Letters/Postcards

As Figure IV–5 shows, First-Class Mail Single-Piece Letters/Postcards volume continues its recent rapid decline. In FY 2011, First-Class Mail Single-Piece Letters/Postcards volume decreased by 3.2 billion pieces, or 10.3 percent. Over the past 10 years, the average annual decrease in First-Class Mail Single-Piece Letters/Postcards volume was 6.4 percent. As a result, First-Class Mail Single-Piece Letters/Postcards has lost 25.2 billion pieces, or about half of its total volume over this period.

First-Class Mail Presort Letters/Postcards

In the past, the growth of First-Class Mail Presort Letters/Postcards mitigated the decline of First-Class Mail Single-Piece Letters/Postcards. Recently, First-Class Mail Presort Letters/Postcards has declined as well by 2.2 percent in FY 2008, 7.8 percent in FY 2009, 3.5 percent in FY 2010, and 3.7 percent in 2011. The decline in First-Class Mail Presort Letters/Postcards volume can be attributed to electronic presentment of bills and financial statements and the economic slowdown which has adversely affected the financial industry.

Figure IV–5—First-Class Mail Single-Piece Letters/Postcards Volume Annual Growth Rates FY 2002–2011

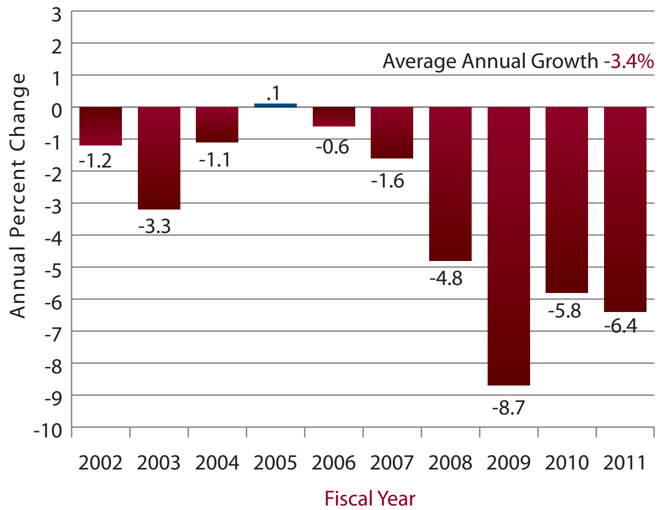


Source: Postal Service Revenue, Piece, and Weight (RPW) reports.

Figure IV–6 shows the annual growth rates for total First-Class Mail over the past 10 years.

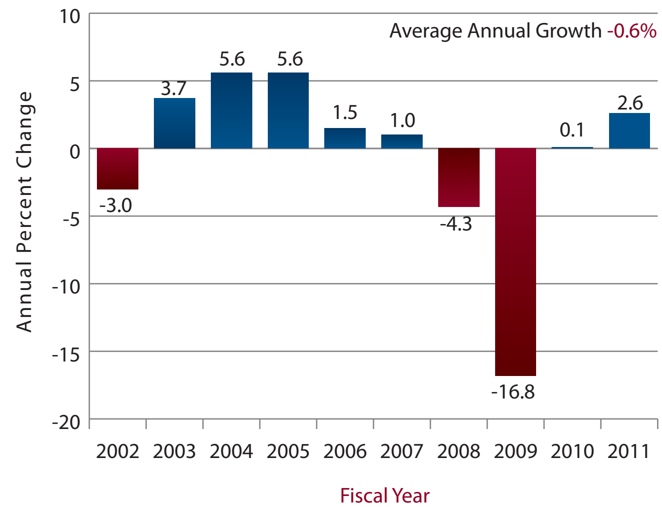
In FY 2011, total First-Class Mail volume decreased by 6.4 percent, or 5 billion pieces. The volume decline continued a downward trend that started

Figure IV–6—Total First-Class Mail Volume Annual Growth Rates FY 2002–2011



Source: Postal Service Revenue, Piece, and Weight (RPW) reports.

Figure IV–7—Standard Mail Volume Annual Growth Rates FY 2002–2011



Source: Postal Service Revenue, Piece, and Weight (RPW) reports.

in 2002. Over the past decade, First-Class Mail volume has lost 30.1 billion pieces, or 29.1 percent of its volume. The average annual rate of loss was 3.4 percent. At the end of FY 2011, First-Class Mail volume was 73.5 billion pieces, about the same level as in FY 1985.

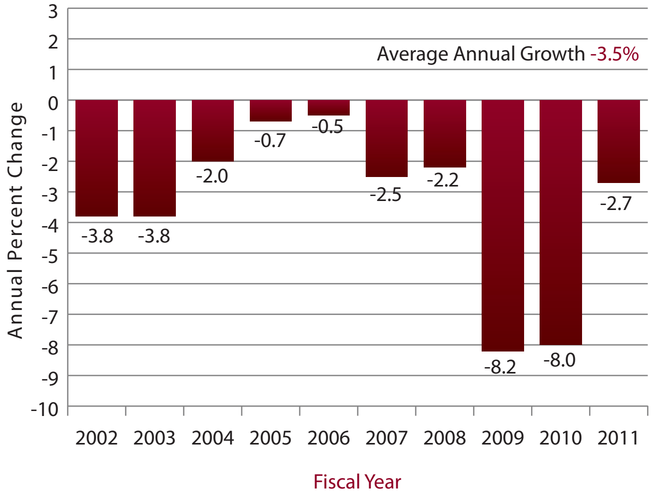
Most of the First-Class Mail volume losses are due to electronic diversion. Therefore, they are likely to be permanent. The permanent loss of First-Class Mail volume is particularly troubling because revenue from this class of mail covers most of the Postal Service's institutional costs. Standard Mail would have to increase by three pieces to compensate for the lost contribution to institutional costs for each lost piece of First-Class Mail.

Standard Mail

Standard Mail is the largest class by volume, comprising 50.4 percent of all mail delivered by the Postal Service in FY 2011. Figure IV–7 presents the annual growth rates for Standard Mail during the past decade. Signs of economic recovery can be seen in Standard Mail volume growth. After declining by 4.3 percent in FY 2008, and 16.8 percent in FY 2009, Standard Mail volume grew by 0.1 percent in FY 2010 and 2.6 percent in FY 2011. Standard Mail volume in FY 2011 was 84.7 billion pieces, 81.8 percent of its peak volume of 103.5 billion pieces in FY 2007. This represents a decline from its peak volume of almost 18.8 billion pieces. Over the past decade, Standard Mail volume declined at an average annual rate of 0.6 percent.

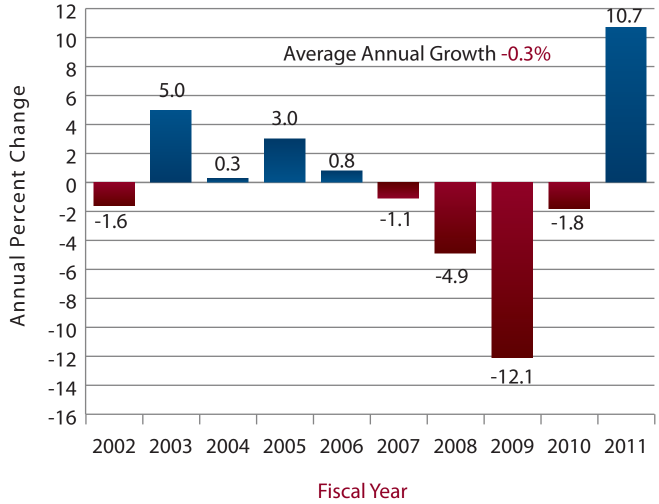
Since FY 2005, Standard Mail volume has exceeded First-Class Mail volume every year, except for FY 2009. However, even if the disparity in contribution per piece between First-Class Mail and Standard Mail can be adjusted, the growth in Standard Mail will not be sufficient to stabilize Postal Service finances.

Figure IV–8—Periodicals Volume Annual Growth Rates FY 2002–2011



Source: Postal Service Revenue, Piece, and Weight (RPW) reports.

Figure IV–9— Package Services Volume Annual Growth Rates FY 2002–2011



Source: Postal Service Revenue, Piece, and Weight (RPW) reports.

Periodicals

Figure IV–8 presents the annual change in Periodicals volume over the past 10 years. In FY 2011, Periodicals volume decreased by 2.7 percent. This is the eleventh consecutive annual volume decline.

During the past decade, Periodicals has lost about one-third of its volume, averaging a decrease of 3.5 percent annually. It is expected that the Periodicals class will continue losing volume in the future. Losses from Periodicals grow even as volume declines. The Postal Service is not able to correct rates using its pricing flexibilities because the CPI cap applies to classes.

Package Services

Package Services faces considerable market competition from private parcel carriers. At the same time, it serves a growing market as consumers increasingly use the Internet for online purchases. Figure IV–9 shows the annual change in Package Services volume over the past decade. The economic recovery has helped reverse the downward volume trends of Package Services. In FY 2011, Package Service's volume grew by 10.7 percent after suffering a 1.8 percent volume decline in FY 2010. Over the past decade, however, Package Services volume has declined at an average annual rate of 0.3 percent.

The growth rates presented in Figure IV–9 were calculated by aggregating the volumes of four market dominant products and two competitive products in order to maintain continuity with prior years' data. The Table IV–7 presents the growth rates for FY 2011 of all six products included in the Package Services growth rate calculations.

The economic recovery had a significant positive impact on Parcel Select volume. In FY 2011, Parcel Select volume increased by 27.8 percent, on top of its growth of 20.4 percent in FY 2010. Parcel Return Service volume continues its unparalleled growth, with annual volume increases of 55.9 percent in FY 2010 and 33 percent in FY 2011. The Postal Service

Table IV–7—Package Services Products FY 2011 Annual Growth Rates

	Percent Change
Market Dominant Products	
Single-Piece Parcel Post	13.4
BPM Flats	9.6
BPM Parcels	0.2
Media and Library Mail	-10.6
Market Dominant Products	2.8
Competitive Products	
Parcel Select	27.8
Parcel Return Service	33.0
Competitive Products	24.4
All Products	10.7

Source: Postal Service RPW report

Table IV–8—Change in Workhours and Compensation by Craft Over Ten FY 2002–2011 ($ in Millions)

	Workhours		Nominal Compensation Change
	Change	Percent Change	
Supervisors	(25.6)	(30.2)	(1,254.04)
Clerks & Mail Handlers	(305.9)	(46.0)	(12,167.20)
City Carriers and Vehicle Drivers	(99.4)	(20.5)	(4,169.26)
Rural Cariers	4.8	2.8	91.43
Other Employees	(26.9)	(14.0)	(1,345.36)
Total	**(453.1)**	**(28.3)**	**(18,844.44)**

Source: USPS Annual Tables, FY 2011 TFP

attributes the significant growth to its effective pricing, and beneficial trends in electronic commerce.[17]

Work Hours

In an effort to control costs, the Postal Service has aggressively reduced work hours each year since FY 2002, with the exception of FY 2005. Table IV–8 presents the cumulative change in work hours and labor compensation over the past 10 years. Over the past decade, the Postal Service shed 453.1 million, or 28.3 percent, of its work hours, saving $18.8 billion in labor costs. These savings averaged more than $1.9 billion per year — a commendable achievement considering the difficulties that the Postal Service had experienced trying to contain work hours in the 1980s and 1990s, despite its heavy investments in automation.

Table IV–9 shows the FY 2011 reduction in Postal Service work hours and savings in labor compensation

Table IV–9—FY 2011 Change in Workhours and Labor Compensation by Craft ($ in Millions)

	Workhours		Nominal Compensation Change
	Change	Percent Change	
Supervisors	(3.6)	-5.7%	(202.6)
Clerks & Mail Handlers	(13.8)	-3.7%	(658.6)
City Carriers and Vehicle Drivers	(8.2)	-2.1%	(401.4)
Rural Carriers	0.6	0.4%	25.0
Other Employees	(9.2)	-5.3%	(491.1)
Total	**(34.1)**	**-2.9%**	**(1,728.6)**

Source: USPS Annual Tables, FY 2011 TFP

17 United States Posted Service 2011 Annual Report to Congress, pages 12 and 13.

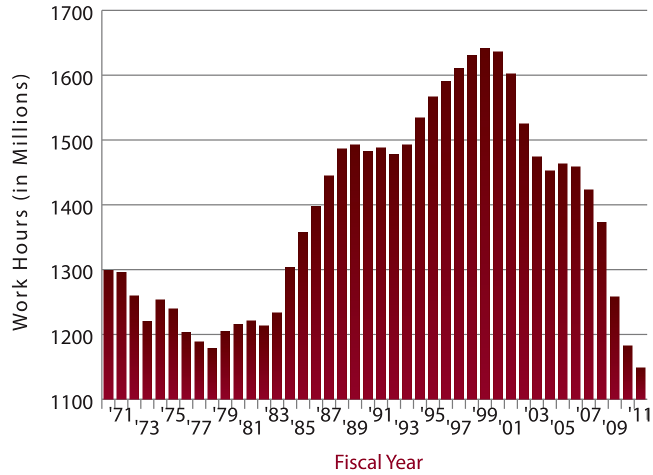
by craft. In FY 2011, responding to lower mail volumes, the Postal Service eliminated 34.1 million (or 2.9 percent) of its work hours, saving $1.7 billion in labor costs. This work hour reduction was equivalent to 26,657 full-time employees.[18] Moreover, it followed reductions of 75.1 million work hours in FY 2010 and 115.3 million work hours in FY 2009.

In FY 2011, work hours for all crafts were reduced except for rural carriers. Similar to FY 2010, clerks and mail handlers experienced the greatest reduction, losing 13.8 million work hours, or 3.7 percent.

The Postal Service eliminated 1,100 delivery routes in FY 2010, and another 6,878 routes in FY 2011.[19] The majority of the route reductions resulted from implementation of the Flat Sequencing System (FSS) and through agreements with the National Association of Letter Carriers re-evaluating the routes of approximately 70,000 city delivery routes in non-FSS delivery facilities. *Id.* According to the Postal Service, FSS automated sequencing reduced the time it takes carriers to sequence mail in the office before they go out on the street to deliver mail. Route evaluations reduced base work hours, which allowed some routes to be eliminated. Both the implementation of the FSS and the re-evaluation of routes enabled the Postal Service to absorb the additional city and rural delivery points for city and rural carriers. City carrier and vehicle service driver hours decreased by 8.2 million, or 2.1 percent, while rural carrier hours increased by 0.6 million, or 0.4 percent. Supervisor work hours decreased by 5.7 percent.

Over the past 3 years and as mail volumes declined, the Postal Service lowered its annual costs by

Figure IV–10—U.S. Postal Service Work Hours FY 1970–2011



Source: USPS Annual Tables, FY 2011 TFP

reducing its FY 2008 career employees of 663,238 to 552,251 in FY 2011—a reduction of 105,987 career employees. *Id.* Over the past 10 years, the Postal Service reduced the work hours of all crafts, except for rural carriers, which have experienced an increase of 2.8 percent. Clerks and mail handlers experienced the greatest reduction, losing 305.9 million work hours, or 46.0 percent. The work hours of supervisors and city carriers decreased by 30.2 percent and by 20.5 percent, respectively.

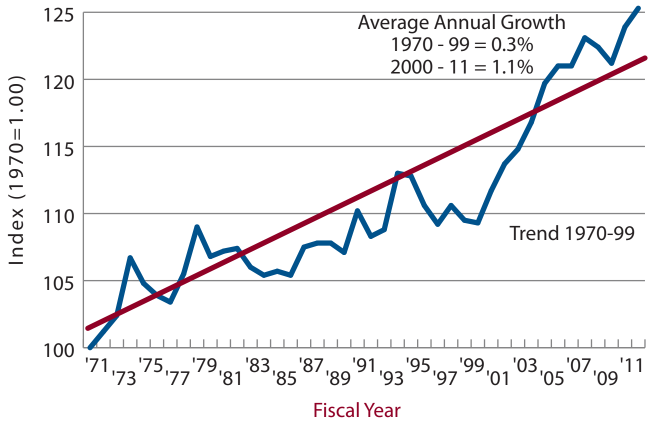
Figure IV–10 depicts the annual number of work hours used by the Postal Service over the past 42 years. In FY 2011, the Postal Service delivered 167.9 billion pieces of mail[20] to 151.5 million delivery points using 1,148.8 million work hours. This is the lowest level of work hours the Postal Service has used over that entire 42-year period.

[18] USPS-FY11-17 – 2011 Annual Report to Congress at 28. *See* also FY 2011 Annual Report to Congress and Comprehensive Statement on Postal Operations at 24.

[19] Postal Service 2011 Annual Report to Congress at 14.

[20] PRC Library Reference 11 Summary_LR-1.

Figure IV–11—U.S. Postal Service Total Factor Productivity (TFP) FY 1970–2011



Source: USPS Annual Tables, FY 2011 TFP

Productivity Measurement

The Postal Service is a labor intensive organization, with 75 percent of the value of its inputs consisting of labor.[21] From 1970 to 1999, the labor force continued to grow despite heavy capital investments in automation (*See* Figure IV–11).

As a result, over this period, TFP growth fluctuated between short periods of productivity increases and productivity declines, creating a trend of insignificant gains in postal efficiency. From FY 1970 through FY 2000, the Postal Service's productivity increased 9.3 percent, resulting in an average annual TFP growth of 0.3 percent. FY 2010 ACD at 38. By decade, the average annual TFP growth rates were as follows: 0.7 percent during the 1970s; 0.0 percent during the 1980s; 0.2 percent during the 1990s and 1.2 percent during FY 2000 through 2010.

From FY 2000 to FY 2011, the Postal Service reduced its labor force aggressively as its workload remained flat or declined. As a result, Postal Service efficiency improved from FY 2000 through FY 2007. During this eight-year period, TFP grew at an average annual rate of 1.5 percent, five times faster than during the last 30 years of the last century. After achieving 8 consecutive years of productivity increase, the Postal Service registered TFP declines of 0.5 percent and 1.0 percent for FY 2008 and FY 2009, respectively. The large drop in mail volume in FY 2008 and the record decline in FY 2009 made it difficult for the Postal Service to achieve productivity growth. In FY 2010, TFP increased by 2.2 percent[22] and in FY 2011, it grew by 1.3 percent.[23] The increase is a positive reflection of Postal Service efforts to cut work hours in the face of declining volumes. Over the past 10 years, TFP grew at an average rate of 1.0 percent annually.

TFP recognizes both mail volume and delivery points as components of the postal workload and assigns about 80 percent weight to mail volume and 20 percent to delivery points. Moreover, before merging mail volume with delivery points to calculate workload, TFP weights the volume of various postal products to account for variations in work content of mailpieces due to factors such as size, weight, preparation, and mode of transportation. Weighting pieces of mail to reflect their unequal work content allows them to be compared on a consistent basis, as "apples to apples."

[21] Source: Postal Service Annual Tables, FY 2011 TFP, Table 47. The value of labor includes all wages and benefits for all employees and retirees, including craft employees, professional, administrative, and technical personnel.

[22] As revised in Postal Service TFP Tables for FY 2011, the growth rates reflect the revised FY 2010 TFP as reported in FY 2011.

[23] Postal Service Response to CHIR 2, question 28.


U.S. POST OFFICE

Chapter V

Performance Plans & Program Performance Reports

Introduction

The PAEA requires the Commission to review the performance goals established in the Postal Service's 2011 Annual Performance Report (2011 Report) and 2012 Annual Performance Plan (2012 Plan). The Commission must evaluate whether the Postal Service has met the performance goals established in the 2011 Report, and evaluate the 2012 Plan. It may also provide recommendations to the Postal Service related to protecting or promoting public policy objectives in title 39. 39 U.S.C. 3653(d).

In the FY 2010 ACD, the Commission found that the 2010 Annual Performance Report (2010 Report) and 2011 Annual Performance Plan (2011 Plan) improved over past filings because they adhered more closely to statutory requirements and addressed the Commission's concerns from prior ACDs. 2010 ACD at 41. However, the quality of information provided in the 2011 Report and 2012 Plan declined compared to what was provided in the previous year. The Postal Service provided fewer details about the performance goals, performance indicators, and strategic initiatives compared to last year's filing.

Future Annual Performance Reports, Annual Performance Plans, and descriptions of strategic initiatives should, at a minimum, contain information similar in the level of detail provided in the 2010 Comprehensive Statement on Postal Operations,[1] 2010 Report, and 2011 Plan.

As with the 2011 Plan, the 2012 Plan does not meet the statutory requirement of covering each program activity set forth in the Postal Service's budget. *See* 39 U.S.C. 2803(a).

1 Docket No. ACR2010, Library Reference USPS-FY10-17, at 51-53 (2010 Comprehensive Statement).

To facilitate analysis and discussion, this chapter is divided into the following sections: Statutory Requirements, Performance Goals and Indicators, Strategic Initiatives, Public Comments, Evaluation of Statutory Requirements, and Review of Performance Goals and Strategic Initiatives.

Statutory Requirements

In each ACR filing, the Postal Service must submit copies of its most recent Annual Performance Report and Plan. 39 U.S.C. 3652(g). Since 2004, the Postal Service has combined the Annual Performance Report and Plan with the Comprehensive Statement on Postal Operations. In FY 2011, the Postal Service combined the Annual Performance Report and Plan, Comprehensive Statement on Postal Operations, and the Annual Report to Congress into a single report.[2] In the 2011 ACR, the Postal Service filed the 2011 Comprehensive Statement on Postal Operations (2011 Comprehensive Statement), the 2011 Report, and 2012 Plan as a library reference.[3]

Annual Performance Plan Requirements

Annual Performance Reports and Plans must meet the requirements set forth in 39 U.S.C. 2803 and 2804.[4] Annual Performance Plans must cover "each program activity set forth in the Postal Service budget…." 39 U.S.C. 2803(a). Section 2803(a) also requires Annual Performance Plans to:

- Establish performance goals defining the level of performance achieved by a program activity;[5]
- Express performance goals in an objective, quantifiable, and measurable form;
- Describe the operational processes, skills and technology, and other resources needed to meet the performance goals;
- Establish performance indicators to measure the relevant outputs, service levels, and outcomes of each program activity;[6]
- Provide a basis for comparing actual program results with established performance goals; and
- Describe the means used to validate measured values.

The Postal Service may express performance goals for a particular program activity in an alternative form if the Postal Service determines that expressing those goals in an objective and quantifiable manner is not feasible. The alternative form must describe "minimally effective" and "successful" programs. 39 U.S.C. 2803(b).

The Postal Service may aggregate, disaggregate, or consolidate program activities when preparing the Annual Performance Plan. It may also prepare a non-public annex covering program activities under certain circumstances. 39 U.S.C. 2803(c) and (d).

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2 Delivering the New Reality: 2011 Annual Report to Congress and Comprehensive Statement on Postal Operations, available at *http://about.usps.com/publications/annual-report-comprehensive-statement-2011/annual-report-comprehensive-statement-2011.pdf (Combined Report).*

3 Library Reference USPS-FY11-17.

4 Chapter 28 of title 39, which includes sections 2803 and 2804, was added by the Government Performance and Results Act of 1993, Pub. L. No. 103-62, 107 Stat. 285 (1993).

5 Performance goal means "a target level of performance expressed as a tangible, measurable objective, against which actual achievement shall be compared, including a goal expressed as a quantitative standard, value, or rate[.]" 39 U.S.C. 2801(3).

6 Performance indicator refers to "a particular value or characteristic used to measure output or outcome[.]" 39 U.S.C. 2801(4).

Annual Performance Report Requirements

Annual Performance Reports must cover program performance for each fiscal year. They must set forth the performance indicators established in the Annual Performance Plan, along with the actual performance achieved compared with the performance goals. If the Postal Service specifies performance goals in an alternative form by describing minimally effective and successful program activities, it must provide program results relating to those categories. Annual Performance Reports must include results for the 3 preceding fiscal years. 39 U.S.C. 2804(a)-(c).

Each Annual Performance Report must (1) review the success of achieving performance goals, (2) evaluate the Annual Performance Plan relative to the performance achieved towards the performance goals, and (3) include summary findings of those program evaluations.[7] If a performance goal has not been met, the Postal Service must explain and describe why the goal was not met, as well as plans and schedules for achieving the goal. If the performance goal is impractical or infeasible, the Postal Service must explain why that is the case and recommend a course of action. 39 U.S.C. 2804(d).

Performance Goals and Indicators

The 2011 Report and 2012 Plan set forth three performance goals: Improve Service, Improve Financial Performance, and Improve Safety and Employee Engagement. Response to CHIR No. 2, question 19. To evaluate its progress towards achieving the performance goals, the Postal Service established seven performance indicators, which are described in more detail below. For each performance indicator, the Postal Service set annual targets for FY 2012 and published them in the 2012 Plan. The 2012 Plan explains how results will be measured and describes any indicator or measurement changes from prior years. Combined Report at 32.

The 2011 Report provides results against FY 2011 targets and serves as a baseline for establishing FY 2012 targets. The Postal Service states that it does not provide detailed data at the program level, but does describe the reporting tools and measurement systems used. *Id.* at 33.

[7] Program evaluation means "an assessment, through objective measurement and systematic analysis, of the manner and extent to which Postal Service programs achieve intended objectives." 39 U.S.C. 2801(6).

Table V–1—Comparison of Results with Targets for Performance Goals

Performance Goals	Performance Indicator	2009 Actual	2010 Actual	2011 Target	2011 Actual	2012 Target
Improve Service	First-Class Mail Single-Piece Letters/Postcards Overnight	96.2%	96.36%	96.65%	96.23%	96.65%
	First-Class Mail Single-Piece Letters/Postcards 2 Days	93.7%	93.71%	94.15%	93.34%	94.15%
	First-Class Mail Single-Piece Letters/Postcards 3-5 Days	92.2%	92.44%	92.85%	91.87%	92.85%
Improve Financial Performance	Operating Income ($ billions)	–	–	(0.9)	(2.2)	(3.0)
	Deliveries per Work Hour	–	–	40.4	39.9	42.2
Improve Safety and Employee Engagement	OSHA Illness and Injury Rate	5.62	5.49	5.39	5.67	5.57
	Voice of the Employee Survey	64.0	62.3	64.5	64.7	64.9

Sources: Combined Report at 33; Response to CHIR No. 4, question 14. Footnotes from the original table have been omitted.

Table V–1 lists the seven performance indicators currently used by the Postal Service to evaluate performance towards achieving its three performance goals of Improve Service, Improve Financial Performance, and Improve Safety and Employee Engagement. For each performance indicator, the Postal Service provided actual results for fiscal years 2009, 2010, and 2011, as well as targets for fiscal years 2011 and 2012. Of the seven performance indicators, three support Improve Service, two support Improve Financial Performance, and two support Improve Safety and Employee Engagement.

FY 2011 Performance Indicator Changes

In past years, the Postal Service used service performance scores for Express Mail, Priority Mail, and Parcel Select as three additional performance indicators under Improve Service. 2010 ACD at 44. However, they were not included as performance indicators in FY 2011.

The Postal Service explains that service performance scores for competitive products were not included as performance indicators because they are commercially sensitive. It notes that while the 2010 Report listed Express Mail, Priority Mail, and Parcel Select as performance indicators, the 2010 Report did not provide service performance scores for those products. Instead, the 2010 Report noted that "[c]ompetitive product performance is not publicly reported." The Postal Service states that it removed competitive products from the list of performance indicators rather than include the same notation in the 2011 Report. Response to CHIR No. 4, question 10.

Also, Table V–1 does not include results for Operating Income and Deliveries per Work Hour (DPWH) in fiscal years 2009 and 2010 because these performance indicators were introduced in FY 2011. In past years, the Postal Service used Total National Revenue and Total Factor Productivity (TFP) as performance indicators for Improve Financial Performance. In FY 2011, the Postal Service replaced them with Operating Income and DPWH. 2010 ACD at 45.

Performance goals and performance indicators are discussed in further detail, below.

Improve Service

The three performance indicators that support Improve Service are First-Class Mail Single-Piece Letters/Postcards Overnight, First-Class Mail Single-Piece Letters/Postcards 2 Days, and First-Class Mail Single-Piece Letters/Postcards 3-5 Days. The Postal Service uses First-Class Mail Single-Piece Letters/Postcards service performance as a model for service performance reporting and management because it is the category of mail most familiar to Postal Service stakeholders. The Postal Service also measures service performance for other categories of mail, including Presort First-Class Mail, Standard Mail, Periodicals, Package Services, and Special Services. It reports measurement methods and quarterly service performance results on its website. Combined Report at 33.

In FY 2011, service performance scores for First-Class Mail Single-Piece Letters/Postcards fell below FY 2011 targets for all three performance indicators (Overnight, 2 Days, and 3-5 Days). The Postal Service explains that natural disasters in different parts of the United States affected its ability to meet FY 2011 targets. It also states that it has been undergoing organization realignment, which diverted some attention from service performance. *Id.* at 34.

The Postal Service explains that unlike in previous years, service performance measurements in FY 2012 will be based on combined domestic First-Class Mail Single-Piece Letters/Postcards and Presort First-Class Mail On-Time Originating and Destinating Composite year-to-date results. To help ensure that it meets FY 2012 targets, the Postal Service states that it will continue to provide the field with useful tools to address the new combined First-Class Mail mix, such as diagnostic reports for Presort First-Class Mail. Response to CHIR No. 4, question 11. For a more detailed discussion of First-Class Mail Single-Piece Letters/Postcards performance, please see Chapter VI on Service Performance.

Improve Financial Performance

In FY 2011, the Postal Service changed the financial performance indicators by discontinuing its use of Total National Revenue and TFP. It replaced Total National Revenue with Operating Income, which is total operating revenues less total operating expenses. Operating expenses include all expenses other than pre-funding the Retiree Health Benefits Fund and adjustments to Workers Compensation liabilities that may result due to changes in discount rates. 2010 ACD at 45.

In FY 2011, the Postal Service had an operating loss of $2.2 billion, which was $1.3 billion higher than the FY 2011 target operating loss of $0.9 billion. For FY 2012, the target is a loss of $3.0 billion. Combined Report at 33.

The Postal Service also replaced TFP with DPWH as a financial performance indicator in FY 2011. DPWH is an efficiency measure comparing the total number of deliveries of all types with the total number of workhours used in all employee categories. The total number of deliveries is calculated by multiplying the number of delivery points by the number of delivery days. This number is then divided by the total number of workhours used in all employee categories, including managers and executives. The result is the number of annual deliveries completed per workhour used. *Id.* at 35.

In FY 2011, DPWH of 39.9 deliveries did not meet the FY 2011 target of 40.4 deliveries. The

Postal Service explains that one major reason for not achieving the target was slippage in the planned development schedule of the Flats Sequencing System (FSS). It notes that the vast majority of planned workhour reductions for FY 2011 were based on expected volume or workload loss and that there was no relief from contractual barriers hindering workforce flexibility. The Postal Service states that it was unable to reduce sufficient workhours at the pace necessary to achieve the target given its largely full-time regular workforce. Response to CHIR No. 4, question 12.

In FY 2012, the target is 42.2. The Postal Service explains that this target was set based on expected large volume declines and projected savings from the Network Rationalization and Retail Access Optimization initiatives. It states that the FY 2012 target will be difficult to achieve because of the Congressional request to delay implementing these initiatives until May 2012. It notes that volumes and workload are exceeding the FY 2012 budget expectation, which requires using additional work hours. *Id.*

Improve Employee Engagement

The Postal Service relies on two performance indicators to evaluate progress towards its performance goal of Improve Safety and Employee Engagement. It uses the Occupational Safety and Health Administration (OSHA) Illness and Injury Rate to measure improvements in safety. The OSHA Illness and Injury Rate measures the number of injuries and illnesses that occur per 100 employees. It is calculated by multiplying the total number of OSHA injuries and illnesses by 200,000 hours, which represents 100 employees working 2,000 hours per year. That number is then divided by the number of hours all employees actually worked, which excludes vacation, sick leave, holidays, and all other non-work time, paid or unpaid.[8] Combined Report at 35.

In FY 2011, the OSHA Illness and Injury Rate of 5.67 did not meet the FY 2011 target of 5.39. The Postal Service explains that the FY 2011 target was not achieved because of unprecedented winter weather across the United States during December 2010 and January and February 2011. It asserts that the weather caused a spike in the OSHA Illness and Injury Rate from which the Postal Service did not recover. Response to CHIR No. 4, question 13.

The target for FY 2012 is 5.57. The Postal Service states that it is on target to achieve this goal and notes that it continually encourages and audits safety program implementation and monitors OSHA Illness and Injury Rates. *Id.*

The Postal Service tracks employee engagement and workplace concerns using an index consisting of employee responses to key questions from the Voice of the Employee (VOE) Survey. The performance indicator is the VOE Survey score, which is the average percent of employees responding favorably to eight questions from the VOE Index. These questions address the following issues: Strategic Direction, Trust, Contribution to Postal Service Growth, Communication, Diversity and Respect, Commitment, Personal Safety, and Work Effort and Quality. Combined Report at 35; Response to CHIR No. 4, question 14.

The Postal Service states that survey responses have remained positive despite the challenges faced by the Postal Service and its employees. In FY 2011, the

8 "How To Compute a Firm's Incidence Rate for Safety Management," Bureau of Labor Statistics, Injuries, Illnesses, and Fatalities, available at *http://www.bls.gov/iif/osheval.htm.*

VOE Survey score was 64.7, which exceeded the FY 2011 target of 64.5 by 0.2 points. Combined Report at 33, 35. The FY 2012 target is 64.9. Response to CHIR No. 4, question 14.

Strategic Initiatives

In the 2008 and 2009 ACDs, the Commission asked the Postal Service to produce Annual Performance Reports and Plans adhering more closely to the requirements of 39 U.S.C. 2803 and 2804. In the 2010 ACR, the Postal Service responded to the Commission's request by introducing and describing nine strategic initiatives to help clarify the connection between performance goals and the actions necessary to achieve them. 2010 ACD at 46.

The strategic initiatives were contained in an appendix to the 2010 Comprehensive Statement. 2010 Comprehensive Statement at 51-53. The Postal Service described the purpose of each strategic initiative, the performance goal(s) supported, FY 2011 targets, and results indicators used to measure success in meeting those targets. Table V–2 displays the information that was reported in the 2010 Comprehensive Statement.

However, the 2011 Comprehensive Statement does not contain as detailed information about the strategic initiatives as the 2010 Comprehensive Statement. The 2011 Comprehensive Statement contains a chart similar to Table V–2 that lists each strategic initiative and describes the progress made for each one during FY 2011. Combined Report at 30. However, the chart does not provide FY 2012 targets for each strategic initiative.[9] Also, it does not describe the purpose of each strategic initiative and the performance goal(s) it supports.

The Postal Service explains that it did not provide FY 2012 targets because it has initiated a comprehensive review of the strategic initiatives due to dramatic changes occurring in the Postal Service's business environment. It notes that this process will restructure some existing strategic initiatives and develop new priorities and initiatives. It states that FY 2012 targets are currently under development. Response to CHIR No. 2, question 23. The Postal Service asserts that stakeholders can expect more details on more programs in FY 2012. Combined Report at 31.

Intelligent Mail

Intelligent Mail is a strategic initiative that measures results based on the percentage of workshared mail containing an Intelligent Mail barcode (IMb). Initially, the FY 2011 target was for 90 percent of workshared mail, excluding Within-County Periodical volumes, to have either a Full-Service or Basic IMb. 2010 ACD at 46. In the 2010 ACR, the Postal Service revised this target.[10]

The Postal Service provides FY 2012 targets in the 2011 ACR. Table V–3 lists the percentage of mail, by class, that is expected to contain a Full-Service or Basic IMb by the end of FY 2012, rounded to the nearest percent.

In FY 2011, the Postal Service states that it has made substantial progress in improving its scanning infrastructure and processes and collaborating with mailers and mailing industry. It reports that the

[9] In response to CHIR No. 2, question 16, the Postal Service provided FY 2012 targets for the Intelligent Mail strategic initiative.

[10] This target assumed that mailers would be required to use IMb by the end of May 2011 to receive an automation discount. The Postal Service revised this target because this assumption was no longer valid. *Id.*

Table V–2—Strategic Initiatives that Support Performance Goals

Strategic Initiative	Performance Goals Supported	Results Indicator	FY 2011 Target
Intelligent Mail	Service Employee Engagement Financial Performance	Increase the percentage of workshared mail containing an Intelligent Mail barcode. (Full-Service and Basic, excluding Periodicals Within-County volumes.)	90% by end of year
Flats Sequencing System	Service Financial Performance	Increase the percentage of flat mail in delivery point sequence for delivery zones on the Flats Sequencing System that have been operating for at least 6 months	72%
Expand Access	Service Financial Performance	Expand share of retail revenue generated by means other than at a postal retail counter.	35%
Optimize Network	Service Financial Performance	Reduce total interior facility space.	Reduce by 2.8 million sq. ft.
Flexible Workforce	Service Employee Engagement Financial Performance	Come in below the Integrated Financial Plan average workhour rate. (Bargaining and casual employees, including wages, benefits, and existing contractual wage increases. Excludes current and prefunding payments for the Retiree Health Benefits Fund.)	$41.69/hour
Reduce Energy Use	Financial Performance	Continue progress toward FY 2015 energy reduction goals.	On target
Reduce Delivery Fixed Costs	Financial Performance	Increase average number of deliveries per route. (Combination of city and rural delivery routes)	589 by end of year
Expand Products, Services, and Features	Service Employee Engagement Financial Performance	Create new products, services, and features.	15 new
Address Overfunded Legacy Costs	Employee Engagement Financial Performance	Address legacy cost funding issues.	All three addressed

Source: 2010 Comprehensive Statement at 53.

percentage of eligible workshared mail containing an IMb increased from 52 percent in Quarter 1 to 72 percent in Quarter 4. Mail using Postnet codes decreased from 44 percent to 25 percent during that same period. Combined Report at 30.

The Postal Service explains that it is taking several steps to increase Full-Service IMb usage in FY 2012. It notes that in January 2012, it provided free visibility (container, tray, and piece level scans) for Full-Service IMb mailings to enable mailers to monitor the movement of mailings throughout the Postal Service network. It anticipates that free visibility will entice

Table V–3—FY 2012 Year End IMb Expectations

Mail Class	Full-Service IMb	Basic IMb
First-Class Mail	55%	34%
Standard Mail	38%	38%
Periodicals	55%	13%

Source: Response to CHIR No. 2, question 16.

mailers who are currently using Basic IMb to move to Full-Service IMb. It states that it is also implementing an IMb Small Business tool to enable small mailers to generate Full-Service IMb mailings through an easy to use web-based tool. Response to CHIR No. 2, question 16.

Flats Sequencing System

The FSS is a strategic initiative that measures results based on the percentage of flat mail in delivery point sequence (DPS) for delivery zones operational on the FSS for at least 6 months. The FY 2011 target was 72 percent. 2010 ACD at 48.

In FY 2011, the Postal Service reports that it increased the percentage of flat mail sorted in DPS. It notes that 23 of the 46 FSS sites have been operating 6 months or more. However, at these sites 59 percent of flats on average were sorted in DPS, falling short of the FY 2011 target of 72 percent. Two sites exceeded the FY 2011 target with scores of 79 percent. Combined Report at 30.

Expand Access

Expanding postal access is a strategic initiative that measures results based on increases in the proportion of retail revenue generated by means other than a postal retail counter. The FY 2011 target was 35 percent. 2010 ACD at 48. The Postal Service exceeded this target by increasing the share of revenue generated from alternate channels to more than 35 percent. It notes that PC Postage led with 28 percent revenue growth and that alternative access transactions have a lower per-dollar transaction rate than similar transactions at postal windows. Combined Report at 30.

Optimize Network

Under this strategic initiative, the Postal Service adapts physical networks to changes in mail volume, mail mix, and customer behavior. Results are measured by reductions in total interior facility space, and the FY 2011 target was a reduction of 2.8 million square feet. 2010 ACD at 48. The Postal Service exceeded this target by reducing interior space by over 4.4 million square feet from property disposals, lease terminations, and leased space reductions. It notes that it reduced annual rent paid to landlords by over $140 million compared to FY 2010. Combined Report at 30.

Flexible Workforce

Under the Flexible Workforce strategic initiative, the Postal Service seeks to reduce workhours and the cost of those hours. *Id.* Results are measured by the average hourly rate for bargaining and casual employees, including existing contractual wage increases. The results exclude Retiree Health Benefits Fund (RHBF) payments, which are not within management's control. In FY 2011, the target was for the average hourly rate to fall below $41.69, the average hourly rate contained in the 2011 Integrated Financial Plan. 2010 ACD at 48. The Postal Service more than met this target with an average hourly rate of $41.60. Combined Report at 30.

Reduce Energy Use

The Postal Service proposes to reduce energy use each year, primarily for transportation fuel and utilities. Results are measured based on continued progress toward meeting the FY 2015 energy reduction goals set forth in the Strategic Sustainability Performance Plan. 2010 Comprehensive Statement at 52. These energy reduction goals include:

- Reduce Scope 1, 2, and 3 greenhouse gas emissions 20 percent by FY 2020;
- Reduce total facility energy use (billion Btu) 30 percent by FY 2015;
- Reduce facility energy intensity (Btu/GSF) 30 percent by FY 2015;
- Reduce Postal-vehicle petroleum fuel use 20 percent by FY 2015;
- Increase Postal-vehicle alternative fuel use 10 percent annually by FY 2015.[11]

The FY 2011 target for the Reduce Energy Use strategic initiative was for the Postal Service to be on track to meet these energy reduction goals. 2010 Comprehensive Statement at 52; 2010 ACD at 49.

As of FY 2010, the Postal Service was on track to meet most of its energy reduction goals.[12] It increased postal vehicle alternative fuel use by 132.7 percent since FY 2005.[13] The Postal Service reports that according to FY 2011 preliminary calculations, it has reduced total facility energy use by 25.6 percent and facility energy intensity by 22.4 percent. It states that it is on target to reducing Scope 1 and 2 greenhouse gas emissions 20 percent by FY 2020. However, it was not on track to meet its goals of reducing postal vehicle petroleum fuel use 20 percent by FY 2015 and select Scope 3 greenhouse gas emissions 20 percent by FY 2020. Response to CHIR No. 5, question 2.

Reduce Delivery Costs

The Postal Service seeks to reduce fixed delivery costs because of declining volume and revenue per delivery point. Results are measured by the average number of deliveries per route for city and rural routes combined. The FY 2011 target was 589 deliveries per route by the end of the year. 2010 ACD at 49.

The Postal Service exceeded the FY 2011 target by increasing the average number of deliveries per route to 592. It notes that implementing the FSS reduced about 4,250 city routes and 154,000 rural workhours. It states that non-FSS route evaluations eliminated approximately 2,100 city routes, and sequencing performance of letter mail also improved. The number of routes eliminated does not include rural routes reduced by the FSS because rural reductions were measured by reduced workhours rather than reduced routes.[14]

Expand Products, Services, and Features

Under this initiative, the Postal Service provides customers with new mailing and shipping products, services, and features to meet their changing needs. Results are measured by the number of new products, services, and features created. The FY 2011 target was 15. 2010 ACD at 49.

[11] Response to CHIR No. 5, question 2.

[12] The Postal Service provided FY 2010 data because FY 2011 results were not yet available. Combined Report at 30 n.1.

[13] FY 2011 Strategic Sustainability Performance Plan, June 3, 2011, at 3, 37, available at *http://about.usps.com/what-we-are-doing/green/sspp/2011/usps_fy2011_sspp.pdf*.

[14] Combined Report at 30; Response to CHIR No. 5, question 3. In FY 2011, the Postal Service reports that it reduced the total number of city and rural delivery routes nationally by 6,878. Combined Report at 14. This number includes both city and rural routes reduced in FY 2011 and does not distinguish between FSS and non-FSS reductions. Response to CHIR No. 5, question 3.

In FY 2011, the Postal Service exceeded its target by unveiling 23 new products, services, and features in the areas of shipping, retail, marketing mail, and transactions and correspondence.[15] It states that 12 new products, services, and features were created to attract new mailers and included multiple new shipping services, Every Door Direct Mail, and a web-based direct mail hub. Combined Report at 9, 30. It explains that 11 new products, services, and features were aimed at improving service to mailers by providing easy and convenient ways to develop direct mail online and manage customers' mail more efficiently. *Id.*

Address Legislative Requirements for Funding

The purpose of this strategic initiative is to address funding requirements for the Civil Service Retirement System, the Federal Employee Retirement System, and the RHBF. The FY 2011 target was for the Postal Service to address all three funding issues. 2010 ACD at 49. The Postal Service met this target by supporting an extensive outreach program to Congress and stakeholders, along with the Commission, the Postal Service Office of the Inspector General, and others. It states that legislation addressing several critical funding issues is being developed or has been introduced. Combined Report at 30.

[15] The 23 new products, services, and features are (1) Critical Mail; (2) ePacket; (3) ePostage; (4) Flat Rate Legal Size Express Mail Envelope; (5) Hold for Pickup; (6) Parcel Select Regional Ground; (7) Prepaid Forever Flat Rate Priority Mail; (8) Priority Mail Regional Rate Boxes; (9) Sample Showcase; (10) Returns Portfolio; (11) Gift Cards; (12) P.O. Box Real Mail Notification; (13) P.O. Box Street Addressing; (14) USPS.com: Spanish and Chinese Translations; (15) USPS.com: New/Updated Applications and Services; (16) USPS.com: New Mobile Devices Releases; (17) DM Hub; (18) Every Door Direct Mail; (19) Improved Saturation/High Density Program; (20) Mobile Barcode Promotion; (21) Alternate Postage; (22) Remittance Mail Redirect; and (23) Reply Rides Free/Second Ounce Free.

Public Comments

In Order No. 1095, the Commission solicited comments from interested persons concerning the Postal Service's progress in meeting its performance goals. Order No. 1095 at 5. Valpak and the Public Representative submitted comments on the 2011 Report and 2012 Plan. Both participants argue that the Annual Performance Report and Plan should include service performance measurements for Standard Mail. The Public Representative argues that the Annual Performance Report and Plan should include on-time service performance for Standard Mail products and establish Standard Mail performance as an organization-wide goal. PR Comments at 29. Similarly, Valpak contends that the Annual Performance Report should recognize Standard Mail as a "program activity" under 39 U.S.C. 2803(a) and provide data on speed and reliability of delivery for Standard Mail products. Valpak Initial Comments at 107.

The Public Representative observes that the quality of information provided in the 2011 Comprehensive Statement declined compared to last year's filing. He argues that the 2012 Plan does not meet the statutory requirement to cover each program activity set forth in the Postal Service's operating budget. He reiterates concerns expressed by the Commission in the 2010 ACD about using Operating Income and DPWH as performance indicators for the Improve Financial Performance performance goal. He notes that the Postal Service did not update the strategic initiatives to include FY 2012 targets and that the Postal Service failed to meet targets set for the Intelligent Mail and FSS strategic initiatives. PR Comments at 28-31.

Evaluation of Statutory Requirements

In the FY 2010 ACD, the Commission found that the 2010 Report and 2011 Plan improved over past filings because they adhered more closely to statutory requirements and addressed the Commission's concerns from prior ACDs. 2010 ACD at 41. However, as the Public Representative notes, the quality of information provided in FY 2011 declined compared to FY 2010. The 2011 Report and 2012 Plan contain less comprehensive descriptions of the performance goals and performance indicators. They also exclude three performance indicators used in the 2010 Report and 2011 Plan. The 2011 Comprehensive Statement omits key details about the strategic initiatives that were provided in the 2010 Comprehensive Statement, such as results indicators and FY 2012 targets.

Future Annual Performance Reports, Annual Performance Plans, and descriptions of strategic initiatives should, at a minimum, contain information similar in the level of detail provided in the 2010 Comprehensive Statement, 2010 Report, and 2011 Plan.

As with the 2011 Plan, the 2012 Plan does not meet the statutory requirement of covering each program activity set forth in the Postal Service's budget. *See* 39 U.S.C. 2803(a).

2011 Report

The 2011 Report satisfies the requirements in 39 U.S.C. 2804, except for section 2804(d)(3)(C). It sets forth the seven performance indicators established in the 2012 Plan and compares FY 2011 results with FY 2011 targets. For each performance indicator, the 2011 Report reviews the Postal Service's success in achieving the performance goals by evaluating progress towards FY 2011 targets. It evaluates the 2012 Plan relative to the performance achieved towards the FY 2011 performance goals and includes results for fiscal years 2008, 2009, and 2010. Combined Report at 33; Response to CHIR No. 2, question 21.

As discussed below, the Postal Service did not meet the performance goals for Improve Service and Improve Financial Performance. In those cases, the Postal Service must explain why it did not meet the performance goal and describe plans and schedules for achieving the performance goal. 39 U.S.C. 2804(d)(3). If the performance goal is impractical or infeasible, the Postal Service must explain why that is the case and what action it recommends for achieving the goal.

For the Improve Service performance goal, the Postal Service explains that First-Class Mail Single-Piece Letters/Postcards performance fell short of FY 2011 targets because of organizational realignment and natural disasters in different parts of the United States. Combined Report at 34. Its plan for improving First-Class Mail Single-Piece Letters/Postcards performance includes continuing to provide the field with useful tools to address the new combined First-Class Mail mix, such as new diagnostic reports for Presort First-Class Mail. Response to CHIR No. 4, question 11.

Similarly, for the performance goal of Improve Financial Performance, the Postal Service explains that it did not achieve the FY 2011 target of 40.4 DPWH because of slippage in the planned development schedule of the FSS and the lack of relief from contractual barriers hindering workforce flexibility. It states that the FY 2012 target of 42.2

would be difficult to achieve due to volumes and workload exceeding FY 2012 budget expectations and delays implementing the Network Rationalization and Retail Access Optimization initiatives. However, the Postal Service does not explain what action it recommends for achieving DPWH targets in future years. *In cases where a performance goal would be difficult to achieve, Annual Performance Reports should explain what action the Postal Service recommends for achieving the performance goal in future years. See 39 U.S.C. 2804(d)(3)(C).*

Finally, the 2011 Report includes summary findings of program evaluations completed during FY 2011. It provides links to the websites of the Commission, the Postal Service Office of the Inspector General, and the Government Accountability Office. Response to CHIR No. 2, question 22.

2012 Plan

The 2012 Plan meets most of the statutory requirements listed in 39 U.S.C. 2803. However, as in previous years, the 2012 Plan does not "[cover] each program activity set forth in the Postal Service budget…."[16] As the Commission previously stated, covering each program activity set forth in the Postal Service's operating budget is an essential requirement of the Annual Performance Plan. 2010 ACD at 50.

The 2012 Plan establishes three performance goals of Improve Service, Improve Financial Performance, and Improve Safety and Employee Engagement that define the level of performance to be achieved by a program activity. Response to CHIR No. 2, question 19. It expresses each performance goal in objective, quantifiable, and measurable forms as the targets and results set for each performance indicator. For example, the Improve Service performance goal is measured by service performance scores for First-Class Mail Single-Piece Letters/Postcards. Likewise, Improve Financial Performance is expressed as Operating Income and DPWH, and Improve Safety and Employee Engagement is measured by the OSHA Illness and Injury Rate and the VOE Survey score. Combined Report at 33.

The 2012 Plan establishes seven performance indicators used to measure or assess relevant outputs, service levels, and outcomes of each program activity. However, as noted below, the Commission is concerned about the adequacy of the performance indicators for the performance goals of Improve Service and Improve Financial Performance. The 2012 Plan also provides "a basis for comparing actual program results with the established performance goals" by comparing FY 2011 results to FY 2011 targets for each performance indicator. *See* 39 U.S.C. 2803(a)(5).

The 2012 Plan "briefly describe[s] the operational processes, skills and technology, and the human, capital, information, or other resources required to meet the performance goals[.]" Response to CHIR No. 2, question 20; *see* 39 U.S.C. 2803. The Postal Service provides further information in the Combined Report by explaining the processes, skills and technology, and resources for its four core business strategies. These strategies are: (1) strengthen the business-to-consumer channel; (2) improve the customer experience; (3) compete for the package business; and (4) become a leaner, faster, and smarter organization. Combined Report at 8-15.

[16] *See* 2010 ACD at 50. Program activity means "a specific activity related to the mission of the Postal Service[.]" 39 U.S.C. 2801(5).

Finally, the 2012 Plan describes the objective measurement systems used to verify and validate measured values. For Improve Service, an independent third-party measures First-Class Mail Single-Piece Letters/Postcards service performance using a sampling system that records transit times between deposit and delivery of mailpieces. The Postal Service also maintains customer experience measurement programs supplemented by independent mystery shopper reports and analyses of complaints and telephone calls to customer contact centers. *Id.* at 34.

For Improve Financial Performance, the Postal Service uses a measurement system that follows applicable rules and regulations of the Securities and Exchange Commission. Accounting systems and financial reports are also independently audited and subject to review by the Postal Service Office of the Inspector General and the Government Accountability Office. For Improve Safety and Employee Engagement, the Postal Service uses the OSHA Illness and Injury Rate, an industry-wide formula required by OSHA, and the VOE Survey score. *Id.* at 35.

Review of Performance Goals and Strategic Initiatives

The PAEA requires the Commission to evaluate whether the Postal Service has met the performance goals established in the 2011 Report and 2012 Plan. 39 U.S.C. 3653(d). The Commission conducts this review by comparing FY 2011 results for each performance indicator against FY 2011 targets to evaluate progress towards meeting each performance goal.

The Commission may also provide recommendations to the Postal Service that relate to protecting or promoting the public policy objectives in title 39. *Id.* Specific recommendations for each performance goal are listed below. In the FY 2010 ACD, the Commission recommended applying consistent terminology throughout Annual Performance Reports and Plans. The Postal Service responded by clearly identifying the performance goals and using unambiguous terms throughout the 2011 Report and 2012 Plan.

Improve Service

The Postal Service did not meet the performance goal of Improve Service. Service performance scores for First-Class Mail Single-Piece Letters/Postcards fell below FY 2011 targets for all three performance indicators (Overnight, 2 Days, and 3-5 Days). They also declined compared to FY 2010 results. In addition, unlike FY 2011 targets, which were slightly higher than FY 2010 targets, FY 2012 targets are identical to FY 2011 targets. These factors indicate that the Postal Service's progress towards meeting the Improve Service performance goal is declining rather than improving.

In the FY 2010 ACD, the Commission expressed concerns about the adequacy of the performance indicators for the Improve Service performance goal. They were limited to service performance scores for one market dominant product (First-Class Mail Single-Piece Letters/Postcards) and three competitive products (Express Mail, Priority Mail, and Parcel Select). The Commission found that the Postal Service's choice of performance indicators provided an incomplete picture of the measurement systems used to track service performance. It stated that limiting performance indicators to First-Class Mail Single-Piece Letters/Postcards, which comprises only 15.4 percent of total mail volume,[17] and three competitive products fails to recognize that the Postal

[17] Revenue, Pieces and Weight Report FY 2011 Summary (Public), November 25, 2011.

Service offers multiple products and services. 2010 ACD at 52.

The Commission recommended that the Postal Service expand the number of performance indicators to include service performance scores for other market dominant products. *Id.* The Postal Service, however, did not adopt these recommendations in the 2011 Report and 2012 Plan. Instead, it reduced rather than expanded the number of performance indicators by removing service performance scores for Express Mail, Priority Mail, and Parcel Select. Again, this indicates that the Postal Service is not progressing towards the Improve Service performance goal.

The Postal Service states that service performance scores for competitive products were not included in the 2011 Report because they contain commercially-sensitive information. Response to CHIR No. 4, question 10. However, in the 2010 ACR, the Postal Service provided service performance targets for Express Mail, Priority Mail, and Parcel Select under seal.[18] Thus, concerns about protecting commercially-sensitive information can be addressed by filing data under seal. *See* 39 U.S.C. 3652(f); 39 U.S.C. 2803(d)(2).

The Commission reiterates concerns about the adequacy of performance indicators for the Improve Service performance goal. *It recommends that the Postal Service expand the number of performance indicators to include service performance scores for other classes of market dominant mail, including Standard Mail. In future filings, the Postal Service should also file under seal both the targets and results for its competitive products, including Express Mail, Priority Mail, and Parcel Select.*

18 Docket No. ACR2010, Library Reference USPS-FY10-NP32.

Improve Financial Performance

The Postal Service did not meet the performance goal of Improve Financial Performance. FY 2011 results fell short of FY 2011 targets for both Operating Income and DPWH. As noted in the FY 2010 ACD, the Postal Service's current financial condition impedes improvements in financial performance. 2010 ACD at 53. Revenues from FY 2007 to FY 2011 have declined from a high of approximately $75 billion in FY 2007 to a low of approximately $66 billion in FY 2011. From FY 2007 to FY 2011, the Postal Service has experienced total cumulative losses of $25.3 billion. Combined Report at 21. For a more detailed discussion of the Postal Service's current financial condition, please see Chapter IV on the Postal Service Financial Condition.

As the Public Representative notes, the Commission expressed concerns in the 2010 ACD about using Operating Income and DPWH as performance indicators for the Improve Financial Performance goal. Operating Income alone will not provide a complete and accurate picture of the Postal Service's financial performance because it ignores the RHBF obligations and changes in Workers Compensation liabilities. While the RHBF obligation is beyond the Postal Service's control, the Postal Service should nonetheless recognize in its performance goals the necessity of generating net income or loss. Otherwise, concentrating on just the "controllable" operating income could undermine the goal-setting process. Thus, the RHBF expenses and Workers Compensation liabilities must be accounted for as an expense of the organization. 2010 ACD at 54.

The Commission also recommended against replacing TFP with DPWH as a measure of productivity because DPWH does not recognize

major workload components, such as collecting, processing, transporting, and sequencing of mail for delivery. It stated that DPWH considers the servicing of the expanding delivery network as the only component of postal workload. *Id.*

The Commission reiterates concerns about using Operating Income and DPWH as financial performance indicators. *It recommends that the Postal Service use TFP as a performance indicator and report the RHBF obligations and Workers Compensation liability adjustments as part of its operating expenses.*

Improve Safety and Employee Engagement

The Postal Service partially met this performance goal. In FY 2011, the VOE Survey score exceeded the FY 2011 target by 0.2 points. The FY 2012 target is 64.9, which is higher than the FY 2011 target by 0.4 points. Response to CHIR No. 4, question 14.

However, the 2011 OSHA Illness and Injury Rate of 5.67 did not meet the FY 2011 target of 5.39. Although the Postal Service states that it is on track to achieve FY 2012 targets and thresholds, the FY 2012 target is worse than the FY 2011 target. This indicates that the Postal Service's progress towards improving safety is declining rather than improving.

Strategic Initiatives

The strategic initiatives facilitate the Commission's review of performance goals under 39 U.S.C. 3653(d). The Commission reviews the strategic initiatives as part of its evaluation of whether the Postal Service met the performance goals established in the Annual Performance Report and Plan.

As noted above, the 2011 Comprehensive Statement contains less detailed information about the strategic initiatives than the 2010 Comprehensive Statement. The Postal Service explains that it began implementing a rigorous, disciplined process for developing, reviewing, and tracking strategic initiatives in FY 2011, and stakeholders can expect more details on more programs in FY 2012. Combined Report at 31. In future filings, the Commission expects that the Postal Service will provide more detailed information about the strategic initiatives as well.

The parts of the 2012 Comprehensive Statement on Postal Operations related to performance plans should, at a minimum, contain information on strategic initiatives similar in the level of detail to that provided in the 2010 Comprehensive Statement.

Specifically, the 2012 Comprehensive Statement on Postal Operations should include a chart similar to the one provided in the 2010 Comprehensive Statement that illustrates the relationships between the strategic initiatives and the three performance goals. This chart should also provide the results indicators used to measure progress in meeting targets. *See* 2010 Comprehensive Statement at 53. The Postal Service should also describe the purpose of each strategic initiative and provide FY 2012 targets, FY 2012 results, and FY 2013 targets. *See id.* at 51-53. This information will facilitate the Commission's evaluation of the progress made for each strategic initiative.

For the Expand Access strategic initiative, the Postal Service reported that it increased the share of revenue generated from alternative channels to more than 35 percent. Combined Report at 30. However, it did not discuss how the scope of access was expanded throughout the nation. For example, it did not state whether the revenue generated from alternative channels came primarily from urban or rural areas.

Distinguishing between revenues generated from urban versus rural areas could help ensure that both urban and rural communities have expanded access to postal services. *In subsequent filings, the Commission recommends that the Postal Service discuss how widely access was expanded throughout the nation for both urban and rural areas.*

For the Expand Products, Services, and Features strategic initiative, the Postal Service reports that it introduced 23 new products, services, and features in the areas of shipping, retail, marketing mail, and transactions and correspondence. Combined Report at 30. However, the Postal Service does not state whether these new products, services, and features generated additional revenues. This information will help determine whether the new products, services, and features supported the performance goal of Improve Financial Performance. *In subsequent filings, the Commission suggests that the Postal Service provide the revenues generated from each new product, service, or feature.*

For the Reduce Energy Use strategic initiative, the Commission suggests that the Postal Service clearly identify the energy reduction goals and state whether it met the targets for each energy reduction goal. The Postal Service provided this information for FY 2011 in response to CHIR No. 5, question 2. However, providing this information in the initial 2011 ACR filing would have facilitated the Commission's review of the strategic initiatives. *In future ACRs, the Postal Service is requested to provide this information in its initial filing.*

The Commission recognizes that some of its recommendations may result in added costs and reporting responsibilities. However, these additional data and reports would provide more robust information for assessing the Postal Service's performance goals and plans that are produced pursuant to 39 U.S.C. 2803 and 2804.


U.S. POST OFFICE

Chapter VI

Service Performance

Introduction

Under the PAEA, the Commission is tasked with reviewing the Postal Service's quality of service for all market dominant products, including speed of delivery, reliability, and the level of customer satisfaction. As noted in the Commission 701 Report[1], reviewing quality of service allows assessment of whether the Postal Service is meeting the objective of maintaining the "high quality service standards established under section 3691," and furthers the objective of increasing transparency. This review is also important in relation to the rate cap requirements of 39 U.S.C. 3622(d)(1)(A) when analyzing whether quality of service is impacted in order to comply with rate cap requirements. In addition, service performance results are an indication of Postal Service efficiency, particularly when the Postal Service is focused on cutting costs. Finally, maintaining high levels of service in First-Class Mail may help the Postal Service retain volume in this class. Improving service in Standard Mail (advertising) and Package Services (fulfillment), two areas where the market is improving, may result in volume growth.

The discussion that follows examines the Postal Service's service performance for market dominant products, customer access or the ability to obtain postal services, and the customer experience with postal services and products. It also includes the Postal Service's progress in implementing meaningful measurement through the use of Intelligent Mail barcodes (IMb).

The fourth quarter of FY 2011 is the first quarter that the Postal Service has reported service performance results for the majority of its market dominant products. The level of Full Service Intelligent Mail participation continues to impact the reliability of many service performance results. Newly implemented critical entry times (CET) have also affected scores for some products. The Postal Service has taken the first steps towards

[1] Section 701 Report Analysis of the Postal Accountability and Enhancement Act of 2006, September 22, 2011.

reporting Standard Mail service performance by individual product, but work remains in providing meaningful, representative results in this area.

The Postal Service is demonstrating success in meeting its service standard goals in the areas of single-piece First-Class Mail and Special Services. However, the Postal Service is having difficulty meeting its service standard goals for most other market dominant products. Overall, the Commission regards low performance results for speed of delivery an important issue the Postal Service must resolve.

Speed of Delivery and Reliability

Measurement Systems

The Postal Service uses several performance measurement systems to measure the speed of delivery and reliability of market dominant products. Market dominant products are measured using (1) the External First-Class Mail (EXFC) system, (2) a hybrid measurement system based upon IMb, (3) the International Mail Measurement System (IMMS), (4) a Delivery Confirmation based system, and (5) Red Tag and Del-Trak. Specialized systems have been implemented for measuring individual Special Services products. The PAEA requires the Postal Service to measure the service performance of each market dominant product using measurement systems that are independent of or external to the Postal Service. 39 U.S.C. 3691(b)(1)(D). The Postal Service may seek an exception to this requirement by requesting approval from the Commission to utilize a measurement system under the direct control of or internal to the Postal Service. 39 U.S.C. 3691(b)(2). In November 2008, the Commission granted a Postal Service request to proceed with development of an internal hybrid measurement system based on Intelligent Mail barcodes (IMb) to measure service performance for many of its products.

EXFC

First-Class Mail Single-Piece Letters/Postcards and the single-piece category of First-Class Mail Flats are measured using the EXFC measurement system.[2] This system is an external destination-based system managed by an independent contractor, IBM, which provides quarterly service performance measurement scores at both the postal area and district level.[3] Delivery performance is measured from the street collection box to the delivery mailbox. When evaluating delivery performance, test mailers record the time they place First-Class Mail in the collection box. Those test mailpieces are sent to a nationwide panel of receivers who record when the mailpiece was delivered to their mailbox.[4] Delivery performance is recorded on the basis of 3-Digit ZIP Code pairs.

Hybrid Measurement System

Most presorted letter and card shaped First-Class Mail and Standard Mail is evaluated through the Intelligent Mail Accuracy and Performance System (iMAPS). This is a hybrid measurement system utilizing both internal and external components. The internal component of the measurement system uses the mail arrival time to start the measurement clock and the final processing scan within the distribution network using IMb to stop the measurement clock. These data are augmented with a last-mile factor externally measured using third-party reporters to provide a complete end-to-end measurement. Data collected is submitted to an external contractor to calculate service performance and generate the necessary reports.

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2 2010 ACD at 58.
3 2009 ACD at 49.
4 *Id.*

Delivery Confirmation based system

First-Class Mail Parcels are measured using the internal Product Tracking System (PTS). This system measures transit time from the time of mailing until the time of delivery of parcels for which customers have requested Delivery Confirmation.

IMMS

The International Mail Measurement System provides an independent measure of the domestic leg of the transit time for Inbound and Outbound Single-Piece First-Class Mail International. Specifically, the system measures the length of time between the domestic collection point and the outbound International Service Center (ISC) for outbound letters and between the inbound ISC and domestic delivery point for inbound letters.[5] The IMMS system tests service in the same 892 3-Digit ZIP Code areas as EXFC. Further, the system employs a limited number of international locations to serve as the origin for inbound mail and the destination for outbound mail so that the mail passes through the ISC gateways where service measurement begins for inbound mail and ends for outbound mail.[6]

Red Tag and Del Trak

The Red Tag Monitoring Service is operated by the not-for-profit Red Tag News Publication Association to monitor service for association members. The Del-Trak System is operated by Time, Inc. to monitor service for several of its publications. Service is measured end-to-end using mailer-reported entry times to start-the-clock and external reporter delivery dates to stop-the-clock.[7] The transit time for each of the tested publications is compared against the service standards for Periodicals. Data from the two external systems are reviewed, combined and weighted by an independent contractor.[8]

Intelligent Mail barcode

IMb is a height-modulated barcode that encodes up to 31-Digits of mailpiece data. The IMb combines and expands the capabilities of the POSTNET barcode and the Planet Code barcode into one unique barcode.[9] Scanning the IMb allows the Postal Service to track a mailpiece throughout the mail processing system.

Mailers are given a choice to register for Basic or Full-Service Intelligent Mail (Full-service). The Postal Service encourages Full-Service participation among mailers, in part because this option provides the data necessary to measure service performance. Full-Service allows the mailer to identify unique mailpieces throughout the mailstream along with other benefits such as start-the-clock notification, discounts, and automated address correction.[10] In quarter 4 FY 2011, only 42 percent of total commercial mail volume was IMb Full-Service certified.[11] Subsequently, the percentage of Full-Service mailers decreased the following October to only 39 percent participation.[12] Table VI–1 compares the Postal Service's 2010 estimate of Full Service IMb participation with actual 2011 participation.

There are significant issues hindering the implementation of IMb as a reliable measurement system. Problems with obtaining large enough sample sizes indicate that for some products the results cannot

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5 Docket No. ACR2011, LR USPS-FY11-29, filename: Annual Report on Service Performance for Market Dominant Products at 3-4.
6 *Id.* at 6.
7 *Id.* at 17.

8 *Id.*
9 73 FR 36136 (June 25, 2008).
10 Retrieved at *http://www.satorisoftware.com/learn/intelligent-mail-basic-vs-full-service.aspx.*
11 Postal Service Presentation to Postal Regulatory Commission, January 17, 2011.
12 The percentage of Standard Mail volumes using Full Service IMb decreased from 34.31 percent to 31.58 percent.

Table VI–1—Pieces in Measurement

Mail Class	FY 2011 Estimated	FY 2011 Actual
First-Class Mail	50.0%	62.0%
Standard Mail	36.5%	31.0%
Periodicals	54.6%	17.0%

Source: 2010 ACD and Postal Service presentation: Intelligent Mail Update

be deemed reliable. The inability to identify individual Standard Mail products means that the Postal Service cannot accurately report service performance measurement by product as required by 39 U.S.C. 3652(a)(2)(B).[13] The Service performance results for many products were only available for quarters 3 and 4 (or in some cases, only quarter 4).

The Postal Service maintains that low participation rates coupled with new procedures for start-the-clock scans are major factors for below-target service performance results. The Postal Service expects service performance for products using IMb to improve as more customers adopt Full-Service Intelligent Mail.[14] It notes an increasing trend in Full-Service participation.[15]

Participant Comments

The Public Representative notes the Postal Service missed its FY 2011 target participation rate of 90 percent.[16] He further contends the low participation rates do not fully explain the poor service performance results. The Public Representative suggests that the Postal Service provide a detailed plan of how it intends to increase participation in the Full-Service Intelligent Mail system.[17]

NPPC notes that the IMb measurement system is just getting underway and hopes that the new measurement system will show improved service performance in the FY 2012 ACR.[18]

Valpak suggests that the Postal Service entice small and larger mailers to use Full-Service IMb by expanding the rate differential.[19]

Commission Analysis

The Postal Service includes service performance results for most products in the FY 2011 ACR but problems remain in reporting Standard Mail. For example, Full-Service Standard Mail represents only a third of total Standard Mail volume. It anticipates total Full-Service participation will increase in FY 2012 resulting in a range of 48 – 55 percent of Full-Service IMb pieces in the mailstream.[20]

The Commission recognizes that Full-Service volume has grown from approximately 7.5 billion pieces in quarter 2 of FY 2010 to approximately 13 billion pieces today.[21] Moreover, Full-Service volume for First-Class Mail and Periodicals has increased to at least half of total volume for these classes.[22] However, the Commission is concerned about the reliability of the reported service performance results for some products given the low participation rates. It is not clear whether the results based on the small sample size are representative of the universe within specific products. It has been 3 years since the Commission approved the use of IMb as a service performance measurement. It is imperative for the Postal Service to

13 2010 ACD at 58.
14 *Id.* at 11.
15 *Id.*
16 PR Reply Comments at 30-31.
17 *Id.* at 33-34.

18 Comments of the National Postal Policy Council, February 3, 2012, at 11.
19 Valpak Comments at 116.
20 Postal Service update on IMb, November 29, 2011.
21 Postal Service Presentation to Postal Regulatory Commission, January 17, 2011.
22 In FY 2010, First-Class Mail and Periodicals participation was 27.9 and 29.2 percent, respectively.

find a reliable way to measure service performance. *The Commission closely monitors progress in service performance measurement and continues to require the Postal Service to provide participation rate reports to the Commission on a monthly basis. If continued progress is not evident, the Commission will review its decision to allow use of the hybrid system for service performance measurement.*

Temporary Waivers and Semi-Permanent Exceptions from Periodic Reporting

The Commission established a framework for the Postal Service to achieve full compliance with all service performance reporting requirements by the filing date of the FY 2011 ACR.[23] As part of this process, the Postal Service was directed to seek temporary waivers from reporting where the Postal Service could not immediately begin reporting on specific products, and semi-permanent exceptions pursuant to 39 CFR 3055.3 where reporting would be impractical.

In FY 2011, the Postal Service requested waivers from service performance reporting requirements on many Postal Service products. The discussion below details the three dockets corresponding to the Postal Service's request.

In Docket No. RM2011-1, the Postal Service requested temporary waivers from reporting for First-Class Mail Flats at the District level; non-retail First-Class Mail Parcels; all categories of Standard Mail; Outside County Periodicals; and non-retail Media Mail, Library Mail, and Bound Printed Matter Parcels.

In Docket No. RM2011-4, the Postal Service requested a semi-permanent exception, or alternative relief, for quarterly reporting of First-Class Mail Flats at the District level.

On November 24, 2010, the Postal Service filed a conditional notice of withdrawal concerning the temporary waiver request for District level reporting of First-Class Mail Flats previously filed in Docket No. RM2011-1.

In Docket No. RM2011-7, the Postal Service requested temporary waivers from quarterly reporting requirements for Standard Mail, Bound Printed Matter Flats, and certain Area and District level data for presort First-Class Mail and End-to-End Periodicals.

The issues appearing in Docket Nos. RM2011-1, RM2011-4, and RM2011-7 were addressed in Order No. 745.[24] The Commission did not find a basis for granting exceptional relief and denied the requests for a waiver, semi permanent exception, or alternative forms of relief concerning First-Class Mail Flats and directed the Postal Service to begin quarterly reporting including District level service performance based upon available data from the existing EXFC system with the next due quarterly report. Standard statistical calculations describing the validity of data were to be included where appropriate.

The Postal Service's request for a temporary waiver for presorted First-Class Mail Parcels appeared moot because this component of First-Class Mail Parcels has been reclassified within competitive products. *See* Docket No. MC2011-22.

The Commission granted the request for a temporary waiver concerning presorted First-Class Mail, and directed the Postal Service to provide status reports as it indicated it would. Beginning with the FY 2011

[23] Docket No. RM2009-11, Order No. 465, Order Establishing Final Rules Concerning Periodic Reporting of Service Performance Measurements and Customer Satisfaction, May 25, 2010, at 18-24.

[24] Docket Nos. RM2011-1, RM2011-4 and RM2011-7, Order Concerning Temporary Waivers and Semi-Permanent Exceptions from Periodic Reporting of Service Performance Measurement, June 16, 2011. (Order No. 745).

quarter 4 report, the Postal Service was directed to report all data regardless of whether the data meets the Postal Service's self-imposed data sufficiency thresholds, and where appropriate, include standard statistical calculations describing the validity of the data.

The Commission denied the request for a waiver concerning Standard Mail because the Postal Service did not comply with Commission directions for seeking waivers which require the Postal Service to present implementation plans including dates and milestones. The Postal Service did not present a plan reasonably calculated to achieve compliance with Standard Mail by the filing of this ACR or any other fixed date. The Commission directed the Postal Service to inform the Commission of its plan concerning the implementation of a measurement system capable of reporting service performance for individual Standard Mail products by August 1, 2011. While this issue was being resolved, the Postal Service was directed to report Standard Mail service performance as outlined in its waiver requests.

The Commission denied the request for a waiver concerning Periodicals because the Postal Service's open-ended request to delay reporting is not consistent with the rules established in Order No. 465 which require the Postal Service to present implementation plans including dates and milestones. Beginning with the FY 2011 quarter 4 report, the Postal Service was directed to report all Periodicals data regardless of whether the data meets the Postal Service's self-imposed data sufficiency thresholds, and where appropriate, include standard statistical calculations describing the validity of the data. The Commission accepted the use of proxies and the use of Red Tag and Del-Trak data while a transition is being made to an IMb-based system.

For commercial Package Services, the Commission did not find acceptable the Postal Service's proposal to move the start-the-clock event to the first en route scan without accounting for the period from when the Postal Service receives the mail until the first en route scan. The Commission determined that this change would not provide service performance measurement representative of the service being provided. The Postal Service was directed to present a plan to the Commission detailing how it intends to account for the period prior to the first en route scan by August 1, 2011.[25] Beginning with the FY 2011 quarter 4 report, the Postal Service was directed to report all Package Services data regardless of whether the data meets the Postal Service's self-imposed data sufficiency thresholds, and where appropriate, include standard statistical calculations describing the validity of the data.

The Postal Service requested a waiver from service performance reporting requirements on Stamp Fulfillment Services to allow time for the Postal Service to explore the feasibility of measuring the service performance of this product. The Postal Service eventually decided it was feasible to measure and report on this product and presented measurement and reporting proposals to the Commission, which the Commission approved.[26]

Finally, the Postal Service was granted a semi-permanent exception from reporting for Applications and Mailing Permits.[27]

[25] *See* Docket Nos. RM2011-1, RM2011-4 and RM2011-7, United States Postal Service Implementation Plan for Periodic Reporting of Service Performance Measurement for Standard Mail and Non-retail Package Services, August 1, 2011.

[26] *See* Order No. 745. ; Docket No. RM2011-14, Order No. 947, Order Establishing Final Rule Concerning Periodic Reporting of Service Performance Measurements for Stamp Fulfillment Services, November 4, 2011.

[27] Docket No. RM2010-14, Order No. 570, Order Approving Semi-

The Postal Service's measurement systems remain a work in progress. As discussed in subsequent sections, the Postal Service is now able to provide some level of reporting for most market dominant products.

First-Class Mail

Single-Piece Letters/Postcards

The EXFC system's statistical design includes First-Class Mail Single-Piece Letters/Postcards. The Postal Service notes the maximum statistical margin of error for the performance estimate of First-Class Mail Single-Piece Letters/Postcards was +/- 2.0 percent with a 95-percent confidence level at the district and overnight, Two-day, and Three-day service standard level.[28]

For First-Class Mail Single-Piece First-Class Letters/ Postcards, service performance was better in quarters 3 and 4 than in quarters 1 and 2. Figures VI–1 and VI–2 illustrate service performance for First-Class Mail Single-Piece Letters/Postcards overnight and two-day mail surpassed its annual targets of 96.65 percent and 94.15 percent, respectively. Figure VI–3 shows First-Class Mail Single-Piece Letters/Postcards three- to five-day narrowly missed the annual service performance target of 92.95 percent on time.

First-Class Mail Single-Piece Letters/Postcards was the only mail product within any class to meet or surpass its annual service performance target for any service standard.

Figure VI–1
Single Piece Letters/Postcards — Overnight

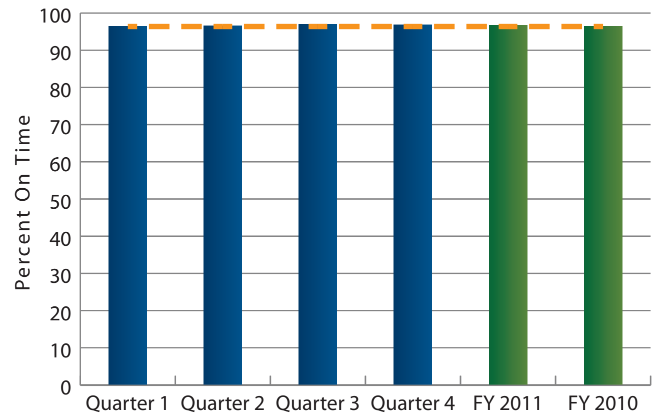


Figure VI–2
Single Piece Letters/Postcards — 2-Day

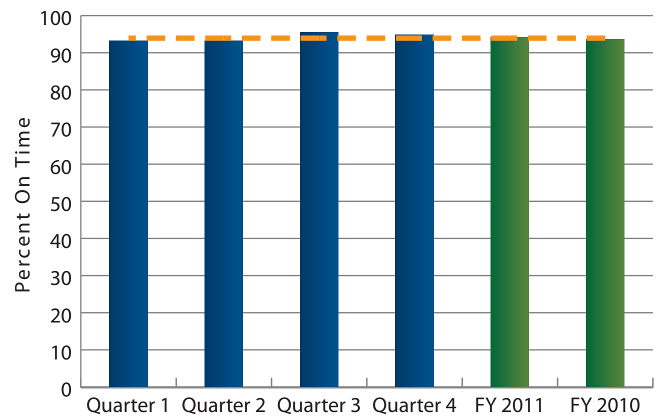
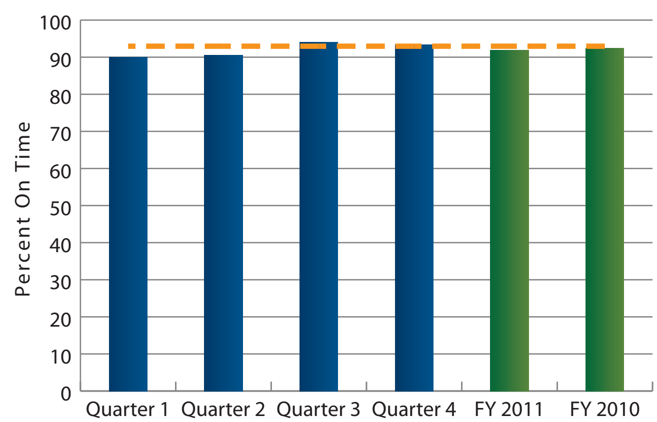


Figure VI–3
Single Piece Letters/Postcards — 3- to 5-Day



permanent Exception from Periodic Reporting of Service Performance Measurement for Applications and Mailing Permits, October 27, 20112010.

[28] Library Reference Docket No. ACR2011, library reference USPS-FY11-29, filename: Annual Report on Service Performance for Market Dominant Products at 7.

Presorted Letters/Postcards

The Postal Service began commercial mail measurement based on Full-Service Intelligent Mail in quarter 4 FY 2010. FY 2011 saw a steady increase in certified mailers with all Full-Service commercial mailers being measured by quarter 4.[29]

As seen in Figure VI–4 service performance increased for overnight mail during the first three quarters of FY 2011 but decreased substantially in quarter 4. Figures VI–5 and VI–6 show that service performance improved from quarter 1 to quarter 4 for Two-day and Three- to Five-day mail.

The Postal Service characterizes service results for Presorted Letters/Postcards as "particularly steady" in quarter 3 and 4.[30] Overnight service, however, declined slightly from 96 percent on time in quarter 3 to 91.1 percent on time in quarter 4. None of the service standard categories met the FY 2011 target. The Postal Service notes that service performance results increased throughout FY 2011 and believes this is due to implementation of a certification program for Full-Service Commercial Mailers. The certification process is designed to improve documentation, mail preparation and mail acceptance.

Prior to the fourth quarter, the Postal Service relied on mailer-provided information for start-the-clock scans and found it to be inconsistent.[31] As a result, new rules for start-the-clock were implemented in FY 2011 quarter 4. The Postal Service claims service performance results of several First-Class Mail

[29] *Id.* at 11.
[30] *Id.* at 10.
[31] Response to CHIR No. 4, question 17. The Postal Service explained that mailer provided scheduled ship date/time could be much earlier than the point it took possession of the mail. For example, if the scheduled ship date/time is prior to the CET but the Postal Service took possession of the mail after the CET, it would lead to start-the-clock being Day 0 instead of Day 1.

Figure VI–4
Presorted Letters/Cards — Overnight

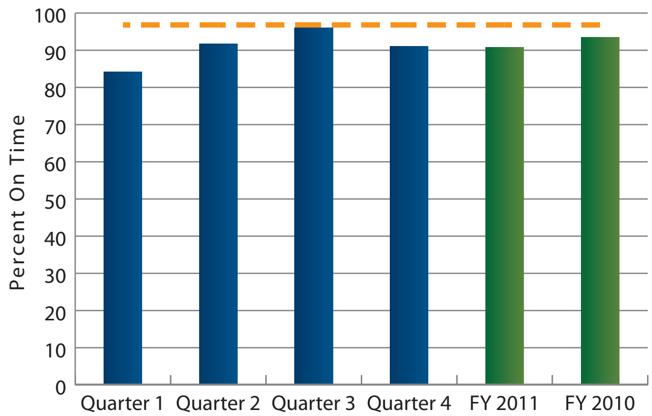


Figure VI–5
Presorted Letters/Cards — 2-Day

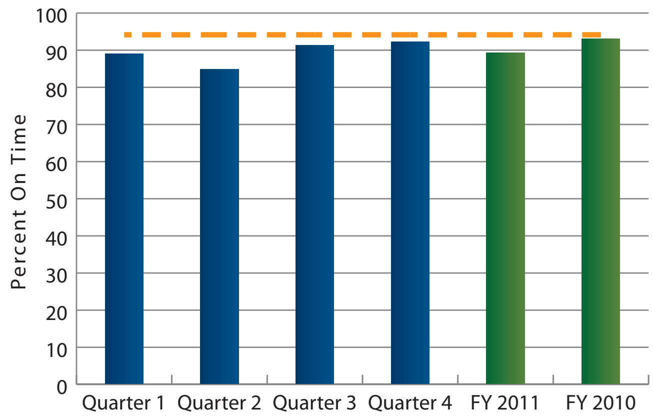
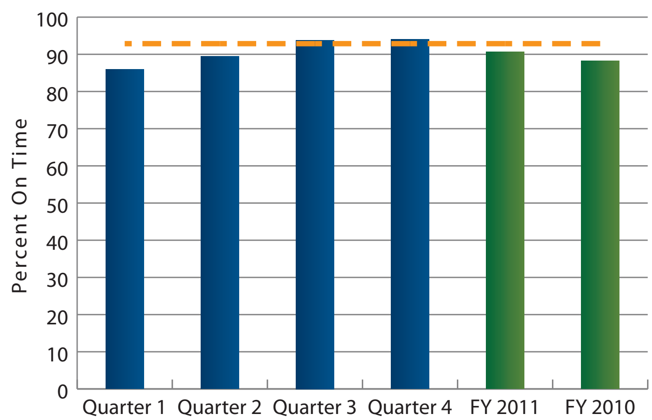


Figure VI–6
Presorted Letters/Cards — 3- to 5-Day



products were adversely affected by the new rules, and the low number of certified mailers.[32]

In an effort to address First-Class Mail service performance, the Postal Service says it is working internally with its plants to address capacity issues and correct sizing for entry volumes.[33] Off-loading is also an operation that the Postal Service wants to ensure is done in a service responsive manner. Further, the Postal Service will review all Customer Supplier Agreements (CSAs) for customer-requested container separations.[34]

The Postal Service's IMb implementation has been a slow process for presorted First-Class Mail. In the first quarter, only 13 presorted First-Class Mail mailers were certified as meeting the criteria for providing accurate information for service measurement.[35] The number of certified mailers grew to 100 mailers the second quarter and 118 in the third.[36] Consequently, the total mail volume qualifying for measurement in the fourth quarter was approximately 30 percent of the total First-Class Mail Presorted Letters/Postcards.[37]

First-Class Mail Presorted Letters/Postcards did not meet its service performance target in FY 2011. The Postal Service expects service performance results to improve in FY 2012. The Commission will monitor results throughout FY 2012 before taking any action regarding this product.

Flats

First-Class Mail Flats include both single-piece and presorted flats. They are measured via the EXFC system following the same process as Single-Piece Letters/Postcards.[38] Single-piece flats performance is used as a proxy for presorted flats because sufficient data on presorted flats is not available.[39]

Figure VI–7
First-Class Flats — Overnight

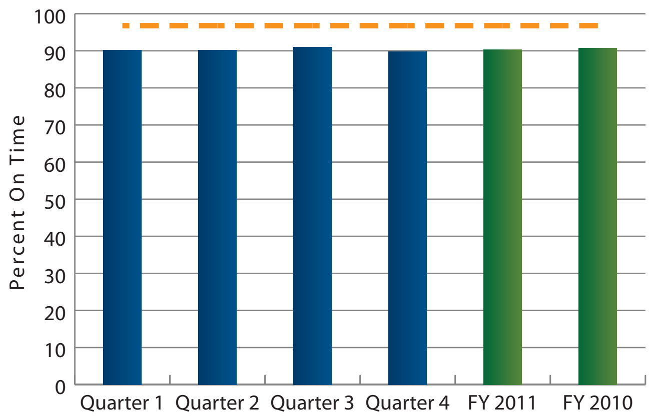
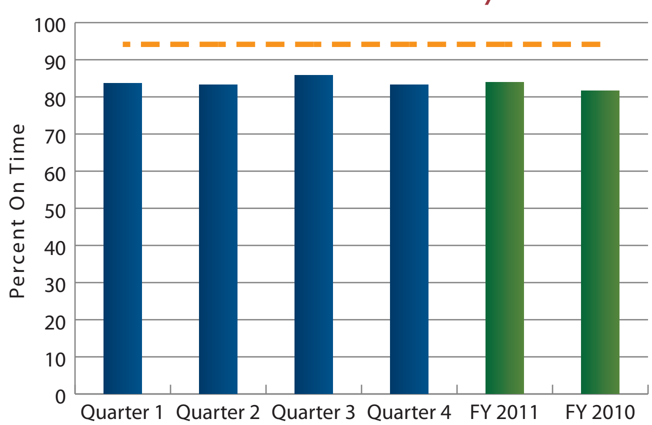


Figure VI–8
First-Class Flats — 2-Day



32 Library Reference Docket No. ACR2011, library reference USPS-FY11-29, filename: Annual Report on Service Performance for Market Dominant Products at 11.

33 *Id.*

34 A CSA is a written notice that confirms, for a commercial mailer, the origin-entry preparation requirements and the acceptance window times necessary for mail to be considered entered into the postal network on start-the-clock day 0. It may also include a schedule of transportation times, mail containerization specifications, designated postal mail facility entry locations, and time-sensitive mail instructions. (Retrieved from *https://www.usps.com/nationalpremieraccounts/csa.htm)).*

35 *Id.* at 6.

36 *Id.*

37 *Id.*

38 *Id.* at 2.

39 2011 ACR at 2. The Postal Service maintains that this approach is consistent with procedures outlined in the June 2008 Service Performance Measurement Plan.

Figure VI–9
First-Class Flats — 3- to 5-Day

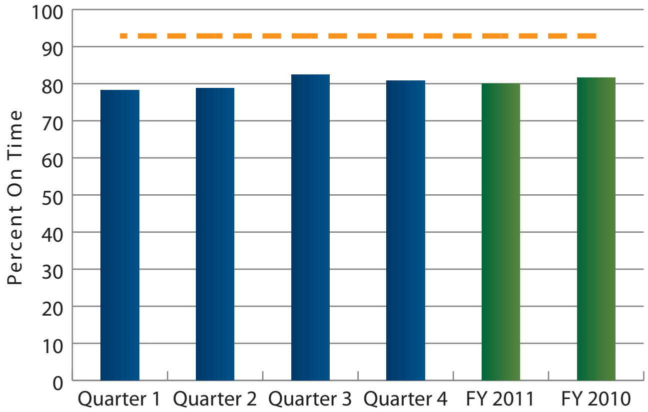
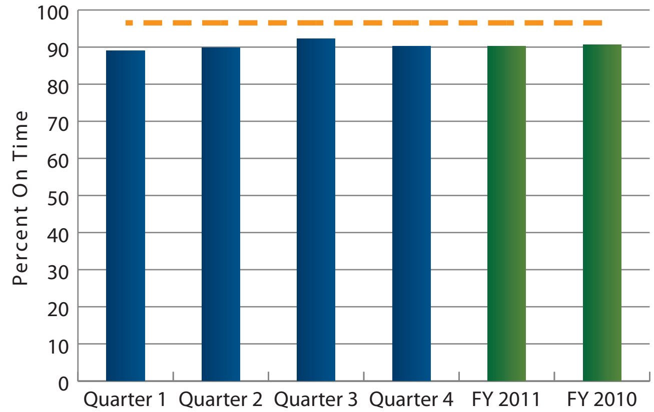


Figure VI–10
Parcels — Overnight

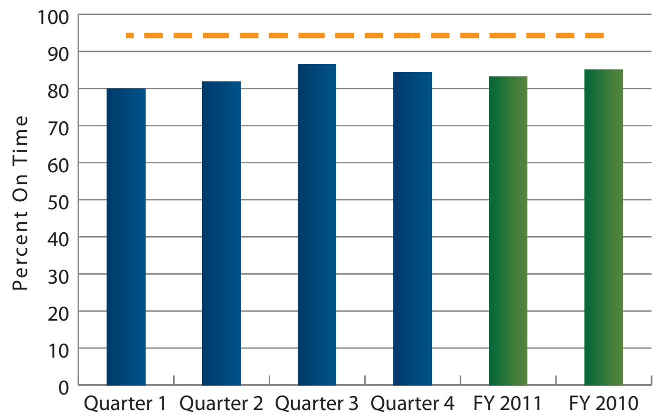


Service performance for overnight, Two-day, and Three- to Five-day was below the annual targets of 96.5, 94.15, and 92.85 percent on time, respectively. Service performance was virtually the same in FY 2011 as it was in FY 2010. In the FY 2010 ACD, the Commission told the Postal Service that it would need to improve service for First-Class Flats. In response to CHIR 5, the Postal Service stated, service performance for quarter 2 was significantly impacted by snow storms and fall flooding. The Postal Service states that a key strategy to improve service performance is to increase automation. Lean Six Sigma projects designed for this purpose were undertaken in FY 2011. *The Commission reiterates the need for service performance to improve for First-Class Flats.*

Parcels

Parcel measurement includes both single-piece and presorted items.[40] In FY 2011, parcel measurement included only retail parcels mailed over-the-counter at post offices because systems were not in place to

Figure VI–11
Parcels — 2-Day



capture the start-the-clock information for commercial pieces mailed in bulk or from other locations.[41] Consequently, 19.9 million parcels, representing only 4 percent of total First-Class Mail Parcels, were included in the measuring sample.[42] The following figures illustrate First-Class Mail Parcels quarterly service performance for FY 2011.

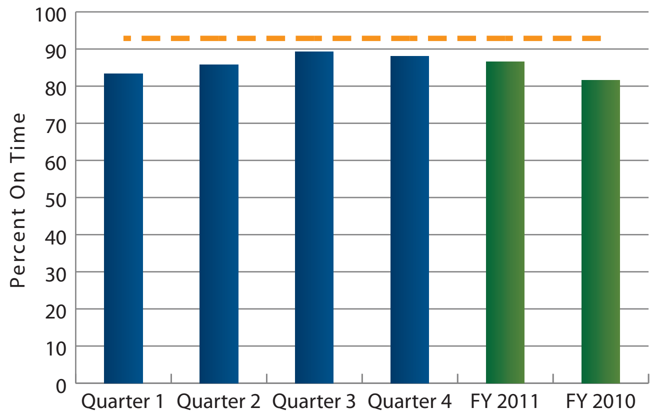
Service performance for First-Class Mail Parcels was below the target in every service standard category. Three- to five-day showed a marked improvement

40 *Id.* at 3. Docket No. ACR2011, library reference USPS-FY11-29, filename: Annual Report on Service Performance for Market Dominant Products at 3.

41 *Id.*

42 *Id.* at 7.

Figure VI–12
Parcels — 3- to 5-Day



from FY 2010, overnight and two-day did not show any improvement. *The Postal Service must improve service performance for this product in FY 2012.*

Inbound/Outbound Single-Piece First-Class Mail International Letters

Both Inbound and Outbound First-Class Single-Piece Mail International are measured using the International Mail Measurement System (IMMS) operated by an outside entity. The figures below illustrate the combined service standards of Inbound and Outbound service performance results increased from FY 2010.

Service performance results for First-Class Mail International was close to meeting target. However, as discussed in detail in the FY 2010 ACD, service performance for First-Class Mail International is measured using two different systems. Under the UNEX system, service performance declined relative to last year. *See* Chapter VII, International Mail, for a detailed discussion.

Figure VI–13
Inbound Single-Piece First-Class Mail International Letters

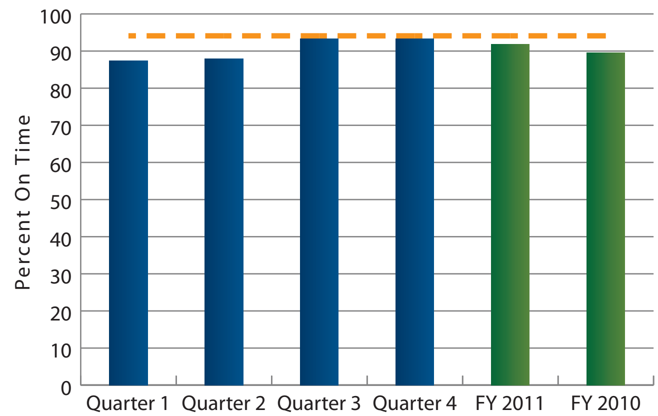
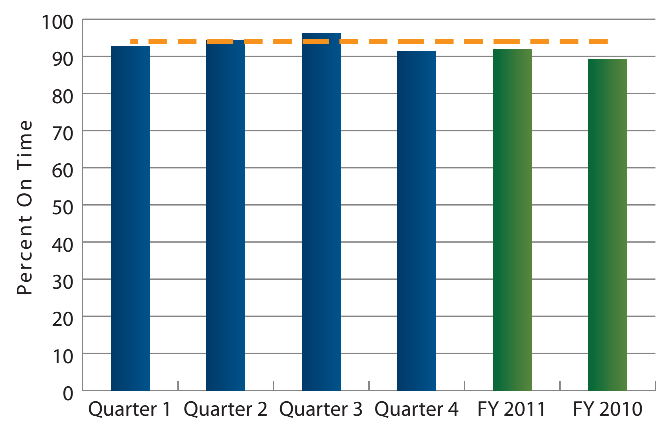


Figure VI–14
Outbound Single-Piece First-Class Mail International Letters



Standard Mail

Introduction

For the majority of Standard Mail products, service performance measurement using IMb began in quarter 3. Prior to that, Standard Mail measurement was based on data from a pilot test. The results for FY 2011 are not comparable to prior years. This section presents the results for all products except parcels,

which were not measured, and separately for mixed products. Participant comments and Commission analysis are discussed at the end of the section.

Mixed Product

In FY 2011, the Postal Service used IMb to measure service performance for Standard Mail and attempted to report service performance results at the product level. Where product information was not available from the electronic documentation provided by Full-Service IMb mailers, the Postal Service reported service performance as either Mixed Product — Letters or Mixed Product — Flats. According to the Postal Service, 61 percent of letter and 91 percent of flat measurable volume fell into these two categories.

As seen in Figures VI–15 and VI–16, service performance results for both categories were below target.

For Standard Mail Letters, non-saturation Flats, and Carrier Route, the Postal Service used documented entry times to start-the-clock and an IMb final processing scan to stop-the-clock.[43]

The Postal Service provides service performance measurement for destination entry mail in quarters 3 and 4 and End-to-End Mail in quarter 4. Figure VI–17 illustrates each product's annual performance results versus target.[44]

Service performance for all but High Density Saturation Letters was significantly below target. The Postal Service states that new business rules for start-the-clock scan policies and increased Full-Service

Figure VI–15
Mixed Product Letters

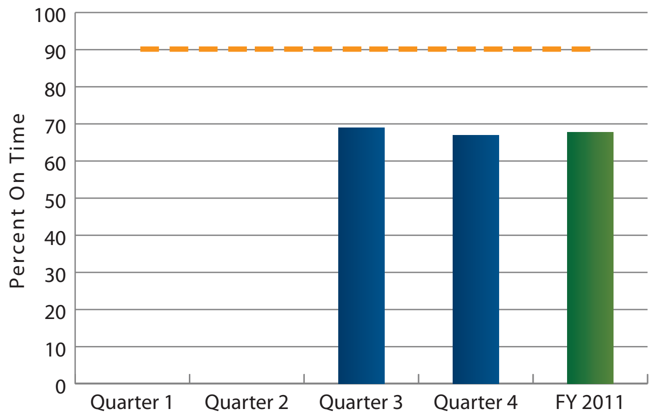


Figure VI–16
Mixed Product Flats

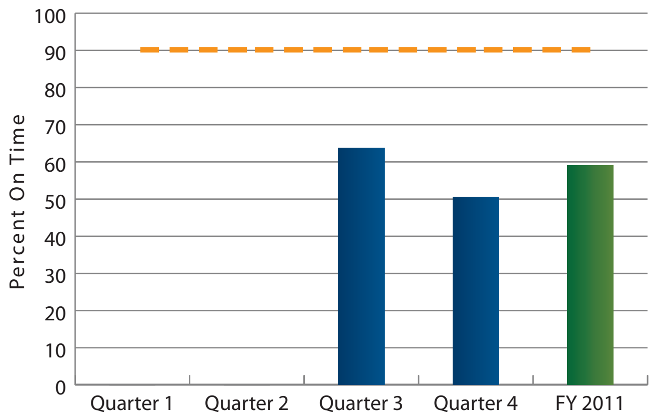
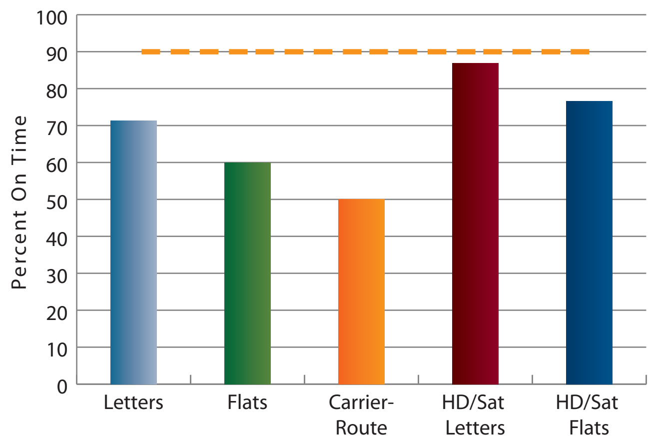


Figure VI–17
Standard Mail Products



43 *Id.* at 11.

44 Not Flat-Machinables and Parcels were not included in FY 2011 measurement. The Postal Service requested a waiver for Standard Mail parcels but, as explained above, the Commission denied this request. The Postal Service expects to begin partial reporting for Standard Mail parcels in FY 2012.

Intelligent Mail participation will increase the service performance results in the future.[45]

Standard Mail Participant Comments

The Public Representative makes two critical assessments of Standard Mail performance. First, the Postal Service should consider improvement of Standard Mail performance an organization-wide goal.[46] Second, the Public Representative stresses that adequate improvement regarding IMb adoption rates has not been made in FY 2011. Consequently, the Public Representative suggests that the Postal Service provide to the Commission a detailed plan of how it intends to increase participation in the Full-Service Intelligent Mail System. The Public Representative concludes that if IMb does not improve, the Commission should review its decision to allow the Postal Service to proceed with the IMb-based hybrid measurement system.

Valpak echoes the Public Representative's concern about the importance of Standard Mail saying, "the Performance Report does not mention Standard Mail…as 'program activity that is a major function or operation…'"[47] Further, Valpak suggests the Postal Service use the IMb system to improve the quality of service provided to Standard mail.[48]

Valpak observes two "non-product" categories presented in the service performance report: mixed letters and mixed flats/parcels.[49] Further, the 4.4 billion pieces recorded in the performance measurement database represent only 5 percent of all Standard Mail (due to the double counting of origin and destinating mail). As a result, Valpak assesses that neither mailers nor the Commission have performance data for individual products within Standard Mail. Valpak's overall assessment of Standard Mail performance is that service received was generally unpredictable and unreliable for any end-to-end Standard Mail product required to travel very far through the postal network. Also, Valpak assumes Standard mail will be the first to suffer and service performance deteriorate if the Postal Service succeeds in eliminating much (or all) of its excess capacity.[50]

Commission Analysis

Although the Postal Service attempted to report service performance results by product, for the majority of Standard Mail volume it was unsuccessful. The Postal Service attributes this failure to missing data on the part of mailers. The Commission notes that product level reporting is required under 39 U.S.C. 3652(a)(2). *The Postal Service must work with mailers to obtain the data necessary to accomplish product level reporting in FY 2012.*

The Commission is also concerned that service performance for a substantial percentage of Standard Mail did not meet its target. The Postal Service indicates that as Intelligent Mail data develops, diagnostic information will help identify specific areas for improvement. The Postal Service is also removing unnecessary processes within its Network Distribution Centers (NDCs) and is working with plants to ensure start-the-clock scans and off-loading are performed in a service-responsive manner. *The Commission will monitor the results of IMb and other Standard Mail service measurement processes throughout FY 2012 before taking any action.*

45 *Id.* at 16.
46 Public PR Comments at 29.
47 Valpak Comments at 107.
48 *Id.* at 116.
49 *Id.* at 110.
50 *Id.* at 116.

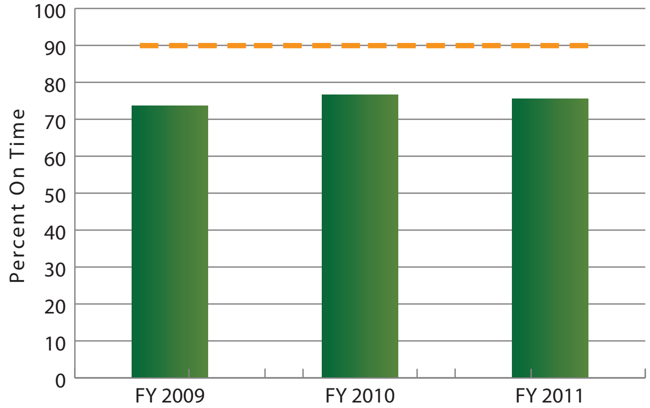
Periodicals

Periodicals service is measured end-to-end using mailer-reported entry times to start-the-clock and external reporter delivery dates to stop-the-clock. In FY 2011, service performance was measured by combining this data with two external measurement systems.[51] The Red Tag and Del-Trak systems do not include a representative sample of destination delivery unit (DDU) or Within County Periodicals. The service performance of all Periodicals is used as a proxy for both Within County and Outside County service performance.[52]

For FY 2011, Periodicals service performance was 75.5 percent on-time versus a service goal of 91 percent on-time.[53] As Figure VI–18 shows, service performance for Periodicals has remained significantly below target since measurement began in FY 2009.

The Postal Service states that one of its key strategies for improving service performance for Periodicals is to maximize processing on automation. Processing on automation will enable service performance to be measured using the IMb rather than relying on Red Tag and Del-Trak systems. The Postal Service has 100 Flats Sequencing Systems (FSS) in 42 processing sites providing flat automation to 42,737 delivery routes. In addition, the Postal Service performs certification audits to ensure compliance with standard operating procedures, adherence to CETs, proper identification of service commitments at postal facilities and automation processing. Finally, the Postal Service employed Lean Six Sigma projects to identify "Best Methods" for upstream bundle operations, staging, signage and sort program scheduling.[54]

Figure VI–18
Periodicals Annual Comparison



Periodical Participant Comments

Time Inc. recognized a trend of increasing non-receipt and late delivery complaints for four weekly magazines. It claims that delivery complaints increased between July and September (when new CETs were implemented).[55] Time Inc. and MPA, ANM, and ABM assert that the Postal Service must stabilize and improve the FSS process, successfully implement network consolidation, and adhere to other goals listed so that Periodicals improves its cost coverage and service performance.[56]

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51 Library Reference Docket No. ACR2011, library reference USPS-FY11-29, filename: Annual Report on Service Performance for Market Dominant Products at 10, 17.

52 *Id.* at 19.

53 Service performance in FY 2009 was 73.7 percent on-time, which illustrates an increase since that time. However, performance has slightly decreased from FY 2010's 76.7 percent on-time performance.

54 *Id.* at 21.

55 The Postal Service established new CET with four possible CETs depending on sortation preparation and FSS-destination ZIP codes. Codes. However, data limitations prompted the Postal Service to modify the CET requirements. Destination entry mail sent to an FSS designated ZIP Code received a CET of 08:00; all other Periodicals mail received 16:00 as the CET.

56 Time Reply Comments at 5; Reply Comments of Magazine Publishers of America, Inc., Alliance of Nonprofit Mailers and American Business Media at 9.

Commission Analysis

Service performance results for Periodicals Mail have not substantially improved since FY 2009 and remain significantly below target. The Joint Periodicals Study,[57] released in October 2011, outlined several operational strategies to increase efficiency of Periodicals mail processing and delivery. The Commission is hopeful that these strategies will improve the service performance of Periodicals Mail. Therefore, the Commission will allow time for these strategies to work before taking action. However, the Commission stresses the importance to Periodical mailers of reliable service performance. *The Postal Service must improve service performance for Periodicals in FY 2012.*

Package Services

Single-Piece Parcel Post

Single-Piece Parcel Post service is measured using an internal system called Product Tracking System (PTS). It measures transit time from the time of mailing until the time of delivery for Parcel Post items for which a customer requested delivery confirmation service. Figure VI–19 shows the quarterly service performance results for FY 2011.

The Two- to Four-day service performance results are substantially higher than the Five- to Twenty-day results for all quarters. As seen in Figure VI–20, combined results for Single-Piece Parcel Post two- to -four day and five- to twenty-day have improved significantly since FY 2007.

[57] Section 708 of the PAEA directed the Postal Service and the Commission to jointly address the quality of data for attributing costs to Periodicals and opportunities for operational efficiencies, including pricing incentives.

Figure VI–19
Single-Piece Parcel Post
Quarterly Data

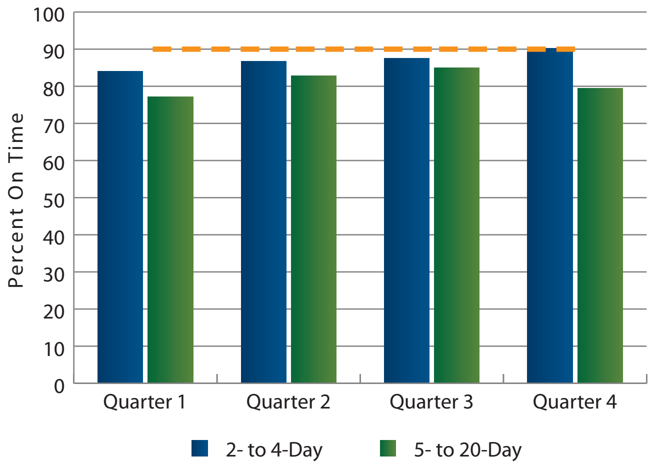
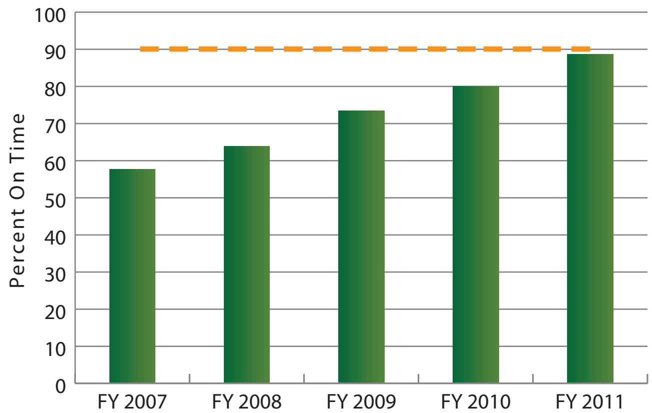


Figure VI–20
Single-Piece Parcel Post Annual Data
FY 2007–FY 2011



The Commission commends the Postal Service for improving its two- to four-day service performance. For five- to twenty-day mail, the Postal Service must address obstacles causing poor performance. If the current service standard is unmanageable, the Postal Service should develop a more realistic service performance target so mailer expectations can be met.

Inbound Surface Parcel Post

Inbound Surface Parcel Post (at UPU rates) consists of items weighing between 4 and 70 pounds that originate in foreign countries and are transported to the United States. Service performance of the domestic leg of the product is estimated using Single-Piece Parcel Post as a proxy.[58] FY 2011 service performance results were below target. However, as with Single-Piece Parcel Post, service performance has improved significantly since FY 2007. Therefore, the Commission takes no action.

Bound Printed Matter Flats

Bound Printed Matter (BPM) Flats is a commercial product used by businesses to send large catalogs and similar flat-shaped items too heavy to categorize as Standard Mail. Performance in FY 2011 is measured using IMb tracking scans and external data to extrapolate results for the entire volume of mail.[59] Results are only available for quarter 4. Service performance results for both DDU entry and end-to-end were significantly below target for quarter 4. Neither DDU entry nor end-to-end reached 45 percent on time performance. Because there is only one quarter of data for which to measure service performance, the Commission cannot assess the actual service performance for FY 2011. *The Commission expects that in FY 2012 the service performance results will be closer to the target.*

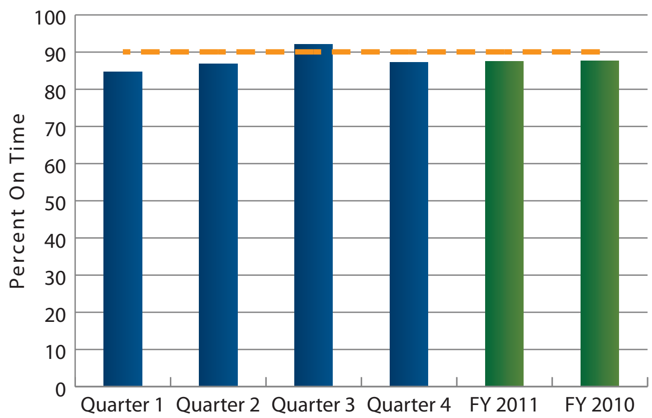
Bound Printed Matter Parcels

BPM Parcels is a commercial product used by businesses to send books, directories, or large catalogs too heavy or rigid to qualify as BPM Flats.[60] In FY 2011, the Postal Service began measuring performance using IMb. Service performance results are available for the fourth quarter only. Because there is only one quarter of data for which to measure service performance, the Commission cannot assess the actual service performance for FY 2011. *The Commission expects that in FY 2012 the service performance results will be closer to the target.*

Media Mail/Library Mail

Media Mail/Library Mail is a product whose content is restricted to books, noncommercial films, computer-readable media and similar media items that typically have educational, cultural, scientific or informational value. Service is measured using PTS in the same manner as Single-Piece Parcel Post.[61] Figure VI–21 illustrates service performance for Media Mail/Library Mail.[62]

Figure VI–21
Media Mail/Library Mail
FY 2007–FY 2011



[58] *Id.* at 23.
[59] *Id.* at 22.
[60] *Id.*

[61] *Id.* at 22.
[62] Library Reference Docket No. ACR2010, library reference USPS-FY10-29. Quarters 1, 2, and 4 resulted in 83.8, 84.7, and 90.4 percent on-time delivery. Quarter 3 results were the highest with 91.8 percent on-time delivery.

Service performance for Media Mail/Library Mail declined slightly from FY 2010 levels. Only quarter 3 results met or exceeded the FY 2011 target. *The Postal Service should improve service performance for this product.*

Special Study on Service Performance in Noncontiguous Areas

The PAEA directed the Commission to submit a report on universal postal service and the postal monopoly. As a result of that study,[63] the Commission found geographic scope to be one of the seven attributes of universal service. To explore whether quality of service was comparable across the geographic scope of the USO, the Commission included requirements for a special study in Order 292 and Order 465 as part of Rule 3055.7.

Pursuant to that order, the Postal Service provided a special study to evaluate final delivery service performance to the remote locations of Alaska, Honolulu and Caribbean Districts as compared to the service performance to the gateway cities of Anchorage, Honolulu and San Juan. Specifically, the study analyzed six 3-Digit ZIP Codes in Alaska; four in the Caribbean Districts; and three in Hawaii. *See* USPS FY2011-29 at 2.

In order to compare delivery service between the gateway and more remote parts of Alaska, Caribbean and Honolulu, results are reported at the 3-Digit ZIP Code level. This approach allowed the Postal Service to distinguish the gateway from the more remote regions, and provide insight into the various geographic parts of each district.

[63] Report on Universal Postal Service and the Postal Monopoly, December 19, 2008

Several outlying areas produced little or no measurable data for First-Class Mail. Further, no overnight service standard exists for First-Class Mail in Alaska. As such, it is difficult to assess overnight and two-day service performance for Alaska and the Caribbean. As seen in Table VI–2, performance for First-Class Mail three- to five-day did not deviate significantly from the gateway.

As seen in Table VI–3, destination entry Standard Mail service performance in Alaska is lower in rural and remote areas than at the gateway. In the Caribbean, destination entered Standard Mail is lower for the gateway than for rural/remote areas. In Hawaii, however, service performance for destination entered Standard Mail is well below target in both the gateway and the islands other than Oahu. For example, service performance for Standard Mail Letters destination entry is 14.2 percent on time at the 968 gateway and 0.3 percent on time at its outlying 969 area. This result means that Standard Mail Letters are virtually never on-time at either the gateway or on the islands other than Oahu. Service performance for end-to-end Standard Mail is below 50 percent on-time in all areas.

Table VI–4 shows the service performance results for Periodicals Mail. Service performance results were lower than the national average in every area where the special study was conducted but particularly so for the Caribbean, where the average score was less than half the national average. Most outlier areas did not deviate significantly from the gateway except Caribbean area 008, whose Periodicals service performance was 16.7 percent on-time delivery.

As seen in Table VI–5, service performance results for Package Services were extremely low in all areas. This is especially true for Honolulu, where on-time

Table VI–2—First-Class Mail Single-Piece Letters/Postcards/Flats

	Overnight	Two-Day	Three-to Five-Day
Alaska	96.3	97.1	91.4
995 Gateway	96.3	99.3	90.5
995 Rural	NSS [1]	97.9	93.7
996	NSS [1]	98.1	95.3
997	NSS [1]	92.9	92.9
998	NSS [1]	96.5	87.6
999	NSS [1]	98.5	89.1
Caribbean	93.8	96.3	85.7
009 Gateway	94.4	97.2	85.6
006	93.7	96.4	84.5
007	93.6	94.7	85.7
008	87.7	96	91.8
Honolulu	97.5	NSS	91.9
968 Gateway	97.7	NSS	86.3
967	97.5	NSS	96.0
969	91.5	NSS	82.8

Presorted First-Class Mail Letters/Postcards

	Overnight	Two-Day	Three-to Five-Day
Alaska	96.6	98.0	93.5
995 Gateway	96.6	No Data	92.9
995 Rural	NSS [1]	98.0	96.0
996	NSS [1]	98.0	95.9
997	NSS [1]	No Data	94.4
998	NSS [1]	No Data	89.5
999	NSS [1]	No Data	87.7
Caribbean	No Data	No Data	85.3
009 Gateway	No Data	No Data	85.7
006	No Data	No Data	83.7
007	No Data	No Data	84.2
008	No Data	No Data	92.1
Honolulu	96.3	NSS [1]	93.9
968 Gateway	97.0	NSS [1]	90.5
967	95.9	NSS [1]	95.9
969	No Data	NSS [1]	89.3

[1] NSS means No Service Standard

service performance scores ranged from 6.0 percent to 8.0 percent. *The Commission finds these results unacceptable and expects the Postal Service to improve service performance in these areas prior to its next scheduled Offshore Special Study. If service performance does not improve the postal Service must provide an explanation.*

In some cases, service performance for the gateway was better than the rural/remote areas and in other cases, rural/remote areas had better service performance than the gateways. As a result, the study concluded that there was no compelling evidence that service performance in the rural/remote areas of the noncontiguous locations is much lower than the gateway. However, in most cases the noncontiguous locations have among the lowest performance in the nation. The authors of the study recommended the Postal Service consider reviewing processing

Table VI–3—Service Performance End-to-End Standard Mail

	Letters		Flats	
	Destination Entry	End-to-End	Destination Entry	End-to-End
Alaska	72.3	30.8	42.0	21.7
995 Gateway	80.3	31.5	46.1	27.8
995 Rural	75.3	31.6	36.8	18.0
996	66.8	28.1	41.4	14.0
997	65.0	36.4	32.6	21.9
998	42.4	22.1	N/A	N/A
999	54.3	31.7	N/A	N/A
Caribbean	68.6	34.0	56.8	29.4
009 Gateway	59.9	34.1	54.9	32.4
006	78.4	31.7	57.2	24.5
007	70.3	34.7	57.9	30
008	57.9	42.7	59.4	29
Honolulu	14.7	6.2	4.0	1.5
968 Gateway	14.2	7.4	7.1	2.6
967	15.1	5.7	2.7	1.0
969	0.3	4.8	1.2	1.2

Table VI–4—Service Performace Periodicals

Alaska	63.1
995 Gateway	68.7
995 Rural	57.2
996	71.4
997	63.7
998	56.7
999	48.2
Caribbean	35.9
009 Gateway	41.8
006	34.1
007	43.7
008	16.7
Honolulu	70.7
968 Gateway	73.8
967	63.0
969	80.4

Table VI–5—Service Performace Package Service

Alaska	25.5
995 Gateway	31.3
995 Rural	21.9
996	25.9
997	21.5
998	21.2
999	21.7
Caribbean	21.0
009 Gateway	19.8
006	23.9
007	24.4
008	7.7
Honolulu	6.4
968 Gateway	6.9
967	6.0
969	8.0

operations and service standards in many of these situations given the unique logistics and circumstances in Alaska, Caribbean and Honolulu. *The Commission agrees with this recommendation.*

Special Services

All special services achieved their target service performance levels. Table VI–6 notes the relatively steady results versus FY 2010.

Table VI–6—Special Services

Special Services	Target	FY 2010 Percent On-Time	FY 2011 Percent On-Time
Ancillary Services	90	93.0	93.4
International Ancillary Services	90	99.2	99.6
Address List Services	90	100	93.3
Caller Services	-	NR [1]	NR [1]
Change of Address Credit Card Authentication	-	NR [1]	NR [1]
Confirm	90	99.6	99.7
International Reply Coupon Service	-	NR [1]	NR [1]
International Business Reply Mail Service	-	NR [1]	NR [1]
Money Orders	90	95.4	97.2
Post Office Box Service	90	94.3	93.1
Customized Postage	-	NR [1]	NR [1]
Stamp Fulfillment Services	-	N/A [2]	N/A [2]

[1] NR indicates not required due to semi permanent exception from reporting

[2] N/A indicates that measurement results are not yet available

Customer Access

Pursuant to 39 CFR 3055.91, the Postal Service is required to provide information on customer access. Customer Access includes evaluation of access to retail facilities, the amount of time a customer has to wait in line to obtain postal services, and the availability of postal collection boxes and other collection points. The

number of delivery points also provides an indication of access to postal services. Post office suspensions and closings are evaluated because of their effect on obtaining postal services. Customer access is important to the Postal Service if it is to stem losses due to volume declines and potential changes in mailer behavior.[64] Over the years, the Postal Service has reduced its retail network by removing collection boxes, closing postal facilities and changing operating hours. Access to postal services, however, may be increasing with alternative marketing channels. With planned plant consolidations and continued postal retail facility closings, it is even more important for the Postal Service to accelerate the development of alternative methods of providing access to postal products and services.

Retail Facilities

Table VI–7 provides the number of retail postal facilities by type for FY 2008 through FY 2011. Also, the changes in the number of facilities from prior years are shown. The Commission observes that the number of retail facilities closed in 2011 increased by more than 70 percent, from 274 facilities closed in FY 2010 to 466 closures in FY 2011. In addition, it should be noted that while the number of Postal Service managed facilities closed in FY 2011 nearly tripled over FY 2010, the rate of closings of contract postal units and community post offices has declined by 40 percent from FY 2010 to FY 2011, from 140 such closings in FY 2010 to 84 in FY 2011.

On July 27, 2011, the Postal Service sought an advisory opinion from the Commission concerning a Postal Service initiative to perform discontinuance studies on over 3,600 postal retail facilities. As shown in Table VI–8, the RAOI identified 3,652 retail facilities (post offices, stations and branches) for possible discontinuance. An additional 728 retail facilities "outside" the scope of the RAOI were also identified for possible discontinuance. Thus, a total of 4,380 retail facilities are being or will be studied for possible discontinuance.

On December 15, 2011, the Postal Service advised the Commission that it "will delay the closing or consolidation of any post office until May 15, 2012".[65] The Postal Service further indicated that

Table VI–7—Postal Service Retail Factilities

Factility Type	FY 2011	FY 2010	FY2011 Change from FY 2010	FY 2009	FY 2010 Change from FY 2009
Postal Managed					
Post Offices	26,927	27,077	(150)	27,161	(84)
Classified Stations, Branches and Carrier Annexes	5,219	5,451	(232)	5,501	(50)
Total Postal Managed	**32,146**	**32,528**	**(382)**	**32,662**	**(134)**
Contract Postal Units	2,904	2,931	(27)	3,037	(106)
Community Post Offices	706	763	(57)	797	(34)
Total Post Offices	**35,756**	**36,222**	**(466)**	**36,496**	**(274)**

Source: Comprehensive Statement of Postal Operations 2010, 2009 and 2008; Form 10-k (2011)

64 One of the Postal Service's FY 2011 strategic initiatives was to expand postal access by means other than a postal retail facility.

65 United States Postal Service Notice of Status of the Moratorium on Post Office Discontinuance Actions, December 15, 2011, at 1 (Notice).

Table VI–8—RAOI and Non-RAOI Listing by Category

Facility Type	No. of Offices
RAOI Category 1	2,825
RAOI Category 2	384
RAOI Category 3	178
RAOI Category 4	265
Total RAOI Offices	**3,652**
Offices "Outside" of the RAOI	728
Grand Total	**4,380**

Category 1 = low earned workload and no greater than $27,500 in total annual revenue
Category 2 = FY 2010 revenue less than $600,000 and less than 2008 or 2009 and located within two miles of at least five Postal Retail/alternative access sites
Category 3 = FY 2010 Revenues less than $1 Million and located within 1/2 mile of at least five Postal Retail/alternative access sites
Category 4 = POs, Stations and Branches undergoing discontinuance studies, but had not advanced to the Community meeting Phase
Category 5 = Non-RAO Offices "outside" the Initiative, from LR - 3

Source: USPS-LR-N2011-1-2 and USPS-LR-N2011-1-3.

it "will proceed with the discontinuance process for any post office in which a Final Determination was already posted as of December 12, 2011, including all pending appeals." *Id.* It stated that the only "post offices" subject to closing prior to May 16, 2012 are those that were not in operation on, and for which a Final Determination was posted as of, December 12, 2011. *Id.* It affirmed that it "will not close or consolidate any other post office prior to May 16, 2012." *Id.* at 2. Lastly, the Postal Service requested the Commission "to continue adjudicating appeals as provided in the 120-day decisional schedule for each proceeding." *Id.*

The Postal Service's Notice outlines the parameters of its newly announced discontinuance policy. Pursuant to the Postal Service's request, the Commission will fulfill its appellate responsibilities under 39 U.S.C. § 404(d)(5).

A determination to close or consolidate any post office may be appealed to the Commission within 30 days after such determination is made available to customers of the office to be closed. The number of appeals filed appears to indicate how much citizens value the regulatory platform the Commission provides to consider Postal Service decisions. In these matters, the Commission's role is limited by 39 U.S.C. 404(d)(5) to assuring that the Postal Service has followed its closing review process, and if not, to remand for further consideration by the Postal Service. In FY 2011, there were 103 appeals dockets reviewed by the Commission. In FY 2010, only 6 appeals were initiated. In FY 2012 to date, 125 appeals dockets had been initiated by the Commission. Table VI–9 shows the disposition of appeals initiated in FY 2010 and FY 2011.

39 U.S.C. 404(b) and the Postal Service's regulations require the Postal Service to follow certain procedures before closing a post office. It must provide notice to the community 60 days prior to closing and invite public comments. In reaching a "Final Determination"

Table VI–9—Disposition of Commission Appeals Dockets FY 2011 and FY 2012

	FY	
Disposition	2011	2012
Affirmed	1	83
Dismissed	3	11
Remanded	1	8
Pending		
Grand Total	6	102
Grand Total	**102**	**125**

Source: PRC Dockets section

to close a post office, the Postal Service must make a written determination which takes into consideration:

- The effect of closing on the community;
- The effect of closing on employees;
- The economic savings to the Postal Service and;
- Whether closing is consistent with postal policy 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."

In an appeal of a post office closure, it is the Commission's responsibility to review the Postal Service's Administrative Record upon which its decision was made. In its decisions, the Commission reviews the facts of each case and explains its reasoning so the public, the affected community and the Postal Service can be aware of the issues involved and the concerns of the Commissioners. The Commission will set aside any determination that is arbitrary, capricious or otherwise not in accordance with the law or is unsupported by substantial evidence in the record. The Commission also appoints an officer of the Commission, or "Public Representative" to represent the interests of the general public. The Commission may either affirm the Postal Service's determination or remand the matter to the Postal Service for further consideration. The Commission may not, however, modify a determination of the Postal Service.

Delivery Points

Table VI–10 provides the number of residential and business delivery points by delivery type for FY 2008 through FY 2011. The change in the number of delivery points in FY 2009, FY 2010 and FY 2011 is also shown. The total number of delivery points continues to grow, but the rate of growth appears to be slowing. The total number of delivery points increased by 636,530 in FY 2011.

Table VI–10—Postal Service Delivery Points

Residential Delivery Points	FY 2011	FY 2010	FY 2011 Change from FY 2010	FY 2009	FY 2010 Change from FY 2009	FY 2008	FY 2003 Change from FY 2008
City Delivery	80,792,112	80,531,231	260,881	80,187,505	343,726	79,848,415	339,090
Rural	39,067,740	38,638,280	429,460	38,264,946	373,334	37,684,158	580,788
P.O. Box	15,891,349	15,739,698	151,651	15,601,883	137,815	15,639,031	(37,148)
Highway Contract	2,639,061	2,607,138	31,923	2,576,166	30,972	2,516,783	59,383
Total Residential Delivery	**138,390,262**	**137,516,347**	**873,915**	**136,630,500**	**885,847**	**135,688,387**	**942,113**
Business Delivery Points							
City Delivery	7,487,332	7,457,500	29,832	7,483,461	(25,961)	7,436,965	46,496
Rural	1,468,861	1,453,292	15,569	1,439,266	14,026	1,407,942	31,324
P.O. Box	4,072,664	4,355,674	(283,010)	4,489,688	(134,014)	4,587,454	(97,766)
Highway Contract	72,872	72,648	224	72,966	(318)	71,538	1,428
Total Business Delivery	**13,101,729**	**13,339,114**	**(237,385)**	**13,485,381**	**(146,267)**	**13,503,899**	**(18,518)**
Total Delivery Points	**151,491,991**	**150,855,461**	**636,530**	**150,115,881**	**739,580**	**149,192,286**	**923,595**

Source: USPS Annual Report to Congress.

Wait Time in Line

In FY 2011, the national average customer wait time in line was 2 minutes and 45 seconds, which the Postal Service indicates was down 12 seconds from last year. The average customer wait time in line for each area was:[66]

- Capital Metro – 2 minutes and 40 seconds - down 21 seconds from last year;
- Eastern – 2 minutes and 26 seconds - equal to last year;
- Great Lakes – 2 minutes and 5 seconds - down 12 seconds from last year;
- Northeast – 2 minutes and 35 seconds – down 13 seconds from last year;
- Pacific – 3 minutes and 16 seconds – down 9 seconds from last year;
- Southwest – 3 minutes and 3 seconds – down 25 seconds from last year; and
- Western – 3 minutes – down 7 seconds from last year.

Beginning in FY 2010, the Postal Service measured wait time in line in the new Customer Experience Survey.[67] Survey participants were asked how long they waited in line for a clerk during their last visit to a post office. The response categories were: one to 3 minutes; 4 to 5 minutes; 6 to 10 minutes; 11 to 15 minutes; and 16 minutes or more.

The average wait time in line results for customer responses for FY 2011 and FY 2010 are shown in Table VI–11 for small to medium size business and residential customers.[68] In FY 2011, 70 percent of

Table VI–11—Wait Time In Line Weighted Average

	Small/Medium Business		Residential	
Wait Time In Line	FY 2011	FY 2010	FY 2011	FY 2010
Less than 1 minute	18%	17%	19%	18%
1-3 minutes	29%	28%	31%	29%
4-5 minutes	23%	23%	24%	23%
Subtotal 5 minutes or less	70%	68%	73%	70%
6-10 minutes	17%	17%	15%	16%
11-15 minutes	7%	8%	6%	7%
16 minutes or more	6%	7%	5%	7%
Total	100%	100%	100%	100%

Source: USPS-FY11-38 and USPS-FY10-38

small to medium business customers estimated they waited in line 5 minutes or less, and 73 percent of residential customers estimated they waited five minutes or less. Each of these results is an improvement over FY 2010 results. At the other end of the spectrum, 30 percent of small to medium business customers reported a wait time in line of over 6 minutes and 27 percent of residential respondents reported wait times of over 6 minutes. Once again, each of these results is an improvement over FY 2010.

Collection Points

Collection points are an important access channel for single-piece First-Class Mail. Collection points are defined locations where a customer drops off mail for collection by the Postal Service. These can include collection boxes, mailchutes, firm pickups, Automated Postal Center (APC) drops, lobby drops and mail collection racks. As shown in Table VI–12, collection boxes were 75 percent of total collection points in FY 2011. All collection points are required to be entered

66 Responses of the United States Postal Service to Questions 1-18 and 26-27 of Chairman's Information Request No. 2, February 7, 2012, question 10 (Response to CHIR No. 2).

67 Library Reference Docket No. ACR2010, library reference USPS-FY10-38, question 11 in residential and small to medium business surveys.

68 Large businesses were not asked this particular question.

in the Collection Point Management System (CPMS) by the responsible district.[69]

Table VI–13 shows the number of collection points by the Postal Service administrative area for 2006, 2010 and 2011 and the percentage change in collection points. Table VI–14 shows similar data, but for collection boxes only. As can be observed from the Tables VI–13 and VI–14, the number of collection points and collection boxes has declined steadily from their 2006 levels by nearly 20 percent and by approximately 3 percent between 2010 and 2011.

The number of collection points by type of location is shown in Table VI–15. The change in the number of collection points between 2006 and 2010 and between 2010 and 2011 is also shown. Table VI–15 illustrates that collection points located in business areas, while still the largest number of collection points, have declined by over 4 percent between 2010 and 2011 and by nearly 23 percent between 2006 and 2011. The number of residential collection points declined by 4 percent between 2010 and 2011 and by almost one-third (32 percent) between 2006 and

Table VI–12—Types of Collection Points by USPS Administrative Area FY 2011

Area	Collection Boxes	Other Collection Points	Total Collection Points	Collection Box Share of Total
Capital Metro	14,968	6,571	21,530	69.5%
Eastern	29,366	9,250	38,675	75.9%
Great Lakes	21,788	6,415	28,203	77.3%
Northeast	32,428	5,976	38,345	84.6%
Pacific	18,596	4,600	23,196	80.2%
Southwest	20,659	11,956	32,127	64.3%
Western	26,204	11,297	37,998	69.0%
Grand Total	**164,009**	**56,065**	**220,074**	**74.5%**

Source: USPS Collection Point Management System.

Table VI–13—Total Collection Points by USPS Administrative Area

Area[1]	2011	2010	2006	2011 Change from 2010	2010 Change from 2006
Capital Metro	21,530	22,239	23,314	-3.2%	-7.7%
Eastern	38,675	40,278	51,395	-4.0%	-24.7%
Great Lakes	28,203	29,196	35,739	-3.4%	-21.1%
Northeast	38,345	39,469	44,891	-2.8%	-14.6%
Pacific	23,196	24,530	29,695	-5.4%	-21.9%
Southwest	32,127	32,169	40,250	-0.1%	-20.2%
Western	37,998	39,516	44,634	-3.8%	-14.9%
Grand Total	**220,074**	**227,397**	**269,918**	**-3.2%**	**-18.5%**

Source: USPS Collection Point Management System.

[1] 2006 and 2010 data adjusted to reflect 2011 Administrative Area Structure Changes

[69] The CPMS is an ongoing operational data system which is not built with a requirement that allows retrospective looks as of some particular point in time. It is frequently updated during any given time period. *See* Responses of the United States Postal Service to Questions 1, 3-6, 8-27, 29-37, and 39-42 of Chairman's Information Request Mo. 1, January 27, 2012, question 27.

Table VI–14—Number of Collection Boxes by USPS Administrative Area

Area	2011	2010	2006	2011 Change from 2010	2011 Change from 2006
Capital Metro	14,968	15,564	19,699	-3.8%	-24.0%
Eastern	29,366	30,298	39,690	-3.1%	-26.0%
Great Lakes	21,788	22,253	28,143	-2.1%	-22.6%
Northeast	32,428	33,121	39,025	-2.1%	-16.9%
Pacific	18,596	20,048	24,905	-7.2%	-25.3%
Southwest	20,659	21,676	28,385	-4.7%	-27.2%
Western	26,204	27,574	31,734	-5.0%	-17.4%
Grand Total	**164,009**	**170,534**	**211,581**	**-3.8%**	**-22.5%**

Source: USPS Collection Point Management System.

[1] 2006 and 2010 data adjusted to reflect 2011 Administrative Area Structure Changes

2011. Collection points located outside of post offices declined by 4 percent between 2010 and 2011 and by 15 percent between 2006 and 2011.

Notably, however, post office lobby collection points increased by 5.6 percent between 2006 and 2011, but decreased by 1 percent between 2010 and 2011. The availability of collection points (boxes and lobby drops as well as APCs) located at post offices is somewhat uncertain since the Postal Service is in the process of closing many retail facilities and also

Table VI–15—Number of Collection Points by Location-Type

	Year			Change in Number	Percent Change	Change in Number	Percent Change
Location Type	2006	2010	2011	2006-2011		2010-2011	
Business	108,418	87,391	83,587	(24,831)	-22.9%	(3,804)	-4.4%
Residential	61,038	43,342	41,513	(19,525)	-32.0%	(1,829)	-4.2%
Post Office Outside	53,665	47,579	45,632	(8,033)	-15.0%	(1,947)	-4.1%
Post Office Lobby	37,110	39,636	39,175	2,065	5.6%	(461)	-1.2%
Customer Lobby	4,057	2,729	3,920	(137)	-3.4%	1,191	43.6%
Other	3,191	4,357	3,772	581	18.2%	(585)	-13.4%
Contract Station	948	873	952	4	0.4%	79	9.0%
Mail Room	807	782	787	(20)	-2.5%	5	0.6%
Customer Dock	464	337	264	(200)	-43.1%	(73)	-21.7%
Airport	152	138	143	(9)	-5.9%	5	3.6%
Goverment Building	68	233	263	195	286.8%	30	12.9%
Approved Shipper			66	66		66	
Grand Total	**269,918**	**227,397**	**220,074**	**(49,844)**	**-18.5%**	**(7,323)**	**-3.2%**

Source: USPS Collection Point Management System

appears to be reducing access to lobbies after hours. This is important since by 2011, there were more collection points located at post offices (both outside and in the lobbies) than at any other type of location and represented nearly 40 percent of total collection points.

The Postal Service's practice is, generally, to remove and relocate blue collection boxes that had been located outside of discontinued post offices. The Postal Service maintains, the critical driver is customer need. If a landowner agrees, a ready means of retrieving mail from the collection box can be found, and customer need exists, the collection box may be retained at the discontinued location. *See* Response to CHIR No. 2, question 27. In addition, the Postal Service has stated that through the RAOI, APC availability will remain as it is, although APCs currently located in offices that are being closed will be relocated.[70] The Postal Service has indicated that its current plans regarding improvement of its collection box network include taking a more active top-down management approach to its collection box network. The aim is to ensure convenient customer access to collection boxes, which may require relocation of boxes to higher traffic areas (grocery stores, shopping centers and other public gathering locations) while minimizing unwarranted collection box removals. In particular, area offices are examining collection box schedules and locations and must approve any local collection system changes. The Postal Service has determined that the need for a time decal box with a last collection of 5:00 p.m. or later is now to be defined in terms of a threshold number of average daily pieces. A business requirement for making a pickup time earlier must justify any such changes. These changes have stabilized last pickup times. Use of high density boxes in locations with multiple boxes should help reduce the cost without impacting customer convenience. The number of minutes between nominal (posted) and actual pickup times has been narrowed to twenty.[71]

Alternative Access

In addition to providing postal products and services at postal retail counters, the Postal Service has continued to expand postal access through additional marketing channels. For FY 2011, over 35 percent of retail revenue was generated through means other than a postal retail counter. Table VI–16 identifies the FY 2011 revenue each retail channel generated, the share of total retail revenue each contributed and the percent change in revenue provided in FY 2011 and FY 2010. The Postal Service had set a goal of expanding alternative access to postal products and services to 35 percent. As shown in Table VI–16, the Postal Service appears to have met that goal at least in a broad sense. What is not clear, is whether alternative access points provide a sufficient range of services to customers in both urban and rural locations throughout the nation.

PC Postage and digital postage meters allow customers who mail frequently to print postage and shipping labels. The proportion of revenue generated by PC postage increased by just over 33 percent; from 12.4 percent of retail revenue in FY 2010 to 16.5 percent in FY 2011. PC Postage vendors have been participating in pilot trials to enhance payment options for package returns. Another

[70] Docket No. N2011-1, Advisory Opinion on Retail Access Optimization Initiative, December 23, 2011, at 109 (Docket No. N2011-1, Advisory Opinion).

[71] Responses of the United States Postal Service to Questions 1-17 of Chairman's Information Request No. 3, February 14, 2012, question 16.

Table VI–16—Retail Revenue by Channel

Services	FY 2011 Revenue ($ Millions)	Share of Total Retail Revenue	Change from FY 2010	FY 2010 Revenue ($ Millions)	Share of Total Retail Revenue	Change from FY 2009
Post Offices	$10,940	64.5%	$(1,193)	$12,133	69.3%	(4.6%)
PC Postage	$2,799	16.5%	$619	$2,180	12.4%	17.3%
Stamps only sales by retail partners	$1,155	6.8%	$12	$1,143	6.5%	(1.1%)
Automated Postal Centers (kiosks)	$544	3.2%	$(35)	$579	3.3%	5.3%
Stamps by Mail/phone/fax	$517	3.0%	$8	$509	2.9%	(0.7%)
Contract Postal Units	$434	2.6%	$(20)	$454	2.6%	0.3%
Usps.com/Click-N-Ship	$462	2.7%	$39	$423	2.4%	16.2%
Other	$103	0.6%	$(9)	$94	0.5%	13.1%
Total	**$16,954**	**100.0%**	**$(579)**	**$17,515**	**100.0%**	**(1.3%)**

Source: ACD 2010, P.75; ACD 2011, CHIR No. 2, Question 25.

initiative focuses on qualifying PC Postage systems for federal government entities, which would provide an alternative to using postage meters and a competitive service for expedited shipments.

The Postal Service's website allows customers to purchase stamps and philatelic products and order free shipping supplies. Also, customers may search and pay for a post office box as well as manage their post office box accounts online. The FY 2011 revenue generated by the Postal Service's website and Click-N-Ship was $462 million, an increase of over 9 percent from FY 2010.

The Postal Service has been selling stamp booklets at supermarkets, drug stores and other commercial outlets since the 1980s. Stamps are available at 70,000 such locations and in FY 2011 generated $1.16 billion which represented 6.8 percent of retail revenue.

Contract Postal Units (CPUs) and Community post offices (CPOs) offer a wide range of postal services other than just stamps and are operated by a host retailer. In FY 2011 there were just over 3,600 operational CPUs. These generated $434 million in revenue which represented a decline from FY 2010 of 4.4 percent. Its share of total retail revenue remained constant at 2.6 percent. Village post offices (VPOs) were introduced as part of the Postal Service's RAOI. VPOs are a new concept for the Postal Service and will be considered in communities which have no post office or lose their post office. VPOs will be located in non-Postal Service establishments such as in a community business, town hall, or government center. By being located at business and other places that customers already frequent, VPOs, it is hoped, will offer Postal Service customers time-saving convenience and in many instances longer hours than regular post offices.[72] The VPO will provide a select range of services that include the sale of First-Class Postage stamps, offering priority flat mail products, delivering to P.O. boxes and accepting mail.

Upon the opening of the Doe Run VPO in Missouri, the Postal Service pointed out that this VPO would be open 24/7 and will feature a blue collection box

[72] United States Postal Service Village Post Office—Fact Sheet, July 2011.

outside as well as post office boxes inside which will be serviced by a clerk from a nearby office who will deliver to these boxes by 2:00 p.m. Monday through Saturday. The Postal Service also notes that the VPO will not weigh or rate packages, but will accept pre-paid packages for free carrier pickup.[73] It remains to be seen whether all VPOs will offer the range of services to be offered at the Doe Run VPO.

As of the end of FY 2011, there were nine VPOs currently in operation. The Commission commends the Postal Service's efforts to continue a high level of service to communities who have no post office or who have lost their post office. However, the Commission noted in an Advisory Opinion that VPOs are limited substitutes for full service postal retail facilities.[74] The effort to establish VPOs will become even more important if the Postal Service continues to reduce the size of its postal-managed retail network.

Post Office Suspensions

Data provided by the Postal Service[75] and shown in Table VI–17, indicates that there were 197 offices under suspension at the beginning of FY 2011. In addition, 179 offices were suspended during FY 2011. The 197 offices under suspension at the beginning of FY 2011 is considerably less than the number under suspension in early February 2010 when data provided by the Postal Service indicated that nearly 400 post offices were under suspension. Thus, it appears that the Postal Service has made progress in resolving its backlog of suspended offices. It should also be noted from Table VI–17 that the status of post offices under suspension at the beginning of FY 2011 is somewhat uncertain. Post offices once suspended can either remain suspended, be closed or be re-opened. One office is currently listed as being studied for closure as part of the RAOI, and 12 more are currently listed as being studied for closure "outside" of the RAOI. For post offices suspended during FY 2011, 77 offices out of a total of 179 suspended offices (43 percent) are being studied for discontinuance. The Postal Service has recently revised its procedures for closing facilities. *The Commission hopes that these streamlined post office closing procedures will result in the need for fewer suspensions and where suspension is necessary, in shorter durations.*

Table VI–17—Number and Discontinuance Status of Suspended Offices

Time Period	Listed for Closure			Total Suspended Offices
	RAOI	Outside of RAOI	Unknown	
Under Suspension at Beginning of FY 2011	1	12	184	197
Suspended During FY 2011	37	40	102	179
Grand Total	38	52	286	440

Source: CHIR No. 1, Question 28

[73] *See* USPS United States Postal Service Press Release, Postal Service to Open Missouri's First Village Post Office, November 21, 2011.
[74] Docket No. N2011-1, Advisory Opinion at 111.
[75] CHIR No. 1, Question 28.

Customer Experience

CEM system

39 U.S.C. 3652(a)(2)(B)(ii) requires the Postal Service to provide measures of the degree of customer satisfaction with the service provided for its market dominant products. In FY 2011, the Postal Service implemented a new approach for measuring customer experience and satisfaction.[76] The CEM system randomly selects residential and small/medium business customers through surveys them via online or hard copy surveys.[77] Large business customers were asked to complete an online survey only. The Commission compared survey responses from FY 2010 and notes there were not any significant shifts in customer satisfaction in FY 2011.

CEM measures customer experience with market dominant products by asking participants to rate their product satisfaction using a six-point scale: Very Satisfied, Mostly Satisfied, Somewhat Satisfied, Somewhat Dissatisfied, Mostly Dissatisfied, and Very Dissatisfied.[78] The Postal Service reported only the top two box scores of Very Satisfied and Mostly Satisfied.

The Postal Service identified more than 318,000 retail customers and 300,000 small businesses to gauge residential and small business customer experience. In FY 2011, approximately 60 percent female and 40 percent male residential participants were surveyed. Forty percent were aged sixty-five or older and 30 percent had at least some college education. Most residential customers responded positively to their experience with the post office and its employees. However, most negative sentiment in FY 2010 and FY 2011 regarded lack of prompt customer service at post office locations. Twenty-three percent of customers responded "Strongly Disagree" or "Somewhat Disagree" when asked "Does your post office location provide enough open lines to appropriately serve customers?" Additionally, 17 percent of participants "Strongly Disagree" or "Somewhat Disagree" when surveyed "Does your post office location provide sufficient self-service alternatives?" Approximately 30 percent of small businesses surveyed were either home offices, stand-alone, or businesses inside buildings with other businesses. Similar to residential customers, small businesses expressed most negative sentiment toward closed or inoperable post office lines and lack of self-service alternatives. Thirty percent of responses either "Somewhat" or "Strongly" disagreed when surveyed "Does your post office location provide enough open lines to appropriately service customers?" Twenty percent of participants surveyed "Somewhat" or "Strongly" disagreed that the post office provides enough self-service alternatives.

[76] 2011 ACR at Page 11.
[77] *Id.* at 12.
[78] *Id.*

Table VI–18—Customer Experience

Mailing Products and Services	Residential %		Small/Medium Business %		Large Business %	
	FY 2010	FY 2011	FY 2010	FY 2011	FY 2010	FY 2011
First-Class Mail	93.7	94.2	92.4	93.0	90.2	92.1
Single-Piece Int'l	85.9	86.6	83.2	84.0	86.3	89.2
Standard Mail	83.3	84.1	85.9	87.0	84.5	85.6
Periodicals	86.1	87.0	83.8	85.1	82.8	84.3
Single-Piece Parcel Post	88.2	89.2	87.0	88.0	84.6	87.5
Media Mail	87.6	88.4	86.4	87.1	85.6	86.7
Bound Printed Matter	85.4	86.2	83.4	85.0	82.4	84.1
Library Mail	86.7	87.0	84.9	86.0	85.1	86.8

Table VI–18 illustrates customer survey responses to questions regarding their feelings on each market dominant product. Specifically, the survey asked them to express their overall satisfaction for each market dominant product. The Postal Service reported only the top two box scores of Very Satisfied and Mostly Satisfied. Overall, customer satisfaction was steady and in some cases exceeded FY 2010 results.

Chapter VII

Market Dominant Products

Introduction

This chapter presents the Commission's analysis, organized by class, of the financial results and rates for each market dominant product, for market dominant NSAs, for market dominant volume incentives, and for market dominant international products. The financial analysis focuses on cost coverage and pricing issues, including whether the class and its products generate adequate revenue to cover attributable costs.

The relationship of revenue to attributable cost for each product is an important consideration and this importance is amplified by the Postal Service's fiscal crisis. In the financial analysis section for each class, the Commission evaluates the relationship of revenue to attributable cost for each product. This relationship is viewed from two perspectives: (1) cost coverage which is a relative measure and (2) contribution which is an absolute measure.

Section 3622 identifies 9 objectives and 14 factors that the Postal Service must balance when setting prices. One of the objectives the Postal Service must consider is revenue adequacy and one of the factors it must take into account is the requirement that each class of mail or type of mail service bear its direct and indirect postal costs.

As the Postal Service, Congress and stakeholders address the Postal Service's deteriorating financial situation, it is imperative to examine all the issues that contribute to the financial challenges including loss-making products and services. Over the past three fiscal years, the Postal Service lost $5.1 billion on products which generated insufficient revenues to cover their attributable costs. These products, because they did not cover their attributable costs, also made no contribution towards the institutional costs of the Postal Service. Such a result appears inconsistent with an objective of the modern system of ratemaking, namely, that the system of ratemaking "assure adequate revenues…to maintain financial stability." *See* 39 U.S.C. 3622(b)(5). The loss


from products that do not cover their attributable cost accounts for $1.6 billion, or 31 percent, of the Postal Service's $5.1 billion net loss in FY 2011.

The PAEA grants the Postal Service expanded pricing flexibility in exchange for stable and predictable rates under an inflation-based price cap. The informed and rational use of that pricing flexibility is an essential component of any long-term strategy to restore the Postal Service to profitability. The Postal Service must use its pricing flexibility to adjust prices for loss making products or risk the long-term sustainability of the postal system. It appears from the analyses in the sections that follow, that the Postal Service has been unable to take advantage of its pricing flexibility, especially in Standard Mail.

Given that attributable (direct and indirect) costs account for only about 60 percent of total costs, adjusting prices to cover attributable cost would not seem to pose a formidable challenge. Yet, the losses from some market dominant products persist. If the Postal Service's revenues covered its total cost, it might be able to sustain the losses from these market dominant products, but it is now in dire financial straits. For these reasons, product cost coverage and plans to bring loss-making products to full cost coverage have to be an important consideration.

The principal findings for FY 2011 are summarized below:

- Ten products and services generated insufficient revenues to cover attributable costs. The total loss from these products is $1.6 billion. This only represents the amount necessary to reach 100 percent cost coverage; increasing the revenue from these products to cover the loss would still not result in any contribution towards institutional costs.
- Two classes of mail fail to cover their attributable cost: Periodicals ($609 million) and Package Services ($191 million).
- Three products account for $1.4 billion of the loss: Standard Flats ($643 million), Standard NFMs/Parcels ($112 million), and Outside County Periodicals ($590 million).
- The Commission finds that the FY 2011 rates for Standard Flats remain out of compliance.
- Per-piece revenue from Standard Mail Nonprofit pieces was 56.38 percent of Standard Mail commercial per-piece revenues. However, the price adjustment proposed in Docket No. R2012-3 is expected to produce an average revenue per piece that is 60 percent of Standard Mail commercial per-piece revenues as required by 39 U.S.C. 3626(a)(6).

Each class section also contains a discussion of worksharing and other rate issues. Methodological issues affecting the development of estimates of worksharing-related cost avoidances are addressed, the resulting cost avoidances are compared with the corresponding discounts, and the discounts and other rate relationships are analyzed for consistency with the applicable statutory provisions.

The workshare findings for FY 2011 are summarized below:

- 35 workshare discounts exceeded avoided costs.
- 15 discounts qualified for a statutory exception.
- 16 discounts did not satisfy 3622(e)(2).
- The Commission is unable to determine if 3 discounts are consistent with section 3622(e) because of problems with the underlying costs.
- The evaluation of one discount has been temporarily suspended pending the outcome of Docket No. RM2010-13.

There are other issues that do not fit neatly elsewhere in this chapter. Thus, in addition to presenting the principal findings, this introduction also includes a discussion of the effects of past and pending rulemakings, the price cap, revised cost avoidance estimates filed by the Postal Service in response to CHIR No. 2, and the basis for year-to-year comparison used in this chapter.

Past and Pending Rulemakings

The Commission calculates worksharing passthroughs utilizing methodologies approved by the Commission prior to the filing of the ACR. In November, the Postal Service filed two petitions to initiate proceedings to consider alternate methodologies, some of which affect cost models used for calculating cost avoidances.[1] One was filed on November 1 and the other on November 30. Although the first rulemaking was approved on January 20, 2012, neither rulemaking was completed prior to the issuance of the ACR. Thus, for the sake of consistency, the entire current ACR should reflect only methodologies approved prior to the issuance of the ACR. The Commission emphasized this point in the last ACD, when it reiterated that the ACR must reflect approved methodologies in accordance with 39 CFR 3050.10. 2010 ACD at 6-7. Despite this clarification, the Postal Service used several unapproved methodologies in the current ACR.

One change involved modifying the IOCS to correctly assign tallies to Parcel Select rather than Parcel Post. The Postal Service incorporated this unapproved methodology because it believes the results to be more accurate. Further, it did not provide a version of the CRA without the change because it is infeasible to do so, it argues, because of all the affected data systems. Thus, the Postal Service presented the Commission with a *fait accompli* and it has no choice but to accept the revised approach and to make its evaluations on that basis. The Commission directs the Postal Service to use approved methodologies in future submissions.

With respect to the use of other unapproved methodologies, most notably, Proposal Eighteen from Docket No. RM2012-2, which relates to the role of FSS in the cost avoidance models, the Commission relies on the methodologies approved prior to the issuance of the ACR in accordance with 39 CFR 3050.1.[2] Accordingly, the discussion and analyses that follow reflect this approach.

Several workshare discounts that exceed avoidable cost in FY 2011 were adjusted to achieve 100 percent passthroughs in Docket No. R2012-3. However, the Postal Service relied on avoidable cost estimates from FY 2010. The Commission approved the rates the Postal Service proposed in Docket No. R2012-3, but some of the discounts that passed through no more than 100 percent of the FY 2010 cost avoided increase to more than 100 percent when FY 2011 costs avoided are used. Thus, in some cases, the Docket No. R2012-3 prices fail to correct discounts that did not comply with section 3622(e) in FY 2011. These issues are discussed in each class sub-section as applicable.

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1 Docket No. RM2012-1, Petition of the United States Postal Service Requesting Initiation of a Proceeding to Consider Proposed Changes in Analytical Principles (Proposals Nine - Fifteen), November 1, 2011. *See* also *Docket No. RM2012-2, Petition of the United States Postal Service Requesting Initiation of a Proceeding to Consider Proposed Changes in Analytical Principles (Proposals Sixteen through Twenty), November 30, 2011.*

2 The other change modified the NSA cost model. That model is generally not evaluated in the ACD process, but rather when the Postal Service submits NSAs.

Price Cap

In the past two ACDs, the Commission has reviewed the application of the price cap from a post-implementation perspective. In accordance with the Commission's rules, when the Postal Service files a notice of market dominant price adjustment, it uses historical billing determinants to ensure compliance with the applicable price cap. The Commission reviews the price adjustments on that basis and this is referred to as a pre-implementation review. However, the pre-implementation review does not account for the effect of price changes on billing determinants. For this reason, the Commission conducts a post-implementation review in the ACD.

In the FY 2009 ACD, the Commission evaluated the effects of the price changes from Docket No. R2008-1 because those rates had been in effect for a year, which is required for a useful comparison. In the FY 2010 ACD, the Commission was able to evaluate the effects of the price changes from Docket No. R2009-2 because there were sufficient data to do so. The Postal Service did not file market dominant price adjustments during FY 2010, so there are no price changes to evaluate. Although price adjustments from Docket No. R2011-2 became effective April 17, 2011, there is not a full year's data available that reflect those prices being in effect. For this reason, the Commission cannot conduct a post-implementation review of the price cap from that docket.

Revised Cost Avoidance Estimates

On March 2, 2012, with its response to Question 2 of Chairman's Information Request No. 1, the Postal Service filed revised Standard Mail letters and First Class Mail letters mail processing cost avoidance models. These models correct errors in the calculations of the incoming secondary mail volume percentages found in USPS-FY10-10 and USPS-FY11-10. In particular, the revision changes the FY 2010 and FY 2011 measures of the proportions of DBCS sorted DPS mail, CSBCS sorted DPS mail, and mail not sequenced.

The mail processing cost models calculate DPS percentages by presort level which are inputs into the delivery cost avoidance model. However, the Postal Service did not update the delivery cost model for First-Class Mail and Standard Mail with the revised DPS percentages from the revised mail processing cost models.

To provide more accurate results, the Commission updated the delivery cost avoidance model to reflect the revised DPS percentages. *See* PRC-ACR2011-LR2. For its cost avoidance calculations for First-Class Mail and Standard Mail, the Commission uses the revised mail processing cost avoidances from the Postal Service's revised Standard Mail letters and First Class Mail letters mail processing cost avoidance models and delivery cost avoidances from the delivery cost model revised by the Commission.

Year-to-Year Comparisons

As explained in Chapter IV, the Postal Service revises some RPW volume and revenue estimates for previous years. In that chapter, the Commission uses the revised figures for year-to-year comparisons. In this chapter, the Commission uses figures from past ACDs for year-to-year comparisons, which do not reflect any post-ACD revisions to RPW figures. Chapter IV provides a more comprehensive view of the Postal Service's finances, whereas this chapter provides a more detailed analysis of products. Because compliance analysis is based on current RPW figures

rather than after-the-fact revisions, using previous ACDs for comparison purposes provides consistency.

First-Class Mail

Introduction

First-Class Mail consists of six products: Single-Piece Letters/Postcards, Presort Letters/Postcards, Flats, Parcels, Outbound Single-Piece First-Class Mail International, and Inbound Single-Piece First-Class Mail International. The class had a volume of 73.5 billion pieces in FY 2011. First-Class Mail accounts for 44 percent of total volume and 66 percent of total contribution. Both volume and contribution decreased from FY 2010 by 6.0 percent and 5.6 percent, respectively.

The principal FY 2011 findings for First-Class Mail are:

- Nine worksharing discounts exceed avoided cost.
  - » Two discounts were properly justified under section 3622(e).
  - » Four discounts were not properly justified under section 3622(e).
    - One discount was properly re-aligned in Docket No. R2012-3.
    - The Postal Service must properly align the other three discounts in the next market dominant price adjustment.
  - » The Commission is unable to determine if two discounts are consistent with the statute because of problems with the underlying costs.
  - » The evaluation of one, the Mixed AADC automation discount, has been temporarily suspended pending the outcome of Docket No. RM2010-13.
- All domestic First-Class Mail products covered cost in FY 2011.

Financial Analysis

The FY 2011 First-Class Mail cost coverage was 199.0 percent. As Table VII–1 shows, total First-Class Mail FY 2011 revenue was $32.2 billion, which covered its attributable cost of $16.2 billion and contributed $16.0 billion to institutional cost. First-Class Mail's cost coverage decreased from 199.3 percent in FY 2010 to 199.0 percent in FY 2011 due to the change in the mail mix.

Increases in unit attributable costs for all domestic First-Class Mail products were less than the 2.7 percent increase in the CPI-U for FY 2011. Compared with FY 2010, the unit attributable cost for single-piece letters and cards increased 2.2 percent; the unit cost for presort letters and cards decreased 0.3 percent; the unit cost for Flats increased 0.9 percent; and the unit cost for Parcels decreased 7.1 percent. For FY 2011, First-Class Mail unit attributable cost increased by 0.7 percent on average. Each domestic First-Class Mail product covered its attributable cost in FY 2011.

In FY 2010, Parcels had a 100.1 percent cost coverage. In Docket No. R2011-2, the Commission approved an above average increase of 2.6 percent for Parcels. The Commission also approved a uniform price for parcels weighing up to 3 ounces. These changes collectively increased the cost coverage for the Parcels product to 110 percent. Additionally, the Commission approved the transfer of commercial First-Class parcels to the competitive products list. The transfer did not occur during FY 2011 and thus does not affect the findings for this fiscal year[3].

3 *See* Postal Service Response to Chairman's Information Request No. 1, question 24

Table VII–1—First-Class Mail
FY 2011 Volume, Revenue, Cost, Contribution, and Cost Coverage by Product

First-Class Mail	Volume	Total Revenue	Attributable Cost	Contribution to Institutional Cost	Rev./Pc.	Cost/Pc. (Cents)	Contribution to Institutional Cost/Pc. (Cents)	Cost Coverage
Single-Piece Letters	24,550,824	11,261,338	6,848,209	4,413,129	45.869	27.894	17.975	164.4%
Single-Piece Cards	1,295,941	382,090	336,435	45,655	29.484	25.961	3.523	113.6%
Total Single-Piece Letters and Cards	**25,846,765**	**11,643,428**	**7,184,644**	**4,458,784**	**45.048**	**27.797**	**17.251**	**162.1%**
Presort Letters	41,740,735	14,963,092	4,963,359	9,999,733	35.848	11.891	23.957	301.5%
Presort Cards	2,753,763	601,837	220,231	381,605	21.855	7.997	13.858	273.3%
Total Presort Letters and Cards	**44,494,498**	**15,564,929**	**5,183,590**	**10,381,338**	**34.982**	**11.650**	**23.332**	**300.3%**
Single-Piece Flats	1,577,051	2,264,945	1,488,616	776,328	143.619	94.392	49.227	152.2%
Presort Flats	653,869	554,219	457,783	96,436	84.760	70.011	14.749	121.1%
Total Flats	**2,230,920**	**2,819,164**	**1,946,399**	**872,764**	**126.368**	**87.246**	**39.121**	**144.8%**
Single-Piece Parcels	621,319	1,260,228	1,143,605	116,623	202.831	184.061	18.770	110.2%
Presort Parcels	16,663	25,775	25,369	407	154.687	152.246	2.441	101.6%
Total Parcels	**637,982**	**1,286,003**	**1,168,973**	**117,030**	**201.573**	**183.230**	**18.344**	**110.0%**
Total Domestic First-Class Mail	**73,210,165**	**31,313,523**	**15,483,607**	**15,829,916**	**42.772**	**21.150**	**21.623**	**202.2%**
Total International First-Class Mail	310,379	864,837	688,184	176,652	278.639	221.724	56.915	125.7%
Total First-Class Mail	**73,520,543**	**32,178,360**	**16,171,791**	**16,006,569**	**43.768**	**21.996**	**21.772**	**199.0%**

Source: PRC-ACR2011-L1

Comments

National Postal Policy Council (NPPC), Direct Marketing Association, Inc./National Association of Presort Mailers/Parcel Shippers Association (DMA/NAPM/PSA) and Pitney Bowes have expressed concerns about the high cost coverage for commercial bulk First Class Letters. DMA/NAPM/PSA assert that the relative contribution of Presort is too high compared with Single-Piece and that the gap between the two has been growing. DMA/NAPM/PSA Comments at 1. DMA/NAPM/PSA also contend that minimizing the disparity in unit contributions between First-Class Mail Single-Piece Letters/PostCards and Presort Letters/Postcards would not only create a more equitable price schedule, but would also increase total contribution. *Id.* at 2 - 3. It claims that Presort Letters/Postcards are more price sensitive than Single-Piece Letters/Postcards. *Id.*

Consequently, the loss of revenue from lowering the price of Presort Letters/Postcards would be more than offset by the gain in revenue from a price cap neutral increase in the price of Single-Piece Letters/Cards. *Id.* They urge the Commission to allow the Postal Service to take incremental steps immediately to minimize this disparity. DMA/NAPM/PSA Comments at 1; Pitney Bowes Comments at 5. NPPC contends that the rates for First-Class Automation and Presort Letters/ Postcards mail product generate an excessive cost coverage. NPPC Comments at 2-3. It suggests that to give "Presort Mailers necessary relief and to ensure ongoing compliance by Presort rates with sections 3622(b)(1) and (b)(8), the Commission should complete its workshare rulemaking…." Docket No. RM2010-13. *Id.* at 7.

Commission Analysis

NPPC draws attention to sections 3622(b)(1) and 3622(b)(8) of the Postal Accountability and Enhancement Act. These sections delineate only two of the nine objectives that the Commission considers when determining compliance. Market dominant mailers also have the additional protection of a price cap to shield them from excessive pricing. One objective of section 3622 is to allow the Postal Service pricing flexibility. Applying the CPI cap at the class level rather than the product level gives the Postal Service ability to apply non-uniform price adjustments within a class.

Worksharing

The following 9 worksharing discounts exceeded avoided cost: (1) Qualified Business Reply Mail (QBRM) Letters; (2) QBRM Cards; (3) Mixed AADC Automation Letters; (4) AADC Automation Letters; (5) Mixed AADC Automation Cards; (6) AADC Automation Cards; (7) 5-Digit Automation Cards; (8) ADC Automation Flats; and (9) 3-Digit Automation Flats. The avoided cost calculations that form the basis of these passthroughs employ the accepted methodology. Table VII–2 shows the workshare discounts for letters, flats, and parcels. Table VII–3 shows the workshare discounts for cards. Below, the Commission discusses passthroughs above 100 percent in the same order as listed above.

QBRM

The discounts for QBRM Letters and Cards passthrough 287.5 percent of avoided cost. *See* Table VII–2 for letters and Table VII–3 for cards. The excessive passthrough appears to result from continuing decreases in avoided cost.

In the FY 2010 ACD, the Commission expressed concern that the current costing methodology underestimated the cost avoidance. A change in methodology is currently under consideration in Docket No. RM2012-2. Pending disposition of that proceeding, the Commission will not determine whether the discounts are consistent with section 3622(e). Accordingly, no further action is warranted at this time.

Automation Letters

The Postal Service calculates the following passthroughs of avoided costs for automation letters: Mixed AADC, 147.1 percent and AADC, 104.8 percent.

In Order No. 536, the Commission suspended the evaluation of the automation Mixed AADC letter discount with regard to section 39 U.S.C. 3622(e) pending the outcome of Docket No. RM2010-13, which seeks to determine the appropriate base or reference group for calculation of costs avoided by

Table VII-2—First-Class Mail Letters, Flats, and Parcels Workshare Discounts and Benchmarks

Type of Worksharing (Benchmark)	FY 2011 Year-End Discount (cents)	Unit Cost Avoidance (cents)	Pass-through
First-Class Mail Automation Letters			
Barcoding & Presorting			
Automation Mixed AADC Letters (Bulk Metered Mail (BMM) Letters)	5.0	3.4	147.1%
Automation AADC Letters (Automation Mixed AADC Letters)	2.2	2.1	104.8%
Automation 3-Digit Letters (Automation AADC Letters)	0.3	0.4	75.0%
Automation 5-Digit Letters (Automation 3-Digit Letters)	2.5	2.5	100.0%
First-Class Mail Automation Flats			
Barcoding & Presorting			
Automation ADC Flats (Automation Mixed ADC Flats)	12.0	5.6	214.3%
Automation 3-Digit Flats (Automation ADC Flats)	5.8	4.6	126.1%
Automation 5-Digit Flats (Automation 3-Digit Flats)	17.4	18.8	92.6%
First-Class Mail Presorted/Business Parcels			
Barcoding & Presorting			
Presort 3-Digit Parcels (Presort ADC Parcels)	8.6	75.6	11.4%
Presort 5-Digit Parcels (Presort 3-Digit Parcels)	13.2	46.4	28.4%
First-Class Mail Nonautomation Letters			
Presorting			
Nonautomation Presort Letters (Bulk Metered Mail (BMM) Letters)	2.6	2.7	96.3%
Qualified Business Reply Mail			
Barcoding			
QBRM [1] (Handwritten Reply Mail)	2.3	0.8	287.5%

[1] The QBRM cost avoidance presented here is estimated using the USPS methodology. The Commission found in R2006-1 that this underestimated avoided costs, but that the alternative on the record overestimated avoided costs.

worksharing. NPPC disagrees with the decision to maintain the link between Presort mail and Single-Piece mail. NPPC Comments at 6. It further asserts that the Single-Piece benchmark is not consistent with the requirement stated in 39 U.S.C. 3622(b)(1) to maximize incentives to reduce cost. *Id.*

The Postal Service justifies the AADC automation letters discounts with the exception granted in 39

U.S.C. § 3622(e)(2)(D) — operational efficiency. The Postal Service explains that it currently has excess mail processing capacity and can absorb extra workload in the incoming mail processing operations. United States Postal Service Notice of Market-Dominant Rate Adjustment, October 18, 2011 at 35. It contends that it can increase efficiency by concentrating as much volume as possible in those operations. *Id.* Giving an added incentive to customers to move from the Mixed AADC worksharing tier into the AADC and 3-Digit worksharing tiers supports its strategy of increasing efficiency. *Id.*

The Commission accepts the justification for automation AADC letters. Nonetheless, the Postal Service should closely monitor the effect of the discount to ensure that its desired objectives are achieved.

Pitney Bowes raises concerns regarding the calculation of cost avoidance for Automated 5-Digit letters. In Docket No. R2012-3, the Postal Service set the price for AADC Presorted letters equal to 3-Digit Presorted letters. Pitney Bowes notes that the Postal Service effectively combined the rate for AADC and 3-Digit letters into one presort tier. Pitney Bowes Comments at 8-9. It further notes that the mailers' choice now is between preparing AADC letters and 5-Digit letters. *Id.* Thus, Pitney Bowes argues that the benchmark rate for Automated 5-Digit Letter Mail should be the AADC rate, not the 3-Digit rate. *Id.*

Pitney Bowes makes some persuasive arguments regarding the calculation of cost avoidance for Automated 5-Digit letters. As the Postal Service's operations and pricing incentives change, it may be necessary to modify the approach used to evaluate the affected discounts. Pitney Bowes may want

Table VII-3—First-Class Mail Cards Workshare Discounts and Benchmarks

Type of Worksharing (Benchmark)	FY 2011 Year-End Discount (cents)	Unit Cost Avoidance (cents)	Passthrough
First-Class Mail Automation Cards			
Barcoding & Presorting			
Automation Mixed AADC Cards (Nonautomation Presort Cards)	2.5	1.9	131.6%
Automation AADC Cards (Automation Mixed AADC Cards)	1.2	1.1	109.1%
Automation 3-Digit Cards (Automation AADC Cards)	0.1	0.2	50.0%
Automation 5-Digit Cards (Automation 3-Digit Cards)	1.4	1.2	116.7%
Qualified Business Reply Mail			
Barcoding			
QBRM [1] (Handwritten Reply Cards)	2.3	0.8	287.5%

[1] The QBRM cost avoidance presented here is estimated using the USPS methodology. The Commission found in R2006-1 that this underestimated avoided costs, but that the alternative on the record overestimated avoided costs.

to consider filing a petition with the Commission to initiate a proceeding to consider the proper calculation of the cost avoidance for Automated 5-Digit Letter Mail.

In its comments, Pitney Bowes also notes that the delivery unit cost differential between AADC and 5-Digit automation letters decreased as a result of a decreased DPS percentage. Id at 10-11. It comments that the use of automation to sort to DPS should increase, not decrease, over time. *Id.* Pitney Bowes asserts that the Commission should retain the use of

the FY 2010 cost difference until the anomalous cost is evaluated.

The Commission appreciates Pitney Bowes' concerns. On March 2, 2012, with its response to Question 2 of Chairman's Information Request No. 1, the Postal Service filed revised Standard Mail letters and First-Class Mail letters mail processing cost avoidance models that included revised DPS percentages. The Commission incorporated these updates in its cost avoidance calculations. For a more complete discussion of these revisions, see the Chapter VII Introduction.

Automation Cards

The Postal Service calculates the following passthroughs of avoided costs for automation cards: Mixed AADC Automation Cards, 131.6 percent, AADC Automation Cards, 109.1 percent and 5-Digit Automation Cards Mixed AADC, 116.7 percent. All of these passthroughs were below 100 percent in FY 2010. However, the cost avoidances have decreased. The Postal Service justifies these discounts by citing the exception granted in 39 U.S.C. 3622(e)(2)(D). *See* revised response to Chairman's Information Request No. 1, question 1. The Postal Service maintains that it is not efficient for the Postal Service to change prices again, just to compensate for the change in cost avoidance with the filing of a new ACR but it does not explain how its operations would be impeded if rates were to be adjusted to restore 100 percent passthroughs. Response to CHIR No. 4, question 1.

In Docket No. R2012-3, the Postal Service proposed, and the Commission approved, discounts for these three presort levels that resulted in passthroughs at or below 100 percent. Due to timing, these discounts were still based on FY 2010 avoided cost estimates. A decrease in avoided costs between FY 2010 and FY 2011 caused the passthroughs for Mixed AADC Automation Cards and 5-Digit Automation Cards to exceed 100 percent.

Section 3622(e) requires that workshare discounts not exceed avoided costs, or that they qualify for at least one of the exceptions in that section. *Therefore, the Commission finds that the discounts for Mixed AADC Automation Cards, AADC Automation Cards, and 5-Digit Automation Cards are not justified by any of the exceptions. In the case of the discount for AADC Automation Cards, the Postal Service's price change in Docket No. R2012-3 realigns the discount with avoided cost, therefore, no further action is required on this issue. With regard to the other two discounts, the appropriate action is for the Postal Service to align the discounts with avoided costs when it files its next general market dominant price adjustment. If, at that time, any of the discounts are subject to one of the exceptions in section 3622(e), the Postal Service may present arguments to that effect.*

Automation Flats

Pitney Bowes asks that the Commission adopt the Outgoing Primary downflow densities in the First-Class Mail flat model as proposed by the Postal Service. Pitney Bowes Comments at 14-15. It also requests that the Commission defer acceptance of the Postal Service's proposal to incorporate FSS processing costs into the model until it is further refined. *Id.*

This issue is under consideration in Docket No. RM2012-2, Proposal Eighteen. Since the rulemaking is still in progress, the Commission continues to employ the accepted method to calculate cost avoidances in this proceeding.

The First-Class Mail Automation Flats passthrough for ADC Automation Flats is 214.3 percent. The Postal Service justifies the passthrough for ADC Automation Flats by citing the exception granted in 39 U.S.C. 3622(e)(2)(B). Revised response to Chairman's Information Request No. 1, question 1. The Postal Service notes that this passthrough has been over 100 percent since Docket No. R2009-2. *Id.* A change in the methodology for estimating the costs of Automation Flats resulted in greater than 100 percent passthroughs[4]. The Postal Service asserts that a large reduction in the discount for ADC Automation Flats to match the cost avoidance would not only impact the price of ADC Automation Flats, but also the prices for 3-Digit and 5-Digit Automation Flats. It asserts that setting this passthrough to 100 percent would cause rate shock, 39 U.S.C. 3622(e)(2)(B).

The Commission finds the Postal Service's reasoning convincing. In Docket No. R2012-3, the Commission found that the discount for ADC Automation Flats was justified even though it resulted in an over 100 percent passthrough. As such, no further action is required.

The First-Class Mail Automation Flats passthrough for 3-Digit Automation Flats is 126.1 percent. In Docket No. R2012-3, the approved rates resulted in a 100 percent passthrough of avoided cost for 3-Digit Automation Flats. However, the avoided cost calculation relied on FY 2010 costs. Using the FY 2011 cost avoidance filed in the FY 2011 ACR, the passthrough exceeds 100 percent. The Postal Service justifies this passthrough by the exception granted in 39 U.S.C. § 3622(e)(2)(D). It states that it is not conducive to efficient postal operations to adjust prices as soon as the cost avoidance changes with the filing of the latest ACR. Response to CHIR No. 4, question 1. The Postal Service makes no claim as to how its operations would be impeded if rates would be adjusted to restore 100 percent passthroughs. As the Commission explained when it rejected use of this exemption in Docket No. R2008-1, the exception applies where there is a reasonable claim on "unusual operational circumstances" that would cause a reduction of the discount to impede the efficient operation of the Postal Service.

Section 3622(e) requires that workshare discounts not exceed avoided costs, or that they qualify for at least one of the exceptions in that section. *The Commission finds that the discount is not justified by any of the exceptions and that the appropriate action is for the Postal Service to align the discount with avoided cost when it files its next general market dominant price adjustment. If, at that time, the discount is subject to one of the exceptions in section 3622(e), the Postal Service may present arguments to that effect.*

Methodology

On behalf of Pitney Bowes, John C. Panzar asserts that discounts that pass through less than 100 percent of the costs avoided prevent efficient providers from entering the market for workshared mail. Comments of John C. Panzar on Behalf of Pitney Bowes Inc. at 1. He asserts that worksharing discounts should be set equal to avoided costs to satisfy both the PAEA mandate and to prevent the exclusion of efficient providers from the market. *Id.* at 2. He presents analysis showing that the Postal Service has an incentive to reduce worksharing discounts during a period of declining volume. *Id.* at 11-13. When a discount is less than avoidable cost, the Postal Service recovers the same per-piece contribution as the full-price piece plus the difference between the

4 *See* Docket No. RM2008-2, Proposal 8.

discount and its avoidable cost. Panzar suggests that such rates are inconsistent with section 3622 (b)(8)—"to establish and maintain a just and reasonable schedule for rates and classifications." *Id.* at 15. Panzer asserts that an "ECP based access pricing *ceiling* (worksharing discount *floor*) should be a part of any modern system for regulating rates." *Id.* at 17 (emphasis in original).

DMA/NAPM/NPPC/PSA (Joint Commenters) agree that discounts less than avoided cost are exclusionary and inefficient. Joint Commenters at 1-2.

The Postal Service disagrees with Panzar's assertions. Postal Service Reply Comments at 2-3. Additionally, it insists that consideration of a change in worksharing rules does not belong in the annual compliance review process. *Id.*

While the Commission appreciates Panzar's analysis, it agrees with the Postal Service that the analysis is beyond the scope of this proceeding. The issue of whether the Commission's rules governing workshare discounts should be modified may be pursued, if appropriate, in a rulemaking proceeding.

Periodicals

Introduction

The Periodicals class includes publications such as magazines, newspapers, journals, and newsletters. Eligibility criteria include a minimum amount of editorial (non-advertising) content.[5] This requirement establishes the Periodicals class as one with educational, cultural, scientific, and informational (ECSI) value. Consequently, the Periodicals Mail class receives several statutory discounts as identified in 39 U.S.C. Section 3626 such as a 5 percent discount for nonprofit and classroom publications.

The Periodicals class is comprised of two products: Within County and Outside County. This division parallels the structure of the class before enactment of the PAEA. The Within County product is typically used by smaller circulation weekly newspapers for distribution within the county of publication. Pricing mainly reflects the number of pieces in a mailing, presort level, and total weight. The Outside County product consists of publications with a wide variety of circulation sizes, distribution patterns, and frequencies. Pricing is based not only on number of pieces and weight, but also on other elements such as bundles, type of container, entry point, machinability, and automation capability.

The profiles of the two Periodicals products differ significantly in terms of volume and revenue. In FY 2011, approximately 662 million copies of Periodicals were mailed at Within County prices, and generated approximately $70 million in revenue for the Postal Service. In contrast, during the same year, 6.42 billion copies of Periodicals were mailed at Outside County prices, and generated approximately $1.75 billion in revenue for the Postal Service. The Postal Service filed several methodological changes to the Periodicals mail processing worksharing cost model prior to filing its FY 2011 ACR. In Docket No. RM2012-2, filed November 30, 2011, the Postal Service proposed major changes to the Periodicals model, including the addition of FSS costs. This Rulemaking docket is still pending.

The principal FY 2011 findings for Periodicals are:

- Within County attributable costs exceeded revenues by $19 million, producing a cost

[5] *See* Domestic Mail Manual: 707.4.0, Basic Eligibility Standards; 707.6.0, Qualification Categories; and 707.4.13, Advertising Standards.

coverage of 78.4 percent.

- Outside County attributable costs exceeded revenues by $590 million, producing a cost coverage of 74.8 percent.
- The Commission agrees with the Postal Service that current rates for Periodicals do not satisfy 39 U.S.C. 3622(c)(2). The Commission recommends that the Postal Service pursue ongoing efforts to reduce the costs of handling flats.
- Ten workshare discounts exceeded avoidable cost, but need not be adjusted since they qualify for the ECSI exception under section 3622(e)(2)(C).
- Worksharing passthrough percentages (especially carrier route) and price-cost ratios for bundle and containers should be moved towards 100 percent to provide incentives for efficient mail preparation.
- Prices were in compliance with the preferred rate requirements identified in Section 3626 of title 39, United States Code.

Financial Analysis

Background

Table VII–4 provides relevant financial data for Within County, Outside County, and the Periodicals class as a whole. It shows volume, revenue, attributable costs, contribution to institutional costs, and cost coverage for each Periodical product in FY 2011.

Table VII–4 shows that Periodicals continue to make a negative contribution to institutional costs and continue to have cost coverage below 100 percent.

Commenters address three broad issues: (1) cost coverage, (2) costs, and (3) the authority of the Commission to find the Periodicals class out of compliance for FY 2011 and order above cap price increases or other remedies. Each of the issues is discussed below followed by the Commission's analysis.

Comments on Cost Coverage

Time states that the FY 2011 cost coverage for Periodicals is a "disappointment." Time Comments at 1. To improve cost coverage, the Postal Service implemented significant operational changes with respect to Periodicals in FY 2011, including the elimination of the "Hot2C" manual processing of Periodicals, establishing earlier Critical Entry Times (CET), and continued the deployment of the Flats Sequencing System (FSS). Time states that "[e]limination of Hot2C processing and earlier CETs have led to an adjustment in the Time production 'closing schedule' and significant operational hurdles and problems for Time." *Id.* at 5. Time hopes that the changes in Periodicals processing implemented

Table VII–4—Periodicals Mail Volume, Revenue, and Cost by Product, FY 2011

Product	Volume	Revenue	Attributable Costs	Contribution	Revenue per Piece	Cost Per Piece	Unit Contribution	Cost Coverage
	(Millions)							
Within County	662	$70	$89	($19)	$0.11	$0.13	($0.03)	78.39%
Outside County	6,415	$1,751	$2,341	($590)	$0.27	$0.36	($0.09)	74.81%
Total	**7,077**	**$1,821**	**$2,430**	**($609)**	**$0.26**	**$0.34**	**($0.09)**	**74.94%**

Source: USPS-FY11-1, FY11PublicCRA.xls

late in FY 2011 will have a positive impact on cost coverage in FY 2012.

Valpak shares Time's hope that the Postal Service will be able to realize significant Periodicals cost savings in FY 2012, but states that Time's comments are "prospective, not retrospective." Valpak Reply at 28. MPA, ANM, and ABM "strongly support the Postal Service's recent (and overdue) initiatives to rationalize its network and operations as warranted by recent and projected declines in mail volume and Postal Service workload. Allowing the Postal Service to cut costs by substantially degrading the quality of service, however, would sabotage the incentives for efficiency created by PAEA." MPA, ANM, and ABM Reply at 9.

The Public Representative states that the Periodicals class "remains significantly underwater and does not satisfy section 3622(c) of title 39." PR Comments at 16. The Public Representative further states "it appears the Periodicals class will not cover its attributable costs anytime soon, if ever." *Id.* at 17. The Public Representative, Time, and Valpak recommend the Postal Service improve worksharing passthroughs in Periodicals to improve the cost coverage.

Valpak states that in FY 2011, the Periodicals Class continued a "15-year run of consistently losing massive amounts of money for the Postal Service." Valpak Comments at 60. Valpak argues that the "Periodicals Study stated categorically that the Postal Service and the Commission are in agreement that price changes will be needed in order for the Periodicals class to cover costs." *Id.* at 71.

Costs

ACMA offered a method of measuring cost increases compared with pricing increases for 5-Digit flat mail. Time stated that "the increases in Periodicals costs are even worse" than the ACMA analysis indicates. Time Reply at 2. MPA, ANM, and ABM state that the ACMA analysis underscores "the urgency of dealing with the real problem: the Postal Service's failure to control its costs." MPA, ANM, and ABM Reply at 10.

MPA, ANM, and ABM and Time are concerned about the impact of FSS deployment on Periodicals costs and service in FY 2011 and future years. Time finds that "in FY 11, the FSS added to Periodicals processing costs." Time Initial at 10. MPA, ANM, and ABM are "increasingly concerned that the Flats Sequencing System ("FSS") — long touted as the savior of flats — will only continue the Postal Service's miserable record in controlling the costs of handling flat-shaped mail. So far, however, FSS has been a failure—driving up both Periodicals costs and customer complaints about service performance." MPA, ANM, and ABM Reply at 11. Valpak states that flat costs have been "resistant to cost-cutting efforts, despite continuing deployment of the FSS." Valpak Comments at 54.

Comments Regarding Commission Authority

Valpak urges the Commission to find that the two Periodicals products violate the factors and objectives of PAEA, as well as 39 U.S.C. 101(d), and use its authority to order "prices be adjusted above the cap" or "that the two Periodicals products as currently fashioned be discontinued and replaced with a discount." Valpak Comments at 80. Valpak burnishes its argument by detailing, by factor and objective, that "most, if not all objectives and factors suggest that Periodicals should receive a higher than CPI rate increase." *Id.* at 72 - 78. Both Valpak and the Public Representative argue that the Commission can order a price increase for loss-making products and alleviate

the need for Postal Service proposals that would decrease service quality, such as the closing of post offices and the elimination of the overnight service standard for First-Class and Periodicals. *Id.* at 79, PR Comments at 11.

Time and MPA, ANM, and ABM argue that the Commission has no authority to impose above-CPI price increases or discontinue the Periodicals class. MPA, ANM, and ABM state that "the CPI-based price cap of section 3622(d) outweighs all of the objectives and factors combined." MPA, ANM, and ABM Reply at 4. MPA, ANM, and ABM also state that the Commission cannot discontinue the Periodicals class because the Commission's remedial authority under section 3622(c) requires a finding of noncompliance, the burden for which has not been met by the FY 2011 prices for Periodicals. MPA, ANM, and ABM further argue that "eliminating the individual product categories within Periodicals mail would not abrogate the price protection given by 39 U.S.C. § 3622(d) to the class." MPA, ANM, and ABM Reply at 8. The Postal Service repeats its statements from Docket No. ACR2010 regarding Commission Authority and "encourages the Commission to determine whether it has the authority under the PAEA to raise rates beyond the price cap." Postal Service Reply Comments at 7.

Commission Analysis

The three issues are somewhat interrelated. Time argues that cost increases have been worse for flats than even the ACMA cost analysis shows and that the Postal Service may not be able to control flat-shaped costs even with the full deployment of the FSS. Time and MPA, ANM, and ABM are concerned that Periodicals costs will continue to rise rapidly, making cost coverage worse.

Valpak's concerns about cost coverage lead it to conclude that the Commission ought to order an above price cap increase or eliminate the Periodicals class and instead establish Periodicals discounts in other classes. Similarly, the Postal Service contends that the Commission should determine if it has the authority to order remedies of the kind that Valpak suggests and if so, then it urges the Commission to take corrective action. Postal Service Reply Comments at 7.

In support of its position, Valpak observes that in past ACDs the Commission has found that there was insufficient evidence that Periodicals' prices were inconsistent with enough factors and objectives to outweigh the price cap limitation. It further states that the vast majority of the factors and objectives of the PAEA encourage the Commission to find that the rates for Periodicals in FY 2011 did not comply with 39 U.S.C. 3622.

Despite the valid concerns raised by the parties, the Commission does not find the rates and fees for the Periodicals class to be out of compliance at this time. The Commission will give the Postal Service time to implement operational changes that may help Periodicals processing become more efficient.

In this regard, the Commission notes that in FY 2011 the Postal Service took substantial steps to address the high costs of processing and delivering Periodicals, following some of the recommendations from the Joint Periodicals Mail Study. In FY 2011 the Commission and the Postal Service released the Joint Periodicals Mail Study, as mandated by section 708 of the PAEA. The principal findings of this report were that Periodicals costs were reasonably accurate for ratemaking purposes but that significant

opportunities for improving processing efficiency and reducing costs exist. While the Commission and the Postal Service disagreed over the precise amount of potential cost savings, the focus on Periodicals brought about by the joint study has lead to several initiatives aimed at improving the Periodicals class cost coverage.

In FY 2011 the Postal Service took the following actions:

- Continued deployment of the FSS
- Eliminated the "Hot2C" manual processing of Periodicals
- Reconfigured and standardized Critical Entry Times
- Completed a Lean Six Sigma project involving bundle breakage
- Continued a "Value Stream Mapping" project to improve Periodicals processing efficiency

Furthermore, in FY 2012 in Docket No N2012-1, the Postal Service has proposed the elimination of the overnight service standard for Periodicals.

The Commission agrees with the Postal Service that the Periodicals class did not meet the section 3622(c)(2) factor which directs the Postal Service to consider the "requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to each class or type of mail service." However, the Commission recognizes that the Postal Service began to implement many operational changes with respect to Periodicals in FY 2011, and has proposed additional significant changes for FY 2012.

The Commission recommends that the Postal Service continue to pursue opportunities identified in FY 2011 to reduce the costs of handling flats. The Commission expects that in the Postal Service's FY 2012 ACR it will identify and report on actions taken to reduce the costs of handling flats, and the impact of those actions on the cost of handling flats and the service received by Periodicals.

Because the Commission has not made a finding of noncompliance in this docket, the Commission does not need to comment on the appropriateness of Valpak's suggested remedies. The Commission will review the suitability of the PAEA modern rate regulations and classes in FY 2016 pursuant to section 3622(d)(3).

Worksharing Discounts

No Within County passthroughs exceeded 100 percent (See Table VII–5). Eleven Outside County passthroughs, identified in Table VII–6, exceeded 100 percent.

Discounts that exceed avoided costs are permissible if a statutory exception applies. *See* 39 U.S.C. 3622(e). The Postal Service justifies the Periodicals discounts that exceeded 100 percent on the basis of section 3622(e)(2)(C), which authorizes workshare discounts greater than avoided cost if provided in connection with a subclass that consists exclusively of mail matter with ECSI value. USPS-ACR2011 at 58.

Comments on Worksharing Discounts

The Public Representative is concerned by the "alarming change" in some Periodicals cost avoidances in FY 2011. The Public Representative points to several Periodicals cost avoidances that decreased over 500 percent in FY 2011 (causing the worksharing passthroughs to increase by over 500 percent). The Public Representative states "the magnitude of the shift in incentives for non-machinable Periodical mailers facing workshare discounts is

Table VII–5—Within County Passthroughs FY 2011

Type of Worksharing	Discount	Avoided Costs	Passthrough
Pre-sorting	(cents per piece)		
3-Digit Presort	1.2	3.2	37.5%
5-Digit Presort	1.3	11.5	11.3%
CR Basic	4.6	15.7	29.3%
High Density	1.6	2.5	64.0%
Saturation	1.4	3.2	43.8%
3-Digit Automation Letter	1.0	1.1	90.9%
5-Digit Automation Letter	0.2	1.9	10.5%
Pre-barcoding			
Basic Automation Flats	1.6	3.2	49.9%
3-Digit Automation Flats	1.2	4.2	28.8%
5-Digit Automation Flats	0.6	1.1	54.3%
Dropshipping			
DDU Dropship	0.8	2.9	27.6%

Source: ACRFY2011-PRC-LR4

disconcerting and largely goes unmentioned by the Postal Service." PR Comments at 23.

Time states that the deployment of the FSS and the cost modeling techniques proposed by the Postal Service "distorts" the true cost differential between 5-Digit and Carrier Route mail. Time Comments at 10. Time is also concerned that the size of the CRA adjustment factor suggests that the Periodicals cost model is not capturing the true cost of piece sorting. Time calculates that the Periodicals worksharing cost model estimates $297 million in piece handling costs in FY 2011, and the CRA attributes nearly $534 million to piece handling activities. The Postal Service states "the Piece Handling cost pool also contains activities other than piece handling."[6]

Table VII–6—Outside County Periodicals Workshare Discounts Exceeding Avoidable Cost in FY 2011

Type of Worksharing	Discount	Avoidable Costs	Passthrough
Pre-sorting	(cents per piece)		
Machinable Nonautomation 5D Flats	9.8	9.0	108.9%
High Density	2.9	2.5	116.0%
Machinable Automation 5D Flats	8.6	8.1	106.2%
Nonmachinable Nonauto ADC Flats	11.6	10.8	107.4%
Nonmachinable Nonauto 3D/SCF Flats	7.5	0.8	937.5%
Nonmachinable Automation 3D/SCF Flats	6.1	0.9	677.8%
ADC Automation Letter	4.0	1.6	250.0%
3-Digit Automation Letter	2.0	0.3	666.7%
5-Digit Automation Letter	6.1	1.9	321.1%
Pre-barcoding			
Machinable Automation MADC Flats	3.2	2.7	118.5%
Nonmachinable Automation MADC Flats	4.5	0.6	750.0%

Source: ACR FY2011-PRC-LR4

Commission Analysis.

The Periodicals class qualifies for ECSI consideration; therefore, the Commission finds that the Outside County discounts that exceed avoidable costs are consistent with section 3622(e)(2)(C). Nine categories that had passthroughs greater than 100 percent in Docket No. R2009-2 also have passthroughs greater than 100 percent using the prices recently approved in Docket No. R2012-3.[7] *See* R2012-3, PRC-LR2.

[6] Docket No. RM2012-2 Reply Comments of the Postal Service Regarding Proposal Eighteen at 7.

[7] Tables displaying the full range of discounts, avoidable costs, and passthoughs for Within County and Outside County Periodicals, as well as prices, bottom-up costs, and price-cost ratios for bundles, sacks, and pallets, appear at the end of this section.

The Commission is currently reviewing the Periodicals mail processing cost model for updates regarding FSS cost, outgoing primary downflows, and pallet bundle breakage. The Commission order in Docket No. RM2012-2 will further analyze Periodicals worksharing passthroughs.

With regard to carrier route passthroughs, Table VII–7 first shows that the Postal Service's pricing decisions have led to an increase in the passthrough for 5-Digit Automation pieces and a decrease in the passthrough for Basic Carrier Route pieces since FY 2008.

The 9.8 cent differential between 5-Digit and Carrier Route has remained unchanged since FY 2008. The Joint Periodicals Mail Study found that Carrier Route presorted pieces were among "the rate elements that provide the most contribution per piece."[8] The passthroughs between Periodicals rate elements provide the Postal Service with pricing flexibility in the Periodicals class. Encouraging Carrier Route mail is one of the only options the Postal Service has to incentivize more profitable mail in Periodicals. The Postal Service has stated "the design is to help ensure efficient mail preparation consistent with the advent of the Flats Sequencing System (FSS) environment …expanding this discount would tend to encourage customers to undertake work that may not be necessary in an FSS-environment."[9] However, available cost data do not indicate that ongoing deployment of the FSS is eroding the value of Carrier Route presorting.

The Postal Service has stated "it has no plans to adjust its Periodicals price schedules to differentiate between FSS and non-FSS zones."[10] FSS zone

Table VII-7—Carrier Route and 5-Digit Automation Passthroughs Over Time

	Passthroughs			
	2008	2009	2010	2011
CR Basic	88.15%	71.52%	71.05%	69.48%
5-Digit Automation	61.37%	96.63%	102.38%	106.17%

Sources: Docket Nos. ACR2007 – ACR2011, PRC-LR4

pricing would allow the Postal Service to efficiently incentivize Carrier Route mail where the FSS is not available, and prevent inefficient presorting of the mail where the FSS is available. The FSS requires very different mail preparation characteristics to maximize its operational potential, and the Postal Service should fully explore pricing avenues to this end. In a price cap environment, pricing efficiently in order to maximize net revenues gains importance. *The Commission recommends the Postal Service improve the efficiency of Periodicals pricing options and worksharing passthroughs to incent more efficient mailer preparation.*

Price-Cost Ratios for Bundles and Containers

Discrete pricing for Outside County bundles, sacks and pallets was introduced in Docket No. R2006-1. The prices, bottom-up costs, and ratios of price to bottom-up cost for each combination of item, presort level, and entry level, are shown in the tables at the end of this section. These price-cost ratios can be thought of similarly to worksharing discounts, in the sense that they reflect many incentives for cost-reducing mail preparation behavior, but unlike worksharing discounts they do not explicitly reflect the relation of discounts to the costs avoided by greater mailer preparation. Price-cost ratios are used to describe how much of a cost is recognized in a given

8 Periodicals Mails Study at 26.
9 Docket No. ACR2010 Postal Service Reply Comments at 39.
10 Docket No. RM2012-2 Reply Comments of the Postal Service Regarding Proposal Eighteen at 6.

price element. The price-cost ratios for bundles, sacks, and pallets are significantly below 100 percent. Price-cost ratios range from a low of 15.2 percent for a mixed ADC sack entered at the Origin Sectional Center Facility (OSCF), to a high of 51.4 percent for a 3-Digit pallet entered at the Origin Network Distribution Center (ONDC).

Comments

The Public Representative states that the Postal Service should improve the efficiency of Periodicals prices, specifically the pricing of sacks, pallets and bundles, because pricing efficiency improvements provide the greatest opportunity the Postal Service has at its disposal to improve Periodicals cost coverage without piercing the price cap. PR Comments at 25.

Commission Analysis

In the most recent Market Dominant Price Adjustment, Docket No. R2012-3, the Postal Service used its pricing flexibility to increase the prices of pallets, on average, by 5.7 percent. However, the Postal Service only increased sacks, on average, by 2.6 percent. This means that the gap between sack price-cost ratios and pallet price-cost ratios will grow in FY 2012. The Postal Service stated this will help "further the goal of more efficient containerization, while being mindful of the impact on those publications that cannot easily change preparation. To encourage efficient preparation of containerize mail, the Postal Service recently added a Mixed ADC Pallet option for mailers in Docket No. R2012-3. The Commission commends the Postal Service for providing mailers the opportunity to improve the efficiency of mail preparation.

Table VII–8—Outside County Passthroughs FY 2011

Type of Worksharing	Discount	Avoided Costs	Passthrough
Pre-sorting	(cents per piece)		
Machinable Nonautomation ADC Flats	3.5	3.9	89.7%
Machinable Nonautomation 3D/SCF Flats	1.7	4.5	37.8%
Machinable Nonautomation 5D Flats	9.8	9.0	108.9%
CR Basic	10.7	15.4	69.5%
High Density	2.9	2.5	116.0%
Saturation	1.9	3.2	59.4%
Machinable Automation ADC Flats	2.6	3.3	78.8%
Machinable Automation 3D/SCF Flats	1.5	4.3	34.9%
Machinable Automation 5D Flats	8.6	8.1	106.2%
Nonmachinable Nonauto ADC Flats	11.6	10.8	107.4%
Nonmachinable Nonauto 3D/SCF Flats	7.5	0.8	937.5%
Nonmachinable Nonauto 5D Flats	11.8	15	78.7%
Nonmachinable Automation ADC Flats	9.6	10.9	88.1%
Nonmachinable Automation 3D/SCF Flats	6.1	0.9	677.8%
Nonmachinable Automation 5D Flats	10.8	14.4	75.0%
ADC Automation Letter	4.0	1.6	250.0%
3-Digit Automation Letter	2.0	0.3	666.7%
5-Digit Automation Letter	6.1	1.9	321.1%
Pre-barcoding			
Machinable Automation MADC Flats	3.2	2.7	118.5%
Nonmachinable Automation MADC Flats	4.5	0.6	750.0%

Source: ACRFY2011-PRC- LR4.

Table VII–9—Outside County Bundle Price/Cost Ratios, FY 2011

Container Level	Bundle Level	Price	Cost	Price as Percent of Cost
		(cents per piece)		%
Mixed ADC	MADC	7.8	20.5	38.1%
	ADC	20.4	54.5	37.4%
	3-D/SCF	27.1	71	38.2%
	5-D	28.0	77.5	36.1%
	Firm Bundle	18.2	102	17.8%
ADC	ADC	11.3	31.6	35.7%
	3-D/SCF	18.6	50.3	37.0%
	5-D	20.2	57.9	34.9%
	CR	31.9	88.7	36.0%
	Firm Bundle	15.1	87.1	17.3%
3-D/SCF	3-D/SCF	12.7	31.5	40.4%
	5-D	14.7	38.8	37.9%
	CR	28.3	63.8	44.3%
	Firm Bundle	13.9	63.8	21.8%
5-D/CR	5-D	14.2	36.1	39.3%
	CR	14.9	33.4	44.6%
	Firm Bundle	7.8	34.5	22.6%

Source: ACRFY2011-PRC-LR4.

Table VII–10—Outside County Sack Price/Cost Ratios, FY 2011

Sack Level	Entry Point	Price	Cost	Price as Percent of Cost
		($ per piece)		%
Mixed ADC	OSCF	$0.43	$2.81	15.2%
	OADC	$0.43	$2.34	18.2%
ADC	OSCF	$2.04	$6.67	30.6%
	OADC	$2.04	$6.50	31.4%
	OBMC	$2.04	$5.74	35.5%
	DBMC	$1.42	$4.28	33.2%
	DADC	$0.81	$2.34	34.8%
3-D/SCF	OSCF	$2.13	$7.15	29.8%
	OADC	$2.13	$6.82	31.2%
	OBMC	$2.13	$5.96	35.7%
	DBMC	$1.52	$4.40	34.6%
	DADC	$1.22	$3.67	33.2%
	DSCF	$0.81	$2.34	34.6%
5-D/CR	OSCF	$2.74	$9.34	29.3%
	OADC	$2.74	$8.63	31.7%
	OBMC	$2.74	$7.82	35.0%
	DBMC	$2.03	$6.31	32.1%
	DADC	$1.73	$5.46	31.6%
	DSCF	$1.32	$4.22	31.2%
	DDU	$0.91	$2.96	30.8%

Source: ACRFY2011-PRC-LR4.

Further, in the Periodicals Mail Study, several of the pricing recommendations involved using pricing signals to improve the net revenue from containers and bundles. These included the following:

- Increase Unit and Container Density
- Lower Transportation Costs
- Align Prices with Processing
- Optimize Bundle Preparation

These goals can only be achieved by improving the price-cost ratios of bundles and containers. While the Commission is mindful of the impact of prices on mailers, progress with respect to improving pricing efficiency is necessary to maximize the realization of operational improvements into cost reductions.

The Commission recommends that the Postal Service improve the efficiency of the bundle and container pricing in Periodicals.

Standard Mail

Introduction

Standard Mail is a market-dominant class that consists of six products: Letters; Flats; Not-Flat Machinables (NFMs)/Parcels; Carrier Route; High Density and Saturation Letters; and High Density and Saturation Flats/Parcels. In FY 2011 Standard Mail volume was 84.7 billion pieces, an increase of 2.2 billion pieces from the 82.5 billion pieces in FY 2010. Standard Mail accounted for 50.4 percent of total mail volume, and 23.3 percent of total contribution to institutional costs. Now that Standard Mail volume, has grown to more than 50 percent of total mail volume the Postal Service must find ways to increase Standard Mail's contribution to institutional costs as part of an improved business model.

The principal FY 2011 findings for Standard Mail are:

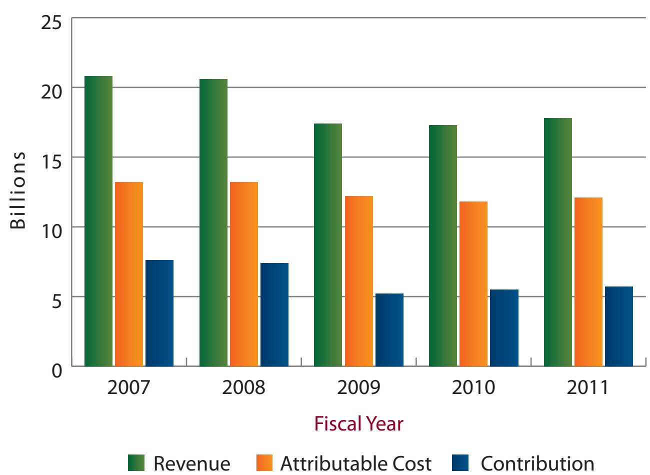
- Standard Mail contributed $5.7 billion to institutional costs.
- Standard Mail Flats had a 79.5 percent cost coverage, resulting in a $643 million loss.
- The rates and fees for Standard Mail Flats remain out of compliance.
- Standard Mail NFMs and Parcels had an 85.4 percent cost coverage, 7.5 percentage points higher than FY 2010, but resulting in a $112 million loss.
- Fifteen workshare discounts exceeded avoided costs.
    - » Four discounts were properly justified under section 3622(e).
    - » Ten discounts were not properly justified under section 3622(e).
    - » The Commission was unable to evaluate whether one discount was consistent with the statute.

Financial Analysis

In FY 2011 the total revenue for Standard Mail was $17.8 billion, which covered its attributable costs of $12.1 billion, and resulted in a 147.6 percent cost coverage (see Table VII–11). Standard Mail contributed $5.7 billion to institutional costs, a 4.3 percent increase from FY 2010.

The overall cost coverage for Standard Mail increased slightly to 147.6 percent from 146.6 percent in FY 2010. Standard Mail volume increased 2.6 percent, or slightly over two billion pieces. Unit revenue and unit cost both increased less than one cent from FY 2010. Increased volume, and minimal changes to unit revenues and unit costs resulted in Standard Mail contributing $236 million more to institutional costs compared to FY 2010. Figure VII–1 demonstrates the increased contribution provided by Standard Mail in FY 2011.

Figure VII–1—Standard Mail Trends



Source: 2007 ACD at 87, 2008 ACD at 59, 2010 ACD at 102, and Table VII–11.

Table VII–11—FY 2011
Volume, Revenue, Cost, Contribution, and Cost Coverage by Product

Standard Mail	Volume (000)	Revenue ($ 000)	Attributable Costs ($ 000)	Contribution to Institutional Costs ($ 000)	Rev./Pc. (Cents)	Cost/Pc. (Cents)	Contribution to Institutional Costs/Pc. (Cents)	Cost Coverage
High Density and Saturation Letters	5,653,875	772,149	349,010	423,139	13.66	6.17	7.48	221.2%
High Density and Saturation Flats and Parcels	11,424,568	1,885,335	882,761	1,002,574	16.50	7.73	8.78	213.6%
Carrier Route	9,367,761	2,235,782	1,647,828	587,954	23.87	17.59	6.28	135.7%
Letters	50,719,613	9,777,603	5,288,553	4,489,049	19.28	10.43	8.85	184.9%
Flats	6,791,672	2,499,669	3,142,862	(643,193)	36.80	46.28	(9.47)	79.5%
Not Flat-Machinables and Parcels	733,770	655,613	767,298	(111,685)	89.35	104.57	(15.22)	85.4%
Inbound Int'l. Negotiated Serv. Agreement Mail1	712	316	87	229	44.40	12.23	32.18	363.2%
Total Standard Mail	**84,691,971**	**17,826,466**	**12,078,399**	**5,748,068**	**21.05**	**14.26**	**6.79**	**147.6%**

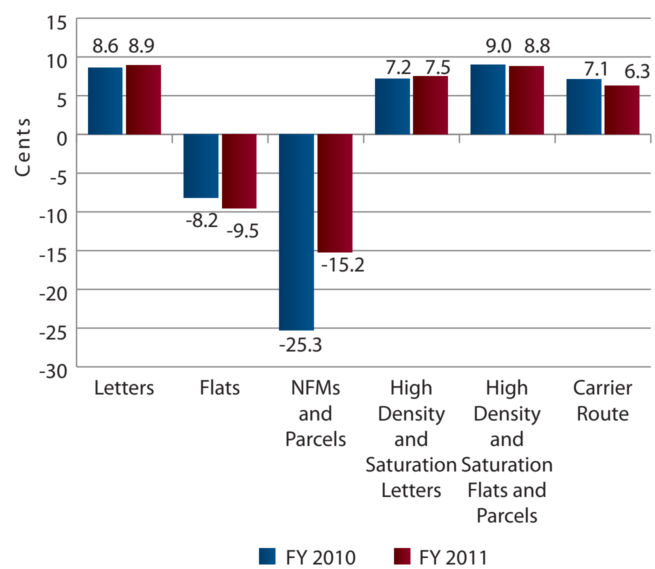
Source: PRC-ACR2011-LR1

Standard Mail as a class contributed $5.7 billion to institutional costs, but not every product within the class contributed. Figure VII–2 shows the unit contribution of each Standard Mail product for FY 2010 and FY 2011. Figure VII–2 also demonstrates the increased unit contribution from Letters, NFMs and Parcels, High Density and Saturation Letters compared to FY 2010 and the reduced contribution of the remaining products.

Standard Mail Letters

Standard Mail Letters had a cost coverage of 184.9 percent, and contributed $4.5 billion to institutional costs. This was a $322 million increase in contribution compared to FY 2010. On a unit basis, the Letters product contributed 8.9 cents to the institutional costs of the Postal Service, a 3.0 percent increase from FY 2010. Letter revenue per piece

Figure VII–2—Unit Contribution by Standard Mail Product FY2010 and FY 2011



Source: 2010 ACD at 102, and Table VII–11.

increased by 0.6 percent, while attributable cost per piece decreased by 1.4 percent. Letter volume increased by 4.6 percent, or 2.2 billion pieces, compared with FY 2010.

Standard Mail Flats

Standard Mail Flats cost coverage was 79.5 percent in FY 2011, which was a decrease from its 81.8 percent cost coverage in FY 2010. The Flats cost coverage has decreased each fiscal year since the passage of the Postal Accountability and Enhancement Act (PAEA), as shown in Table-VII-12.

Similar to FY 2010, neither the commercial nor the nonprofit portions of the Standard Mail Flats product had a cost coverage above 100 percent, as shown in Figure-VII–3.

In the 2010 Annual Compliance Determination (ACD) the Commission found that the prices in effect in FY 2010 did not comply with section 101(d) of title 39. Pursuant to 3653(c), the Commission directed the Postal Service to increase the cost coverage of the Standard Mail Flats product through a combination of cost reductions and above-average price adjustments, consistent with the price cap requirements, until such time that revenues exceed attributable costs. As is shown in Figure-VII–4, unit revenues for Standard Mail Flats increased by 0.1 cents in FY 2011, while unit attributable costs increased by 1.4 cents, resulting in contribution per piece decreasing by 1.3 cents.

Table VII–12—FY 2011

	2008	2009	2010	2011
Standard Flats	94.4%	82.3%	81.8%	79.5%

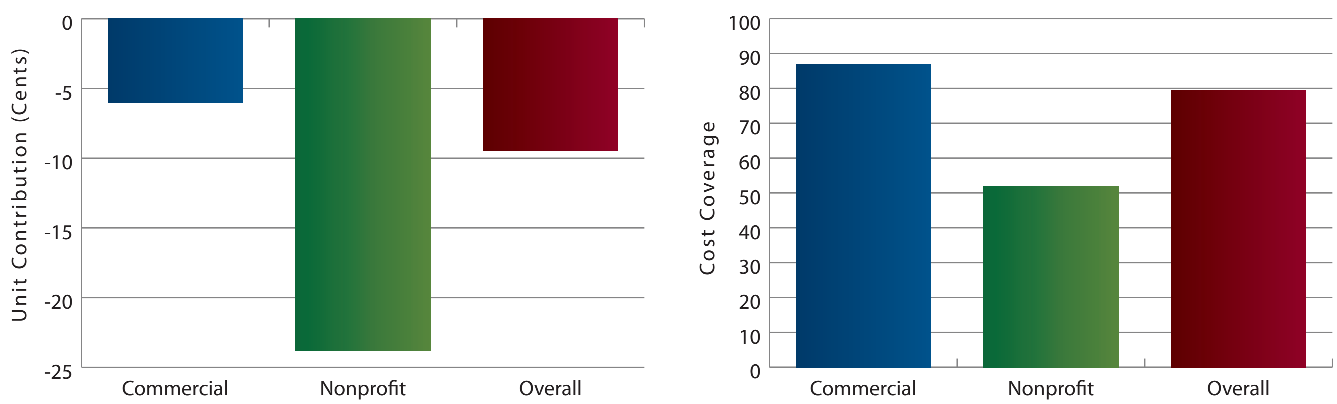
Source: PRC-ACR2011-LR3

As Figure-VII–5 demonstrates, Letters contributed 18.4 cents more per piece than Flats in FY 2011. Standard Carrier Route pieces contributed 15.8 cents more per piece than the Flats product.

In the FY 2010 ACD the Commission also required that the Postal Service file the following information regarding Standard Mail Flats:

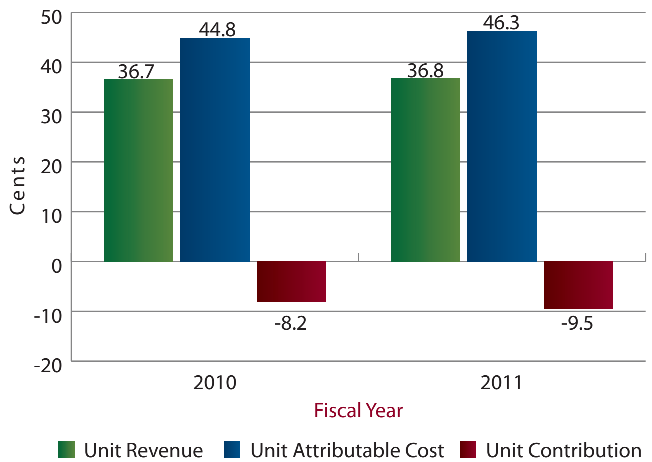
- A description of all operational changes designed to reduce flat costs in the previous fiscal year and an estimate of the financial impact of such changes;
- A description of all costing methodology or measurement improvements made in the previous fiscal year and an estimate of the financial effects of such changes;

Figure VII–3—Contribution and Cost Coverage for Standard Mail Flats



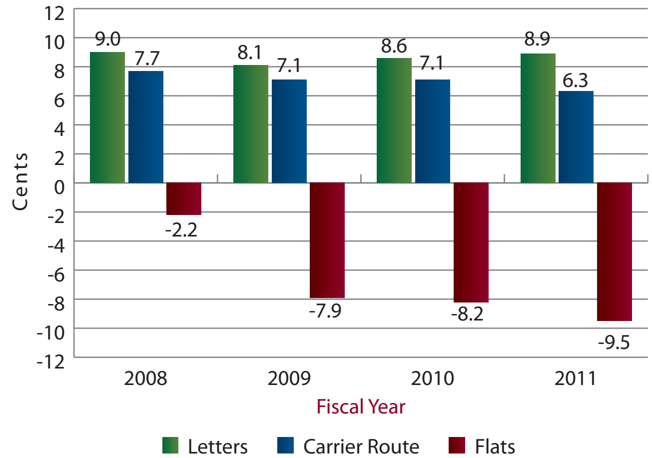
Source: PRC-ACR2011-LR3

Figure VII–4—Standard Mail Flats FY 2010 vs. FY 2011



Source: 2010 ACD at 102, and Table VII–11.

Figure VII–5—Unit Contribution for Standard Mail Letters, Flats and Carrier Route



Source: PRC-ACR2011-LR3

- A statement summarizing the historical and current fiscal year subsidy of the Flats product; and, the estimated timeline for phasing out the subsidy. 2010 ACD at 107.

The Postal Service appealed the Commission's FY 2010 ACD findings and directive. The matter is currently awaiting judicial decision in the Court of Appeals. 2011 ACR at 28-29. In the Postal Service's 2011 Annual Compliance Report it noted the status of the appeal and did not provide the information required by the FY 2010 ACD. *Id.* at 28.

In its response to the Chairman's Information Request asking for information in compliance with the FY 2010 ACD, the Postal Service explains that the number of operational FSS machines has increased from 13 machines at 8 sites to 100 machines at 47 sites. Response to CHIR No. 1, question 9. These 100 machines now serve 43,534 delivery routes. *Id.* In addition to FSS deployment, the Postal Service explains that it modified mail preparation requirements in FY 2011 to allow mailers the option to prepare FSS-schemed bundles and two levels of pure FSS pallets, and introduced the FSS label lists. *Id.* The Postal Service believes "these efforts are expected to improve efficiencies and productivities, and reduce overall flats costs." *Id.*

The Postal Service also identifies Proposal Eighteen in Docket No. RM2012-2 as a cost measurement improvement related to Standard Mail Flats. *Id.* Proposal Eighteen reflects new equipment deployments, specifically the FSS, into the mail processing cost models for Standard Mail Flats, First-Class Mail Flats, and Periodicals.[11] *Id.*

Based on the slightly above average price increase for Standard Mail Flats in Docket No. R2012-3, the Postal Service anticipates that the cost coverage for Standard Mail Flats will increase to 84.0 percent in FY 2012, with an estimated contribution loss of $458 million.

[11] Proposal Eighteen is awaiting final disposition by the Commission in Docket No. RM2012-2.

Comments

The Commission received comments from Valpak, L.L. Bean, Inc. (L.L. Bean), American Catalog Mailer Association (ACMA), and the Public Representative related to the Standard Mail Flats product. The comments cover three distinct areas, (1) cost coverage and compliance, (2) anomalous flats costs, and (3) measurement of the intra-class cross-subsidy. The remainder of this section will discuss each of these areas.

Cost Coverage and Compliance

Valpak notes that four years of CRA cost and revenue data are available for Standard Mail Flats and the total negative contribution from the product is now over $2 billion. Valpak Comments at 53. Valpak also observes that the contribution losses for the Standard Mail Flats product have consistently increased over the past four years, therefore cost cutting strategies have not worked, and the Postal Service should institute above-average price increases for Standard Mail Flats. *Id.* at 54.

Valpak criticizes the Postal Service's failure to comply with the Commission's FY 2010 ACD directives. *Id.* at 60. Valpak suggests that if the appeal of the FY 2010 ACD results in a decision favorable to the Commission that "the Commission should move quickly to direct that a substantial increase be made in Standard Flats rates, moving them toward full coverage plus a reasonable contribution to institutional costs in no more than three years." *Id.* Valpak also reiterates that the Commission should make a determination of noncompliance for Standard Mail Flats. Valpak Reply Comments at 20. Valpak contends that if the Commission does not make an express finding of noncompliance, it would imply a rebuttable presumption of compliance pursuant to 39 U.S.C. 3653(e). *Id.*

L.L. Bean also expresses concerns about the pricing of the below-cost Standard Mail Flats product. L.L. Bean Comments at 1. It questions the Postal Service's price adjustments that have consistently given the Carrier Route product, which makes a positive contribution to institutional costs, higher increases than the Flats product, which does not cover its attributable costs or contribute to institutional costs. *Id.* at 2-3. L.L. Bean agrees with Valpak that the Commission should make a formal finding of noncompliance for the Standard Mail Flats product, to avoid the appearance that the Standard Mail Flats product is in compliance in FY 2011. L.L. Bean Reply Comments at 3.

The Public Representative contends that the recent above average price increase for Standard Mail Flats demonstrates the Postal Service's action towards ending the intra-class cross-subsidy. Public Representative Comments at 18-19. The Public Representative also notes that the Postal Service did not initially file the reports requested by the Commission in the FY 2010 ACD, and requests that the Commission request a plan from the Postal Service to bring Standard Mail Flats into compliance under the price cap constraint. *Id.*

Anomalous Flats Costs

ACMA states that costs for Standard Mail Flats have increased excessively and there is no plausible explanation for the increases. ACMA Comments at 33. ACMA concludes, based on the cost increase, that the costs are not reliable, and suggests that the "costs are out of compliance" [emphasis omitted]. Id at 25. ACMA does not believe that the costs are "an adequate basis for evaluating rates or assessing

compliance." *Id.* In addition ACMA claims that a case cannot be made that the Standard Mail Flats product is being cross-subsidized. *Id.*

In support of its argument that the Postal Service's costs are unreliable, ACMA creates cost indices for Standard Letters, Standard Flats, Standard Carrier Route and Periodicals. ACMA then compares these cost indices to factor prices.[12] Compared to factor prices, ACMA finds, for Standard Mail products, that from FY 1998 to FY 2011 (1) Standard Mail Letters cost index was 17.0 percentage points less than factor prices; and (2) Standard Mail Flats cost index was 61.6 percentage points more than factor prices. *Id.* at 4-8. In addition, ACMA finds that from FY 2008 to FY 2011 the Carrier Route cost index approximately equaled the factor prices. *Id.* at 9.

After reviewing overall cost index changes for the three Standard Mail products and Periodicals, ACMA considers the mail processing and delivery costs for Letters, Flats and Carrier Route.[13]

Valpak, L.L. Bean and the Public Representative respond to ACMA's comments concerning anomalous Postal Service costs. Valpak states that the Commission should reject ACMA's recommendation that the Commission find the CRA level costs out of compliance. Valpak Reply Comments at 9. Valpak contends that ACMA's cost indices only demonstrate the fact that Standard Mail Flat costs have increased faster than other Standard Mail products and Standard Mail Flats price increases have failed to match cost increases. *Id.* at 3-4. L.L. Bean expresses that it, like ACMA, is concerned over the increasing cost trends for the Standard Mail Flats product. L.L. Bean Reply Comments at 1. However, L.L. Bean presumes that the Postal Service has been "diligently investigating these costs and the reliability of its costing systems." *Id.* It notes that ACMA does not show that the anomalous costs overcome the shortfall in the Standard Mail Flats product cost coverage, and therefore concludes that the costs using the current methodology are "the best estimates of the true operational costs of Standard Flats." *Id.*

The Public Representative believes that ACMA has provided an innovative approach in analyzing historic cost trends, but provides several critiques of ACMA's rate and cost indices. Public Representative Reply Comments at 10. He notes a small error in ACMA's measurement of the rate index, and recommends that the proper formula for a continuous rate index be used, which avoids calculating different percentage changes in rates depending on different base years. *Id.* Then he explains that additional data are needed to calculate cost indices that are not included in ACMA's analysis. *Id.* at 11. For example, the Public Representative believes the Postal Service needs to identify cost centers and associated volumes by product along with the relevant per-unit attributable cost for each of the Postal Service's process steps. *Id.* In light of the additional data needed, the Public Representative suggests that Commission, together with the Postal Service, determine the feasibility of acquiring the necessary data and potentially developing a cost index. *Id.* at 12.

12 ACMA uses the measurement of total factor productivity (TFP) as its index of factor prices.

13 ACMA finds that (1) The unit mail processing costs for 5-Digit automation letters has increased 18.9 percent, while 5-Digit automation flats unit mail processing costs have increased 130.0 percent, and the unit mail processing costs for Carrier Route have increased 84.5 percent and (2) the unit delivery costs for 5-Digit automation letters has increased 22.1 percent, while the unit delivery costs for 5-Digit automation flats has increased 155.0 percent, and the unit delivery costs for Carrier Route have increased 76.4 percent. *Id.* at 16-19.

Measurement of Intra-Class Cross-Subsidy

ACMA argues that cross-subsidy testing must evaluate all possible combinations of products before concluding that the Standard Mail Flats product is cross-subsidized. *Id.* at 31. ACMA states that cross-subsidy testing, in addition to an incremental cost test, must also include a burden test which analyzes the effects of withdrawing products that are complements or substitutes for one another.[14] *Id.* ACMA finds that applying the burden test to the trio of Standard Mail Flats, commercial Carrier Route Flats, and commercial High-Density Flats demonstrates that "volume losses would occur for other products, resulting in significant contribution losses." *Id.* at 32. ACMA concludes that "no finding of cross-subsidy can be supported" for the trio of Standard Mail Flats, commercial Carrier Route Flats, and commercial High-Density Flats and that Standard Mail Flats are a "key component in the array of products offered." *Id.*

Valpak contends that incremental costs are higher than attributable costs, because incremental costs include other non-attributable costs that would be avoided if the product ceased to be offered. Valpak Reply Comments at 14. Valpak also disagrees with ACMA's assertion that the Standard Mail Flats are fair and equitable because the duo of Standard Mail Flats and Carrier Route cover costs.

L.L. Bean argues the fact that the Standard Mail Flats product has below-cost rates results in other Standard Mail products being charged higher rates than are warranted. L.L. Bean Reply Comments at 2. L.L. Bean concludes that this constitutes an unfair cross-subsidy. *Id.*

The Public Representative does not agree with ACMA, and believes product cost coverage should continue to be used to evaluate potential cross-subsidization. Public Representative Reply Comments at 7. He states that "[i]f the revenue from a product does not recover its marginal costs, it is very likely being subsidized." *Id.* at 9. He concludes that "the Commission is right to recommend remediation when the cost coverage of a product falls below 100 percent." *Id.*

Commission Analysis

Fiscal Year 2011 is the fourth consecutive year Standard Mail Flats revenue and cost data have been available, and this is the fourth year that the product has had substantial losses. As Table VII–13 shows, cumulatively, over the past four years the Standard Mail Flats product has lost over $2 billion. In the FY 2010 ACD, when the cumulative loss was $1.4 billion, the Commission found the Standard Mail Flat product out of compliance with section 101(d) of title 39. 2010 ACD at 106. This was after the Commission had encouraged the Postal Service to improve the cost coverage in the FY 2008 ACD and the FY 2009 ACD.

The unit contribution for the Standard Mail Flats product has now decreased to negative 9.5 cents per piece. Since FY 2008, the unit contribution has decreased by a total of 7.3 cents. The Postal Service responds that all pricing decision are made by the Board of Governors based on statutory and regulatory requirements as well as an evaluation of market dynamics and business strategy considerations. Response to CHIR No. 1, question

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[14] ACMA explains that the burden test first focuses on the financial effect of withdrawing Commercial Standard Flats, Commercial Carrier Route Flats, and Commercial High-Density Flats. *Id.* The next step in the burden test is to estimate the net financial effect of all further volume responses to the withdrawal of Commercial Standard Flats, Commercial Carrier Route Flats, and Commercial High-Density Flats. *Id.*

Table VII–13—Contribution of Standard Mail Flats FY 2008-FY 2011 (S in Millions)

FY	Contribution
2008	$(217.83)
2009	$(615.57)
2010	$(576.99)
2011	$(643.19)
Total	**$(2,053.59)**

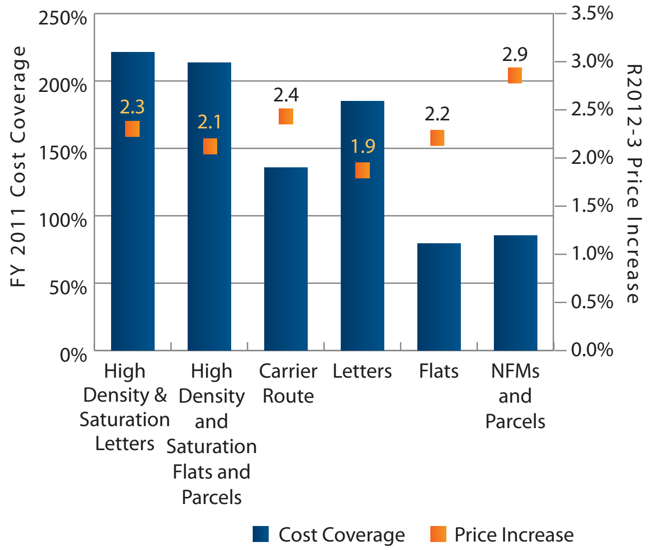
Source: 2008 ACD at 59, 2009 ACD at 84, 2010 ACD at 102, and Table VII–11.

9(c). The Postal Service explains that pricing decisions can only be made in the context of the circumstances that exist at the time a price change is approved. *Id.* In Docket No. R2012-3 the Postal Service gave Standard Mail Flats a 2.2 percent increase, slightly above the 2.1 percent price cap. Figure VII–6 shows the cost coverage and price increase for each Standard Mail product in Docket No. R2012-3.

ACMA contends that a burden test[15] should be conducted in addition to measuring cost coverage to determine if there is an intra-class cross-subsidy within Standard Mail. The Commission appreciates ACMA's contention, but observes that, as noted by Valpak, L.L. Bean and the Public Representative, measuring cost coverage is a reasonable way to test for intra-class cross-subsidies.

The Postal Service estimates that the increase for Standard Mail Flats will reduce the Standard Mail Flats shortfall to $458 million in FY 2012, with an 84.0 percent cost coverage. *See* Response to CHIR No. 1 Question 9(d)-(e). As the Commission expressed in the FY 2010 ACD, price increases in conjunction with cost reductions are necessary

Figure VII–6—FY 2011 Cost Coverage and R2012-3 Price Increase by Product



Source: Table VII–11 and PRC-R2012-3-LR3.

to improve the cost coverage of the Standard Mail Flats product. The Postal Service did not, however, provide any cost savings estimates, despite requests for estimates. *See* 2010 ACD at 107; *See also* CHIR No. 1, question 9.

In the FY 2010 ACD, the Commission highlighted the revenue shortfalls in Standard Mail Flats, and found that the Standard Mail Flats product was not in compliance with title 39. Standard Mail Flats has now continued on its downward trend, and losses now total $2 billion over the past four years. The Commission finds that Standard Mail prices continue to reflect an unfair an inequitable apportionment of the costs of postal operations to all Standard Mail users. While the Postal Service did give the Standard Mail Flats product a slightly above average price increase in the Docket No. R2012-3, the Postal Service calculates that the increase is not projected to significantly move the Standard Mail Flats product

[15] The mechanics of the burden test are described in section 1.c of this chapter, "Measurement of Intra-Class Cross-Subsidy."

toward cost coverage in FY 2012. *See* Response to CHIR No. 1 Question 9(e). The Postal Service has also not filed a plan with the Commission outlining when intra-class cross-subsidy would be eliminated. Because the intra-class cross-subsidy discussed in the FY 2010 ACD has worsened, the Commission finds that the prices in effect in FY 2011 for Standard Mail Flats remain out of compliance. However, given the pending litigation the Commission will not require remedial action at this time.

Several commenters have discussed potential anomalies in Standard Mail Flats unit attributable costs. Cost anomalies may indeed mean that costing for Standard Flats could be improved. However, the fact that some costs rise faster than others is not per se an indicator that cost estimates are incorrect or anomalous. CRA level costs are reasonably accurate for evaluating product costs and related prices.[16] Persuasive evidence is required to discard and replace a litigated costing framework that has been developed and refined over 40 years. Parties alleging that the CRA costing methodology is not reliable must demonstrate flaws underlying the costing methodology or data collection in order to merit consideration. The anecdotal evidence of possible costing anomalies appearing in the results of the CRA cost models for specific types of costs, as presented in this docket, is not sufficient.

It may be possible to improve the costing approach for Standard Mail Flats within the CRA framework to rectify possible anomalies. The Commission welcomes petitions from interested parties that not only investigate anomalies in the methodologies underlying the current cost models, but also present solutions. For example, a party could present an alternate methodology for distributing costs. The Commission encourages interested parties to continue to attempt to identify specific anomalies in conjunction with proposed solutions to correct methodologies that produce anomalous costs.

Standard Mail NFMs and Parcels

The NFMs and Parcels product did not produce sufficient revenues to cover its attributable costs in FY 2011. The NFMs and Parcels product had an 85.4 percent cost coverage and had a net loss of $111.7 million. This is a $60.8 million improvement over the FY 2010 loss of $172.5 million. Unit contribution increased from negative 25.3 cents in FY 2010 to negative 15.2 cents in FY 2011.[17] Unit attributable costs decreased 8.5 percent, and unit revenues slightly increased, 0.3 percent.

During FY 2011 the Commission approved the Postal Service's proposal to transfer a portion of the NFMs and Parcels product to the competitive product list. *See* Order No. 689. This transfer was not completed until January 22, 2012 when the Postal Service gave the transferred pieces a sufficient price increase to satisfy the requirements of section 3633 of title 39. In Docket No. R2012-3, the Postal Service proposed and the Commission approved an above-average price increase of 2.864 percent for the portion of the NFMs and Parcels product that remained part of the market dominant product. This was the fourth consecutive above-average price increase for the NFMs and Parcels product.

In FY 2011, the revenue generated from NFMs and Parcels was not sufficient to recover the attributable

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[16] *See* Periodicals Mail Study, Joint Report of the United States Postal Service and Postal Regulatory Commission, September 2011 at 57-60 (finding that CRA-developed costs are reasonably accurate for rate-setting purposes).

[17] In this case, the unit contribution is negative, which represents a loss.

cost of the product or make a contribution to institutional costs. In light of the restructuring of the NFMs and Parcels product and the Postal Service's efforts to resolve the intra-class cross-subsidy, the Commission finds that the Postal Service's approach to ending the intra-class cross-subsidy is appropriate and it should continue using its pricing flexibility to give the NFMs and Parcels product above-average price increases. The Commission also encourages the Postal Service to continue reducing Parcels and NFMs costs, as it did in FY 2011.

High Density and Saturation Letters

In FY 2011, the High Density and Saturation Letters product had a cost coverage of 221.2 percent, and contributed 7.5 cents per piece to institutional costs. The product contributed a total of $423.1 million to institutional costs, with commercial pieces contributing $414.6 million and nonprofit pieces contributing $8.6 million.

Valpak argues that no product should produce revenues that are greater than twice their attributable costs. Valpak Comments at 38. Valpak requests that the Commission "roll back the most recent price increases." *Id.* In light of some products with cost coverages below 100 percent, Valpak suggests that price increases on products with high elasticities and cost coverages over 200 percent be suspended until those products' cost coverages are no longer above 200 percent. *Id.*

High Density and Saturation Letters received an above average price increase in the Docket No. R2012-3 price adjustment, but that fact alone does not warrant Commission action. In general, the Postal Service is accorded pricing flexibility under title 39 to allow these kinds of pricing decisions.

High Density and Saturation Flats and Parcels

Revenues for the High Density and Saturation Flats/Parcels product exceeded its attributable costs, which resulted in cost coverage of 213.6 percent in FY 2011. The product as a whole contributed $1.0 billion to the institutional cost of the Postal Service. Table VII–14 shows the volume and contribution distribution of High Density and Saturation Flats and High Density and Saturation Parcels.

This table shows that flats comprise more than 99 percent of the product contributing slightly more than $1.0 billion. This represents the second highest contribution in Standard Mail with Letters ranking first. In contrast, the parcel portion shows a loss of $234,330.

In Docket No. R2012-3, the Postal Service proposed and the Commission approved a slightly above average price increases for High Density and Saturation Parcels. *See* PRC-R2012-3-LR3.

Carrier Route

In FY 2011, revenues from the Standard Mail Carrier Route Product (which includes letters, flats, and parcels) exceeded the product's attributable costs with a cost coverage of 135.7 percent. The Carrier Route product contributed $588 million toward the Postal Service's institutional costs. In FY 2011 unit attributable costs increased by 6.3 percent, while unit revenues increased by 0.9 percent. The nonprofit component of the Carrier Route product failed to cover its attributable costs, which resulted in a negative contribution of $16.7 million.

Comments

Valpak addresses two issues related to Carrier Route. First, Valpak comments that the Postal Service's pricing

Table VII–14—FY 2010 High Density and Saturation Volume and Contribution by Shape

	Flats	Parcels	Total
Volume	11,424,050,472	517,668	11,424,568,140
Contribution	$1,002,808,705	$(234,330)	$1,002,574,375

Source: PRC-ACR2011-LR3

strategy is neither profit-maximizing or demand-based because the Postal Service gave a greater price increase to those products with high cost coverages. Valpak Comments at 33.

Second, Valpak comments that the unit delivery cost for a Carrier Route letter has increased 88 percent since FY 2010, and finds that the cost must be anomalous by comparing it to the unit delivery costs of other pieces. Valpak Comments at 100. Valpak concedes that Carrier Route Letters only constitute two percent of the volume within the product, which may create a sampling problem. *Id.* Valpak requests that Postal Service in its ACR explain any unit cost that fluctuates more than 50 percent from the prior year. *Id.* The Postal Service agrees that the unit delivery cost is anomalous due to "the fact that Carrier Route letter volume is disappearing and a pricing structure that causes no financial penalty for mismarking the pieces." Response to CHIR No. 4, question 4. The Postal Service notes that there has been a 91 percent decrease in the volume of Carrier Route letters since FY 2009. *Id.* The Postal Service suggests that, due to the fact that Carrier Route Letter volume is disappearing, it may no longer compute separate unit delivery costs for Carrier Route letters because Carrier Route letters and Carrier Route flats pay the same rate. *Id.*

Commission Analysis

The Postal Service has given several reasons why the cost estimate is not reliable, including for example, mismarked pieces. Response to CHIR No. 4, question 4. The Postal Service provides two scenarios that result in mismarked pieces: (1) mailers may pay the lower, less presorted, 5-Digit automation rate and retain the Carrier Route marking; or (2) letter pieces paying the flat rates, which are the same as the letter rates. *Id.*

The information provided by the Postal Service is helpful in understanding the reasons the estimate for the unit delivery cost for Carrier Route letters is not reliable and possible solutions to remedy the problem. The Commission understands that the Postal Service is encouraging the use of 5-Digit automation for letters and discouraging the use of Carrier Route letters.[18] The Postal Service may elect to initiate a rulemaking with the Commission if it wishes to eliminate the Carrier Route letter rate category or aggregate Carrier Route letter cost data with Carrier Route flat data.

Worksharing

In FY 2011, the worksharing passthroughs for 15 Standard Mail discounts exceeded avoidable costs.

Table VII–15 shows the passthroughs by shape for dropship Carrier Route, High Density, and Saturation categories. All of the passthroughs are less than 100 percent.

Tables VII–16 and VII–17 show the passthroughs for the remaining products Letters, Flats, and NFMs/ Parcels. In its discussion of discounts that exceed avoidable costs, the Commission follows the order of

[18] See Docket No. R2011-2, United States Postal Service Notice of Market-Dominant Price Adjustment, January 13, 2011 at 18.

Table VII–16 as closely as practicable. Accordingly, the Commission first discusses Letters, then Flats, and finally the NFMs and Parcels product.

Letters

Four discounts for Standard Mail Letters exceeded avoidable cost in FY 2011: (1) non-automation AADC machineable letters, (2) non-automation ADC non-machinable letters, (3) non-automation 3-Digit non-machinable letters, and (4) non-automation 5-Digit non-machinable letters. The Postal Service has also made two modifications to its letter mail processing cost models that resolve previous anomalies, which are discussed first.

First, the Commission is unable to evaluate the presort discount for non-automation AADC machinable letters (*see* Table VII-16, note 1). In response to the Commission 2010 ACD the Postal Service filed Proposal Twelve[19] to disaggregate the previously combined non-automation machinable AADC and mixed AADC categories. Proposal Twelve was not approved by the Commission until after the Postal Service filed its 2011 Annual Compliance Report. As a result, the avoidable costs for FY 2011 have not been modified to reflect the new methodology. For this reason, the discount is not evaluated in this ACD. However, the Commission appreciates the Postal Service's compliance with the FY 2010 ACD request, and the relationship between the discount and its avoided cost will be evaluated in future ACDs.[20]

Second, in previous ACDs, the avoided cost estimate between automation and non-automation Mixed AADC machinable letters was negative.[21] The Commission approved a modified version of Proposal Nine of Docket No. RM2011-5, which resulted in a positive estimate for this avoided cost. The estimated avoided cost for this discount is now positive at 1.7 cents, and the passthrough is under 100 percent. The Commission appreciates the Postal Service's efforts to obtain a reasonable avoided cost estimate for the automation Mixed AADC machinable letters avoided cost.

The presort discounts for: (1) non-automation ADC non-machinable letters, 9.4 cents; (2) non-automation 3-Digit non-machinable letters, 3.8 cents; and (3) non-automation 5-Digit non-machinable letters, 9.3 cents, exceeded the estimated avoided cost in FY 2011. In Docket No. R2011-2, the passthroughs for non-automation ADC non-machinable letters, and non-automation 5-Digit non-machinable letters were below 100 percent. In Docket No. R2012-3, the Postal Service proposed, and the Commission approved, discounts for these three presort levels that resulted in passthroughs below 100 percent. Due to timing, these discounts were still based on FY 2010 avoided cost estimates. A decrease in avoided costs between FY 2010 and FY 2011 caused each of these passthroughs to exceed 100 percent. The Postal Service claims that each of these discounts is justified under section 3622(e)(2)(D). The Postal Service states,

> *It would be inefficient and unduly disruptive to our business and our customers' businesses to immediately adjust prices to reflect new lower avoided costs. The inability of customers to rely on stability of prices between regularly scheduled price adjustments would significantly undermine the ability of the Postal Service to use prices to signal efficient behaviors.*

Response to CHIR No.1, question 8.

[19] *See* Docket No. RM2012-1

[20] In the Postal Service's ACR it reports that this discount would have had a 69.6 percent passthrough in FY 2011. *See* USPS-FY11-3, FY11.3Alternate.Worksharing Discount Table_Final.xls.

[21] *See* 2010 ACD at 110.

Table VII–15—Standard Mail Carrier Route, High Density, and Saturation by Shape Workshare Discounts and Benchmarks

Type of Worksharing (Benchmark)	Year-end Discount (cents)	Unit Cost Avoidance (cents)	Passthrough
Presorting (dollars/piece)			
High Density Letters (Carrier Route Letters)	7.0	38.1	18.4%
High Density Flats (Carrier Route Flats)	4.5	5.8	77.6%
High Density Parcels (Carrier Route Parcels)	13.6	75.7	18.0%
DropShip (dollars/pound)			
DNDC Letters (Origin Letters)	16.0	31.7	50.5%
DSCF Letters (Origin Letters)	20.8	37.7	55.2%
DNDC Flats (Origin Flats)	16.0	22.8	70.2%
DSCF Flats (Origin Flats)	20.8	26.4	78.8%
DDU Flats (Origin Flats)	25.0	30.4	82.2%
DNDC Parcels (Origin Parcels)	20.8	109.5	19.0%
DSCF Parcels (Origin Parcels)	44.5	134.4	33.1%
DDU Parcels (OriginParcels)	62.1	149.0	41.7%

Source: PRC-ACR2011-LR3

However, the Postal Service does not explain how its operations would be impeded if rates would be adjusted to restore 100 percent passthroughs. As the Commission explained when it rejected use of this exemption in Docket No. R2008-1, the exception applies where there is a reasonable claim that "unusual operational circumstances" would cause a reduction of the discount to impede the efficient operation of the Postal Service.[22]

Section 3622(e) requires that workshare discounts not exceed avoided costs, or that they qualify for at least one of the exceptions in that section. *The Commission finds that the discounts for non-automation ADC non-machinable letters, non-automation 3-Digit non-machinable letters, and non-automation 5-Digit non-machinable letters are not justified by any of the exceptions and that the appropriate action is for the Postal Service to align the discounts with avoided costs when it files its next general market dominant price adjustment. If, at that time, any of the discounts are subject to one of the exceptions in section 3622(e), the Postal Service may present arguments to that effect.*

[22] Order No. 66, Docket No. R2008-1, Review of Postal Service Notice of Market Dominant Price Adjustments, March 17, 2008.

Table VII–16—Standard Mail Carrier Route, High Density, and Saturation by Shape Workshare Discounts and Benchmarks

Type of Worksharing (Benchmark)	Year-end Discount (cents)	Unit Cost Avoidance (cents)	Passthrough
Standard Mail Letters			
Standard Mail Automation Letters			
Presorting (dollars/piece)			
Automation AADC Letters (Automation Mixed AADC Letters)	1.6	1.7	94.1%
Automation 3-Digit Letters (Automation AADC Letters)	0.2	0.3	66.7%
Automation 5-Digit Letters (Automation 3-Digit Letters)	1.8	1.9	94.7%
Pre-barcoding (dollars/piece)			
Automation Mixed AADC Letters (Nonautomation Machinable Mixed ADC Letters)	0.3	1.8	16.7%
Standard Mail Nonautomation Letters			
Presorting (dollars/piece)			
Nonautomation AADC Machinable Letters (Nonautomation Mixed AADC Machinable Letters)	1.7	-	See Note[1]
Nonautomation ADC Nonmachinable Letters (Nonautomation Mixed ADC Nonmachinable Letters)	9.4	7.9	119.0%
Nonautomation 3-Digit Nonmachinable Letters (Nonautomation ADC Nonmachinable Letters)	3.8	2.5	152.0%
Nonautomation 5-Digit Nonmachinable Letters (Nonautomation 3-Digit Nonmachinable Letters)	9.3	7.6	122.4%
Standard Mail Flats			
Standard Mail Automation Flats			
Presorting (dollars/piece)			
Automation ADC Flats (Automation Mixed ADC Flats)	1.0	1.0	100.0%
Automation 3-Digit Flats (Automation ADC Flats)	5.6	4.6	112.0%
Automation 5-Digit Flats (Automation 3-Digit Flats)	7.9	11.7	67.5%
Pre-barcoding (dollars/piece)			
Automation Mixed ADC Flats	5.7	2.3	247.8%
(Nonautomation Mixed ADC Flats)			
Standard Mail Flats--Nonautomation			
Presorting (dollars/piece)			
Nonautomation ADC Flats (Nonautomation Mixed ADC Flats)	3.3	5.0	66.0%
Nonautomation 3-Digit Flats (Nonautomation ADC Flats)	5.2	5.4	96.3%
Nonautomation 5-Digit Flats (Nonautomation 3-Digit Flats)	8.2	7.8	105.1%

[1] Note: The Postal Service letters mail processing cost model only estimates costs for the combined non-automation machinable AADC and Mixed AADC categories.

Table VII–17—Standard Mail Letters, Flats, and Parcels (Commercial and Nonprofit) Presorting/Pre-barcoding Workshare Discounts and Benchmarks

Type of Worksharing (Benchmark)	Year-end Discount (cents)	Unit Cost Avoidance (cents)	Passthrough
Dropship			
Standard Mail Letters			
Drop Ship (dollars/pound)			
DNDC Letters (Origin Letters)	16.0	31.7	50.5%
DSCF Letters (Origin Letters)	20.8	37.7	55.2%
Standard Mail Flats			
Drop Ship (dollars/pound)			
DNDC Flats (Origin Flats)	16.0	22.8	70.2%
DSCF Flats (Origin Flats)	20.8	26.4	78.8%
Standard Mail Machinable Parcels			
Drop Ship (dollars/pound)			
DNDC Machinable Parcels (Origin Machinable Parcels)	20.8	109.5	19.0%
DSCF Machinable Parcels (Origin Machinable Parcels)	44.5	134.4	33.1%
DDU Machinable Parcels (Origin Machinable Parcels)	62.1	149.0	41.7%
Standard Mail Irregular Parcels, NFMs			
Drop Ship (dollars/pound)			
DNDC Irregular Parcels, NFMs (Origin Irregular Parcels, NFMs)	20.8	109.5	19.0%
DSCF Irregular Parcels, NFMs (Origin Irregular Parcels, NFMs)	44.5	134.4	33.1%
DDU Irregular Parcels, NFMs (Origin Irregular Parcels, NFMs)	62.1	149.0	41.7%
Standard Mail Parcels			
Presorting (dollars/piece)			
NDC Machinable Parcels (Mixed NDC Machinable Parcels)	41.5	36.2	114.6%
5-Digit Machinable Parcels (NDC Machinable Parcels)	34.7	59.0	58.8%
NDC Irregular Parcels (Mixed NDC Irregular Parcels)	39.1	13.0	300.8%
SCF Irregular Parcels (NDC Irregular Parcels)	43.7	29.9	146.2%
5-Digit Irregular Parcels (SCF Irregular Parcels)	4.0	43.3	9.2%
Pre-barcoding (dollars/piece)[2]			
Mixed NDC Machinable Barcoded Parcels[3] (Mixed NDC Machinable Nonbarcoded Parcels)	6.4	4.1	156.1%
Mixed NDC Irregular Barcoded Parcels[3] (Mixed NDC Irregular Nonbarcoded Parcels)	6.4	4.1	156.1%
Standard Mail NFMs			
Presorting (dollars/piece)			
NDC NFMs (Irregular Parcels) (Mixed NDC NFMs (Irregular Parcels))	41.5	23.0	180.4%
SCF NFMs (Irregular Parcels) (NDC NFMs (Irregular Parcels))	37.2	26.7	139.3%
5-Digit NFMs (Irregular Parcels) (SCF NFMs (Irregular Parcels))	2.4	42.6	5.6%
Pre-barcoding (dollars/piece)[2]			
Mixed NDC Barcoded NFMs[3] (Mixed NDC Nonbarcoded NFMs)	6.4	4.1	156.1%

Source: PRC-ACR2011-LR3

[2] The Postal Service charges a surcharge for nonbarcoded pieces.

[3] The Postal Service Standard Mail NFM/Parcel mail processing cost model does not estimate costs separately for pre-barcoded and non-barcoded pieces. The Postal Service uses a pre-barcoding avoidable cost for BPM as a proxy. See Table VII–21 pre-barcoding workshare discounts.

Flats

Three discounts[23] for Standard Mail Flats exceeded their avoided cost in FY 2011. Two presort discounts exceed avoided costs: automation 3-Digit flats, and 5-Digit non-automation flats. In addition, the pre-barcoding discount for automation mixed ADC flats exceeded its avoided costs.

In Docket No. R2011-2, both of the above presort discounts were set at or below their avoided cost. However, a decrease in avoided costs between FY 2010 and FY 2011 caused these passthroughs to exceed 100 percent. In Docket No. R2012-3 the presort discounts were again set at or below their estimated FY 2010 avoided costs. The Postal Service claims that each of these discounts is justified under section 3622(e)(2)(D). The Postal Service asserts that immediately aligning discounts with avoided costs would be inefficient, both for the Postal Service and its customers, would reduce pricing stability for mailers, and would undermine the Postal Service's ability to use efficient pricing signals. *See* Response to CHIR No.1, question 8.

The Postal Service does not explain how its operations would be impeded if rates would be adjusted to restore 100 percent passthroughs. As the Commission explained when it rejected use of this exemption in Docket No. R2008-1, the exception applies where there is a reasonable claim on "unusual operational circumstances" that would cause a reduction of the discount to impede the efficient operation of the Postal Service.[24]

Section 3622(e) requires that workshare discounts not exceed avoided costs, or that they qualify for at least one of the exceptions in that section. *The Commission finds that the above-referenced presort discounts are not justified by any of the exceptions and that the appropriate action is for the Postal Service to align the discounts with avoided costs when it files its next general market dominant price adjustment. If, at that time, any of the discounts are subject to one of the exceptions in section 3622(e), the Postal Service may present arguments to that effect.*

The Postal Service justifies the excessive pre-barcoding discount for Automation Mixed ADC flats under section 3622(e)(2)(D). Postal Service Response to CHIR No. 1, question 8. The Postal Service states that the excessive discount is necessary to encourage pre-barcoding of flats as a way to support the implementation of the FSS program. However, the Postal Service notes its intention to phase this discount out over time. *Id.* The Commission finds this discount satisfies 39 U.S.C. 3622.

NFMs/Parcels

Eight worksharing discounts for Standard Mail NFMs/Parcels exceeded their avoided costs in FY 2011. The following five presort discounts exceeded avoided costs: (1) NDC Machinable Parcels, 41.5 cents, (2) NDC Irregular Parcels, 39.1 cents, (3) SCF Irregular Parcels, 43.7 cents, (4) NDC NFMs (Irregular Parcels), 41.5 cents, and (5) SCF NFMs (Irregular Parcels), 37.2 cents. In addition the following three pre-barcoding discounts exceeded their avoided costs: (1) Mixed NDC Machinable

23 In the Postal Service's ACR it states that four discounts for Standard Mail Flats exceeded avoidable cost in FY 2011. However, the Postal Service included Proposal Eighteen, Modification 1 from Docket No. RM2012-2 in its Standard Mail Letters mail processing cost model. The Commission has not yet issued a Final Order regarding Docket No. RM2012-2. Therefore, the Commission has modified the Postal Service's models to remove the impact of Proposal Eighteen. *See* PRC-ACR2011-LR8.

24 Order No. 66, Docket No. R2008-1, Review of Postal Service Notice of Market Dominant Price Adjustments, March 17, 2008.

Barcoded Parcels, 6.4 cents, (2) Mixed NDC Irregular Barcoded Parcels, 6.4 cents, and (3) Mixed NDC Barcoded NFMs, 6.4 cents.

In Docket No. R2011-2, the five excessive presort discounts and the three excessive pre-barcoding discounts all exceeded their estimated avoided costs. The Postal Service justified these excessive passthroughs based the need to phase in a pricing structure that aligns with the new avoided cost estimates.[25] *See* Order No. 675 at 27. In Docket No. R2012-3 only NDC Machinable Parcels and SCF Irregular Parcels had passthroughs at or below 100 percent. Due to a decrease in avoided cost estimates between FY 2010 and FY 2011, the passthroughs for NDC Machinable Parcels and SCF Irregular Parcels again exceeded their avoided costs.

The Postal Service justifies the five excessive presort discounts citing sections 3622(e)(2)(B) and 3622(e)(2)(D). First, regarding the 3622(e)(2)(B) justification, the Postal Service explains that it will "attempt to reduce or eliminate these excess presort discounts in the next general price change, when it can do so without running the risk of rate shock." *See* Response to CHIR No. 1, question 8. The Postal Service neither identifies the specific disounts it wishes to apply this justification to, nor quantifies the impact of any rate shock. *See* Response to CHIR No. 4, question 3. Concerning the 3622(e)(2)(D) justification, the The Postal Service asserts that immediately aligning discounts with avoided costs would be inefficient, both for the Postal Service and its customers, would reduce pricing stability for mailers, and would undermine the Postal Service's ability to use efficient pricing signals. *See* Response to CHIR No.1, question 8.

The Postal Service makes no claim to how its operations would be impeded if rates would be adjusted to restore 100 percent passthroughs. As the Commission explained when it rejected use of this exemption in Docket No. R2008-1, the exception applies where there is a reasonable claim on "unusual operational circumstances" that would cause a reduction of the discount to impede the efficient operation of the Postal Service.[26]

Section 3622(e) requires that workshare discounts not exceed avoided costs, or that they qualify for at least one of the exceptions in that section. *The Commission finds that the above-referenced presort discounts are not justified by any of the exceptions and that the appropriate action is for the Postal Service to align the discounts with avoided costs when it files its next general market dominant price adjustment. If, at that time, any of the discounts are subject to one of the exceptions in section 3622(e), the Postal Service may present arguments to that effect.*

The Postal Service applies a non-barcoded surcharge to all Standard Mail NFMs/Parcels that do not bear a correct routing barcode. The Postal Service Standard Mail NFMs/Parcel mail processing cost model now estimates costs separately for pre-barcoded and non-barcoded pieces.[27] The Postal Service reduced the Standard Mail Parcel non-barcoded surcharge in Docket No. R2011-2 from 7.0 cents to 6.4 cents. In Docket No. R2012-3 the Postal Service maintained the 6.4 cents discount. The Postal Service justified this discount in excess

[25] In FY 2011, the Commission approved the use of a new cost model for Standard Mail Parcels and NFMs. *See* Order No. 658. The new model has changed the avoided cost estimates for NFMs and Parcels. ACR at 56.

[26] Order No. 66, Docket No. R2008-1, Review of Postal Service Notice of Market Dominant Price Adjustments, March 17, 2008.

[27] *See* Docket No. RM2010-12, Proposal Seven.

of estimated avoided cost on the basis of efficient operations, citing section 3622(e)(2)(D). *See* Response to CHIR No. 1, question 8. Specifically, the Postal Service cites its desire to "promote a totally pre-barcoded incoming parcel mailstream which would allow elimination of key stations at sorting facilities, and to facilitate implementation of electronic manifesting." *Id*. The Commission finds that for FY 2011, the pre-barcoding discounts for Standard Mail Parcels satisfy 39 U.S.C. 3622.

Standard Nonprofit Mail

39 U.S.C. 3626(a)(6) requires nonprofit prices to be set in relation to their commercial counterparts regardless of nonprofits' independent costs. In Docket No. R2011-2, Nonprofit prices were set to yield per-piece average revenues that were 60 percent of commercial per-piece average revenues at the class level. The Commission calculates that in FY 2011, the actual per-piece revenue from Standard Mail Nonprofit pieces was 56.38 percent of Standard Mail commercial per-piece revenue.

The prices approved in Docket No. R2012-3 are expected to produce average per-piece revenue for Nonprofit mail equal to 60 percent of the average per-piece revenue for Commercial mail. No remedial action, therefore, is warranted.

Standard Mail Incentive Programs

There were two Standard Mail Incentive programs in effect during FY 2011: (1) the Saturation Mail Incentive Program and (2) the Mobile Barcode Promotion Program. The Commission also received finalized data from the 2010 Standard Mail Volume Incentive Pricing Program in FY 2011.

The Saturation Mail Incentive Program began on January 1, 2011 and ended on December 31, 2011. The Postal Service has not yet provided finalized data for the incentive.

The 2011 Mobile Barcode Promotion started on July 1, 2011 and ended on August 31, 2011. The intent of the promotion was to generate awareness of how mobile technology can be integrated into mail campaigns. The Postal Service gave a three percent discount to First-Class and Standard cards, letters, and flats that included a two-dimensional mobile barcode. The Postal Service gave $29 million in discounts for 4.5 billion Standard Mail pieces.

The 2010 Standard Mail Volume Incentive Program was designed to increase incremental Standard Mail volume and revenue during a typically low volume period. The 2010 Standard Mail Volume Incentive Program provided a 30 percent discount on incremental volume above a mailer specific volume threshold. In May 2011 the Postal Service filed the final portion of the 2010 Standard Mail Volume Incentive Program data.[28] In Response to CHIR No. 4, questions 15, 19 and 20 the Postal Service compiled the data filed with the Commission in its December 2010 and May 2011 data reports.[29] The Postal Service's data indicate that it gave $91 million in rebates for 4.3 billion Standard Mail pieces. The Postal Service's data also indicates that there were $1.2 million in administrative costs associated with the 2010 Standard Mail Volume Incentive Program.

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28 *See* Docket No. R2010-3 2010 Standard Mail Volume Incentive Program Final Data Collection Report, May 16, 2011.

29 *See* Responses of the United States Postal Service to Questions 15 and 20 of Chairman's Information Request No. 4, March 21, 2012. See *also* Responses of the United States Postal Service to Question 19 of Chairman's Information Request No. 4, March 16, 2012.

It is the Commission's intent to report on these incentive programs separately. The report (or reports as the case may be) will evaluate the initiatives to determine, among other things, their value and whether they fulfill their objectives.

Package Services

Introduction

The Package Services class consists of five products: (1) Single-Piece Parcel Post; (2) Bound Printed Matter (BPM) Flats; (3) Bound Printed Matter (BPM) Parcels; (4) Media Mail/Library Mail; and (5) Inbound Surface Parcel Post (at UPU rates).[30] These products have common characteristics, such as: none are sealed against inspection; none receive preferential handling or transportation; and generally, each consists of parcels containing merchandise, although heavier catalogs and directories may also be mailed within the Package Services class. In FY 2011, 675 million pieces were mailed as Package Services. This accounts for less than one-half of one percent of total domestic market dominant mail volume.

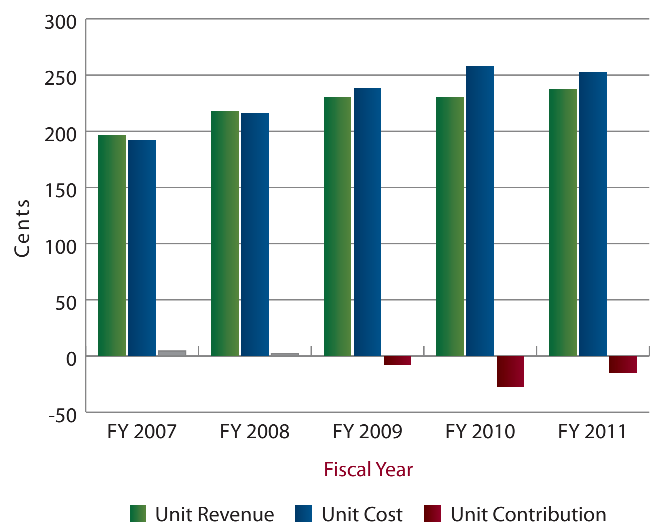
The principal FY 2011 findings for Package Services are:

- The attributable costs for the Package Services class, as a whole, exceeded revenues by $97.3 million, resulting in a cost coverage of 94.3 percent.
- Single-Piece Parcel Post revenues did not cover attributable costs by $88.2 million, resulting in a cost coverage of 89.3 percent.
- BPM Parcels revenues did not cover attributable costs by $3.9 million, resulting in a cost coverage of 98.8 percent.
- Media Mail/Library Mail revenues did not cover attributable costs by $98.5 million, resulting in a cost coverage of 77.2 percent.
- Two worksharing discounts exceed avoidable costs, and thus did not satisfy 3622(e)(2).
- Media Mail/Library Mail prices complied with the preferred rate requirements identified in 3626(a)(7).

Financial Analysis

Table VII–18 displays the FY 2011 financial performance for the Package Services class. Table VII–18 shows that the Package Services class had a cost coverage of 94.3 percent. Although the revenues for Package Services failed to cover attributable costs for the third consecutive year, the cost coverage for Package Services improved 5.0 percentage points over FY 2010. Figure VII–7 shows the continuation of unit contribution shifting from being slightly positive in FY 2007 and FY 2008, to slightly negative in FY 2009, FY 2010, and FY 2011.

Figure VII–7—Package Services Financial Performance FY 2007– 2011



30 The Inbound Surface Parcel Post (at UPU rates) product is discussed in the Market Dominant International Mail Section.

Table VII–18—FY 2011
Volume, Revenue, Cost and Cost Coverage for Package Services

Package Services	Volume (000)	Total Revenue ($000)	Attributable Cost ($000)	Contribution to Institutional Cost ($000)	Rev./Pc. (Cents)	Cost/Pc. (Cents)	Contribution to Institutional Cost/Pc. (Cents)	Cost Coverage
Single-Piece Parcel Post	70,217.810	732,901.429	821,118.831	(88,217.402)	1,043.754	1,169.388	(125.634)	89.3%
Inbound Surface Parcel Post (at UPU Rates)	1,017.314	24,250.499	10,725.437	13,525.062	2,383.777	1,054.290	1,329.487	226.1%
Bound Printed Matter Flats	251,831.376	205,155.956	125,416.932	79,739.024	81.466	49.802	31.664	163.6%
Bound Printed Matter Parcels	245,281.592	310,641.889	314,561.644	(3,919.755)	126.647	128.245	(1.598)	98.8%
Media and Library Mail	107,828.747	332,607.496	431,067.651	(98,460.155)	308.459	399.771	(91.312)	77.2%
Inbound NSA Mail Intl	13.695	29.827	1.674	28.153				
Total Package Services	**675,173.220**	**1,605,587.096**	**1,702,892.170**	**(97,305.074)**	**237.804**	**252.216**	**(14.412)**	**94.3%**

Source: PRC-ACR2011-NP-LR1

BPM Flats and Inbound Surface Parcel Post (at UPU rates) were the only Package Services products with revenues exceeding attributable costs in FY 2011. The remaining three products, Single-Piece Parcel Post, BPM Parcels, and Media Mail/Library Mail, had an overall negative contribution of $190.6 million.

Single-Piece Parcel Post

The FY 2011 cost coverage for Single-Piece Parcel Post was 89.3 percent, a 7.1 percentage point increase from FY 2010. This is the fifth consecutive year that Single-Piece Parcel Post did not generate sufficient revenues to cover attributable costs. Unit attributable costs decreased by 50.1 cents and unit revenues increased by 41.9 cents, which led to an increase in the contribution per piece of 92.0 cents from FY 2010 to FY 2011. Despite this improvement, Single-Piece Parcel Post's contribution remained negative. In FY 2011, Single-Piece Parcel Post's contribution was negative $88.2 million.

BPM Flats

For the third consecutive year, BPM Flats was the only domestic Package Services product that generated sufficient revenues to cover attributable costs. In FY 2011, BPM Flats had a cost coverage of 163.6 percent and contributed $79.7 million towards the Postal Service's institutional cost. BPM Flat's cost coverage improved 15.7 percentage points from FY 2010.

BPM Parcels

In FY 2011, BPM Parcels had a net loss of $3.9 million. The FY 2011 cost coverage for BPM Parcels was 98.8 percent, an increase of 6.4

percentage points compared with FY 2010. Despite the improvement in cost coverage, this is the third consecutive year that BPM Parcels did not generate sufficient revenues to cover attributable costs.

Media Mail/Library Mail

In FY 2011, Media Mail/Library Mail are preferred categories and had a cost coverage of 77.2 percent, a 3.4 percentage point decrease from FY 2010. Media Mail/Library Mail had a net loss of $98.6 million. This is the fifth consecutive year that Media Mail/Library Mail's attributable costs exceeded its revenues.

Media Mail/Library Mail's volumes decreased by 11.8 percent. In addition, its unit revenues decreased by 10.0 percent in FY 2011, and its unit attributable costs rose by 6.6 percent. As a result, Media Mail/Library Mail incurred a larger loss, per piece, compared with FY 2010. As Figure VII–8 shows, the unit contribution for Media Mail/Library Mail continues to decline each fiscal year.

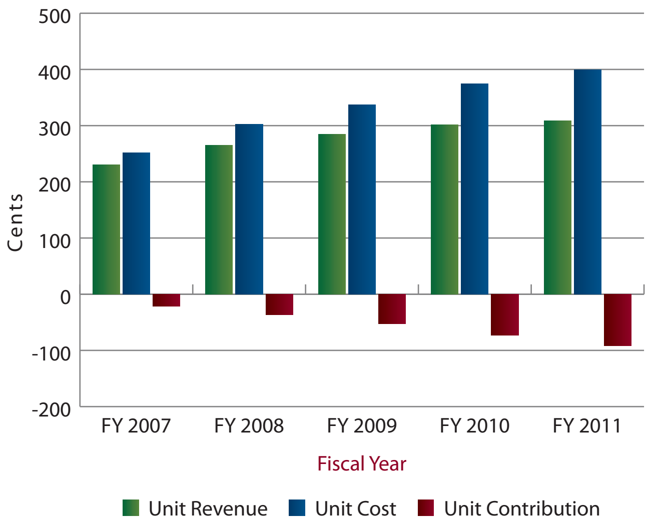
Comments

Comments were filed by the Public Representative. No other party filed comments concerning Package Services. The Public Representative states that recent price increases given to Package Services products in Docket Nos. R2011-2 and R2012-3 indicate that the Postal Service is working to alleviate low cost coverages in Package Services. The Public Representative suggests that the Postal Service should continue its efforts to bring Package Services to full cost coverage.

Commission Analysis

The Postal Service's two most recent price adjustments indicate that the Postal Service is attempting to resolve

Figure VII–8—Media Mail/Library Mail Financial Performance FY 2007 –2011



the cost coverage issues for Single-Piece Parcel Post, BPM Parcels, and Media Mail/Library Mail within the constraints of the annual price cap limitation by proposing above average price increases.[31] However, the Postal Service asserts that the price cap limitation strains its ability to improve Media Mail/Library Mail cost coverage. Response to CHIR No. 1, question 10. Nevertheless, the Postal Service contends that it will continue to increase Media Mail/Library's prices in order to help move the product towards full cost coverage.

In addition to proposing above average increases for loss-making Package Services products, the Postal Service implemented product actions that should help improve the cost coverage for BPM Parcels and Media Mail/Library Mail. Effective January 22, 2012, the Postal Service eliminated the

[31] See Docket No. R2011-2, Order Revising Postal Service Market Dominant Price Adjustments, February 16, 2011 (Order No. 675) and Docket No. R2012-3, Order on Price Adjustments for Market Dominant Products and Related Mail Classification Changes, November 22, 2011 (Order No. 987). The approved rate increases went into effect on April 17, 2011 and January 22, 2012, respectively.

three-cent barcoding discount for BPM Parcels and Media Mail/Library Mail. *Id.* The elimination of the barcoding discount should further increase revenues for BPM Parcels and Media Mail/Library Mail, improving each product's cost coverages.

The Package Services class, as well as Single-Piece Parcel Post, BPM Parcels, and Media Mail/Library Mail, did not recover attributable costs or make a reasonable contribution to institutional costs. *Although Package Services attributable costs continue to exceed revenues, the Commission finds that the cost coverages for each product, except for Media Mail/Library Mail, improved over FY 2010.*

The Postal Service should continue to price Single-Piece Parcel Post, BPM Parcels, and Media Mail/Library Mail in a way that moves each product to full cost coverage. In addition, for Media Mail/Library Mail, whose financial performance has not improved over the past five fiscal years, the Postal Service should explore opportunities to achieve efficiencies in handling this type of mail. The Commission directs the Postal Service to report on its efforts to improve Media Mail/Library Mail's cost coverage in its FY 2012 Annual Compliance Report.

Statutory Preferences

Section 3626(a)(7) requires Library Mail prices to be set at 95 percent of Media Mail prices. The Postal Service asserts that the current prices meet this requirement. ACR at 42. *The Commission finds that for FY 2011, the prices for Media Mail/Library Mail complied with section 3626(a)(7).*

Table VII–19—Media/Library Mail Workshare Discounts and Benchmarks

FY 2011

Type of Worksharing (Benchmark)	Year-End Discount (cents)	Unit Cost Avoidance (cents)	Passthrough[1]
Media Mail			
Presorting (cents/piece)			
Basic (Single Piece)	39.00	47.00	83.0%
5-Digit (Basic)	36.00	39.00	92.3%
Pre-barcoding (cents/piece)			
Single Piece Barcoded	3.00	4.00	75.0%
Library Mail			
Presorting (cents/piece)			
Basic (Single Piece)	37.00	47.00	78.7%
5-Digit (Basic)	34.00	39.00	87.2%
Pre-barcoding (cents/piece)			
Single Piece Barcoded (Single Piece Non-barcoded)	3.00	4.00	75.0%

Source: PRC-ACR2011-LR5

[1] The calculated passthroughs are based on rounded unit avoidable costs.

Worksharing

Three Package Services products offered workshare discounts in FY 2011: Media Mail/Library Mail, BPM Flats, and BPM Parcels.

Media Mail/Library Mail

There were six discounts offered for Media Mail/Library Mail in FY 2011. All Media Mail/Library Mail workshare discounts were less than their respective avoided costs in FY 2011. Table VII–19 shows the FY 2011 discounts, avoided costs, and passthroughs for Media Mail/Library Mail.[32]

[32] While the basic presort discount did not exceed avoided costs in

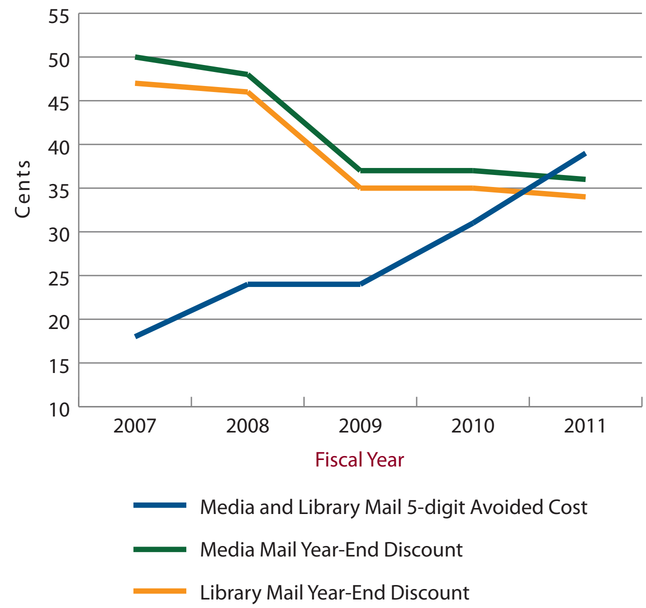
This is the first compliance review where the 5-Digit presort discount for Media Mail and Library Mail did not exceed avoided costs. Figure VII–9 shows the past disparity between the 5-Digit discount and the unit avoided cost for Media Mail/Library Mail. In its past four ACDs, the Commission recommended that the Postal Service continue moving towards alignment of the 5-Digit presort discounts with their avoided costs. The Commission commends the Postal Service's efforts to ensure that the 5-Digit presort discounts did not exceed their avoided costs in FY 2011.

BPM Flats and BPM Parcels

In FY 2011, there were 15 discounts offered for BPM Flats and 15 discounts for BPM Parcels. Table VII–20 and Table VII–21 show the FY 2011 discounts, avoided costs, and passthroughs for BPM Flats and BPM Parcels, respectively.

Only the Destination Network Delivery Center (DNDC) dropship discount for both BPM Flats and Parcels exceed avoidable costs.[33] In Docket No. R2011-2, the Commission approved the Postal Service's DNDC dropship discounts for both BPM Flats and BPM Parcels which reflected a 100 percent passthrough of avoidable costs. Since then, the unit avoidable costs for DNDC dropship BPM Flats and BPM Parcels decreased, resulting in the passthroughs increasing to 102.4 percent. The Postal Service plans to realign the discount in its next price adjustment. FY 2011 ACR at 60.

Figure VII–9—Media and Library Mail 5-Digit Presort Avoided Cost and Discount



In response to CHIR No. 1, question 12, the Postal Service explains that both discounts exceed 100 percent of avoided cost because setting the discounts below 100 percent would impede the efficient operations of the Postal Service. Response to CHIR No. 1, question 12. Thus, the Postal Service claims the statutory exception in section 3622(e)(2)(D) applies here. It further explains that during the previous two price adjustments, it attempted to reduce the passthroughs, but its efforts had to be balanced with competing interests, including "efforts to improve cost coverage and encourage dropshipping, the price cap size limitation, and the desire to keep the

FY 2011, the Commission notes this could change in the future. The Commission recently approved modifications to the Postal Service's Media Mail/Library Mail mail processing cost model for FY 2012. See RM2012-1, Order Concerning Analytical Principles for Periodic Reporting (Proposals Nine Through Fifteen), Proposal 13, January 20, 2012, (Order No. 1153). In its ACR filing, the Postal Service provided FY 2011 avoided cost estimates based on the updated mail processing cost model. On this basis, the avoided costs for basic presorting are less than the current basic presort discount approved in Docket No. R2012-3. *See* Library Reference USPS-FY11-3, Excel file 'FY11.3Alternate.Worksharing Discount Table_Final.xls.' The Commission encourages the Postal Service to adjust the basic presort discount as applicable to maintain compliance.

33 The Postal Service's ACR reported three discounts exceeded avoided costs. However, the Commission determined that the passthrough for Destination Delivery Unit (DDU) dropshipped BPM Parcels was incorrectly calculated, and that the passthrough complied with 3622(e). *See* Table VII–21.

Table VII–20—Bound Printed Matter Flats Workshare Discounts and Benchmarks

Type of Worksharing (Benchmark)	FY 2011 Year-End Discount (cents)	Unit Cost Avoidance (cents)	Passthrough[3]
BPM Flats			
Presorting (cents/piece)[1]			
Basic Flats (Single Piece Flats)	32.6	See Note [1]	
Carrier Route Flats (Basic Flats)	9.8	15.3	64.1%
Presorting (cents/pound)[1]			
Basic, Carrier Route Flats (Single Piece Flats)	3.0	4.0	75.0%
Zones 1 & 2	7.3	See Note[1]	
Zone 3	8.7	See Note[1]	
Zone4	8.5	See Note[1]	
Zone 5	9.2	See Note[1]	
Zone 6	9.4	See Note[1]	
Zone 7	9.4	See Note[1]	
Zone 8	10.5	See Note[1]	
Pre-barcoding (cents/piece)[2]			
Single Piece Automatable Flats (Single Piece Nonautomatable Flats)	3.0	See Note[2]	
Basic, Automatable Flats Basic Nonautomatable Flats	3.0	See Note[2]	
Carrier Route Automatable Flats (Carrier Route Nonautomatable Flats)	3.0	See Note[2]	
Drop Ship (cents/piece)			
Basic, Carrier Route DNDC Flats/IPPs Basic, Origin Flats)	17.4	17.0	102.4%
Basic, Carrier Route DNDC Flats (Basic, Origin Flats)	61.5	65.5	93.9%
Basic, Carrier Route DDU Flats (Basic, Origin Flats)	76.2	78.9	96.6%

[1] The BPM cost model does not estimate cost differences between single piece and presorted BPM. Single piece BPM is a residual category with low volume and adequate data are not available. Previously, rate differences between single piece and presorted BPM were based on an assumption that unit mail processing costs for single piece BPM were twice that of presorted BPM. See Docket No R2006-1, USPS-T-38, p. 8.

[2] Separate estimates of pre-barcoding cost savings are not available for BPM Flats. Based on the cost savings for BPM Parcels, the pre-barcoding discount for BPM Flats implies a passthrough of 73.2%.

[3] The calculated passthroughs are based on rounded unit avoidable costs.

price adjustments uniform across all weights and zones." *Id.*

Commission Analysis

Section 3622(e)(2) requires the Commission to ensure workshare discounts do not exceed estimated avoided costs unless otherwise allowed by a statutory exception. To determine if workshare discounts comply with section 3622(e)(2), the Commission analyzes the passthroughs for each workshare discount. For FY 2011, Media Mail/Library Mail passthroughs complied with section 3622(e)(2). In addition, with the exception of the DNDC dropship discounts, the passthroughs for BPM Flats and BPM Parcels complied with section 3633(e)(2).

With respect to the DNDC dropship discounts for BPM Flats and BPM Parcels, the Commission does

Table VII–21—Bound Printed Matter Parcels Workshare Discounts and Benchmarks

Type of Worksharing (Benchmark)	FY 2011 Year-End Discount (cents)	FY 2011 Unit Cost Avoidance (cents)	FY 2011 Passthrough[2]
BPM Parcels/IPPs			
Presorting(cents/piece)[1]			
Basic Parcels(?? missing text) (Single Piece Parcels/IPPs)	56.9	See Note[1]	
Carrier Route Parcels/IPPs (Single Piece Parcels/IPPs)	9.8	15.3	64.1%
Presorting(cents/pound)[1]			
Basic, Carrier Route Parcels/IPPs (Single Piece Parcels/IPPs)			
Zones 1 & 2	4.5	See Note[1]	
Zone 3	4.4	See Note[1]	
Zone 4	4.3	See Note[1]	
Zone 5	3.7	See Note[1]	
Zone 6	3.6	See Note[1]	
Zone 7	2.2	See Note[1]	
Zone 8	1.2	See Note[1]	
Pre-barcoding(cents/piece)			
Single Piece Barcoded Parcels/IPPs (Single Piece Nonbarcoded Parcels/IPPs)	3.0	4.1	73.2%
Basic Barcoded Parcels/IPPs (Single Piece Nonbarcoded Parcels/IPPs)	3.0	4.1	73.2%
Carrier Route Barcoded Parcels/IPPs (Single Piece Nonbarcoded Parcels/IPPs)	3.0	4.1	73.2%
Drop Ship(cents/piece)			
Basic, Carrier Route DNDC Parcels/IPPs (Basic, Origin Parcels/IPPs)	17.4	17.0	102.4%
Basic, Carrier Route DSCF Parcels/IPPs (Basic, Origin Parcels/IPPs)	61.6	65.5	94.0%
Basic, Carrier Route DDU Parcels/IPPs (Basic, Origin Parcels/IPPs)	76.2	78.9	96.6%

[1] The BPM cost model does not estimate cost differences between single piece and presorted BPM. Single piece BPM is a residual category with low volume and adequate data are not available. Previously, rate differences between single piece and presorted BPM were based on an assumption that unit mail processing costs for single piece BPM were twice that of presorted BPM. See Docket No R2006-1, USPS-T-38, p. 8.

[2] The calculated passthroughs are based on rounded unit avoidable costs.

not accept the Postal Service's justification for the discounts' excessive passthroughs. The Postal Service does not cite specific operations that would be impeded if the discounts were aligned with avoided costs. Thus, the Postal Service provides no plausible rationale justifying an exception under section 3622(e)(2)(D). *The Commission directs the Postal Service to align the DNDC dropship discounts with their avoided costs for BPM Flats and BPM Parcels at the Postal Service's next price adjustment.*

Special Services

Introduction

The Special Services class consists of 12 products. These products can be categorized as Ancillary Services, "stand-alone" Special Services, and International Special Services. Though it is comprised of several services, Ancillary Services is classified as a single product. The stand-alone Special Services are comprised of eight products. International Special Services consists of three products.

The principal FY 2011 findings for Special Services are:

- Special Services contributed $658.7 million toward institutional costs, the third highest contribution among all market dominant mail classes; and
- The attributable costs for Stamp Fulfillment Services exceed revenues.

Financial Analysis

In FY 2011, the Special Services class, including International mail services, earned $2.8 billion in revenue and incurred $2.1 billion in attributable cost.[34] The Special Services class had an aggregate cost coverage of 130.8 percent. Table VII–22 provides the financial information for each of the Special Services products.

Ancillary Services

The Ancillary Services product is comprised of 22 services that may only be used in conjunction with other mail services.[35] In FY 2011, the Ancillary Services product earned $1.7 billion in revenue and incurred $1.3 billion in attributable cost. Ancillary Services contributed $324.2 million towards the institutional costs of the Postal Service and had a cost coverage of 124.2 percent. The Postal Service attributes revenue for some Ancillary Services to their host mail class as fee revenue. For those Ancillary Services, the revenue is not included in the calculation of the cost coverage for Ancillary Services.[36]

In FY 2011, Collect on Delivery (COD) revenues were $6.7 million and attributable costs were $4.4 million, resulting in COD contributing $2.3 million towards institutional costs.[37] The FY 2011 cost coverage, of 152.7 percent, was a substantial increase of 73.6 percentage points above the FY 2010 cost coverage. In FY 2011, the unit cost for COD declined 46.0 percent from the unit cost reported in FY 2010.[38] Volumes declined 1.8 percent, from 834,483 in FY 2010 to 819,400 in FY 2011. Figure VII–10 shows the declining volume trend for COD from FY 2001 to FY 2011.

In Docket No. R2011-2, the Commission approved the Postal Service's request to raise COD average prices by 4.2 percent. Although COD volumes continued to decline in FY 2011, the rate increase enabled unit revenues to increase as unit costs

34 For a discussion of International Special Services, see the Market Dominant International section.

35 The domestic Ancillary Services product includes the following services: (1) Address Correction Service; (2) Applications and Mailing Permits; (3) Business Reply Mail; (4) Bulk Parcel Return Service; (5) Certified Mail; (6) Certificate of Mailing; (7) Collect on Delivery; (8) Delivery Confirmation; (9) Insurance; (10) Merchandise Return Service; (11) Parcel Airlift; (12) Registered Mail; (13) Return Receipt; (14) Return Receipt for Merchandise; (15) Restricted Delivery; (16) Shipper-Paid Forwarding; (17) Signature Confirmation; (18) Special Handling; (19) Stamped Envelopes; (20) Stamped Cards; (21) Premium Stamped Stationery; and (22) Premium Stamped Cards.

36 The services, for which the Postal Service attributes revenue to the underlying mail class as fee revenue, are: (1) Address Correction Services; (2) Applications and Mailing Permits; (3) Business Reply Mail; (4) Bulk Parcel Return Service; (5) Certificate of Mailing; (6) Merchandise Return Service; (7) Parcel Airlift; (8) Return Receipt for Merchandise; (9) Shipper Paid Forwarding; and (10) Special Handling.

37 2011 ACR at 42-43.

38 *Id.* at 42; 2010 ACD at 124.

Table VII–22—Market Dominant Special Services
Fiscal Year 2011 Volume, Cost, Revenue, and Cost Coverage by Product

Market Dominant Special Services	Units (000)	Total Revenue ($000)	Attributable Cost ($000)	Contribution to Institutional Cost ($000)	Unit Revenue (Cents)	Unit Cost (Cents)	Contribution to Institutional Unit Cost (Cents)	Cost Coverage
Domestic Special Services								
Ancillary Services Product								
Certified Mail	251,222.212	708,755.088	599,327.569	109,427.519	282.123	238.565	43.558	118.3%
Collect On Delivery	819.400	6,677.514	4,373.217	2,304.297	814.927	533.710	281.218	152.7%
Insurance	34,573.190	116,651.990	103,411.365	13,240.625	337.406	299.109	38.297	112.8%
Registered Mail	2,687.960	45,236.486	42,809.327	2,427.159	1,682.930	1,592.633	90.297	105.7%
Stamped Cards[2]	53,696.000	1,610.880	819.854	791.026	3.000	1.527	1.473	196.5%
Stamped Envelopes	-	10,649.631	6,885.551	3,764.080	-	-	-	154.7%
Other Ancillary Services[1]	1,698,367.845	771,745.803	579,484.663	192,261.140	45.440	34.120	11.320	133.2%
Total Ancillary Services	**2,041,366.607**	**1,661,327.392**	**1,337,111.546**	**324,215.846**	**83.582**	**67.270**	**16.311**	**124.2%**
Stand-Alone Products								
Address Management Services	2,707.223	16,440.630	10,120.686	6,319.944	607.288	373.840	233.447	162.4%
Caller Service[2]	182.638	92,162.055	27,785.207	64,376.848	50,461.530	15,213.247	35,248.283	331.7%
Change of Address Credit Card Auth.[3]	12,060.836	12,059.412	1,174.245	10,885.167	99.988	9.736	90.252	1027.0%
Confirm Service	-	3,014.225	1,090.449	1,923.776	-	-	-	276.4%
Customized Postage	-	900.000	50.000	850.000	-	-	-	1800.0%
Money Orders	115,510.031	172,696.294	123,438.493	49,257.802	149.508	106.864	42.644	139.9%
Post Office Box Service[2]	13,897.301	801,898.619	592,763.214	209,135.405	5,770.175	4,265.312	1,504.863	135.3%
Stamp Fulfillment Services[4]	2,711.459	3,126.445	5,238.523	(2,112.078)	115.305	193.199	(77.895)	59.7%
Total Stand-Alone Services	**147,069.489**	**1,102,297.680**	**761,660.817**	**340,636.864**	**749.508**	**517.892**	**231.616**	**144.7%**
Total Domestic Special Services	**2,188,436.096**	**2,763,625.072**	**2,098,772.363**	**664,852.710**	**126.283**	**95.903**	**30.380**	**131.7%**
International Special Services[5]	1,845.294	32,707.099	38,810.880	(6,103.781)	1,772.460	2,103.236	(330.776)	84.3%
Total Special Services	**2,190,281.390**	**2,796,332.171**	**2,137,583.243**	**658,748.928**	**127.670**	**97.594**	**30.076**	**130.8%**

[1] The Postal Service includes USPS volumes for Return Receipts in its RPW volumes. Those volumes should not be included, in order to correctly report unit revenues, costs and contribution to institutional costs. The 2011 ACR did not isolate costs for Other Ancillary Services.
[2] Volume from REV USPS-FY11-4, filename - FY 2011 PO Boxes.xls.
[3] *Id.*, filename — FY 2011 Special Services.xls.
[4] Volume from Postal Service response to CHIR No. 1, question 17, filename — CHIR1.Q17.xls.
[5] International Special Services are found in the International Mail section.

Figure VII–10—Collect On Delivery Volume and Trend FY 2001–2011

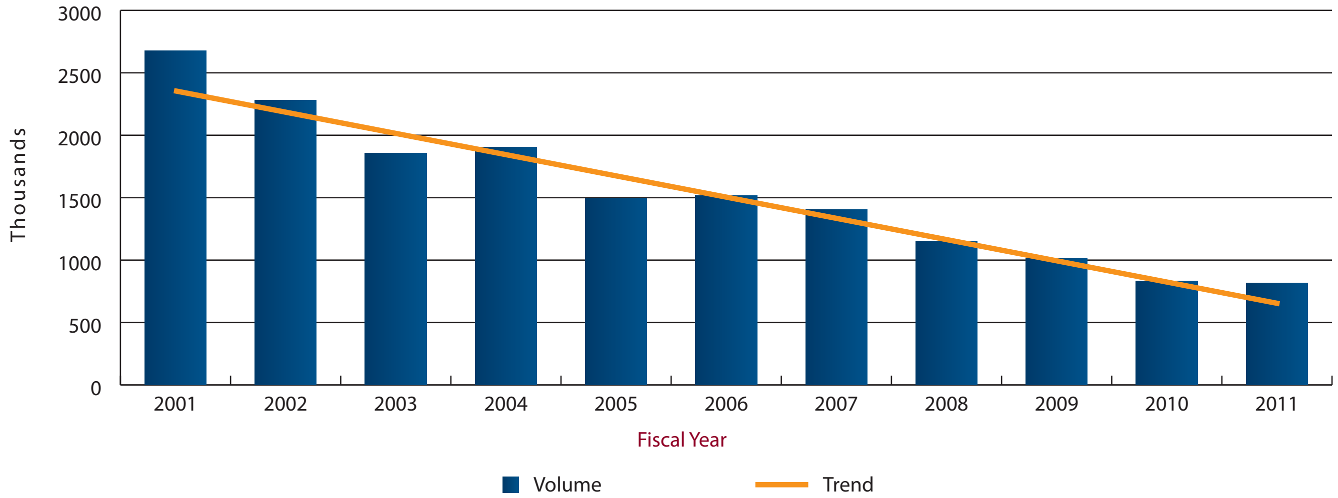
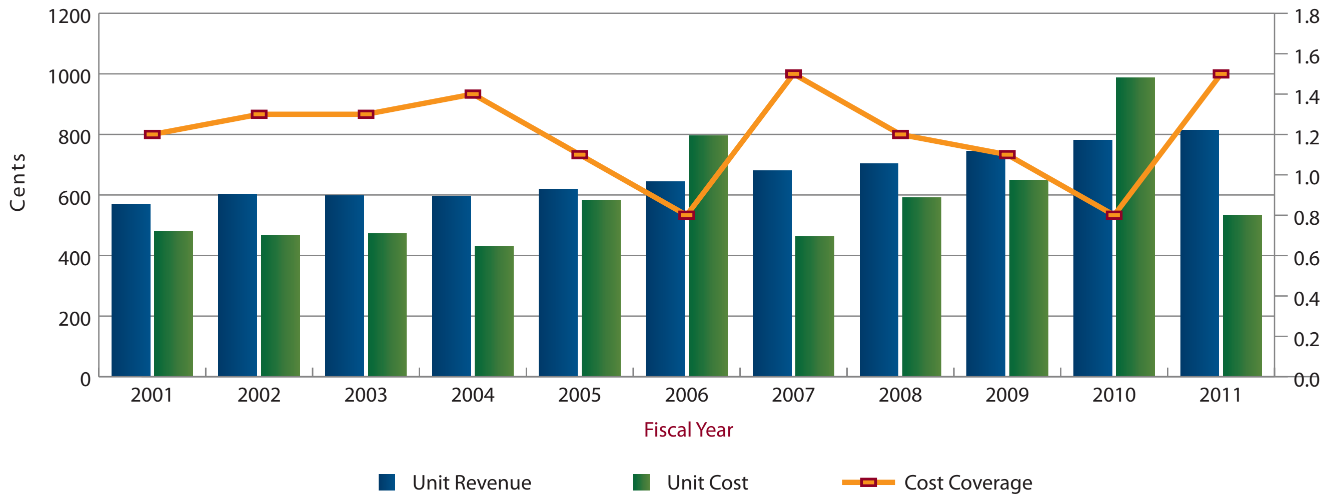


Figure VII–11
Collect On Delivery Unit Revenue, Unit Cost, and Cost Coverage Comparison FY 2001–2011



declined. As Figure VII–11 shows, the cost coverage for COD remains volatile. The COD unit revenue increased 245.4 cents (or 43.1 percent) between FY 2001 and FY 2011.[39]

Due to the variability of COD cost estimates as well as the declining volume, in the FY 2010 ACD, the Commission recommended that the Postal Service consider using a moving average to calculate COD's attributable costs, or investigate sampling alternatives. 2010 ACD at 125. The Postal Service continued to calculate COD attributable costs as it has in the past.

Stand-Alone Special Services

The eight products that comprise the stand-alone Special Services are Address Management Services, Caller Service and Reserve Number, Change of Address Credit Card Authorization, Confirm Service, Customized Postage, Money Orders, Post Office Box

[39] 2011 ACR at 42; *See also* 2010 ACD at 125.

Service and Stamp Fulfillment Services. Only one product, Stamp Fulfillment Services, did not generate enough revenue to cover its attributable costs. Each of the other seven stand-alone Special Services products satisfied the applicable provisions of chapter 36 of title 39.

Address Management Services

The AMS consists of 34 services that enable bulk business mailers to better manage the quality of their mailing lists. The Commission added AMS to the market dominant product list in 2010.[40] Accordingly, this is the second year that the Postal Service has identified the costs for the AMS product. In FY 2011, AMS generated $16.4 million in revenue, a decline of 9.3 percent from FY 2010 revenue.[41] AMS incurred $10.1 million in attributable costs in FY 2011, a decline of 53.2 percent from FY 2010 costs. As a result, product cost coverage for FY 2011 was 162.4 percent, 78.6 percentage points higher than the FY 2010 cost coverage. The Postal Service reports that it subsequently discovered that some of the cost elements submitted in the 2010 ACR were erroneously included.[42] The Postal Service reported that approximately 63 percent of the revenue decline from FY 2010 to FY 2011 is attributable to exceptional non-recurring revenue received as a result of billing changes made to one of the addressing service vendors in FY 2010 as well as a non-recurring settlement collection for a revenue assurance issue. The remaining revenue decrease was due to FY 2011 sales declines. The Postal Service reports that it expects some improvement in revenues for its addressing products when the economy improves, however, the Postal Service does not expect a repeat of the exceptional revenue received in FY 2010.[43]

Caller Service

The Caller Service product is a premium service available to customers who require more than free carrier service or who receive mail in volumes greater than what can be delivered to the largest installed post office box at a postal facility. Customers who use this service pick up their mail at a post office call window or loading dock.

In FY 2011, Caller Service earned $92.2 million in revenue and incurred $27.8 million in attributable costs. The product contributed $64.4 million toward institutional costs and had a cost coverage of 331.7 percent.

Change-of-Address Credit Card Authentication

The Change-of-Address Credit Card Authentication product allows customers to file change-of-address requests online and over the telephone. The Postal Service charges a $1 fee to verify the customer's identity and has an agreement with a credit card vendor to manage the Change-of-Address program. This is the third year that the CRA has isolated cost data for the Change of Address Credit Card Authentication product.

In FY 2011, the Postal Service processed 12.1 million Internet and telephone Change-of-Address applications, collectively, generating $12.1 million in revenue and incurring $1.2 million in attributable costs.[44] However, the Postal Service earned only a portion of this revenue as some revenue was

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40 Docket No. MC2009-19, Order No. 391, Order Approving Addition of Postal Services to the Mail Classification Schedule Product Lists, January 13, 2010.

41 In February 2011, the Commission approved an AMS product price increase of 1.69 percent. *See* Docket No. R2011-2, Order No. 675, Order Revising Postal Service Market Dominant Price Adjustments, February 16, 2011 at 53.

42 Postal Service Response to CHIR No. 1, question 20.

43 *Id.*

44 Postal Service library reference USPS-FY11-1. *See also*, 2011 ACR at 43.

retained by the credit card vendor.[45] As a result, the Postal Service indicates that the cost coverage for the Change-of-Address Credit Card Authentication product does not equal the revenue divided by the attributable cost figure. Rather than provide revenue data, the Postal Service supplemented its filing by providing a non-public library reference that showed the actual revenue earned by the product (once the portion of the revenue paid to the third party vendor is removed) and the costs it incurred in FY 2011.[46] Based on a review of the non-public library reference, the Commission finds that the revenues for Change-of-Address Credit Card Authentication covered its attributable costs in FY 2011.

Change-of-Address Credit Card Authorization revenues and volumes are reported in the Public CRA and Billing Determinants. However, the revenues and volumes are not reported in the Postal Service's Revenue, Pieces and Weight report (RPW).[47] *The Commission recommends that the Postal Service update the RPW to include the revenues and volumes for the Change of Address Authorization product.*

Confirm

Confirm consists of four subscription tiers that allow business mailers to receive scan (tracking) data about mailpieces.[48]

In FY 2011, Confirm earned $3.0 million in revenue and incurred $1.1 million in costs. The product contributed $1.9 million towards institutional costs and had a cost coverage of 276.4 percent. From FY 2010 to FY 2011, the cost coverage of Confirm service increased by 35.9 percentage points. In Docket No. R2012-3, the Postal Service reported that it intends to discontinue Confirm service once the subscriptions of existing customers expire.[49] A similar service will become a feature of the mail classes that use an IMb containing a Mailer Identification (MID) code registered to receive scan data.[50]

Customized Postage

For a fee, the Customized Postage product authorizes vendors to produce stamps bearing customer-provided images or logos.[51]

In FY 2011, Customized Postage earned $900,000 in revenue and incurred costs of $50,000. The product contributed $850,000 towards institutional costs and had a cost coverage of 1,800.0 percent. The revenues, attributable costs, and cost coverage for Customized Postage reported in the FY 2011 ACR are identical to those reported in the FY 2010 ACD.[52]

Money Orders

The Money Order product enables customers to purchase an instrument for the payment of a specified sum of money. A customer may purchase a domestic postal Money Order up to a maximum value of $1,000.

In FY 2011, Money Orders generated $172.7 million in revenue and incurred attributable costs of $123.4 million. Money Orders contributed $49.3 million towards institutional costs and had a cost coverage of 139.9 percent, a drop of a 5.1

45 2011 ACR at 45.
46 *See* Library Reference USPS-FY11-NP26, Excel file, "COACreditCard2011.xls."
47 2011 ACR at 8, Docket No. ACR2011, library reserve, USPS-LR-11-4 and USPS-LR-11-1.
48 Mailers can subscribe to the Bronze, Gold, Silver and Platinum tiers and may purchase additional IDs which allow mailers to receive scan data for their clients.
49 Docket No. R2012-3, United States Postal Service Notice of Market-Dominant Price Adjustment, October 18, 2011, at 27.
50 *Id.*
51 2011 ACR at 46.
52 *See* 2010 ACD at 124; library reference PRC-ACR 2011-NP-LR1.

percentage points from FY 2010.[53] In FY 2011, Money Orders unit revenue increased by 0.7 percent, however, the unit attributable cost for Money Orders increased 4.4 percent.

Post Office Boxes

The Post Office Box (P.O. Box) product enables customers to rent a locked receptacle and to receive mail during specified hours of access. P.O. Boxes are available in five different sizes and are assigned to one of eight Fee Groups (1-7 and E), seven of which are priced according to the market value of the postal facilities.[54] The Fee Groups determine the price that a customer must pay to rent a P.O. Box. The most expensive P.O. Boxes are in Fee Group 1 and the least expensive P.O. Boxes are in Fee Group 7.

On July 29, 2011, the Commission approved the Postal Service's request to transfer P.O. Box Service at approximately 6,800 locations from the market dominant product list to the competitive product list.[55] The 6,800 P.O. Box locations were transferred to the competitive product list in January 2012, with new rates taking effect on January 22, 2012.[56] In addition, the Postal Service added, to its competitive P.O. Box Service, rates for three-month P.O. Box rentals for each of the seven fee groups and for each of the five box sizes.

On June 9, 2011, the Commission approved the Postal Service's request to treat the attributable costs for Group E P.O. Boxes as institutional rather than attributable to P.O. Box Service.[57] The Postal Service indicates that the institutionalization of the costs of the Group E P.O. Boxes, plus a decline in facility related expenses such as depreciation, caused market dominant P.O. Box costs to decline from $674.9 million in FY 2010 to $592.8 million in FY 2011.[58]

In FY 2011, P.O. Boxes generated $801.9 million in revenue and incurred $592.8 million in costs. The P.O. Boxes product contributed $209.1 million towards institutional costs and had a cost coverage of 135.3 percent.

Stamp Fulfillment Services

The Stamp Fulfillment Services product provides shipping and handling for all orders placed by mail, phone, fax, or online by customers to Stamp Fulfillment Services in Kansas City, Missouri.[59] Orders mailed to domestic destinations are charged a $1.00 handling fee, plus an additional $2.00 for customized orders.[60] Orders mailed to non-domestic destinations are charged a $6.00 handling fee, plus an additional $2.00 for customized orders. On January 22, 2012, Stamp Fulfillment Service rates increased. For orders mailed to domestic destinations, the handling fee increased to $1.25 for orders up to $50.00 and to $1.75 for orders greater than $50.00. For orders mailed to non-domestic destinations, the handling fee increased to $6.25 for

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53 2010 ACD at 124. *See also* library reference PRC-ACR2011-LR1.

54 Fee Group E is offered free-of-charge to customers where the Postal Service does not provide carrier delivery.

55 Docket No. MC2011-25, Order No. 780, Order Approving Request to Transfer Additional Post Office Box Service Locations to the Competitive Product List, July 29, 2011, at 1,14. Request of the United States Postal Service to Transfer Post Office Box Service in Selected Locations to the Competitive Product List at 1; and Postal Bulletin 22328 (1-12-12) 13.

56 Docket No. CP2012-2, Order No. 1062, Order Approving Changes in Rates of General Applicability for Competitive Products, December 21, 2011, at 1. Letter to the Hon. Shoshana M. Grove, December 29, 2011. The Postal Service did not request that any Group E boxes be transferred.

57 Docket No. RM2011-9, Order Concerning Analytical Principles Used in Periodic Reporting (Proposal One), June 9, 2011 (Order No. 744) at 4.

58 ACR 2011 at 46.

59 The Stamp Fulfillment Services center handles orders for stamps and two nonpostal services: Philatelic sales and Officially Licensed Retail Products.

60 A custom order is a stamp order in a configuration other than those listed in the USPS Philatelic catalog.

orders up to $50.00 and to $6.75 for orders greater than $50.00. [61]

In FY 2011, Stamp Fulfillment Services generated $3.1 million in revenue and incurred $5.2 million in attributable costs. Stamp Fulfillment contributed a negative $2.1 million toward the institutional costs of the Postal Service and had a cost coverage of 59.7 percent, which is 6.6 percentage points higher than the FY 2010 cost coverage. However, the Postal Service indicated that by implementing large price increases (42.1 percent) for Stamp Fulfillment Services, on January 22, 2012, it expects significant improvements to the product's cost coverage.[62]

As noted above, the CRA includes nonpostal philatelic sales revenue and costs with Stamp Fulfillment Services revenues and costs. The Postal Service indicated that its best estimate is that revenue from combined orders could be allocated 90 percent to stamps, 5 percent to philatelic sales and 5 percent to combined orders while costs from combined orders could be allocated 80 percent to stamps, 15 percent to philatelic sales and 5 percent to combined orders that include both Stamps and Philatelic items.[63] Based on this estimate, FY 2011 revenue for Stamp Fulfillment Services and Philatelic Sales products are $2,954,491 and $171,954 respectively, and costs for Stamp Fulfillment Services and Philatelic Sales products are $4,400,360 and $838,164, respectively."[64] Therefore, the Commission finds that Stamp Fulfillment Services failed to cover its attributable costs in FY 2011. However, given the relatively large rate increase that the Postal Service implemented in January 2012, the Commission concludes that no further action is required.

In order for the RPW report to correctly identify all postal product revenue and volumes, the Commission recommends the Postal Service report revenues and volumes for Stamp Fulfillment Services in the FY 2012 RPW. In addition, as the Commission's FY 2010 ACD noted, the revenue and costs associated with Philatelic sales should not be included with Stamp Fulfillment Services in the CRA.[65] *The Commission recommends the Postal Service report the revenues and costs for Stamp Fulfillment Services and Philatelic sales in the CRA.*

Market Dominant International Products

Introduction

Market dominant international mail consists of six products: Outbound Single-Piece First-Class Mail International, Inbound Single-Piece First-Class Mail International (at UPU rates), Inbound Surface Parcel Post (at UPU rates), International Ancillary Services, International Reply Coupon Service, and International Business Reply Mail Service.

The Postal Service establishes rates and fees of general applicability for Outbound Single-Piece First-Class Mail International, outbound services within the International Ancillary Services product, International Reply Coupon Service, and International Business Reply Mail Service pursuant to the provisions of 39 U.S.C. 3622.[66] For Inbound Single-Piece First-

61 Docket No. R2012-3, library reference PRC-R2012-3-LR5.
62 Docket No. R2012-3, Order No. 987, Order on Price Adjustments for Market Dominant Products and Related mail Classification Changes, November 22, 2011, at 45.
63 Postal Service Response to CHIR 2, question 3.
64 *Id.*

65 2010 ACD at 152.
66 Rates and fees of general applicability in effect during FY 2011 for market dominant international mail products were announced by the Postal Service in United States Postal Service Notice of Market Dominant Price Adjustment, Docket No. R2009-2, February 10,

Class Mail International, Inbound Surface Parcel Post (at UPU rates), and inbound services within the International Ancillary Services product, rates are determined by international agreement through the Universal Postal Union (UPU).[67] The Postal Service also establishes rates and fees for inbound international mail through Negotiated Service Agreements with foreign postal operators.

The principal findings for FY 2011 for market dominant international mail are:[68]

- Revenues exceeded attributable costs for market dominant international products, including Negotiated Service Agreements, by $184.3 million—a decrease of 34.8 percent compared to FY 2010;
- Revenues exceeded attributable costs for the Outbound Single-Piece First-Class Mail International and Inbound Surface Parcel Post (at UPU rates) products by $209.6 million and $13.5 million, respectively;
- Revenues for Inbound Single-Piece First-Class Mail International did not cover attributable costs by $33.0 million;
- Revenues for International Ancillary Services did not exceed attributable costs by $6.1 million because Inbound Registered Mail service failed to cover attributable costs by $13.9 million.
- Revenues for inbound international products consisting of Negotiated Service Agreements exceeded attributable costs by $3.4 million.

The section below presents a financial analysis of market dominant international mail products featuring rates and fees of general applicability. It is followed by a discussion of the Quality of Service Link to Terminal Dues system and market dominant international products consisting of Negotiated Service Agreements.

Market Dominant International Products with Rates of General Applicability

Outbound Single-Piece First-Class Mail International (FCMI) and International Ancillary Services showed a decrease in contribution over FY 2010. Only Inbound Surface Parcel Post (at UPU rates) increased its contribution compared to FY 2010. For Inbound Single-Piece First-Class Mail (at UPU rates), revenues remained below attributable costs, although the loss in contribution was less than in FY 2010. Each of these products is discussed below.

Outbound Single-Piece First-Class Mail International

Outbound Single-Piece First-Class Mail International is the largest source of market dominant international mail contribution, amounting to $209.6 million in FY 2011. The cost coverage was 147.8 percent. Compared to FY 2010, the contribution for Outbound Single-Piece First-Class Mail International decreased by 36.0 percent and the cost coverage decreased 42.4 percentage points.

2009 (implemented May 11, 2009), and United States Postal Service Notice of Market Dominant Price Adjustment, Docket No. R2011-2, January 13, 2011 (implemented April 17, 2011.

67 The Universal Postal Union is a United Nations technical agency through which international treaties governing the exchange of international mail, including the rates, are negotiated among its 192 members. The United States is a member of the UPU.

68 Unless stated otherwise, this section analyzes revenues and expenses for international mail products developed according to the "booked" accounting method. The use of booked revenues and expenses ensures that the Commission's financial analyses are consistent with the Postal Service's audited financial statements. The Postal Service also uses "imputed" revenues, reported in the FY 2011 ICRA, for purposes of analyzing inbound international mail. Imputed revenues differ from booked revenues reported in the Postal Service's financial statements and the Revenue, Pieces and Weight (RPW) report, During FY 2010, the Postal Service implemented the Foreign Post Settlement (FPS) system, a new method for estimating revenue, pieces and weights for inbound international mail presented in the RPW and ICRA. The FPS system will replace both the booked and imputed methods.

The decrease in Outbound Single-Piece First-Class Mail International contribution is largely caused by a decrease in contribution from Outbound Single-Piece FCMI to Canada. For the first time since enactment of the PAEA, outbound FCMI to Canada reported a loss in contribution during FY 2011. The Postal Service explains that decreases in transportation and non-transportation costs were offset by settlement costs which increased between FY 2010 and FY 2011 under the booked methodology. Response to CHIR No. 1, question 37. This increase reflects "adjustments for overpayments of prior years' provisional [settlement] payments" in FY 2010. *Id.* According to the Postal Service, these accounting adjustments resulted in a "lower FY 2010 base" and, by comparison, higher settlement costs in FY 2011. *Id.* In contrast to the booked method, "there are no adjustments [for overpayments of provisional settlement payments] for prior years' in the Imputed version of the ICRA." Response to CHIR No. 3, question 6(e).

Nevertheless, outbound FCMI to Canada under the imputed method also reported a loss in contribution during FY 2011. In response to an inquiry, the Postal Service states that under the imputed method Outbound Single-Piece First-Class Mail International as a whole provided positive contribution to the Postal Service of which the loss from outbound FCMI to Canada was a small portion.[69] The Postal Service also states that prices for outbound FCMI to Canada were increased in FY 2011 and were designed to be compensatory over a full fiscal year. *Id.* However, FY 2011 prices were not in effect for the entire fiscal year. *Id.* Given the Postal Service's flexibility to set rates for Outbound Single-Piece First-Class Mail International to Canada, the Commission finds the loss in contribution for such mail to be problematic.

Inbound Single-Piece First-Class Mail International

Inbound Single-Piece First-Class Mail International consists of inbound "letterpost" sent from foreign postal operators for delivery in the U.S.[70] Foreign postal operators remunerate the Postal Service for the delivery of inbound letterpost at UPU terminal dues rates or negotiated rates established in bilateral or multilateral agreements.

The Postal Service presents financial results for four products under the heading Inbound Single-Piece First-Class Mail International. One product is Inbound Single-Piece First-Class Mail International (at UPU rates), which consists of inbound letterpost subject to UPU terminal dues rates. The other three products consist of one or more Negotiated Service Agreements with foreign postal operators.[71] These products feature negotiated rates for inbound letterpost from Canada and a number of other countries.

For FY 2011, attributable costs exceeded revenues for Inbound Single-Piece First-Class Mail International as a whole by $33.0 million.[72] The resulting

[69] Response to CHIR No. 4, question 8 (non-public).

[70] The term "letterpost" is the name given to international mail that is not classified as Parcel Post or Express Mail (EMS). Also known as LC/AO mail (*i.e.*, letters and cards, and all other, including flats and small packets), letterpost consists of mail similar to domestic First-Class Mail, Periodicals, Standard Mail, Bound Printed Matter, and Media/Library Mail, weighing up to 4.4 pounds (2.0 kilograms).

[71] The three products are 1) Canada Post United States Postal Service Contractual Bilateral Agreement for Inbound Market Dominant Services, 2) the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1, and 3) Global Direct Entry with Foreign Postal Administrations. Although not listed on the market dominant product list, Global Direct Entry with Foreign Postal Administrations is treated as a product for purposes of this analysis.

[72] The Commission relies on revenues presented in the RPW report, which are consistent with the Postal Service's audited financial statements. In the RPW, the Postal Service reported revenues for Inbound Single-Piece First-Class Mail International that include revenues from the Inbound Single-Piece First-Class Mail International (at UPU rates) product and the other three products consisting of

cost coverage is 86.8 percent, an increase from 79.4 percent in FY 2010. An analysis of Inbound Single-Piece First-Class Mail International (at UPU rates) follows. In the section titled Market Dominant International Products Consisting of Negotiated Service Agreements (below), a discussion of the other three products is presented.

The reported loss for Inbound Single-Piece First-Class Mail (at UPU rates) was $36.1 million for FY 2011.[73] This represents a smaller negative contribution compared to FY 2010. The cost coverage also improved to 79.0 percent in FY 2011 from 77.3 percent in FY 2010.

Despite the improvement in cost coverage, the Postal Service states that the "UPU per item and per kilogram terminal dues rates were . . . not based upon USPS costs" and, therefore, did not generate sufficient revenues to cover costs in FY 2011. FY 2011 ACR at 18. In addition, terminal dues rates are set according to a formula that is renegotiated in the UPU once every four years. Thus, the Postal Service does not "independently determine [the] prices [paid by foreign postal operators] for delivering foreign origin mail" in the U.S. *Id.*

The Commission recognizes that the current formula used to derive terminal dues rates is non-compensatory for inbound letterpost entering the U.S. Moreover, the current UPU terminal dues rates will remain in effect through 2013, with modest annual increases. As a result, the current terminal dues rates will continue to adversely affect the financial performance of Inbound Single-Piece First-Class Mail International (at non-UPU rates) in the immediate future.

During the past several years the United States has played an active role in the UPU seeking ways to develop a more compensatory terminal dues formula for inbound letterpost to be implemented in 2014. In this regard, the Commission has provided its views and technical expertise to assist the Department of State in assessing the financial impact of terminal dues proposals considered by the UPU.

The Commission recommends that the Postal Service, in coordination with the Department of State, which has lead responsibility for formulating international postal policy, continue efforts to negotiate more compensatory terminal dues rates in the UPU Terminal Dues Group and pursue adoption of the most compensatory rates possible at the 2012 UPU Congress.

Pursuant to the UPU Convention, the Postal Service (or any postal administration) may negotiate bilateral (or multilateral) rate agreements with other postal operators as an alternative to the UPU terminal dues rates for some or all of its inbound letterpost. In this regard, the Postal Service negotiated terminal dues rates applicable to inbound letterpost in bilateral agreements concluded with Canada Post, Post NL (Netherlands), the China Post Group, and Hong Kong Post that were effective in FY 2011.[74] In addition to

NSAs. By contrast, the costs reported for Inbound Single-Piece First-Class Mail International included only the costs of the Inbound Single-Piece First-Class Mail International (at UPU) product. In its financial analysis, the Commission adjusts the costs of Inbound Single-Piece First-Class Mail International in order to match costs with the revenues of the three inbound NSA products. *See* Library Reference PRC-ACR2011-NP-LR1 - FY 2011 Postal Service's Product Finances (Non-public), Excel file 11 Summary_NPLR1.xls.

[73] Public Cost and Revenue Analysis, Fiscal Year 2011, Library Reference USPS-LR-FY11-1, Excel file FY11PublicCRA.xls, worksheet tab Cost1.

[74] *See* PRC Order No. 375, Order Concerning Bilateral Agreement with Canada Post for Inbound Market Dominant Services, Docket Nos. MC2010-12 and R2010-2, December 30, 2009; PRC Order No. 549, Order Adding Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 to the Market Dominant

these agreements, the Postal Service more recently concluded bilateral agreements with Singapore Post and Australia Post.[75] These agreements, approved by the Commission, will be effective in FY 2012.

The Commission commends the Postal Service for its successful negotiation of these two additional bilateral agreements. It also notes with favor the Postal Service's "strategy for improving the total inbound cost coverage via bilateral agreements with some of its larger exchange partners in the upcoming calendar year." 2011 ACR at 18. *The Commission recommends that the Postal Service continue efforts to negotiate additional compensatory bilateral (or multilateral) agreements with foreign postal operators in the upcoming fiscal year, particularly with its largest exchange partners.*

Inbound Surface Parcel Post (at UPU Rates)

During FY 2011, revenues from Inbound Surface Parcel Post (at UPU rates) exceeded attributable costs by $13.5 million, resulting in a cost coverage of 226.1 percent. Both contribution and cost coverage for Inbound Surface Parcel Post (at UPU rates) increased compared to FY 2010.

International Ancillary Services

For FY 2011, attributable costs exceeded revenues from International Ancillary Services by $6.1 million, resulting in cost coverage of 84.3 percent.[76] This stands in marked contrast to FY 2010 when International Ancillary Services produced $1.5 million in contribution and cost coverage of 105.5 percent. The Postal Service states that the negative contribution for the International Ancillary Services product is "fully attributable to inbound registered mail." 2011 ACR at 44. For FY 2011, Inbound Registered Mail costs exceeded revenues by $13.9 million—a significant increase compared to the loss of $6.2 million reported in FY 2010.

The increase in negative contribution of Inbound Registered Mail resulted from cost increases in customer service "finance numbers." Response to CHIR No. 3, question 4(b). The Postal Service also cites changes in operating procedures and, as a result, the need to review "IOCS encirclement rules" used to assign operating costs to Inbound Registered Mail. Response to CHIR No. 1, question 35(b). The Postal Service cautions that such rules "should be updated before concluding that inbound Registered [Mail] does not cover costs." Response to CHIR No. 3, question 4(b). The Postal Service contemplates requesting "a rulemaking if a revision to the encirclement rules is deemed appropriate." Response to CHIR No. 1, question 35(b).

The Commission understands that revenues received by the Postal Service for handling Inbound Registered Mail are constrained by fixed rates of reimbursement established pursuant to the UPU Convention. These rates are renegotiated by UPU-member countries once every four years. In this regard, the Commission notes that the UPU is working to improve reimbursement rates for handling Inbound Registered Mail and that

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Product List and Approving Included Agreements, Docket Nos. MC2010-35, R2010-5 and R 2010-6, September 30, 2010; and, PRC Order No. 1058, Order Approving Request to Include Hong Kong Post Group Bilateral Agreement Within an Existing Market Dominant Product, Docket No. R2012-4, December 20, 2011.

75 *See* Notice of United States Postal Service of Type 2 Rate Adjustment, and Notice of Filing Functionally Equivalent Agreement, Docket No. R2012-1, October 14, 2011 (Singapore Post); *see* also Notice of United States Postal Service of Type 2 Rate Adjustment, and Notice of Filing Functionally Equivalent Agreement, Docket No. R2012-2, October 14, 2011 (Australia Post).

76 The International Ancillary Services product consists of the following special services: Certificate of Mailing, Registered Mail, Inbound Registered Mail, Return Receipt, Inbound Return Receipt, Restricted Delivery, Inbound Restricted Delivery, and Customs Clearance and Delivery Fee (Inbound).

a minimal increase was implemented by the UPU in 2011. *The Commission therefore recommends that the Postal Service work within the UPU to ensure a more compensatory increase in rates for Inbound Registered Mail during the 2012 UPU Congress.*

International Reply Coupon Service and International Business Reply Mail Service

International Reply Coupon Service permits a mailer of outbound letterpost to prepay the postage for a reply by purchasing reply coupons from the Postal Service that are exchangeable for postage stamps by foreign postal operators located in member countries of the UPU. International Business Reply Mail Service allows a business mailer to include within its outbound mail envelops and cards that are deposited with and returned by foreign postal operators through the Postal Service to the business mailer in the U.S. without the prepayment of postage. Instead, postage and fees for these inbound envelops and cards (*i.e.*, letterpost) are collected at delivery from the business mailer.

For FY 2011, International Reply Coupon Service and International Business Reply Mail Service each generated $0.2 million in revenue. 2011 ACR at 45. However, the Postal Service states that the ICRA does not report costs for either service. *Id.* at 45-46. In the case of International Reply Coupon Service, cost data are not separately collected for this service. Response to CHIR No. 2, question 6(a). Rather, such cost data are included in the costs reported for Inbound Single-Piece First-Class Mail International, *i.e.*, Inbound Air LC/AO. *Id.* Similarly, costs for International Business Reply Mail Service "are reported as part of the parent product, Inbound Air LC/AO." Response to CHIR No. 2, question 6(b).

The Postal Service also observes that "costs associated with two IOCS tallies for [International Business Reply Mail Service] were incorrectly encircled to domestic Ancillary Other Services." *Id.* Although the "impact is minimal," the Postal Service "will propose a change to the [IOCS] encirclement methodology to correct this." *Id.*

The Commission requests that the Postal Service report on the feasibility of providing separately reported costs for International Reply Coupon Service and International Business Reply Mail Service.

Quality of Service Link to Terminal Dues

Revenues for the delivery inbound letterpost are derived from terminal dues payments. Under the UPU's Quality Link Measurement System (QLMS), such payments are adjusted for the quality of service provided in the country of destination for inbound letterpost coming from other countries participating in the system. The UNEX system, managed by the International Post Corporation, measures the service performance of letterpost in the country of destination.[77]

As an incentive for participating in the system, the Postal Service receives an automatic 2.5 percent increase in its terminal dues payments from other participating postal operators. The Postal Service is also eligible for an additional 2.5 percent bonus payment if service performance achieves the UPU-established annual performance target. For the Postal Service, the FY 2011 target was 88 percent for inbound letterpost delivered within the domestic

[77] Located in Brussels, Belgium, the International Post Corporation works on behalf of postal administrations to improve service quality, promote cooperation and interoperability, and provide intelligence about postal and related markets. For more information, *see* www.ipc.be.

overnight, two-day, and three-day service standards for First-Class Mail.

As discussed above, terminal dues payments from UPU-member countries to the Postal Service for delivering inbound letterpost did not cover attributable costs during FY 2011. The Postal Service met the UPU quality of service target for calendar year 2010,[78] receiving a 2.5 percent bonus payment, and thereby generating a small amount of additional revenue for the first quarter (October-December 2010) of FY 2011.

Preliminary service performance scores for January through November 2011, however, generally show a notable decrease in the monthly on-time performance scores compared to the same monthly scores reported in FY 2010. This suggests that the Postal Service may not exceed the UPU quality of service target for calendar year 2011.

The Postal Service attributes this possible outcome to several factors. First, weather-related events in January, February and August 2011 adversely affected transportation and service performance. Response to CHIR No. 3, question 2. In its request to exclude test pieces used to measure service performance during these months due to *force majeure*,[79] the Postal Service reports that the UPU rejected all but a portion of the February 2011 test pieces. *Id.* The Postal Service also cites the effect of a Canada Post labor strike during June 2011 that caused Canada Post to enter, when operations resumed, "much larger volumes of mail" with the Postal Service for processing and delivery "in a shorter period of time." *Id.* In addition, the Postal Service relocated processing operations for inbound FCMI letters and flats from the New York JFK International Service Center to the Morgan Processing and Distribution Center in Manhattan, New York. *Id.* The Postal Service states such relocations, which involve changes in facility operation plans and employee reassignments and training, "often disrupt usual service performance for some period of time until the new conditions become routine." *Id.* Finally, the Postal Service observes there are "some large-volume countries" that do not participate in the Quality Link Measurement System whose inbound volumes are nevertheless included in the service measurement results. According to the Postal Service, "these countries do not adhere to the mail preparation standards necessary to support achieving the targets for the quality link to terminal dues." *Id.*

Given the effect on service performance and terminal dues revenues, *the Commission encourages the Postal Service to ensure that all inbound letterpost volumes meet the preparation requirements of, or otherwise seek means for excluding such volumes from inclusion in, the Quality Link Measurement System.*

Market Dominant International Products Consisting of Negotiated Service Agreements

The Postal Service reports financial results for two Inbound International products that are comprised of Negotiated Service Agreements. The Canada Post United States Postal Service Contractual Bilateral Agreement for Inbound Market Dominant Services and the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 products are included on the market dominant

[78] Response to CHIR No. 1, question 29(a)-(b) (non-public).
[79] *Force majeure*, literally "greater force," is often the name given to clauses in a contract or other agreement that excuse a party from performing its obligations under the contract as a result of some unforeseen event beyond the control of that party, such as war, natural disasters or other "Acts of God."

product list. In addition, the Postal Service reports financial results for Global Direct Entry with Foreign Postal Administrations. Both Inbound International products and Global Direct Entry with Foreign Postal Administrations contain rates for inbound letterpost that are established through negotiated agreements with foreign postal operators as an alternative to UPU terminal dues rates.

For FY 2011, collective revenues exceeded attributable costs of the Inbound International products and Global Direct Entry with Foreign Postal Administrations by $3.4 million and therefore provided contribution to the institutional costs of the Postal Service.[80] Each is discussed below.

Canada Post United States Postal Service Contractual Bilateral Agreement for Inbound Market Dominant Services. Revenues from terminal dues rates negotiated through the bilateral agreement with Canada Post covered attributable costs during FY 2011. These financial results represent an improvement compared to FY 2010, when inbound letterpost from Canada did not cover attributable costs. Moreover, FY 2011 is the first year since enactment of the PAEA that revenues for inbound letterpost from Canada exceeded attributable costs.

Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1. This Inbound International product is comprised of Negotiated Service Agreements with three foreign postal operators: China Post Group, Post NL (Netherlands), and Hong Kong Post. For FY 2011, revenues from terminal dues rates negotiated pursuant to these agreements collectively covered attributable costs.

[80] Public Cost and Revenue Analysis, Fiscal Year 2011, Library Reference USPS-LR-FY11-1, Excel file FY11PublicCRA.xls, worksheet tab Cost1.

However, revenues for inbound letterpost entered by Post NL did not cover attributable costs. Moreover, if inbound letterpost from Post NL had been entered at the UPU Target System terminal dues rates, the cost coverage would have been higher—albeit less than 100 percent.

In its request seeking Commission approval of the Post NL agreement, the Postal Service maintained that the negotiated rates established pursuant to this agreement would result in an improvement over the "default" UPU Target System rates that would otherwise be applicable to inbound letterpost from Post NL. The Postal Service explains that the cost coverage for the Post NL agreement did not exceed the cost coverage for inbound letterpost entered at UPU Target System rates because of an initial misestimate in the percentage of certain inbound letterpost items to be entered by Post NL.[81] The Postal Service states that it has already taken steps to improve the cost coverage of inbound letterpost entered pursuant to the Post NL agreement. *Id.*

Global Direct Entry with Foreign Postal Administrations. Global Direct Entry with Foreign Postal Administrations consists of "arrangements" with eight foreign postal operators. These arrangements permit the foreign postal operators to enter inbound letterpost bearing the indicia of the respective domestic mail classes directly with the Postal Service for delivery in the U.S. Such inbound letterpost is entered at negotiated rates. During FY 2011, inbound letterpost items entered pursuant to these arrangements were received from the postal operators of five countries: Belgium, France, Germany, Singapore, and Switzerland. Response to CHIR No. 2, question 12.

[81] Response to CHIR No. 4, question 5 (non-public).

The Postal Service notes that these largely "informal" arrangements predate Commission regulation of market dominant products pursuant to the PAEA.[82] As a result, these arrangements are not included on the market dominant product list. The Postal Service also states that during FY 2011, efforts were made to update the arrangements, and consideration was given to "including some of the arrangements in broader bilateral agreements." Response to CHIR No. 3, question 12. The Postal Service adds that it "plans to continue its efforts to formalize these arrangements in the coming fiscal year and request to add the resulting bilateral agreements to the Mail Classification Schedule." *Id.*

Based upon the FY 2011 financial results provided for the five foreign postal operators, revenues exceeded attributable costs for Global Direct Entry Contracts with Foreign Postal Administrations as a whole, thereby contributing to the institutional costs of the Postal Service. *The Commission recommends that the Postal Service act promptly to add these bilateral agreements to the market dominant product list as part of the Mail Classification Schedule.*

Market Tests

Three market dominant market tests were in effect during FY 2011: Alternate Postage Payment Method for Greeting Cards, Every Door Direct Mail (EDDM), and Mail Works Guarantee. Section 3641 authorizes the Postal Service to conduct market tests of experimental products. A product may not be tested, however, unless it satisfies each of the following conditions:

1. the product is significantly different from all products offered by the Postal Service within the two-year period preceding the start of the test (section 3641(b)(1));
2. the product will not result in undue market disruption, especially for small business concerns (section 3641(b)(2)); and
3. the product is correctly characterized as either market dominant or competitive (section 3641(b)(3)).

In addition, market tests of experimental products may not exceed 24 months (section 3641(d)), or annually exceed $10 million in revenue (section 3641(e)). The Commission may exempt a market test from the $10 million revenue limitation for certain market tests up to a $50 million annual revenue limit (section 3641(e)(2)).

None of the market dominant market tests in effect during FY 2011 exceeded 24 months in duration or exceeded the applicable statutory revenue limits.

Alternate Postage Payment Method for Greeting Cards. In Docket No. MT2011-1, the Commission authorized the Postal Service's request to conduct a 24-month market test for Alternate Postage Payment Method for Greeting Cards. This product enables individuals to mail greeting cards without affixing postage. The Commission also granted the Postal Service an exemption from the $10 million revenue limitation for this experimental market test.[83]

The Alternate Postage Payment Method for Greeting Cards market test began on or about January 1, 2011. For FY 2011, the Postal Service reports a volume of 2,978,783 Greeting Cards sold using the

[82] Response to CHIR No. 3, question 12. The Postal Service states that, "Except for Deutsche Post DHL and Swiss Post, these arrangements were entered into informally." *Id.*

[83] Docket No. MT2011-1, Order No. 617, Order Approving Market Test of Alternate Postage Payment Method for Greeting Cards, December 21, 2010. There is a $50 million annual limitation.

Alternate Postage Payment Method. The total revenue for Alternate Postage Payment Method in FY 2011 was $1,420,358. For FY 2011, the Postal Service reported $773,297 in information technology cost.

Every Door Direct Mail (EDDM). In Docket No. MT2011-3, the Commission approved the EDDM market test on March 1, 2011.[84] EDDM is restricted to locally-entered and locally-paid mail and must be delivered to every household on a delivery route. Participants are limited to sending 5,000 pieces per post office, per day. In order to make mail more accessible to small and medium businesses, the market test does not require a mailer to acquire a permit or pay mailing fees. The market test also institutes simplified qualification and preparations requirements. Pieces are priced using the Standard Mail Commercial Saturation Flats pricing schedules.

In FY 2011, the Postal Service reports that the revenue for the market test was $5.0 million and the attributable cost was $2.3 million, resulting in $2.7 million in contribution to institutional costs. The Postal Service also reports that 35 million pieces were sent under the EDDM market test. In Order No. 1164, the Commission granted the Postal Service an exception for the $10 million limitation. There is a $50 million annual limitation.

Mail Works Guarantee. In Docket No. MT2011-4, the Commission authorized the Mail Works Guarantee market test on May 15, 2011[85]. For this market test, the Postal Service and each participant jointly develop a unique set of metrics to measure the effectiveness of a particular direct mail campaign. The Postal Service plans to provide assistance to the mailer in developing its direct mail and in benchmarking and measuring the test metric. To safeguard participants, the Postal Service offers a postage back guarantee up to $250,000 per participant if a campaign fails to achieve the pre-established metric, as verified by the Postal Service.

The market test began on June 14, 2011. In FY 2011, no customers committed to using the mail in a way that would qualify for the Mail Works Guarantee. The Postal Service states that it is actively working with potential customers, and expects that some customers will begin participating in the market test soon.

Market Dominant Negotiated Service Agreements

In FY 2011, the Postal Service had three market dominant negotiated service agreements (NSAs) in effect. These agreements offer specific mailers discounts (rebates) designed to encourage higher mail volumes. The NSAs with Bradford Group (Docket No. MC2007-4) and Lifeline (Docket No. MC2007-5) were in the final year of 3-year agreements. The Postal Service implemented an agreement with Discover (Docket No. R2011-2) during FY 2011. The Commission reviews market dominant NSAs on contract years, so next year's ACD will mark the first review for the Discover NSA.

The Postal Service did not provide any discounts to Lifeline pursuant to its NSA in FY 2011 because its volume did not exceed the discount threshold.

The Bradford Group mailed 179 million pieces in contract year 3, roughly 15 million fewer pieces than the before-rates volume of 194 million pieces as forecasted by the Postal Service in Docket No. MC2007-4. However, the Bradford Group mailed

84 *See* Order No. 675.
85 *See* Order No. 730.

65.7 million Standard Mail Flats, nearly 9 million pieces above the discount threshold for Flats. The Bradford group received discounts of $114,000 in contract year 3 on nearly 9 million pieces above the discount threshold.

To assess performance under an agreement, the Commission uses the accepted methodology which incorporates contract year after-rates volume, the marginal discount earned, and the Standard Regular and ECR own-price elasticities.[86] In the second year of its 3-year agreement, the Bradford Group received $114,000 in rebates on over 9 million pieces. The Commission's analysis shows that roughly 3.5 million incremental pieces can be attributed to the rebates.[87] This implies rebates were paid on 5.2 million pieces that would have been sent without the incentive. In contract year three, the rebated mail pieces sent by the Bradford Group were a mix of Standard Mail Flats and Carrier Route Flats. The Standard Mail Flats sent by Bradford had an average contribution of negative 11.4 cents per piece, while the Carrier Route Flats had an average contribution of 6.3 cents per piece. Due to the negative per piece contribution from Standard Mail Flats, the mail mix of incentivized pieces had an average contribution of 2.2 cents per piece, before the discount. With the discount, the average contribution was 0.9 cents per piece. Due to the low contribution per piece of Standard Mail Flats, the net benefit to the Postal Service of the NSA

Table VII–23—FY 2011 Summary of NSA Net Effect on Contribution ($ in Thousands)

	FY 2009	FY 2010	FY 2011	Total
Lifeline	25	104	0	129
Bradford	93	-72	-37	-16
Total	**118**	**32**	**-37**	**113**

with Bradford Group in contract year 3 was negative $37,389.

Table VII–23 contains a summary of the net effect on the contribution to institutional costs from these two agreements.

Section 3622(c)(10) of title 39 encourages special classifications that improve the net financial position of the Postal Service or improve operational performance, while not causing competitive harm. The Bradford Group NSA is estimated to have had a minor negative effect on the net financial position of the Postal Service in FY 2011. The 3-year agreement with the Bradford Group, as a whole, also had a minor negative effect on the finances of the Postal Service.

The Commission finds the Bradford Group market dominant NSA was not consistent with 39 U.S.C.3622(c)(10) in FY 2011. However, as the agreement has concluded, there is no need for remedial action.

86 The Postal Service's estimates reflect subclasses, rather than products, that were used prior to the PAEA. Standard Regular includes the following commercial Standard Mail products: Letters. Flats, and NFMs/Parcels. ECR refers to Enhanced Carrier Route. It includes the following commercial products: Carrier Route, High Density and Saturation Letters, and High Density and Saturation Flats and Parcels.

87 The accepted methodology was developed in Docket No. MC2004-3. The 2011 Standard Mail Regular elasticity is -0.355 and the Carrier Route elasticity is -0.782, as provided in the attachment to the January 20, 2012 letter from Andrew German.

Chapter VIII

Competitive Products

Introduction

In this chapter, the Commission reviews competitive mail products, including competitive negotiated service agreements, to determine whether any rates or fees in effect during FY 2011 were not in compliance with applicable provisions of chapter 36 of title 39. The Commission's review is guided by section 3633(a) of title 39, which sets forth the legal standards applicable to rates for competitive products. Section 3633(a) directs the Commission to promulgate regulations to:

- Prohibit subsidization of competitive by market dominant products — section 3633(a)(1);
- Ensure that each competitive product covers its attributable costs — section 3633(a)(2); and
- Ensure that, collectively, competitive products cover an appropriate share of the Postal Service's institutional costs — section 3633(a)(3).

The Commission also includes an analysis of Competitive Market Tests and the Competitive Products Fund at the end of this Chapter.

The principal FY 2011 findings for competitive products are:

- Revenues for competitive products, as a whole, exceeded the incremental costs of competitive products. Thus, market dominant products did not subsidize competitive products during FY 2011, satisfying section 3633(a)(1).
- Revenues for the following three products did not cover attributable costs and thus, did not comply with section 3633(a)(2): Global Plus 2A contracts, Inbound International Expedited Services and International Money Transfer Services-Inbound. The Commission orders the Postal Service to take corrective action.

- Competitive products, collectively, contributed 7.8 percent towards the Postal Service's institutional costs, which exceeded the 5.5 percent regulatory requirement. As a result, competitive products complied with section 3633(a)(3) during FY 2011.

The list of competitive products for FY 2011 is shown in Table VIII–1.

Table VIII–1—FY 2011 Competitive Domestic and International Products

Domestic
Express Mail
Priority Mail
Parcel Select
Parcel Return Service
Address Enhancement Service
Competitive Ancillary Services
Greeting Cards and Stationery
Premium Forwarding Service
Post Office Box Service
Shipping and Mailing Supplies
Domestic Competitive NSA Products[1]

International
Outbound International Expedited Services
Outbound Priority Mail International
Inbound Air Parcel Post (at UPU rates)
International Priority Airlift (IPA)
International Surface Airlift (ISAL)
International Direct Sacks M-Bags
International Ancillary Services
International Money Transfer Service - Inbound
International Money Transfer Service - Outbound
International Competitive NSA Products[2]

[1] *See* Library Reference, USPS-FY2011-NP27 for a complete list of FY 2011 Domestic Competitive NSAs.

[2] *See* Library Reference, USPS-FY2011-NP2 for a complete list of FY 2011 International Competitive NSAs.

Table VIII–2 contains FY 2011 revenue, cost, and volume for several groupings of competitive products. Table VIII–2 shows the Commission's audited FY 2011 figures.

Although volume for competitive products, as a whole, grew by 3.8 percent in FY 2011, revenue and contribution shrunk, with aggregate contribution decreasing from $2.4 billion in FY 2010 to $2.3 billion in FY 2011. Similarly, cost coverage decreased from 138.7 percent in FY 2010 to 134.6 percent in FY 2011.

Figure VII–1 shows contribution for the last five years for selected groupings of competitive products. Priority Mail continues to be the contribution leader for competitive products, generating almost $1.2 billion in contribution. Across all products, market dominant and competitive, Priority Mail ranks fourth in contribution behind First-Class Single-Piece Letters, First-Class Presort Letters, and Standard Mail Letters.

Competitive international mail continues to do well. Although volumes for competitive international mail decreased by 9.2 million pieces in FY 2011, or 3.5 percent, contribution increased from $513 million to $569 million. The increase in contribution is due to the success of NSAs. Within competitive products, international mail's contribution ranks second. This is the third year in a row that contribution has increased.

Cross-Subsidy Provision: 3633(a)(1)

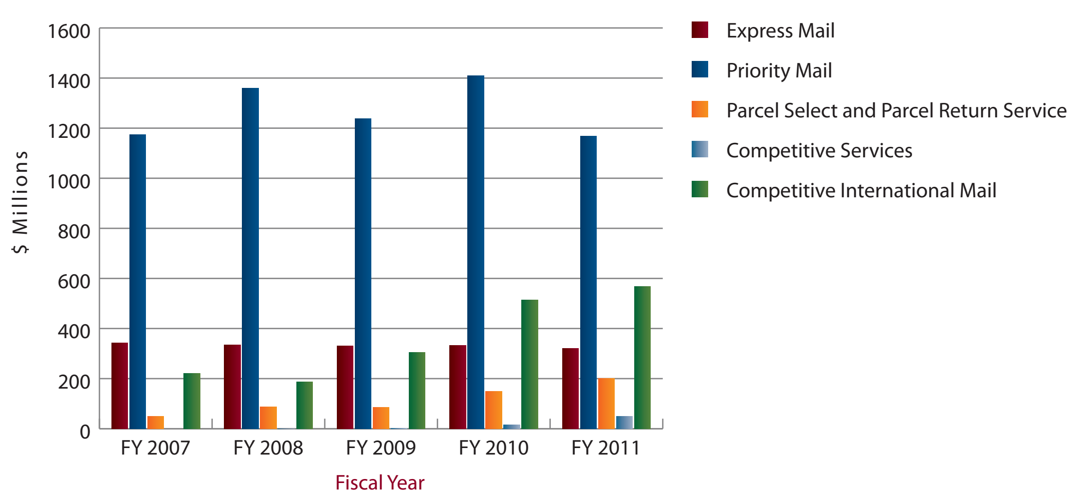
The incremental costs of the competitive products are used to test whether revenues from market dominant products cross-subsidize competitive products. In Order No. 399, the Commission approved the Postal Service's hybrid incremental cost methodology. Under this methodology, the Postal Service aggregates the following three cost categories: (1) incremental

Table VIII–2—Fiscal Year 2011 Volume, Revenue, Cost and Cost Coverage Selected Competitive Products and Competitive Product Groupings

Competitive Products	Volume (000)	Revenue ($000)	Attributable Cost ($000)	Contribution to Institutional Cost ($000)	Rev./Pc-. (Cents)	Cost/Pc. (Cents)	Contribution to Institutional Cost/Pc. (Cents)	Cost Coverage
Express Mail	40,491.995	799,500.058	479,432.267	320,067.791	1,974.464	1,184.017	790.447	166.8%
Priority Mail	790,633.182	5,638,962.796	4,469,853.934	1,169,108.862	713.221	565.351	147.870	126.2%
Parcel Select and Parcel Return Service	380,834.112	718,401.893	516,545.208	201,856.685	188.639	135.635	53.004	139.1%
Competitive International Mail	261,536.498	1,674,743.437	1,105,964.592	568,778.845	640.348	422.872	217.476	151.4%
Competitive Domestic Services[1]	83,437.960	146,646.327	101,732.142	44,914.185	175.755	121.925	53.829	144.1%
Competitive International Services[2]	2,021.239	11,687.784	6,476.146	5,211.638	578.248	320.405	257.844	180.5%
Total Competitive Mail and Services	**1,473,495.787**	**8,989,942.295**	**6,680,004.289**	**2,309,938.006**	**610.110**	**453.344**	**156.766**	**134.6%**

[1] Competitive Domestic Services include the following six products: Address Enhancement Service; Competitive Ancillary Services; Greeting Cards and Stationery; Post Office Box Service; Premium Forwarding Service; and Shipping and Mailing Supplies.
[2] Competitive International Services include the following three products: International Ancillary Services; International Money Transfer Service - Inbound; and International Money Transfer Service-Outbound.

Figure VIII–1—Competitive Products Five Year Contribution by Selected Product Groupings



costs for domestic competitive mail; (2) attributable costs for international competitive products;[1] and (3) competitive group-specific costs.

For FY 2011, the hybrid incremental cost methodology produced an incremental cost for competitive products of $6.8 billion. The total revenues for competitive products in FY 2011 were $9.0 billion. *See* Table VIII–2. Accordingly, revenues from competitive products exceed the FY 2011 hybrid incremental costs. Consequently, the Commission finds that revenues from market dominant products did not subsidize competitive products, satisfying section 3633(a)(1).

Product Cost Coverage Provision: 3633(a)(2)

Section 3633(a)(2) requires the revenues for each competitive product to cover attributable costs. Below, the Commission separately discusses the FY 2011 financial performance for the following: domestic competitive products; domestic competitive Negotiated Services Agreements; international competitive products; and international competitive Negotiated Services Agreements.

Domestic Competitive Products

In FY 2011, there were 10 domestic products featuring rates and fees of general applicability. Those products are: (1) Express Mail; (2) Priority Mail; (3) Parcel Select; (4) Parcel Return Service; (5) Address Enhancement Service; (6) Competitive Ancillary Service;[2] (7) Greeting Cards and Stationery; (8) Premium Forwarding Service; (9) Post Office Box Service; and (10) Shipping and Mailing Supplies.

In FY 2011, each domestic competitive product generated sufficient revenue to cover attributable costs. Collectively, domestic competitive products generated $7.3 billion in revenue, and incurred $5.6 billion in cost. Thus, domestic competitive products contributed $1.7 billion towards the Postal Service's institutional costs. *The Commission finds that all domestic competitive products complied with 3633(a)(2).*

Domestic Competitive Negotiated Service Agreements

For FY 2011, the Postal Service provided total volume, revenue and cost data on each Domestic Competitive Negotiated Service Agreement (NSA) that was in effect during the fiscal year. Commission rule 3050.21(g)(2) requires the Postal Service to file data with the Commission to evaluate each NSA for compliance with section 3633. *See* 39 CFR 3050.21(g)(2). FY 2011 marks the first year that the Postal Service provided NSA data sufficient to allow the Commission to evaluate each agreement.[3]

Pursuant to section 3633(a)(2), each NSA product must cover its attributable costs. There were 45 domestic competitive NSA products in effect and active during FY 2011. *The Commission has determined that each NSA covered its attributable costs and complied with the statutory requirements of section 3633(a)(2).*

[1] *See* Order Accepting Analytical Principles Used in Periodic Reporting (Proposals Twenty-Two through Twenty-Five), January 27, 2010, Proposal Twenty-Two (Order No. 399). Order No. 399 established that in lieu of incremental costs, international competitive mail would use attributable costs because incremental costs are not available for international products.

[2] Competitive Ancillary Services was the only new competitive product offered in FY 2011. *See* Docket Nos. MC2011-23 and CP2011-62, Order Approving Request to Add New Product to the Competitive Product List, March 28, 2011 (Order No. 703).

[3] The Commission commends the Postal Service for collecting and providing agreement-specific volume information for FY 2011. However, due to pricing changes throughout the year, the agreement-specific revenue data can be improved in future years by collecting volume data for each pricing period.

International Competitive Products

Competitive International mail consists of nine products featuring rates and fees of general applicability.[4] These products are: Outbound International Expedited Services, Outbound Priority Mail International, Inbound Air Parcel Post (at UPU rates), International Priority Airmail (IPA), International Surface Airlift (ISAL), International Direct Sacks-M-Bags, International Money Transfer Service — Outbound, International Money Transfer Service — Inbound, and International Ancillary Services

For FY 2011, revenues for competitive International mail products with rates of general applicability collectively covered their attributable costs and provided a contribution to the institutional costs of the Postal Service.[5] Eight competitive International mail products provided contribution to institutional costs. They include Outbound International Expedited Services, Outbound Priority Mail International, Inbound Air Parcel Post (at UPU rates), International Priority Airmail (IPA), International Surface Airlift (ISAL), International Direct Sacks-M-Bags, International Ancillary Services and International Money Transfer Service — Outbound (IMTS-Outbound).[6]

The Commission concludes that for FY 2011, each of the above-referenced competitive international mail products featuring rates of general applicability satisfy section 3633(a)(2). However, revenues did not cover the attributable costs of the International Money Transfer Service — Inbound (IMTS-Inbound) product.

International Money Transfer Service-Inbound. FY 2011 represents the first year in which the Postal Service separately reports the financial results for the IMTS-Outbound and IMTS-Inbound products in the International Cost and Revenue Analysis (ICRA) report.[7] The Postal Service observes that IMTS, considering both outbound and inbound products together, "provided a positive net contribution to the Postal Service in FY 2011."[8] Nevertheless, revenues did not cover the attributable costs of the IMTS-Inbound product. 2011 ACR at 63.

Revenues for IMTS-Inbound are derived from commissions and per-item fees received from foreign postal administrations. These commissions and fees were negotiated with 10 foreign postal administrations and formalized in agreements that

4 Rates and fees of general applicability in effect during FY 2011 for competitive International mail products were announced by the Postal Service in Docket No. CP2009-23, Notice of the United States Postal Service of Changes in Rates of General Applicability for Competitive Products Established in Governors' Decision No. 09-01, February 10, 2009 (implemented May 11, 2009); Docket No. CP2010-8, Notice of the United States Postal Service of Changes in Rates of General Applicability for Competitive Products Established in Governors' Decision No. 09-13, November 4, 2009 (implemented January 4, 2010); and, Docket No. CP2011-26, Notice of the United States Postal Service of Changes in Rates of General Applicability for Competitive Products Established in Governors' Decision No. 10-4, November 2, 2010 (implemented January 11, 2011).

5 Unless stated otherwise, this section analyzes revenues and expenses for International mail products developed according to the "booked" accounting method. The use of booked revenues and expenses ensures that the Commission's financial analyses are consistent with the Postal Service's audited financial statements. The Postal Service also uses "imputed" revenues, reported in the 2011 ICRA, for purposes of analyzing inbound international mail. Imputed revenues differ from booked revenues reported in the Postal Service's financial statements and the Revenue, Pieces and Weight (RPW) report. During FY 2010, the Postal Service implemented the Foreign Post Settlement (FPS) system, a new method for estimating revenue, pieces and weights for inbound international mail presented in the RPW and ICRA. The FPS system will replace both the booked and imputed methods.

6 The competitive International Ancillary Services product consists of the following services: Certificate of Mailing, Registered Mail, Return Receipt, Restricted Delivery, Insurance, and Customs Clearance and Delivery Fee (Inbound).

7 USPS-FY11-NP2, Excel file Reports (Booked).xls, worksheet tab A Pages (c), at page A-2. The ICRA report presents revenues, costs, and volumes for each of the Postal Service's outbound and inbound international mail products.

8 2011 ACR at 63-64. The IMTS-Outbound product features prices of general applicability for postal money orders sold by the Postal Service and cashed (or electronic transfers accessed) in foreign countries. The IMTS-Inbound product provides for Postal Service payment of foreign money orders presented at post offices in the U.S. There is no charge to the recipient for receiving payment.

pre-date the PAEA. According to the Postal Service, the Department of State has determined that these agreements are "international law agreements" and therefore "cannot be terminated or renegotiated without delegated authority." *Id.* The Postal Service "continues to pursue the authority to terminate or renegotiate these agreements." *Id.* Until that time, however, the Postal Service states "it must continue to honor the agreements." *Id.*

The Commission recognizes that these circumstances make it more difficult to improve the financial performance of the IMTS-Inbound product. For FY 2011, however, the Commission concludes that the IMTS-Inbound product did not comply with section 3633(a)(2). *The Commission orders the Postal Service to take corrective action.*

Although separately reported, the financial results for the IMTS-Inbound product do not include transaction volume. The Postal Service states that "volume data for the overall Inbound IMTS product is not available." Response to CHIR No. 3, question 5. More specifically, the Postal Service states that it "has no method for retrieving inbound IMTS product information from the non-POS-enabled offices. . . . For this reason, the Postal Service currently has no plans to use the POS [Point-of-Sale] System to determine volume data for the IMTS-Inbound product." *Id.*

The absence of transaction volume for the IMTS-Inbound product is problematic. Such transaction volume is used to calculate unit revenues and costs, which permit the Commission to evaluate and compare the year-to-year financial performance of a product.

In Docket No. RM2011-5, the Postal Service proposed to provide IMTS-Inbound transaction volume when it presented Proposal Eleven, which described the methodology to establish separate reporting of IMTS-Outbound and IMTS-Inbound financial results.[9] In Proposal Eleven, the Postal Service explained that the "Point of Sale System (POS) volume can be retrieved via back-end queries and, as a result, [the] POS volume figure will be used as IMTS-Inbound volume."[10] Moreover, Commission Order No. 724 approved Proposal Eleven with the clear understanding that transaction volume would be provided for the IMTS-Inbound product.[11] The Postal Service's announcement that it has "no plans" to use the POS System to provide IMTS-Inbound transaction volume is contrary to its statements in Docket No. RM2011-5 relied upon by the Commission.

Proposal Eleven represents the established methodology for reporting of IMTS-Outbound and IMTS-Inbound financial results—including the provision of IMTS-Inbound transaction volume. Consistent with that methodology, *the Commission directs the Postal Service to provide IMTS-Inbound transaction volumes based upon the POS system as presented in Proposal Eleven, or otherwise estimate IMTS-Inbound transaction volumes, for reporting in the Postal Service's 2012 ACR.* If the Postal Service no longer believes that Proposal Eleven is feasible, it should propose a modification by following accepted procedures, *i.e.*, initiating a rulemaking proceeding.

9 Docket No. RM2011-5, Petition of the United States Postal Service Requesting Initiation of a Proceeding to Consider Proposed Changes in Analytic Principles (Proposals Nine – Twelve), December 20, 2010, Proposal Eleven.

10 *Id.*, Proposal Eleven at 2; *see also* Docket No. RM2011-5, Response of the United States Postal Service to CHIR No. 1, question 1.

11 Docket No. RM2011-5, Order Concerning Analytical Principles for Periodic Reporting (Proposals Ten Through Twelve), at 6 (Order No. 724).

International Competitive Negotiated Service Agreements

Competitive International mail also consists of a number of products whose rates and fees are established pursuant to one or more NSAs—negotiated contracts between the Postal Service and a qualifying mailer or foreign postal operators that govern outbound or inbound international mail. Such contractual agreements often require a minimum volume and/or revenue commitment by mailers or foreign postal operators in exchange for reduced rates from the Postal Service.

In general, each International NSA or contract is classified as a separate competitive product on the competitive product list.[12] Accordingly, the Commission must evaluate each international contract classified as a separate competitive product for its consistency with section 3633(a)(2), which requires that each product cover its attributable costs. However, international contracts that exhibit similar cost or market characteristics are generally grouped together into a single product under one product heading. Such international contracts as a group are classified as the product and collectively evaluated for consistency with section 3633(a)(2).

The Postal Service reports volume, revenue and cost data on each international NSA or contract. For FY 2011, the Postal Service provides such data on 299 international NSAs, of which 282 apply to outbound mail and 17 apply to inbound mail. The financial results for competitive Outbound International and Inbound International products that consist of international contracts are separately discussed below.

[12] Docket No. RM2007-1, Order No. 43, Order Establishing Ratemaking Regulations for Market Dominant and Competitive Products, October 29, 2007, sections 2177, 3001.

Competitive Outbound International Products Consisting of Negotiated Service Agreements

Competitive Outbound International products featuring negotiated rates are classified on the competitive product list under the following product headings: Direct Entry Parcels Contracts, Global Direct Contracts, Global Expedited Package Services (GEPS) Contracts, Global Expedited Package Service Non-published Rates 2 (GEPS—NPR 2), Global Plus Contracts and Global Reseller Expedited Package Services 1 (GREPS 1). Table VIII–3 below shows the competitive Outbound International product headings and the products. In some cases, the product heading is the name of the product; in others, separate products are established under a product heading.

For FY 2011, the Postal Service reports financial results for outbound contracts under the product headings

Table VIII–3—FY 2011 Competitive Outbound International Products Grouped by Product Heading

Product Heading	Product
Direct Entry Parcels Contracts	Direct Entry Parcels 1
Global Expedited Package Services Contracts	(Same)
Global Direct Contracts	GEPS 1
	GEPS 2
	GEPS 3
Global Expedited Package Service Non-published Rates 2	(Same)
Global Plus Contracts	Global Plus 1A
	Global Plus 1B
	Global Plus 2A
	Global Plus 2B
Global Reseller Expedited Package Services 1	(Same)

Global Direct Contracts, GEPS Contracts, GEPS — NPR 2, Global Plus Contracts and GREPS 1. Based upon the data provided, 279 of the 282 outbound international contracts generated sufficient revenues to cover their attributable costs. Three contracts did not generate sufficient revenue to cover their attributable costs. Of those contracts, two are included in the Global Plus 2A product and caused revenues for that product not to exceed attributable costs. The third, a Global Plus 2B contract, did not cause a negative contribution for the Global Plus 2B product as a whole.[13] For FY 2011, the Commission concludes that with the exception of the Global Plus 2A product, all competitive Outbound International products consisting of NSAs provided contribution to the institutional costs of the Postal Service and therefore comply with section 3633(a)(2).

Global Plus 2A. Global Plus 2A contracts provide price incentives to Postal Qualified Wholesalers (PQW) and other large businesses that offer mailing services to their customers and other end users that ship mail using Global Direct (GD) and/or Global Bulk Economy (GBE). The GD service offers customers a price for mail acceptance within the United States and transportation to a foreign country. The GBE service permits customers to send outbound letter post items that are entered in bulk quantities via surface transportation to foreign countries.

The Postal Service states that during FY 2011, attributable costs exceeded revenues of the GBE service within the Global Plus 2A product. Response to CHIR No. 3, question 7. The Postal Service observes that compared to its financial models, actual "[c]osts exceeded the projected costs because international transportation and settlement expenses were greater than expected." *Id.* The Postal Service also states that prices for the GBE service have been increased for CY 2012. Moreover, the financial model supporting the CY 2012 prices show that revenues should be sufficient to cover the attributable costs of each Global Plus 2C contract—the successors to the Global Plus 2B contracts.[14]

For FY 2011, the Commission concludes that the Global Plus 2A product did not comply with section 3633(a)(2). However, the Commission notes that this is the first year in which revenues for Global Plus contracts did not cover their attributable costs. Given the Postal Service's ability to negotiate rates for Global Plus contracts and, if necessary, reject contracts that are not compensatory to the Postal Service, the Commission finds the loss in contribution for the Global Plus 2A product to be problematic. The Commission recommends that the Postal Service modify its financial models by increasing the contingency factor to accommodate unexpected changes in costs to ensure that proposed prices can generate sufficient revenues to exceed attributable costs. *The Commission orders the Postal Service to take corrective action.*

Competitive Inbound International Products Consisting of Negotiated Service Agreements

Like competitive Outbound International products, competitive Inbound International products featuring

[13] This contract is one among others within the Global Plus 2B product and therefore is not subject to Commission review for compliance with section 3633. However, because market dominant products must not subsidize competitive products, the Postal Service should not continue any competitive contract that results in a negative contribution to institutional costs.

[14] *Id.; see also* Docket Nos. MC2012-5, CP2012-10 and CP2012-11, Request of the United States Postal Service to Add Global Plus 2C to the Competitive Products List and Notice of Filing Two Functionally Equivalent Global Plus 2C Contracts Negotiated Service Agreements and Application for Non-Public Treatment of Materials Filed Under Seal, December 30, 2011.

negotiated rates are classified on the competitive product list under product headings: Inbound International Expedited Services, Inbound Air Parcel Post (at non-UPU rates), Inbound Surface Parcel Post (at non-UPU rates), Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1, Inbound Direct Entry with Foreign Postal Administrations, and International Business Reply Service Competitive Contract 1, 2 and 3. Table VIII–4 shows the competitive Inbound International product headings and the products. As with competitive Outbound International products, sometimes the product heading is also the name of the competitive Inbound International product.

For FY 2011, the Postal Service reports financial results for 17 inbound contracts under the following product headings: Inbound International Expedited Services, Inbound Air Parcel Post (at non-UPU rates), Inbound Surface Parcel Post (at non-UPU rates), Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1, Inbound Direct Entry with Foreign Postal Administrations, and International Business Reply Service. With one exception, all inbound contracts generated sufficient revenues to cover attributable costs.[15] The lone exception is the Inbound International Expedited Services 2 product.

Inbound International Expedited Services. The Postal Service has bilateral agreements with more than 180 foreign postal administrations that were concluded under the auspices of the Express Mail Service (EMS)

Table VIII–4—FY 2011Competitive Inbound International Products Grouped by Product Heading

Product Heading	Product
Inbound International Expedited Services	Inbound International Expedited Services 2
	Inbound International Expedited Services 3
	Inbound International Expedited Services 4
Inbound Air Parcel Post (at non-UPU rates)	Royal Mail Group Inbound Air Parcel Post Agreement
Inbound Surface Parcel Post (at non-UPU rates)	Canada Post-United States Postal Service Contractual Bilateral Agreement for Inbound Competitive Services
Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1	(Same)
Inbound Direct Entry Contracts with Foreign Postal Operators	Inbound Direct Entry Contracts with Foreign Postal Operators 1
International Business Reply Service Competitive Contract 1	(Same)
International Business Reply Service Competitive Contract 2	(Same)
International Business Reply Service Competitive Contract 3	(Same)

Cooperative of the Universal Postal Union (UPU). Such agreements govern the exchange and delivery of expedited inbound international mail, commonly referred to as Inbound EMS. Inbound EMS volumes that enter the U.S. pursuant to these agreements comprise the Inbound International Expedited Services 2 product. Rates for the Inbound International Expedited Services 2 product are established by the Postal Service through notice to, and publication by, the UPU.

[15] The Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 and Inbound International Expedited Services 3 products covered costs under the booked method but not under the imputed method. The Postal Service relies on imputed costs in the financial models to justify entering into these contracts. The Postal Service should modify its financial models by increasing the contingency factor to ensure that proposed prices generate sufficient revenues to cover costs under both the booked and imputed methods.

In addition, the Postal Service has separate bilateral agreements with the China Post Group and Canada Post.[16] The negotiated bilateral rates applicable to inbound EMS from China and Canada each constitute a separate product on the competitive product list. Each of these products generated sufficient revenues to cover attributable costs in FY 2011.

By contrast, in FY 2011, revenues for inbound EMS entering the United States at rates set by the Postal Service for the Inbound International Expedited Services 2 product did not cover attributable costs using either the booked or imputed accounting methods. The Postal Service states that price increases for Inbound EMS were implemented in January 2011, and that those higher prices applicable to CY 2011 were not reflected in the first quarter results of FY 2011 (October to December 2010). 2011 ACR at 64. Nevertheless, the Postal Service observes that under the booked method, the "FY 2011 improvement [in cost coverage] compared to FY 2010 is the result of a[n] [ ] increase in revenue." Response to CHIR No. 1, question 33(a). This increase in revenue was offset somewhat by increases in mail processing and domestic transportation unit costs. *Id.* Under the imputed method, however, financial results did not improve as both revenue and contribution decreased between FY 2010 and FY 2011.[17]

The Postal Service defends its CY 2011 price increase by noting that the revenue and cost estimates presented in the financial model used to support the January 2011 prices showed that sufficient revenues would be generated to cover costs and thereby satisfy the statutory pricing criteria for competitive products. 2011 ACR at 64. Responding to an inquiry seeking an explanation as to the difference between the FY 2011 actual results and the projected financial performance presented in its financial models supporting both the CY 2010 and CY 2011 prices that were in effect during FY 2011, the Postal Service confirms that the financial models were "based upon 'imputed' revenues and expenses." Response to CHIR No. 1, question 34. However, it discusses only the financial model underlying the CY 2011 prices, which "were only in place for the last three quarters of FY 2011." *Id.*

The Postal Service notes that the financial model "used the FY09 ICRA as the basis for projecting costs into the CY 2011 time period." *Id.* After updating the original financial model with FY 2011 data from the ICRA for the first three quarters of CY 2011 and projecting the last quarter of CY 2011 using the latest inflation factors plus a contingency factor, the Postal Service observes: "Although higher than anticipated costs exacerbated the [difference between projected and actual performance,] lower than projected volume, weight and resulting revenue were the major causes of the difference . . ." *Id.*

[16] *See* Docket Nos. MC2010-13 and CP 2010-12, Request to Add Inbound Expedited Services 1 to the Competitive Product List, and Notice of United States Postal Service of Filing China Post Group—United States Postal Service Contractual Bilateral Agreement (Under Seal), November 20, 2009. In approving the Postal Service's request, the Commission designated the new product Inbound International Expedited Services 3. Docket Nos. MC2010-13 and CP 2010-12, Order No. 365, Order Adding Inbound International Expedited Services 3 to the Competitive Product List, December 22, 2009, at 1.; *see also* Docket Nos. MC2010-37 and CP2010-126, Request to Add Inbound International Expedited Services 4 to the Competitive Product List, and Notice of United States Postal Service of Filing Canada Post – United States Postal Service Contractual Bilateral Agreement (Under Seal), September 30, 2010.

[17] *Compare* USPS-FY11-NP2, Excel file Reports.xls, worksheet tabs A-Pages (c) and Pivot3, and Library Reference PRC-ACR2010-NP-LR3 (Nonpublic), Excel file PRC-ACR2010-NP-LR3_Imputed ICRA.xls, worksheet tab China IB EMS.

The Postal Service asserts that it is addressing the financial performance of Inbound EMS by "again raising Inbound International Expedited Services 2 rates." 2011 ACR at 64. These new rates became effective in January 2012, "and are expected to contribute to an improved cost coverage for this product in FY 2012." Response to CHIR No. 1, question 33(a). Moreover, "[i]n the future, the Postal Service will consider additional price increases and will attempt to make improvements to cost coverage through bilateral agreements with foreign postal operators." *Id.*

The Postal Service is responsible for setting inbound EMS rates annually, which are then implemented on a calendar year basis rather than on a fiscal year basis. FY 2011 represents the second fiscal year in which revenues for the Inbound International Expedited Services 2 product did not cover attributable costs using either the booked or imputed methods. The Postal Service asserts that new prices for CY 2012 will have the effect of improving the cost coverage of this inbound EMS product. It made a similar claim for the CY 2011 prices. While the CY 2012 price increases may improve cost coverage, the Commission is less optimistic that revenue generated from such prices will exceed attributable costs for FY 2012. The Postal Service's financial models showing that the calendar year prices in effect during the past two fiscal years will cover attributable costs are not reflected in the actual financial performance.

For FY 2011, the Commission concludes that the Inbound International Expedited Services 2 product did not comply with section 3633(a)(2). The Postal Service needs to ensure that Inbound EMS rates cover attributable costs for the entire fiscal year. The Postal Service could negotiate separate bilateral agreements with foreign postal operators that will generate a positive cost coverage for Inbound EMS. In the alternative, the Commission recommends that in future financial models the Postal Service increase the cost contingency factor used for setting Inbound International Expedited Services 2 rates, or set such rates so that the cost coverage on Inbound EMS from each country covers costs. *The Commission orders the Postal Service to take corrective action.*

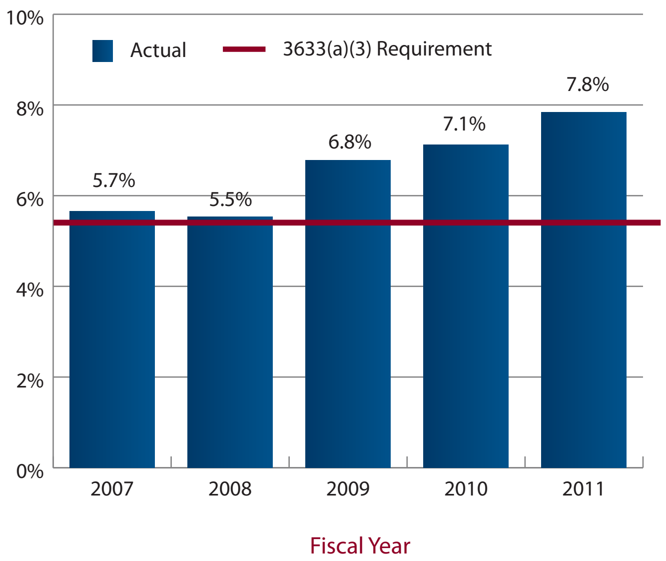
Appropriate Contribution Provision: 3633(a)(3)

Section 3633(a)(3) requires the Commission to ensure that all competitive products collectively cover what the Commission determines to be an appropriate share of the institutional costs of the Postal Service. In implementing section 3633(a)(3), the Commission established regulations stating that if competitive products contributed at least 5.5 percent towards the Postal Service's institutional costs, then competitive products, as a whole, would recover an appropriate share of the Postal Service's total institutional costs. *See* 39 CFR 3015.7(c).

In FY 2011, the Postal Service reported total institutional costs for all products to be $29.6 billion. Therefore, in order to comply with 3633(a)(3) for FY 2011, competitive products must contribute at least $1.6 billion towards the Postal Service's institutional costs. As Table VIII–2 shows, in FY 2011, the total competitive products contribution, as a whole, towards institutional costs was $2.3 billion – 7.8 percent of the Postal Service's total institutional costs. *Therefore, the Commission finds that in FY 2011, competitive products satisfied 3633(a)(3) by recovering an appropriate share of the Postal Service's institutional costs.*

Section 3633(b) requires the Commission to review the minimum contribution requirement 5 years after the date of enactment of the PAEA, and every subsequent 5 years, to determine whether the contribution requirement should be retained in its current form, modified, or eliminated. In Docket No. RM2012-3, the Commission initiated its first 5-year review of the minimum contribution that competitive products should be required to make towards the Postal Service's institutional costs.[18] Figure VIII–2 displays the competitive products contribution as a percentage of the Postal Service's institutional costs for FY 2007 – FY 2011.

Figure VIII–2
Competitive Products
Contribution to Institutional Cost



Competitive Market Tests

Section 3641 authorizes the Postal Service to "conduct market tests of experimental products in accordance with this section." A product may not be tested, however, unless it satisfies each of the following conditions:

- The product is significantly different from all products offered by the Postal Service within the 2-year period preceding the start of the test (section 3641(b)(1));
- The product will not result in undue market disruption, especially for small business concerns (section 3641(b)(2)); and
- The product is correctly characterized as either market dominant or competitive (section 3641(b)(3)).

In addition, market tests of experimental products may not exceed 24 months (section 3641(d)), or exceed $10 million in annual revenue (section 3641(e)).

There were two competitive market tests in effect during FY 2011: Collaborative Logistics and Gift Cards. Each market test is discussed below.

Collaborative Logistics. In Docket No. MT2009-1, the Commission authorized the Collaborative Logistics market test, which was the first market test under the PAEA[19] Under the Collaborative Logistics market test, the Postal Service sold available space within its transportation network. The Postal Service defined the experiment as "transportation of an article or multiple articles on a pallet or other unit load, on a space-available basis, in postal transportation." *Id.* at 3. The Postal Service recently informed the Commission

[18] *See* Docket No. RM 2012-3, Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, January 6, 2012 (Order No. 1108).

[19] Docket No. MT2009-1, Order Concerning Collaborative Logistics Market Test, May 7, 2009 (Order No. 211).

that the Collaborative Logistics market test ended on September 19, 2011.[20]

In FY 2011, the Collaborative Logistics market test earned $2,278,674 in revenue. 2011 ACR at 66. The Postal Service provided a total cost figure under seal for Collaborative Logistics in USPS-FY10-NP27. The audited revenue figure presented by the Postal Service is greater than the cost figure presented under seal, demonstrating that Collaborative Logistics provided a contribution to institutional costs in FY 2011.

Gift Cards. In Docket No. MT2011-2, the Commission authorized the Postal Service's request to conduct a 24-month market test for a new competitive product, Gift Cards.[21] Under the market test, customers may purchase two types of gift cards: fixed and variable. Fixed gift cards are available in amounts of $25 or $50. Variable gift cards are available in amounts ranging between $25 and $100. The market test was launched in June 2011 at 2,000 retail locations that currently sell greeting cards. In its request, the Postal Service stated that it intended to expand the market test to up to a total of 3,000 locations, including locations without greeting cards, by October 2011.[22]

In FY 2011, the Gift Cards market test earned $96,012 in revenue and incurred $20,489 in total costs. FY 2011 ACR at 66. Thus, the Gift Cards provided a contribution to institutional costs of $75,523 in FY 2011.

Commission analysis. The costs associated with both market test have been added to the group specific cost category to ensure competitive products as a whole are in compliance with section 3633(a)(1). *The Commission finds that the Collaborative Logistics and Gift Cards market tests made contributions to institutional costs in FY 2011.*

Competitive Products Fund

The Competitive Products Fund was created by 39 U.S.C. 2011 to deposit receipts from competitive products revenues, returns on investments and other amounts directly associated with the competitive products enterprise. It is a revolving fund and can be used for withdrawals within mandated limits for the payment of costs attributable to competitive products. The Postal Service has filed all of the competitive products financial statements as required under Commission rules 3060.20 and 3060.30 as Library Reference USPS-FY11-39.

The fund balance in the Postal Service Competitive Products Fund after September 30, 2011 stands at $1.1 billion. Table VIII–5 shows the income and fund balance data for the competitive products.

Table VIII–5—FY 2011 Competitive Products Income and Fund Balance

Fiscal Year	Investment Income ($000)	Pre Tax Income ($000)	Income Tax ($000)	Balance in Competitive Products Fund[1] ($000)
2008	0	14,386	4,935	9,451
2009	2	368,228	128,880	248,801
2010	198	549,407	192,292	606,114
2011	290	691,131	240,896	1,055,639

1 The balance of the Competitive Products Fund held within the U.S. Treasury and listed in Table III-Detail of Treasury Securities Outstanding, January 31, 2012 of the Monthly Statement of Public Debt.

20 *See* Docket No. MT 2009-1,Notice of The United States Postal Service of Termination of Market Test, August 19, 2011.

21 Docket No. MT2011-2, Order Authorizing Gift Card Market Test, April 28, 2011 (Order No. 721).

22 *See id.* at 4. *See also Postal Bulletin* No. 22324, November 17, 2011, at 7, which shows that the Postal Service carried out its intention to expand its gift cards market test. Gift Cards are now available at approximately 5,000 locations. *Id.*

The FY 2011 competitive products income statement shows total net income from competitive products before tax was $691.1 million, an increase of $141.7 million over FY 2010. The assumed Federal Income Tax on these earnings was $241.9 million. This amount was transferred to the Postal Service Fund on January 15, 2012 as required by 39 U.S.C. 3634(b).

Chapter IX

Nonpostal Services

Introduction

In Docket No. MC2008-1, the Commission authorized 14 nonpostal services to continue.[1] Of these, 2 were designated as market dominant and 12 were designated as competitive. *Id.* The two market dominant services are: (1) MoverSource; and (2) Philatelic Sales. *Id.* The 12 competitive services are: (1) Affiliates for Website; (2) Affiliates–Other (Linking Only); (3) Electronic Postmark; (4) FedEx Drop Boxes; (5) Licensing Programs Other than Officially Licensed Retail Products; (6) Metered Manufacturers Marketing Program; (7) Non-Sale Lease Agreements (Non-Government); (8) Officially Licensed Retail Products (OLRP); (9) Passport Photo Service; (10) Photocopying Service; (11) Training Facilities (in part); and (12) Warranty Repair Program. *Id.*

FY 2011 Financial Analysis

Commission rule 3050.21(i) requires the Postal Service to report revenues, volumes, and expenses for nonpostal services. In its 2011 ACR, the Postal Service reported financial data for the two market dominant nonpostal services in the public portion of its report. 2011 ACR at 67. The Postal Service reported financial data for 10 of the 12 competitive nonpostal services in a non-public annex.[2] In the non-public annex, the Postal Service explained why there is no FY 2011 financial data for two competitive nonpostal services, Metered Manufacturers Marketing Program and Warranty Repair.[3]

[1] *See* Docket No. MC2008-1, Review of Nonpostal Services Under the Postal Accountability and Enhancement Act, December 19, 2008 (Order No. 154). *See also* Docket No. MC2008-1, Errata Notice, January 9, 2009.

[2] *See* Library Reference USPS-FY11-NP27, 2011 Competitive NSA and Nonpostal Materials.

[3] *See* the non-public annex for more information concerning why the Postal Service did not provide financial data on Metered Manufacturers Marketing Program and Warranty Repair.

As Table IX–1 shows, in FY 2011, nonpostal services generated $172.7 million in revenue and incurred $31.7 million in expenses, which resulted in a net income of $141.0 million. Market dominant nonpostal services produced $51.2 million in net income and competitive nonpostal services produced $89.8 million in net income.

The non-public financial data show that two services, Philatelic Sales and Electronic Postmark, failed to generate sufficient revenues to cover expenses. *See* 2011 ACR at 67-68; Library Reference USPS-FY11-NP27. With respect to Philatelic Sales, the Postal Service explains that the revenue and expense estimates reflect fulfillment orders only. Response to CHIR No. 2, question 9. The Postal Service asserts the added revenues and expenses for the actual sales of philatelic items would show that there is no shortfall. *Id.* In addition, the Postal Service notes that on January 22, 2012, it substantially increased fees for fulfilling philatelic orders. *Id.* With respect to the Electronic Postmark service, the Postal Service states that the service did not generate sales in FY 2011. *Id.* However, the Postal Service explains that even when no sales occur, there are costs associated with maintaining the Electronic Postmark service. *Id.* The Postal Service further states that it expects to have new Electronic Postmark sales in the future that would help cover costs. *Id.*

Similar to last year's ACD observations, the Commission noticed instances where nonpostal services were included with Special Services. In the 2011 CRA, the revenues, volumes, and costs for Philatelic Sales were included with the Stamp Fulfillment Services (SFS) product. Also, the non-public RPW and the Competitive billing determinants identified Officially Licensed Retail Product as a Competitive Special Service. *In subsequent ACR filings, the Postal Service's CRA, RPW, and billing determinants should not include nonpostal services with postal services.* Including the financial data for nonpostal services with postal products distorts the financial performance of the postal products. For example, when reviewing SFS's financial data in the FY 2011 CRA, it appears that the revenue and attributable cost are $3.1 million and $5.2 million, respectively. However, the actual SFS revenue and attributable costs are $3.0 million and $4.4 million, respectively.

Table IX–1—FY 2011 Volumes, Revenue, Expenses, and Net Income Nonpostal Services

Market Dominant Nonpostal Services	Volume	Revenue	Expenses	Net Income (Loss)
MoverSource	NA	$53,664,715	$1,790,445	$51,874,270
Philatelic Sales	173,144	$171,954	$838,164	($666,210)
Total Market Dominant Nonpostal Services	173,144	$53,836,669	$2,628,609	$51,208,060
Total Competitive Nonpostal Services[1]	28,857,214	$118,872,899	$29,086,619	$89,786,280
Total Nonpostal Services	29,030,358	$172,709,568	$31,715,228	$140,994,340

[1] Does not include financial data for Metered Manufacturers Marketing Program and Warranty Repair Program.

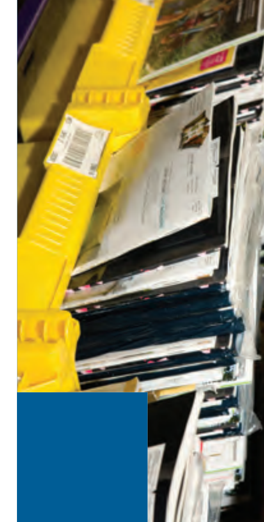
Appendix A

Financial Results Under Previous Classification

This appendix presents Postal Service financial results for FY 2011 using the mail classification system in place prior to the passage of the PAEA. Prior to the PAEA, mail classes were subdivided into subclasses, and the financial reports reflected that organization. The PAEA uses the term product, defined as "a postal service with a distinct cost or market characteristic for which a rate or rates are, or may reasonably be applied." 39 U.S.C. 102(6). Within classes, the Postal Service reports data by product, not by subclass. To facilitate historical comparisons, Table A–1 presents volumes, revenues, attributable costs, and contribution to institutional cost using the former classification scheme of subclasses.

Table A–1—Fiscal Year 2011 Volume , Revenue, Cost and Cost Coverage by Class Previous Classification (Subclasses)

	Volume (000)	Revenue ($000)	Attributable Cost ($000)	Contribution to Institutional Cost ($000)	Rev./Pc. (Cents)	Cost/Pc. (Cents)	Contribution to Institutional Cost/Pc. (Cents)	Cost Coverage
Competitive Mail								
Express Mail	40,492	799,500	479,432	320,068	1,974.464	1,184.017	790.447	166.8%
Priority Mail	790,633	5,638,963	4,469,854	1,169,109	713.221	565.351	147.870	126.2%
Parcel Select and Parcel Return Service (PRS)	380,834	718,402	516,545	201,857	188.639	135.635	53.004	139.1%
Competitive International Mail	261,531	1,674,743	1,105,965	568,779	640.362	422.881	217.481	151.4%
Competitive Domestic Services	83,407	146,646	101,732	44,914	175.820	121.971	53.849	144.1%
Competitive International Services	2,021	11,688	6,476	5,212	578.248	320.405	257.844	180.5%
Total Competitive Mail and Services	**1,473,490**	**8,989,942**	**6,680,004**	**2,309,938**	**610.112**	**453.346**	**156.766**	**134.6%**
Market Dominant Mail								
First-Class Mail								
Letters, Flats & Parcels	69,160,461	30,329,597	14,926,941	15,402,656	43.854	21.583	22.271	203.2%
Cards	4,049,704	983,926	556,666	427,260	24.296	13.746	10.550	176.8%
Standard Mail								
Regular	47,001,679	11,358,500	7,403,012	3,955,488	24.166	15.751	8.416	153.4%
Nonprofit	11,243,376	1,574,384	1,795,701	(221,317)	14.003	15.971	(1.968)	87.7%
Regular and Nonprofit	58,245,055	12,932,884	9,198,713	3,734,171	22.204	15.793	6.411	140.6%
Enhanced Carrier Route (ECR)	24,298,722	4,655,881	2,638,793	2,017,088	19.161	10.860	8.301	176.4%
Nonprofit ECR	2,147,482	237,385	240,805	(3,420)	11.054	11.213	(0.159)	98.6%
ECR and NECR	26,446,204	4,893,266	2,879,598	2,013,668	18.503	10.889	7.614	169.9%
Periodicals								
Within County	661,561	69,966	89,250	(19,283)	10.576	13.491	(2.915)	78.4%
Outside County	6,415,178	1,751,169	2,340,774	(589,605)	27.297	36.488	(9.191)	74.8%



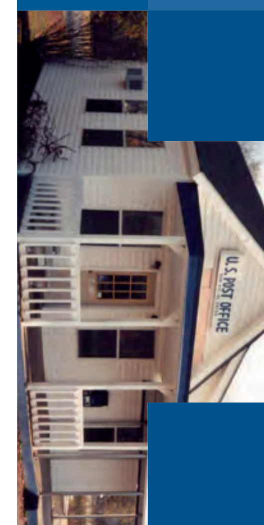


Table A–1—Fiscal Year 2011 Volume , Revenue, Cost and Cost Coverage by Class Previous Classification (Subclasses)—Continued

	Volume (000)	Revenue ($000)	Attributable Cost ($000)	Contribution to Institutional Cost ($000)	Rev./Pc. (Cents)	Cost/Pc. (Cents)	Contribution to Institutional Cost/Pc. (Cents)	Cost Coverage
Package Services								
Single-Piece Parcel Post	70,218	732,901	821,119	(88,217)	1,043.754	1,169.388	(125.634)	89.3%
Bound Printed Matter	497,113	515,798	439,979	75,819	103.759	88.507	15.252	117.2%
Media Mail	100,565	311,743			309.990			
Market Dominant International Mail	7,263	20,865			287.259			
Total Market Dominant Mail	**107,829**	**332,607**	**431,068**	**(98,460)**	**308.459**	**399.771**	**(91.312)**	**77.2%**
Market Dominant Services	434,596							
Certified Mail	61,854		51,111	(51,111)		82.631		
COD	311,104	889,433	698,999	190,435	285.896	224.683	61.213	127.2%
Insurance	**166,460,877**	**53,431,549**	**32,434,216**	**20,997,333**	**32.099**	**19.485**	**12.614**	**164.7%**
Registered Mail								
Stamped Envelopes	251,222	**708,755**	**599,328**	**109,428**	**282.123**	**238.565**	**43.558**	**118.3%**
Stamped Cards	819	6,678	4,373	2,304	814.927	533.710	281.218	152.7%
Money Orders	34,573	116,652	103,411	13,241	337.406	299.109	38.297	112.8%
Post Office Box Service	2,688	45,236	42,809	2,427	1,682.930	1,592.633	90.297	105.7%
Caller Service		10,650	6,886	3,764				154.7%
Other Special Services		1,611	820	791				196.5%
International Services	115,510	172,696	123,438	49,258	149.508	106.864	42.644	139.9%
Other Income		801,899	592,763	209,135				135.3%
International Services	1,845	32,707	38,811	(6,104)				**84.3%**
Other Income		397,737		397,737				
Total Mail and Services	**167,934,367**	**65,615,560**	**41,251,803**	**24,363,757**	**39.072**	**24.564**	**14.508**	**159.1%**
Institutional Costs			29,553,781					
Appropriations: Revenue Forgone		95,285						
Investment Income		28,167						
Total Revenues		**65,739,012**						
Total Costs			**70,805,584**					
Net Income (Loss)		(5,066,572)						

Source: Library Reference PRC-ACR2011-LR1


U.S. POST OFFICE

Appendix B

Methodology Changes

In FY 2011, the Postal Service filed six petitions to change analytical principles relating to its periodic reports. A summary of the proposed changes and the Commission's analysis and findings are provided below. The Postal Service also filed a petition to change analytical principles early in FY 2012 containing two proposals which it used in constructing the ACR. The Commission approved those proposals on January 20, 2012 (*See* Order No. 1153). For this reason, these two proposals are also discussed in this appendix.

RM2011-5: Proposal 9

The Postal Service proposed seven changes to the First-Class Mail presort letters and Standard Mail presort letters mail processing cost models. The changes related to the following items: (1) automation density table; (2) manual density table; (3) post office box destination percentage; (4) plant carrier route finalization percentage; (5) manual incoming secondary and post office box walling productivities; (6) remote barcode system leakage rate; and (7) bundle sorting cost methodology.

Automation density table. The Postal Service proposed to modify the automation density table by incorporating the assumption that no presort letters flow from outgoing sorting operations to the incoming secondary operation. These tables show the percentage of mail that flows from one operation to another.

The Postal Service explained that it can usually identify the class of letter mail that it has processed to a particular sort level (*e.g.*, First-Class Mail), but cannot identify the specific product within that class (*e.g.*, single-piece or presort). Instead of directly measuring what proportion of letter mail that it has processed to a particular sort level was entered as single-piece or presort, the Postal Service proposed to incorporate the assumption that the presort letter volume finalized to the 5-Digit level in all outgoing operations is zero into the First-Class Mail presort letters and Standard Mail presort letters automation density tables.

The Postal Service further explained that regulations limit a presort First-Class Mail mailing to one overflow tray, that 90 percent of outgoing First-Class Mail letter volume is single-piece, and that a large portion of single-piece mail is turnaround mail that goes straight to an incoming secondary sort. For this reason, it concluded that little First-Class Mail letter mail flowing from outgoing operations directly into incoming secondary operations is presorted mail.

The Commission agreed with the Postal Service that this change is likely to improve the accuracy of the letter cost avoidance models and approved it.

Manual density table. The Postal Service proposed to replace the density values for the manual outgoing primary operation (MODS operation number 030) and for the manual outgoing secondary and manual incoming managed mail program (MMP) operations (MODS operation numbers 040 and 043, respectively).

As with the Automation Density Table, the Postal Service proposed to incorporate an assumption that the percentage of presorted letter mail flowing from the outgoing primary operation to the secondary 5-Digit level is zero.

The Postal Service conducted two special studies of the density of manual letter mail flows, one in 2008 and one in 2010. According to the Postal Service, for both studies the density figures provided by the plants were distorted by the presence of substantial quantities of single-piece mail.

For the manual outgoing secondary and incoming MMP operations, the Postal Service was unable to obtain robust data. Thus, instead it used destinating Origin Destination Information System (ODIS) data for First-Class Mail presort letters and Standard Mail presort letters to estimate the density values for the manual outgoing secondary operation.

The Postal Service explained that the letter cases in the manual outgoing secondary operation will typically distribute mail to the plant level only. Consequently, the next operation for this mail is either an incoming MMP operation or an incoming sectional center facility (SCF)/primary operation.

The Postal Service reviewed the August 2010 webMODS reports for each plant and assembled a list of plants that maintained both a manual incoming MMP operation and a manual incoming SCF primary operation. When calculating the manual outgoing primary density values, the Postal Service assumed the next operation for a given plant would be the incoming MMP operation if that plant maintained a manual MMP operation and served multiple plants, or if that plant was not an area distribution center (ADC) but was served by an ADC plant that maintained a manual MMP operation. For the remaining plants, the Postal Service assumed the next operation would be the incoming SCF/primary operation.

The Postal Service also developed new manual incoming MMP density estimates using destinating ODIS data. Given the lack of direct data available from the plants, these estimates were developed using system wide plant-specific ODIS data combined with information about which plants were on the MMP list.

The Commission found that these results were an improvement to previous densities which relied on the less representative 1999 study. Accordingly, the Commission accepted the proposed changes to manual densities.

Post office box destination percentage. The Postal Service proposed to update the estimate of letter

volume that is delivered to post office boxes. However, the ODIS data on which the former estimates were based are no longer available; so the Postal Service used Carrier Piece Count (CPC) data instead. The Postal Service estimated the percentage of post office box mail by dividing the CPC post office box volume by the total Revenue, Pieces and Weight System (RPW) letter volume excluding First-Class Mail and Standard Mail non-machinable letters, Standard Mail saturation letters, and Standard Mail high-density letters. Proposal Nine at 6-7.

The Public Representative found it reasonable to use CPC data for this purpose; but he questioned the reasonableness of using data from a different data system (RPW machine volume) as the denominator. PR Comments at 3. In consideration of this issue, the Postal Service provided an estimate of the post office box percentage using total CPC volume in the denominator.

The Commission found that ratio developed using CPC volume in the denominator was preferable to using data from different data systems. Consequently, the Commission approved the proposed methodology change with a modification—using CPC volume data in place of RPW volume data.

Plant carrier route finalization percentage. The Postal Service proposed to reduce the plant carrier route finalization percentage to zero. It explained that manual incoming secondary distribution has been decentralized from the plants and moved to the delivery units for all shapes of mail. Consequently, it concluded that only plants that essentially house delivery units have manual incoming secondary operations. While this change resulted in a significant reduction of the plant carrier route finalization percentage in the presort letters mail processing cost models, the Postal Service contended that this reflects current operations.

The Commission found that the proposed reduction of the plant carrier route finalization percentage to zero improves the accuracy of the cost models. While the assumption that it is zero may understate the actual percentage of letters manually finalized at plants, the understatement is likely less than 1 percent. Thus, the Commission accepted the use of a zero assumption.

Manual incoming secondary and post office box walling productivities. The Postal Service conducted a field study during the summer and fall of FY 2010 to update the following productivity values: the manual incoming secondary productivity performed at delivery units, the post office box Delivery Point Sequence (DPS) "walling"[1] productivity, and the post office box non-DPS "walling" productivity.

The Commission found that the data contained a wide range of observed productivities, which when combined with a relatively small sample size, raised serious concerns about the representativeness of the study's results. Since there were no changes in the equipment or methods used for these operations since the 1995 study that formed the basis of the accepted methodology, there were no compelling reasons incorporate these uncertain results. For these reasons, the Commission denied the proposed modification.

Remote barcode system leakage rate. "Leakage rate" refers to the percentage of mail not retrieved from the Remote Encoding process. This occurs when the computer system is down or the processing window is closed. This results in mailpiece being sorted manually.

1 "Walling" is a term that refers to the placement of mailpieces into post office boxes.

The Postal Service proposed to use the Operations leakage target of 5 percent in the presort letter mail processing cost models. The Postal Service claimed that measuring leakage has become difficult due to changes in the Postal Service's data collection systems. The Postal Service had used this method previously in Docket No. R2000-1.

The Commission found that the Postal Service had not provided adequate support for its proposal. Historical leakage rates provided by the Postal Service showed, with the exception of a single accounting period in 1999 that the leakage rate remained in excess of 5 percent. Thus, the Commission denied the use of the 5 percent Operations leakage target.

Bundle sorting cost methodology. The Postal Service proposed a new bundle sorting methodology to be used in the mail processing cost models to reflect the operational changes that have occurred since the last time letter bundle costs were modeled. The Postal Service explained that only a small percentage of letters is now entered as bundles and, consequently, bundle sorting operations that are used exclusively to process letter bundles are rare. The Postal Service maintained that letter bundles are typically either processed with flats bundles or are processed in manual piece distribution operations.

The proposed methodology incorporates revised figures for the number of bundle handlings, bundle sorting cost estimates based on piece distribution models, and an updated productivity for manually sorting bundles. Because the modification reflects the significant operational changes in bundle sorting described by the Postal Service, the Commission accepted the proposal.

RM2011-5: Proposal Ten

The Postal Service proposed to modify the assignment of clerk and mailhandler labor costs of Inbound International mail to the three country groups (*i.e.*, Canada, Industrialized Countries, and Developing Countries) within the In-Office Cost System (IOCS) so that normal downstream Cost and Revenue Analysis (CRA) and International Cost and Revenue Analysis (ICRA) processes can automatically distribute costs to those country groups using a methodology that is consistent with other mail products. This proposal extends proposal six in Docket No. RM2010-12 to incorporate the methodology change of using results of the mail processing model within the ICRA.

Prior to the FY 2010, the assignment of such costs to country groups was implemented using only direct mailpiece tally data from the IOCS data system. This approach ignored the impact of downstream computer processing steps that distribute mixed mail and allied costs back to products based on factors such as cost pools, container types and shape.

In approving Proposal Ten, the Commission concluded that this proposed change represented an improvement in the assignment of mail processing costs for Inbound International Mail. The Proposal Ten methodology was incorporated into the ICRA beginning with FY 2010. *See* Order No. 724.

RM2011–5: Proposal Eleven

The Postal Service proposed a methodology to report volumes, revenues, and attributable costs separately for International Money Transfer Service (IMTS)-Inbound and IMTS-Outbound products in the ICRA report. The Postal Service noted that its proposal responded to the Commission's 2010 Annual Compliance Determination recommendation that the

Postal Service develop a way to report separate results for the two products.

The Commission approved the Postal Service's proposal, noting that it was a reasonable method for identifying revenues and volumes for IMTS-Inbound and IMTS-Outbound products, as well as distributing total IMTS attributable costs between both products. However, because the attributable costs are based, in part, on only a few IOCS tallies, the Commission expressed concerns about the reliability of the resulting unit cost estimates for the two products. Accordingly, the Commission recommended that the Postal Service investigate a way to provide reliable attributable cost estimates for the IMTS-Inbound and IMTS-Outbound products. The methodology was incorporated into the 2011 ACR. *See* Order No. 724.

RM2011-5: Proposal Twelve

The Postal Service proposed to develop alternative data inputs to the Media Mail/Library Mail mail processing cost model, the Bound Printed Matter (BPM) transportation cost model and the Bulk Parcel Return Service (BPRS) cost model. Alternative data were necessary because the intra-NDC and inter-NDC data from single-piece Parcel Post were no longer available after the single-piece Parcel Post rate structure was redesigned in Docket No. R2009-2.

The Media/Library Mail mail processing cost model relied on intra-NDC and inter-NDC volume distributions. The Postal Service suggested replacing the former proxy with the assumption that volume in zones 1, 2, and 3 of single-piece Parcel Post was a good approximation of intra-NDC volume, and the remaining volume was inter-NDC volume.

The BPM transportation cost model used single-piece Parcel Post zone related percentages. As an alternative, the Postal Service suggested using the zone-related percentages found in cost segment 14.3.

The BPRS cost model used transportation leg and cost data from the previous Parcel Post model. As an alternative, the Postal Service suggested using similar data from the Standard Mail destination entry cost model (USPS-FY09-13).

The Commission approved Proposal Twelve and found that the Postal Service's proposed data input replacements were reasonable and had a minimal impact on the effected cost models. In addition, the Commission modified the cost pool allocation methodology for Media/Library Mail consistent with the general approach used in Docket No. R2006-1 (with respect to letter mail processing), and was applied to parcels in Docket No. RM2012-12 (Proposal Seven) and RM2011-6 (Proposal Thirteen). *See* Order No. 724.

RM2011-6: Proposal Thirteen

The Postal Service proposed to develop a new Parcel Select/Parcel Return Service (PRS) mail processing cost model. The proposed model reflected the current Parcel Select and PRS products, as well as updated productivity estimates developed in Docket No. RM2011-5, Proposal Seven. The proposed model also reflected an assumption that all mailer-entered parcels are submitted in containers and are no longer bedloaded. The Commission approved Proposal Thirteen, but modified the cost pool allocation methodology to be consistent with the general approach used in Docket No. R2006-1 (with respect to letter mail processing), and was applied to parcels in Docket No. RM2012-12 (Proposal Seven). *See* Order No. 719.

RM2011-6: Proposal Fourteen

The Postal Service proposed five modifications to the Parcel Select/PRS transportation cost model: (1) the transportation cost estimates should only be presented for the current price categories; (2) the transportation legs for the non-dropship price categories should be estimated using 2010 PostalOne! data; (3) the official RPW volumes should be incorporated into the analysis; (4) the PRS transportation costs should be distributed using the same method that is relied upon to distribute the Parcel Select transportation costs; and (5) a new methodology should be used to estimate the return network distribution center (RNDC) cubic foot miles by zone.

The Commission found that the proposed model was an improvement over the previous model because it better reflected the current Parcel Select and PRS products. The Commission approved Proposal Fourteen. *See* Order No. 719.

RM2011-9: Proposal One

The Postal Service proposed to treat the costs associated with Fee Group E Post Office Box service (Group E) as institutional rather than as part of the attributable costs of the Post Office Box service product. The Postal Service explained that Group E service offers one post office box at no charge to any customer ineligible for carrier delivery. In addition, the Postal Service explained that it views Group E service as a universal service obligation. For this reason, it argued that the attributable cost of these boxes should be borne by all mailers rather than P.O. Box users only.

The Commission approved the Postal Service's proposal and it was implemented in the 2011 ACR. *See* Order No. 744. In approving the proposal, the Commission noted that the proposed change in analytical methods corrects the inequity of Group E attributable costs being borne solely by other post office box holders.

RM2011-10: Proposal Two

The Postal Service sought approval of four changes to competitive Negotiate Service Agreements (NSAs) cost models. First, the Postal Service proposed to modify the Priority Mail NSA cost model to exclude mail processing costs associated with handling retail Priority Mail pieces. The Postal Service explained that Priority Mail NSA pieces are entered in bulk at Postal Service plants, and thus, bypass mail processing operations at retail post offices. Second, the Postal Service proposed to modify the Priority Mail and Parcel Select – PRS NSA models to incorporate applicable CRA D-Report adjustments for Priority Mail, Parcel Select, and PRS.[2] Third, the Postal Service proposed to modify the Priority Mail NSA cost model to align the model's Alaska Air transportation component with its applicable C-Report adjustment.[3] Fourth, the Postal Service proposed to modify the Parcel Select – PRS NSA model to distribute the "Other" costs category on a per-piece basis, rather than proportional to mail processing, transportation, and delivery costs.

The Commission accepted the four modifications and they were implemented in the 2011 ACR. *See* Order No. 751. In approving the proposal, the Commission concluded that the modifications would improve the cost models by reflecting current business and costing practices.

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[2] There are six reports, labeled A through I, used to develop the final CRA Report. The Postal Service uses the reports to make necessary adjustments to the cost estimates.

[3] Air transportation is used in Alaska to transport all Postal Service products to remote locations that cannot be reached by road or water.

RM2011-11: Proposal Three

The Postal Service proposed to change its methodology for distributing Postage in the Hands of the Public (PIHOP) to products and its methodology for reconciling revenues from the RPW system with the trial balance. PIHOP is the difference between postage purchased and postage used. The Postal Service also refers to this difference as the PIHOP liability or the PIHOP adjustment.

At the time of the petition, the Postal Service distributed the PIHOP adjustment to products using a distribution of revenue by product. This latter distribution reflected revenues from the ODIS-RPW. The Postal Service explained that using the ODIS-RPW distribution key leads to inaccurate results. As an example, the Postal Service noted that the distribution key distributes too much of the stamp PIHOP liability to Priority Mail when this mail hardly uses any stamps. For this reason, the Postal Service proposed using a separate distribution key for stamp PIHOP based on the ODIS-RPW distribution of stamp revenue and a separate distribution key for meter PIHOP using the ODIS-RPW distribution of meter revenue. Other PIHOP liability would continue to be distributed to product using the FY 2010 key, except updated from year to year.

The Postal Service further explained that it collects revenues by product from two systems. One system is the Bulk Revenue, Pieces and Weight (BRPW) system, which is a census system for bilk mail. The other system is the ODIS-RPW used for single-piece mail. The revenues from each system, when summed to a grand total, should match the total revenue in the trial balance, which is used as the control total. When the totals do not match, the Postal Service assumes the BRPW revenues are correct because they come from a census system, and therefore adjusts the sampled revenues so that the all the revenues collected by product when totaled match the control total. The Postal Service refers to this as the book revenue adjustment.

The difference between the trial balance total revenue and the total revenue from the BRPW and sampling system is referred to as the residual. Because the Postal Service proposed to distribute the PIHOP liability separately for stamps and meters, and because other PIHOP liability would continue to use the FY 2010-type distribution key, the Postal Service explained that stamp and meter PIHOP liability would be double counted. It therefore proposed to remove stamp and meter PIHOP liability from the residual.

The Commission agreed with the Postal Service's conclusions and approved the proposal. The FY 2010-type methodology was inaccurate because it did not properly reflect the actual relative proportions of stamp and metered revenue, the most glaring example being the distribution of stamp revenue to Priority Mail. Further, the Commission also agreed that the procedure for the book revenue adjustment had to be revised to avoid double counting of stamp and meter PIHOP liability. By removing stamp and meter PIHOP liability from the residual, which would be distributed to product as described above, only other PIHOP would remain in the residual. Thus, double counting would be avoided.

RM2011-12: Proposal Four

The Postal Service proposed to change the current method for estimating revenue, pieces and weight for Inbound International Mail products presented in the RPW report and rely instead on a new method based on the Foreign Postal Settlement (FPS) system. The FPS system would also replace the current accrual

settlement payment system used in the ICRA report. As a result, revenue, pieces and weight presented in the RPW and ICRA would be consistent with the audited financial statements of the Postal Service.

The FPS system, implemented in January 2010, is an accounting accrual system for settlement payments between foreign postal administrations and the Postal Service related to the exchange of International mail. Under the FPS system, piece and weight data would be used to calculate revenue on the number of inbound pieces processed in a month, as well as an accrual of revenue reflecting an estimate of the number of pieces received but not yet processed. At the time of final settlement, generally months after the close of a calendar year, the difference between the accrued revenue and the final settlement revenue is posted. The piece and weight data would also be reported in the RPW.

In addition, the proposal would change the reporting of prior-year settlement revenues and currency gains and losses on foreign exchange. The FPS system isolates prior-year from current-year settlement revenues, which are recorded separately for market dominant and competitive inbound international products. However, the FPS system only records the total amount of currency gains and losses. *Id.* Such currency gains and losses would be distributed to market dominant and competitive inbound international products and reported in Other Mailing Services Revenue (market dominant) and Other Shipping Services Revenue (competitive) along with prior-year settlement revenues.

The proposal would also revise the inbound mail categories presented in the RPW report to align more closely with the proposed Mail Classification Schedule (MCS).

The Commission concurred with the Postal Service view that the proposal would substantially improve the reporting on inbound international products in the RPW. Using the FPS system, more timely data would be available for estimating inbound revenues, and reporting revenue, piece and weight information at a greater level of detail than currently, including current-year piece and weight information for the first time for some inbound products. In addition, the separate reporting of current-year settlement revenues from prior-year settlement revenues and currency gains and losses would improve accuracy of reported revenues. For these reasons, the Commission approved this proposal and it was implemented during FY 2011. *See* Order No. 920.

RM2011-12, Proposal Five

The Postal Service proposed introducing a cost pool within CRA cost segment 3.1 for Flats Sequencing System (FSS) operations. As anticipated, the scale of FSS operations had increased rapidly since FY 2010. FSS costs had been previously assigned to the AFSM 100 cost pool. The proposed new FSS cost pool would consist of MODS operations 530 (Stand Alone Mail Prep) and 538 (FSS DPS Mode). There would also be an FSS cost pool in the NDC group. The Postal Service also reasoned the FSS may have a distinct mail mix (*e.g.*, non-saturation carrier route presort flats), further justifying a separate cost pool.

The Commission accepted the rationale set forth by the Postal Service and approved the proposal. The addition of a new cost pool to reflect significant changes in postal operations due to new equipment deployment is consistent with past practices. The Commission believes that a differing FSS mail-mix (from AFSM 100) suggests that the distribution of attributable cost by product will differ. Thus, separate recognition

via separate cost pools would ensure a more accurate distribution of cost to product.

RM2011-12: Proposal Six

Proposal Six sought to modify the non-Management Operating Data System (MODS) mail processing cost pool by introducing five additional cost pools for certain special service activities. The proposal establishes separate cost pools for the following activities: (1) sorting mail into post office boxes; (2) bulk mail acceptance activities; (3) computer forwarding system activities; (4) business reply mail activities; and (5) activities related to accountable items, such as carriers' keys scanners and mail with certain special services. The Postal Service argued that the changes will improve the alignment between MODS and non-MODS mail processing cost pools for post offices.

The Commission found that this proposed change would improve product costing for non-MODS facilities, and more closely align MODS and non-MODS cost pools in post offices. Therefore, the Commission approved this proposal and the changes were incorporated in the 2011 ACR. *See* Order No. 920.

RM2011-12: Proposal Seven

The Postal Service proposed to change the distribution key methodology for MODS allied labor cost pools. Currently, MODS allied labor costs are distributed to products using tallies from all MODS cost pools. The proposal sought to use only IOCS tallies from MODS cost pools associated with non-International Service Center (ISC) plant operations. The distribution keys will be established based on IOCS direct tallies from all MODS function 1 (mail processing plant) cost pools. The proposal excludes direct tallies of MODS function 4 (post offices) and ISC cost pools. The Postal Service claimed that the change will reduce potential bias in MODS allied labor mixed-mail distributions by excluding MODS post office tallies, which include tallies of products bypassing plants. The proposal also should avoid the disproportionate allocation of costs to certain international products by excluding ISC direct tallies from the calculation of mixed-mail distribution keys for MODS allied labor costs.

The Commission agreed that the proposed change should reduce potential bias in MODS allied labor mixed-mail distributions. The Commission noted that the distribution keys will be calculated using fewer IOCS tallies. However, the effect of removing those tallies on the statistical reliability of the estimates should be minimal. The Commission found that the benefits from using the proposed approach outweigh the loss of statistical reliability from removing those tallies from the calculation of the distribution key. The Commission maintained that the proposed change improves the distribution of MODS allied mixed-mail labor costs to products. The Commission approved the proposal and it was implemented in the 2011 ACR. *See* Order No. 920.

RM2011-12: Proposal Eight

The Postal Service proposed to modify the manner in which delivery scanning costs are attributed to the delivery of Express Mail where the sender waives the signature requirement. The Postal Service explained that Express Mail with a Signature Waiver should not be classified as accountable mail. Accordingly, the Postal Service proposed to modify its attribution procedure to reflect the change in postal operations.

Because it better reflected current postal operations, the Commission approved Proposal Eight. *See* Order No. 744.

RM2012-1: Proposal Ten

The Postal Service proposed to change the treatment of costs for undeliverable-as-addressed (UAA) Parcel Select pieces. In its Petition, the Postal Service stated that for most of FY 2011, it charged Parcel Post prices for UAA Parcel Select pieces, and assigned the related IOCS tallies for those pieces to the Parcel Post product. The Postal Service further explained that on June 24, 2011, it began charging UAA Parcel Select pieces the equivalent of the Parcel Select non-presort price plus an additional $3.00 fee. Consistent with this change, the Postal Service stated that it began allocating the revenue for UAA Parcel Select pieces to the Parcel Select product. *Id.* With Proposal Ten, the Postal Service proposed to assign the related UAA Parcel Select IOCS tallies to the Parcel Select product.

The Commission approved the proposal. *See* Order No. 1153. In approving the proposal, the Commission concluded that since the revenues for UAA Parcel Select pieces were assigned to Parcel Select, the related costs should also be assigned to ParcelSelect. The changes were incorporated into the 2011 ACR.[4]

RM2012-1: Proposal Eleven

The Postal Service proposed changes to the Express Mail NSAs delivery cost savings workpapers to be consistent with the Commission's recent approval of a related proposal. In Docket No. RM2011-12, the Commission approved Proposal Eight, which modified the Express Mail delivery cost savings workpapers to reflect a change in postal operations where carriers no longer attempt to obtain signatures for Express Mail pieces that contain signature waivers.[5] In addition, Proposal Eight updated the Express Mail workpapers with new Carrier Cost Systems (CCS) data. The Postal Service stated that the Commission's approval of Proposal Eight necessitated corresponding changes to the workpapers related to Express Mail NSAs delivery cost savings.

The Commission accepted the proposed changes. *See* Order No. 1153. In approving the changes, the Commission noted that the Postal Service's proposal aligned the Express Mail NSA models with the Express Mail models to reflect new postal operations and CCS data. The changes were incorporated into the 2011 ACR.

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4 The Commission accepted Proposals Ten and Eleven after the Postal Service submitted its 2011 ACR. *See* Proposal Eleven *infra*. The Commission's rules require the Postal Service's ACR to use the established methodology at the time of filing. For proposals that were still pending before the Commission, the Postal Service's 2011 ACR provided two versions of its ACR cost models, the established methodology and the recently proposed methodology. However, for Proposals Ten and Eleven, the Postal Service explained that it was unable to provided two versions and it incorporated the methodologies into its ACR filings. *See* 2011 ACR at 6. The Commission will allow this approach this time because the proposals were minor. However, the Commission expects the Postal Service to file future proposals to change analytical principles in sufficient time so that the proposals are approved before the Postal Service files its upcoming ACR.

5 *See* Docket No. RM2011-12, Order Concerning Analytical Principles for Periodic Reporting (Proposals Four through Eight), October 21, 2011 (Order No. 920).

Appendix C

Abbreviations and Acronyms

Long Version	Abbreviation/Acronym
Address Management Services	AMS
Alliance of Nonprofit Mailers	ANM
American Business Media	ABM
American Catalog Mailer Association	ACMA
Annual Compliance Determination	ACD
Annual Compliance Report	ACR
FY 2011 Annual Performance Plan	2011 Plan
2012 Annual Performance Plan	2012 Plan
FY 2010 Annual Performance Report	2010 Report
Postal Service's 2011 Annual Performance Report	2011 Report
Area Distribution Center	ADC
Automated Area Distribution Center	AADC
Automated Postal Center	APC
Base Realignment and Closure	BRAC
Bound Printed Matter	BPM
Bulk Metered Mail	BMM
Carrier Sequence Bar Code Sorter	CSBCS
Chairman's Information Request	CHIR
Collect on Delivery	COD
Collection Point Management System	CPMS
Commission on Postal Reorganization	CPR
2010 Comprehensive Statement on Postal Operations	2010 Comprehensive Statement
Consumer Price Index	CPI
Consumer Price Index for all urban consumers	CPI-U

Long Version	Abbreviation/Acronym
Community Post Offices	CPOs
Cost and Revenue Analysis	CRA
Critical Entry Times	CET
Customer Experience Measurement	CEM
Customer Supplier Agreements	CSAs
Deliveries per Work Hour	DPWH
Delivery Bar Code Sorter	DBCS
Delivery Point Sequence	DPS
Destination Sectional Center Facilities	DSCF
Destination Area Distribution Center	DADC
Destination Delivery Unit	DDU
Destination Bulk Mail Center	DBMC
Destination Network Delivery Center	DNDC
Direct Marketing Association, Inc.	DMA
Educational, cultural, scientific or informational [value]	ECSI
Every Door Direct Mail	EDDM
Express Mail Service	EMS
External First-Class Measurement System	EXFC
Federal Employee Retirement System	FERS
First-Class Mail International	FCMI
Flats Sequencing System	FSS
Foreign Post Settlement	FPS
Global Bulk Economy	GBE
Global Direct	GD
Global Expedited Package Services	GEPS
Global Expedited Package Service Non-published Rates 2	GEPS—NPR 2
Global Reseller Expedited Package Services 1	GREPS 1
Gross Domestic Product	GDP
Integrated Financial Plan	IFP
Intelligent Mail Barcode	IMb
Intelligent Mail Accuracy and Performance System	iMAPS
International Cost and Revenue Analysis	ICRA
International Mail Measurement System	IMMS
International Money Transfer Service – Outbound	IMTS-Outbound
International Priority Airmail	IPA
International Service Center	ISC
International Surface Airlift	ISAL
In-Office Cost System	IOCS
Mailer Identification	MID
Mixed Area Distribution Center	MADC
National Association of Presort Mailers	NAPM
National Postal Policy Council	NPPC

Long Version	Abbreviation/Acronym
Negotiated Service Agreement	NSA
Network Distribution Center	NDC
Not-Flat Machinables	NFMs
Office of Personnel Management	OPM
Officially Licensed Retail Products	OLRP
Occupational Safety and Health Administration	OSHA
Origin Area Distribution Center	OADC
Origin Bulk Mail Center	OBMC
Origin Network Distribution Center	ONDC
Origin Sectional Center Facility	OSCF
Parcel Shippers Association	PSA
Point of Service	POS
Post Office Box	PO Box
Postal Accountability and Enhancement Act	PAEA
Postal Qualified Wholesalers	PQW
Product Tracking System	PTS
Qualified Business Reply Mail	QBRM
Quality Link Measurement System	QLMS
Postal Service Retirement Health Benefits Fund	RHBF
Retail Access Optimization Initiative	RAOI
Revenue, Pieces, and Weights	RPW
Sectional Center Facility	SCF
Securities and Exchange Commission	SEC
Stamp Fulfillment Services	SFS
The Postal Service Financial Responsibility and Management Assistance Authority	The Authority
Total Factor Productivity	TFP
Universal Postal Union	UPU
Village Post Offices	VPO
Voice of the Employee	VOE


U.S. POST OFFICE

Appendix D

Commenters—2011 Annual Compliance Determination

Commenter	Comment Citation	Citation Short Form
American Catalog Mailers Association	Comments of the American Catalog Mailers Association (ACMA)	ACMA Comments
	February 3, 2012	
American Catalog Mailers Association	Reply Comments of the American Catalog Mailers Association (ACMA)	ACMA Reply Comments
	February 17, 2012	
American Postal Workers Union, AFL-CIO	Reply Comments of American Postal Workers Union, AFL-CIO	APWU Reply Comments
	February 23, 2012	
Direct Marketing Association, Inc., National Association of Presort Mailers, and Parcel Shippers Association	Comments of the Direct Marketing Association, Inc., the National Association of Presort Mailers, and the Parcel Shippers Association	DMA/NAPM/PSA
	February 3, 2012	
Direct Marketing Association, Inc., Major Mailers Association, National Association of Presort Mailers, National Postal Policy Council, and Parcel Shippers Association	Joint Comments of the Direct Marketing Association, Inc., the Major Mailers Association, the National Association of Presort Mailers, the National Postal Policy Council, and the Parcel Shippers Association	DMA et al. Joint Comments
	February 3, 2012	
L.L.Bean, Inc.	Comments of L.L.Bean, Inc.	L.L.Bean Comments
	February 3, 2012	
L.L.Bean, Inc.	Reply Comments of L.L.Bean, Inc.	L.L.Bean Reply Comments
	February 17, 2012	
Magazine Publishers of America, Inc., Alliance of Nonprofit Mailers, American Business Media	Reply Comments of Magazine Publishers of America, Inc., Alliance of Nonprofit Mailers and American Business Media	MPA/ANM/ABM Reply Comments
	February 17, 2012	

Commenter	Comment Citation	Citation Short Form
National Postal Policy Council	Comments of the National Postal Policy Council February 3, 2012	NPPC Comments
National Postal Policy Council	Reply Comments of the National Postal Policy Council February 17, 2012	NPPC Reply Comments
Pitney Bowes, Inc	Comments of Pitney Bowes Inc. February 3, 2012	PB Comments
Pitney Bowes, Inc.	Supplemental Comments of Pitney Bowes Inc. March 12, 2012	PB Supplemental Comments
Pitney Bowes, Inc.	Comments of John C. Panzar on Behalf of Pitney Bowes Inc. February 3, 2012	Panzar Comments
Public Representative	Public Representative Comments February 2, 2012	PR Comments
Public Representative	Public Representative Reply Comments in ?? February 17, 2012	PR Reply Comments
Time Inc.	Initial Comments of Time Inc. on USPS FY 2011 Annual Compliance Report February 3, 2012	Time Comments
Time Inc.	Reply Comments of Time Inc. on USPS FY 2011 Annual Compliance Report February 17, 2012	Time Reply Comments
United States Postal Service	Reply Comments of the United States Postal Service February 17, 2012	Postal Service Reply Comments
Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc.	Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. Initial Comments on the United States Postal Service FY 2011 Annual Compliance Report February 3, 2012	Valpak Comments
Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc.	Valpak Direct Marketing Systems, Inc. and Valpak Dealers' Association, Inc. Reply Comments on the United States Postal Service FY 2011 Annual Compliance Report February 17, 2012	Valpak Reply Comments

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