Postal Regulatory Commission

Annual Report
to the President and Congress
Fiscal Year 2008

POSTAL REGULATORY COMMISSION

ANNUAL REPORT
TO THE PRESIDENT AND CONGRESS
FISCAL YEAR 2008

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December 2008

Dan G. Blair
Chairman

On behalf of the Postal Regulatory Commission, I am pleased to submit the Commission's first Annual Report. This report reviews the significant activities of the Commission during the past fiscal year.

Fiscal Year 2008 (FY 2008) saw the Commission working hard to implement key provisions of the Postal Accountability and Enhancement Act, Public Law 109-435. Significantly, the Commission issued regulations, eight months ahead of the statutory schedule, creating a new framework for price adjustments for postal products in this reform environment. Our Annual Report for 2008 will highlight further steps taken by the Commission in fulfilling our responsibilities under the new law.

This report is being issued at a financially challenging time for the U.S. Postal Service. The on-going economic slowdown has contributed to a large decline in mail volumes; and the Service is faced with a second consecutive year of multi-billion dollar losses, with the Postmaster General predicting a similar scenario for next year as well. Therefore, our mission of ensuring the transparency and accountability of the Postal Service is more important than ever.

Over the course of the past several months, the Commission has proposed a series of new regulations which include updating the rules for complaints by establishing a new two-track system; and prescribing the form and content of information the Postal Service will routinely report to the Commission to achieve transparency and accountability of the service. The Commission carefully crafted the draft periodic reporting regulations with an eye toward balancing the burden of information production with the mailing public's right to know.

A priority of the new law was granting the Postal Service increased pricing and product flexibility. For the first time, the Postal Service was specifically authorized to negotiate customer-specific service agreements for both market dominant and competitive products. It is worth noting that since the new rules governing these agreements went into effect last year, the Commission has approved approximately two dozen competitive agreements. The Commission stands ready to work with the Postal Service, its customers, and postal stakeholders in the interest of future agreements.

We plan to finish this year by publishing rules on Accounting Practices and Tax Rules for Competitive Products, and issuing our report to Congress on universal postal service and the postal monopoly in the United States, including the monopoly on mail delivery and access to mailboxes. As always, the Commissioners and I look forward to public review and feedback on our efforts. As FY 2009 approaches, we must be vigilant if we are to achieve our mission of fostering a vital and efficient universal mail system.

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Fiscal Year 2008 At A Glance

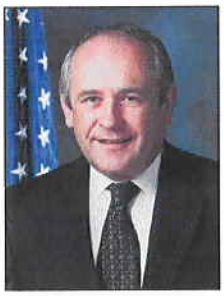
- Smooth transition to rate adjustments, for both market dominant and competitive products, under the Postal Accountability and Enhancement Act
- Met or exceeded all FY 2008 statutory deadlines, including early completion of the regulations pertaining to a Modern System of Ratemaking
- Twenty-two negotiated service agreements approved
- Six rulemakings encompassing data requirements, complaint procedures, treatment of confidential information, accounting rules, and modifications to cost methodologies initiated
- Extensive public outreach efforts

Chapter I – About the Commission

ABOUT THE COMMISSION

The Commission is an independent agency that has exercised regulatory oversight over the U.S. Postal Service since its creation by the Postal Reorganization Act of 1970 (PRA). The Commission is composed of five Commissioners, each of whom is appointed by the President, with the advice and by consent of the U.S. Senate, for a term of six years. The Chairman is designated by the President and serves as the head of the agency. A Commissioner may continue to serve after the expiration of his or her term for up to one year. No more than three members of the Commission may be from the same political party.

Commissioners



Dan Blair, Chairman

Appointed as a Commissioner December 9, 2006. Designated Chairman by President George W. Bush on December 15, 2006. Term expires October 14, 2012. Formerly served as both Acting Director and Deputy Director, U.S. Office of Personnel Management. Former Senior Counsel to Senator Fred Thompson (R-TN) on the Senate Committee on Governmental Affairs. Former Staff Director, U.S. House of Representatives Subcommittee on the Postal Service, under Representative John McHugh (R-NY). Former Minority General Counsel, U.S. House of Representatives Committee on Post Office and Civil Service.

Nanci E. Langley, Vice-Chairman

Appointed June 6, 2008. Appointed Vice-Chairman October 16, 2008. Term expires November 22, 2012. Former Director of Public Affairs and Government Relations, Postal Regulatory Commission. Former Deputy Staff Director to Senator Daniel K. Akaka (D-HI), U.S. Senate Committee on Homeland Security and Governmental Affairs' Subcommittee on Oversight of Government Management, the Federal Workforce and the District of Columbia Communications Director to former U.S. Senator Spark M. Matsunaga (D-HI).

Ruth Y. Goldway

First appointed in April 1998. Term expires November 22, 2014. Former Manager of Public Affairs for the Getty Trust. Former Director of Public Affairs, California State University, Los Angeles. Former Council Member and Mayor, City of Santa Monica. Founder and Former Chairperson, Santa Monica Pier Restoration Corporation. Former Assistant Director of California's Department of Consumer Affairs. Co-founder of Women in Logistics and Delivery Services. Former Director of California State University, Los Angeles.

Tony Hammond

Appointed in August 2002. Term expires October 14, 2010. Former owner and managing member, T. Hammond Company, LLC. Former Senior Consultant to Forbes 2000, Incorporated. Former Senior Vice President of the direct marketing firm, FL&S. Served as Director of Campaign Operations for the Republican National Committee for the 1998 election cycle. Former Executive Director and Finance Director, Missouri Republican Party. Staff to former U.S. Representative Gene Taylor (R-MO).

Mark Acton

Appointed August 3, 2006. Term expires October 14, 2010. Served as Special Assistant to former Postal Rate Commission Chairman George Omas. Former Staff Director, Republican National Committee (RNC) Counsel's Office. Former Deputy to the Chairman of the 2004 Republican National Convention. Served as Special Assistant to the RNC Chief Counsel as well as RNC Counsel's Office Government Relations Officer and Redistricting Coordinator. Formerly served as both Executive Director, Republican National Convention, Committee on Permanent Organization and Deputy Executive Director, Committee on Rules. Former Executive Director of the RNC Redistricting Task Force.

Assisting the Commission is a staff with expertise in law, economics, finance, statistics, and cost accounting. The Commission is organized into four operational offices:

- Accountability and Compliance;
- General Counsel;
- Public Affairs and Government Relations; and
- Secretary and Administration.

The Commission maintains an independent office for its Inspector General.

MISSION STATEMENT

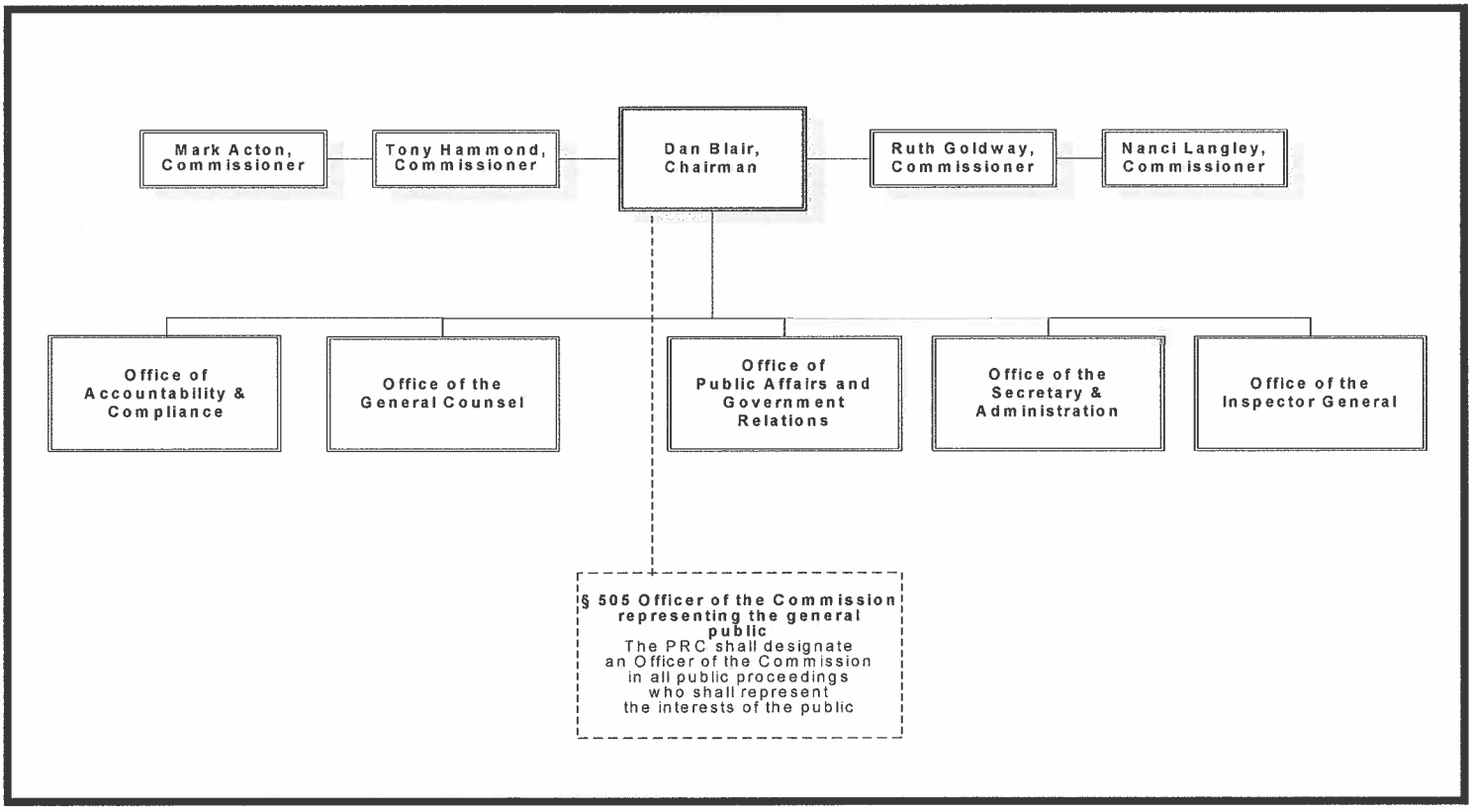
Ensure transparency and accountability of the United States Postal Service and foster a vital and efficient universal mail system.

GUIDING PRINCIPLES

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

- *Openness;*
- *Stakeholder (public) participation;*
- *Collegiality and multi-disciplinary approaches;*
- *Timely and rigorous analysis;*
- *Fairness and impartiality;*
- *Integrity;*
- *Commitment to excellence; and*
- *Merit.*

FY 2008 Postal Regulatory Commission Organizational Chart



THE POSTAL ACCOUNTABILITY AND ENHANCEMENT ACT

On December 20, 2006 President George W. Bush signed into law the Postal Accountability and Enhancement Act (PAEA). This Act, the culmination of a ten-year journey, produced the most significant changes in the regulatory landscape for the U.S. Postal Service and the U.S. postal system since 1970. The Act is founded on the principles of flexibility, transparency, accountability and predictability. Its purpose is to ensure a robust, affordable and quality universal mail service in the United States. The Act gives the Postal Service new tools to meet the challenges of the changing postal environment, including greater pricing flexibility, while balancing these tools with new responsibilities for oversight by a more formal regulator.

The PAEA transformed the Postal Rate Commission into the Postal Regulatory Commission and assigned significant new responsibilities to the agency. It requires the Commission to develop and maintain regulations for a modern system of rate regulation, consult with the Postal Service on delivery service standards and performance measures, consult with the Department of State on international postal policies, prevent cross-subsidization (or other anticompetitive postal practices), promote transparency and accountability, and adjudicate complaints.

The PAEA also assigns new and continuing oversight responsibilities to the Commission, including annual determinations of Postal Service compliance with applicable laws, development of accounting practices and procedures for the Postal Service, review of the universal service obligation, and assurance of transparency through periodic reports. New enforcement tools include subpoena power, authority to direct the Postal Service to adjust rates and to take other remedial actions, and levy fines in cases of deliberate noncompliance with applicable postal laws.

Under the new Act, all postal products and services are categorized as either market dominant or competitive. Market dominant products include First-Class letters and cards, advertising mail, Periodicals and single-piece parcels. Competitive products include Priority Mail, Express Mail, and bulk Parcel Post.

EFFECTIVENESS OF THE COMMISSION'S RULES IN ACHIEVING PAEA GOALS

The Commission must now annually assess the effectiveness of its rules and regulations in achieving the goals of the PAEA. Fiscal Year 2008 was the first full year under the PAEA. The Commission made significant progress toward implementing rules and regulations designed to meet the goals of the PAEA. The rules for a modern system of ratemaking, published eight months before the statutory deadline, introduced predictability and stability into the ratemaking process. The Commission's review of Postal Service rate adjustments under the new rules highlighted inconsistencies with the PAEA, thereby requiring minor changes to the proposed rates. Further, reviews of

competitive negotiated service agreements have been completed in a timely fashion and have balanced greater pricing flexibility with increased accountability.

Due to the implementation of rules and regulations for a modern system of rate making, data related to postal operations under the PAEA are now becoming available. While there is not enough data for FY 2008 to reasonably assess the effectiveness of the rules and regulations in meeting the goals of the PAEA, the Commission expects to perform such an assessment beginning in FY 2009.

Lastly, the Commission has proposed rules in the areas of accounting for competitive products, periodic reporting, treatment of confidential material, and complaint procedures, all of which will be finalized shortly. These rules are designed to enhance transparency and accountability, and increase efficiency of postal operations.

COMMISSION'S STRATEGIC PLAN

One of the Commission's first acts as the newly formed Postal Regulatory Commission was to organize and assign the existing operational framework to meet the challenges of the PAEA. Efforts began immediately to develop the Postal Regulatory Commission's first Strategic and Operational Plan for Fiscal Years 2008 through 2012. This Plan outlines the Commission's core Mission and Vision for the first five years, the key Strategic Goals to help the Commission fulfill its Mission and Vision, and the Operational Strategies to meet statutory requirements of the Act. These strategies will help ensure transparency and accountability of the United States Postal Service and foster a vital and efficient universal mail system.

The Plan is designed to guide the Commission as it implements the key provisions assigned under the PAEA. As the Commission carries out its responsibilities and duties, and evaluate its progress and performance based on the strategic goals outlined in this Plan, it will make appropriate modifications as new challenges arise.

The Strategic Plan can be viewed in its entirety on the Commission's website at www.prc.gov.

Chapter II – Technical Analysis

During FY 2008, the Commission worked to consistently develop procedures, enact regulations and respond administratively to support the goals of the PAEA. In fulfilling these duties, the Commission strives to be cognizant of and responsive to the comments received from all interested persons, as well as competitive market concerns and realities of the Postal Service and other affected branches of government. The following sections highlight some of the Commission's achievements during the first full fiscal year of the PAEA.

Rules for a Modern System of Ratemaking

Commission Order No. 43 established rules for changing rates for both market dominant and competitive products. Under the PAEA, changes in rates for market dominant products may not exceed an annual limitation. Different rules apply for competitive rate changes. Order No. 43 was issued on October 29, 2007, eight months prior to the June 2008 statutory deadline. As a result, the rules provided the Postal Service with the option to file a change in rates for market dominant products under the PAEA limited to the rate of inflation, or request one final cost of service change in rates in a 10-month rate proceeding under the authority and policies of the Postal Reorganization Act.

Market Dominant Products

One of the key features of the price cap as outlined in Order No. 43 is the significantly reduced time required for regulatory review. The new rules allow 45 days for review of the Postal Service's proposed rates. While increases for each class are generally capped by the Consumer Price Index, the Postal Service has the flexibility to vary the percentage changes for categories within the class.[1]

The price cap is set by the percent change in the level of the seasonally unadjusted Consumer Price Index for All Urban Consumers (CPI-U), between the most recent average 12 month period from the date the Postal Service files its notice of rate adjustment and the average of the immediately preceding 12 month period. The following rudimentary example illustrates the computation of the price cap.

[1] This process contrasts sharply with that employed under the PRA where rate changes were proposed by the Postal Service, interested parties were allowed to conduct discovery, open public hearings were held, and the Commission made final recommendations to the Postal Board of Governors. That process was conducted over a ten month period.

Table 1 - Illustration of Price Cap

Sum of CPI-U values for most recent 12 month period divided by 12 (Recent Average)	2,573/12 = 214.46
Sum of CPI-U values for the 12 month period immediately preceding, the recent 12 month period divided by 12 (Base Average)	2,464/12= 205.34
Percent Change equals Recent Average divided by Base Average minus 1 expressed as a percent	(214.46/205.34) -1= 4.4%

The use of a 12 month average corresponds to the U.S. Bureau of Labor Statistics method for calculating annual changes in CPI and provides greater stability and predictability. This method was proposed by the Commission and endorsed by the mailing community.

The difference between the annual price cap and the percentage change proposed by the Postal Service is known as the unused rate authority. Because the cap is applied at the class level, the unused rate authority may differ by class. Cumulative unused rate authority can be reserved for use for up to five years. This banked rate authority, which is a feature of PAEA can be used to increase rates beyond the annual price cap, with a limitation of two percent in each class in a given year.

Alternate rules are available to calculate the appropriate cap for rate increases other than one year apart.

Order No. 43 also established rules for expeditiously processing negotiated service agreements (NSA) between the Postal Service and individual mailers. For market dominant NSAs, the rules direct the Postal Service to provide details demonstrating compliance with statutory requirements of 39 U.S.C. 3622(c)(10), that such NSA results in either financial or operational benefits to the Postal Service and does not cause undue harm to the market. The Commission directs the Postal Service to provide data within 60 days of the anniversary date of implementation of each agreement to allow the Commission to test compliance with the above stated goals.

In addition, Order No. 43 established rules for "exigent" rate adjustments based on exceptional circumstances requiring astringent 90 day public notice and an active but

expeditious Commission review in keeping with the urgency and uniqueness of this type of rate request.

Furthering the principles of predictability and stability in the setting and maintenance of rates, the Commission in its final rules directed the Postal Service to maintain a "Schedule for Regular and Predictable Rate Changes", which allows mailers to adapt their businesses accordingly. The Postal Service chose to raise market dominant rates annually in May.

Additionally, the Commission promoted transparency through its final rules by providing an opportunity for review of rate adjustments by the public through the publication of a notice in the *Federal Register*, the posting of an extensive docket for each adjustment on its website at www.prc.gov, the incorporation of an adequate period for public comment, and the addressing of amendments, if any. The public notification is published at least 45 days before the intended implementation, with the exception of exigency-based rate adjustments.

COMPETITIVE PRODUCTS

The PAEA provides the Postal Service flexibility to price competitive products subject to certain conditions. The law directs the Commission to formulate regulations to: (1) prevent cross-subsidization of competitive products by market dominant products; (2) ensure that each competitive product covers its attributable costs; and (3) ensure that all competitive products collectively contribute a share of Postal Service total institutional costs as set by the Commission currently at 5.5 percent.

The new rules allow the Commission 30 days to determine whether the Postal Service's proposed rates for competitive products are meeting these conditions. The Commission, in its final rules, specified that it will use an incremental cost test to validate compliance with the cross subsidy requirement that revenue generated from competitive products equals or exceeds the incremental costs of such products. Further, the Commission determined that the appropriate share of institutional costs to be borne by competitive products is 5.5 percent, subject to revision as needed.

For competitive NSAs, the rules allow for not less than a 15 day review of all agreements. Competitive NSAs are at evaluated for compliance with the statutory requirements for competitive products.

POSTAL PRODUCTS

Finally, 39 U.S.C. 3642 provides that the Postal Service may not offer any product until it has been assigned to the market dominant or the competitive category of mail. The Commission, in its final rules, detailed procedures for establishing, revising and publishing product lists in a "Mail Classification Schedule" that categorizes postal

products in one of the above two categories. The "Mail Classification Schedule" can be modified, by adding, removing, or transferring products between lists, through proceedings initiated either by the Postal Service, by a user of the mail, or by the Commission itself. However, the PAEA prohibits the transfer from the market dominant category of products covered by the postal monopoly.

In Order No. 43, the Commission sought to implement the PAEA by adopting regulations designed to foster predictability and stability in rates and to afford the Postal Service pricing flexibility while taking into consideration administrative burdens and promoting transparency of the ratemaking process.

RATE ADJUSTMENTS

During FY 2008, the Commission reviewed the Postal Service's first-ever rate adjustments for market dominant and competitive products under the PAEA. The Postal Service notice of rate adjustments for market dominant products was filed February 10, 2008. On March 12, 2008, during the Commission's review of the notice for market dominant rate adjustments, the Postal Service filed its notice of rate adjustments for competitive products. The Commission's reviews were completed in a timely fashion and permitted the Postal Service to implement the scheduled rate changes as planned.

Market Dominant Products Rate Adjustment

On March 17, 2008, the Commission found that the Postal Service's planned rate adjustments did not exceed the statutory Consumer Price Index-based price cap of 2.9 percent for the 12 months ending December 2007. The Commission's review, completed in 35 days, encompassed the Postal Service's notice and supporting materials, including public comments from 17 participants and updated information submitted by the Postal Service.

In addition to limiting market dominant products' rate adjustment, on average, to the rate of inflation, the PAEA imposes a separate limitation on workshare discounts, *i.e.*, reduced rates based on costs avoided by the Postal Service when mailers undertake certain mail preparation and processing tasks. Section 3622(e)(2) directs the Commission to ensure that workshare discounts do not exceed the costs avoided by the Postal Service as a result of the workshare activity, unless certain exceptions are met. This provision effectively limits the Postal Service's ability to set workshare discounts that exceed 100 percent of avoided costs. Accordingly, Commission rules require the Postal Service to justify any proposed workshare discounts that exceed 100 percent of avoided costs by explaining how it meets one of four exceptions under the PAEA.

In response to the Postal Service notice, the Commission requested additional written justification from the Postal Service regarding 14 workshare discounts. Of those 14, the Postal Service identified six discounts within the Standard Mail class that had passthroughs—the ratio of the discount to the associated avoided costs, expressed as a

percent—exceeding 100 percent. Upon review of the Postal Service's written justification, the Commission found all but one of the discounts to be adequately supported. The lone exception was a 1.4 cent discount for applying a barcode to certain Standard Mail letters that saved 0.3 cents in avoided costs for the Postal Service. This resulted in an initial proposed passthrough of 557.8 percent.

As required by the Commission's rules, the Postal Service subsequently filed an amended notice of market dominant rate adjustment addressing this finding. In its amended notice, the Postal Service conformed to the requirement of section 3622(e) by shrinking the rate differential between non-automation letters and prebarcoded (automation) letters. The Postal Service did so by reducing the rate for non-automation letters by 1.1 cents, thereby making the workshare discount for automation letters equal to the costs avoided by the Postal Service—an option suggested by the Commission.

On April 9, 2008, the Commission completed its review of the amended notice, and found the planned rates for non-automation machinable mixed AADC letters to be consistent with section 3622(e). These changes reduced the class average increase for Standard Mail from 2.875 percent to 2.838 percent, and increased the amount of unused rate authority "banked" by the Postal Service from 0.025 to 0.062. The Commission's 14-day review of the Postal Service's amended notice permitted Postal Service implementation of the rate changes for market dominant products on May 12, 2008, as planned.

The percentage increase by class and the unused rate authority is shown in the table below:

Table 2 - Market Dominant Rate Adjustments

	Rate Changes (%)	**Unused Rate Authority** (%)
First-Class Mail	2.886	0.014
Periodicals	2.724	0.176
Standard Mail	2.838	0.062
Package Services	2.875	0.025
Special Services	2.848	0.052

Competitive Products Rate Adjustment

The Commission's review of rate adjustments for competitive products is governed by section 3633(a) of the PAEA. Section 3633(a) establishes three statutory standards, incorporated into the Commission's rules, applicable to competitive products. First, each competitive product must cover its attributable cost. Second, competitive products must collectively cover their appropriate share of the Postal Service's institutional costs, which the Commission has determined to be, at a minimum, 5.5 percent of the Postal

Service's total institutional costs. Third, competitive products may not be cross-subsidized by market dominant products.

The Postal Service's notice of rate adjustments for domestic competitive products covered Priority Mail, Express Mail, Parcel Select and Parcel Return Service. International products affected by the rate changes included Priority Mail International, Express Mail International, Global Express Guaranteed, International Priority Airmail, and International Surface Airlift, among others. Rate changes were also planned for International Ancillary Services, such as International Certificates of Mailing, International Registered Mail, and International Return Receipt.

On April 10, 2008, the Commission completed its review of the Postal Service's notice of rate adjustments for competitive products, supporting material and analysis and public comments from seven participants. That review found the Postal Service's planned rate changes met the statutory and regulatory requirements that each competitive product recover its direct costs, pay an appropriate share of institutional costs, and that market dominant products do not cross-subsidize competitive products. Moreover, the Commission's review, completed in 29 days, permitted the Postal Service to implement the competitive product rate changes on the same date as the rate changes for market dominant products, May 12, 2008.

While finding the proposed rate changes lawful, the Commission's review was hampered by limited explanations and information presented in the initial Postal Service filing. One difficulty involved a lack of clarity in the use of calendar days versus workdays to calculate incentive rebates to commercial mailers for Express Mail. Such a difference is important because it affects the level of rebates and thus the financial impact of the planned rate changes.

The Commission expects future competitive product rate adjustments to contain a more detailed and much clearer demonstration that, with the planned changes, rates will satisfy the applicable statutory criteria of section 3633(a). Moreover, the Commission understands that the Postal Service data collection systems do not yet fully reflect the changes required by the PAEA, *e.g.,* to collect cost data by product and distinguish between competitive and market dominant products. Recognizing that this proceeding was the first under the Commission's recently adopted rules governing competitive (and market dominant) rate changes, such factors were taken into consideration during the Commission deliberations.

NEW REPORTS REQUIRED UNDER PAEA

The PAEA requires the Postal Service to provide to the Commission, (no later than 90 days after the end of each fiscal year) a report which demonstrates in sufficient detail all products during the year that have complied with all requirements of the PAEA. The Commission, in turn, is to analyze the data and report on Postal Service compliance. The PAEA also requires the Commission to prepare longer-term reports and

assessments to elicit various managerial reports and to oversee specialized financial reporting such as those required by 39 U.S.C. 2803 and 2804 and to have access to audit information and other supporting documentation. The Commission is also required to report on the Postal Service's universal service obligation and mail monopolies.

ANNUAL COMPLIANCE DETERMINATION FOR FY 2007

On March 27, 2008, the Commission issued its first Annual Compliance Determination (ACD), analyzing the performance of the Postal Service for FY 2007. The Commission's ACD was completed within the statutory 90-day period established for review of the Postal Service's Annual Compliance Report (ACR), which included substantial supporting data on costs, revenues, volumes, rates, and quality of service.

Significant findings included:

- The Postal Service had a $1.6 billion profit on operations; however, statutory funding requirements for retiree health benefits resulted in a net loss of $5.1 billion.

- Between FY 2006 and FY 2007, total First-Class Mail volume declined by 1.6 percent and First-Class single-piece volume dropped 4.5 percent to continue a nine-year decline.

- Five market dominant postal services did not cover their attributable costs: Periodicals; Single-Piece Parcel Post; Media/Library Mail; Registered Mail; and First-Class Mail International (inbound).

- Two competitive postal services did not cover their attributable costs: Parcel Return Service and International Surface Parcel Post at non-Universal Postal Union (UPU) rates (inbound).

- Competitive products, as a group, slightly exceeded the requirement that they contribute at least 5.5 percent of Postal Service institutional costs.

- Market dominant Negotiated Service Agreements (NSAs) with five mailers provided a $2.5 million net increase in contribution, largely from reduced costs.

- Service performance data were available for less than 20 percent of the mail due to the lack of performance measurement systems. The volume of mail covered is expected to increase as planned new measurement systems are implemented.

- The Postal Service has made significant progress toward achieving its strategic performance goals to Improve Service, Generate Revenue, Increase Efficiency, and Establish a Customer-Focused Culture, but the results were mixed.

Commission preparation of the ACD was aided by development of additional information, as well as public comments. The Commission formally submitted three sets of information requests to the Postal Service. These information requests were supplemented by informal queries and conversations among Commission staff and the Postal Service. Collectively, the information requests and informal queries prompted the filing of more recent data, produced correction of minor errors, or otherwise clarified ambiguities in the Postal Service's ACR.

Additional information was also developed through Commission-sponsored technical conferences, in response to Postal Service introduction of a new methodology for estimating Periodicals costs developed in the final rate case under the Postal Reorganization Act of 1970, in Docket No. R2006-1. Two technical conferences were held to facilitate Commission and public understanding of the nature and reasons for the changes. The Postal Service subsequently filed additional materials as requested, including corrections and explanations, spreadsheets, and materials related to the measurement of Periodicals cost avoidance.

Pursuant to its regulations, public comments were solicited by the Commission concerning the Postal Service's ACR. Comments and reply comments were received from 21 participants. These comments covered a wide variety of issues, many of which involved matters of first impression concerning the Commission's procedures, the policies of the PAEA, and the application of those policies in evaluating the Postal Service's first ACR. Other comments addressed specific costs (including costs avoided), revenues, volumes, pricing (including workshare discounts), and competitive product issues.

Despite the development of additional information, Commission analysis was complicated by several matters. The most important centered on whether to apply the rate setting standards of the PRA or the PAEA to the various rates charged during FY 2007. Those rates, established pursuant to the PRA, were intended to satisfy a similar, but nonetheless different combination of policies than those of the PAEA.

The Commission concluded that the applicable standards for review were those found in the PAEA. In reaching this conclusion, the Commission observed that doing so would not have far reaching effects. Domestic rates in effect during FY 2007, established under the PRA to recover costs and reward worksharing savings achieved in a future fiscal year, were actually designed with projected FY 2008 costs in mind. Nevertheless, to the extent any FY 2007 rates failed to satisfy PAEA policies, Postal Service rate adjustments for market dominant and competitive products, approved separately during preparation of the ACD, obviated any need for corrective actions by the Commission to make those rates consistent with the PAEA policies. Moreover, by the terms of the PAEA, Commission review of service performance was limited to those areas where service standards were in effect. For many of its products, the Postal Service did not have service standards or service measurement procedures in effect during FY 2007.

Further complications arose from the submission of the cost, volume, revenue and performance data typically submitted with a rate case, but lacked analysis relative to the factors and objectives of the PAEA. Moreover, the reported data were not modified to organize the data around the new market dominant and competitive "products" established by the Commission's rules. The Commission recognizes that reporting under the PAEA is new and will require additional refinements over time. To this end, the Commission has proposed periodic reporting rules in Order No. 104 to establish the form and content of materials to be provided in future Postal Service reports to the Commission.

Chapter III – Reports on the Universal Service Obligation and Mail Monopoly

Status Report of the Universal Service Obligation and Mail Monopoly

The PAEA requires the Commission to submit a Report to the President and Congress on Universal Postal Service and the Postal Monopoly by December 19, 2008. The law asks the Commission to include in its report several relevant items such as: (1) a comprehensive review of the history of universal service and the postal monopoly; (2) the scope and standards of universal service and the postal monopoly under current law; (3) a description of geographic areas, populations, communities, and other groups not receiving service or receiving deficient service; (4) the scope and standards of universal service and the postal monopoly likely to be needed in the future; and (5) Commission recommended changes to universal service and the postal monopoly. The law also requests the Commission to solicit written comments from the Postal Service and to consult with the Postal Service, other federal agencies, users of the mails, enterprises in the private sector engaged in the delivery of mail, and the general public.

Of special interest is the Commission's approach to obtaining input from those whom Congress specifically identified in the above paragraph. The Commission initiated Docket No. PI2008-3 to solicit comments from all interested parties. The Commission sent letters to federal agencies thought to be stakeholders in the postal system to ensure their participation. Because the general public does not generally participate in Commission proceedings, a national survey was conducted by George Mason University, a contractor to the Commission, on the needs and expectations of household single-piece mailers. Also, to capture the needs and expectations of rural and regional communities, the Commission held field hearings in Flagstaff, Arizona; St. Paul, Minnesota; and Portsmouth, New Hampshire. Further, the Commission held a workshop in its hearing room to engage mailers and others in a dialogue concerning universal service and the postal monopoly. Lastly, the Commission held a hearing in Washington, DC to solicit comments from the postal unions, management associations and others.

As of the preparation of this annual report, the Commission has completed gathering all the information mandated by the PAEA, and is in the process of writing the report with the intention of releasing the report in December 2008.

Estimated Cost of Universal Service

The PAEA requires the Commission to report annually on the estimated cost to the Postal Service of providing universal service. The law requests three separate estimates: 1) the cost of providing service to areas of the Nation that would not receive service but for the universal service obligation; 2) the revenue foregone by providing

free or reduced rates for postal services as required by 39 U.S.C; and 3) other public services or activities related to the universal service obligation. Because the Commission's report on universal service and the monopoly is still in progress, estimates for 1) and 3) will be withheld until publication of the report.

The Postal Service provides statutory discounted rates for the nonprofit rate categories in Periodicals, Standard Regular, and Standard Enhanced Carrier Route (ECR). Additionally, statutory discounts are given to Periodicals Classroom and Science of Agriculture and to Library Rate. The table below presents the Commission's estimates of revenue forgone by the Postal Service in providing discounted rates to preferred categories of mail in FY 2007.

Table 3 – Revenue Foregone from Free and Reduced Price Mail for FY 2007 ($000)

Periodicals	**Foregone Estimate Revenue**
Nonprofit	12,976
Classroom	582
Total Periodicals	**$13,558**
Standard Mail	
Nonprofit	757,169
Nonprofit - ECR	150,449
Total Standard Mail	**$907,618**
Library Rate	(196)
Free-for-the-Blind Mail	61,168
Total	**$982,148**

Chapter IV – Legal Proceedings

Rulemakings Initiated in FY 2008

RM2008-4: Periodic Reporting Rules

On August 22, 2008, the Commission filed Order No. 104 which proposed rules on periodic reporting requirements for the Postal Service. The proposed rules are designed to implement all of the PAEA's provisions that make the Postal Service operations and finances transparent and accountable. The rules describe the scope of reporting and level of detail the Commission believes is needed to provide accountability and transparency with respect to Postal Service operations.

The proposed rules direct the Postal Service to provide, among other things, reports that support the Service's Annual Compliance Report, including:

- Cost and Revenue Analysis (CRA) Report;
- Cost Segments and Components (CSC) Report;
- Revenue, Pieces, and Weight (RPW) Report;
- Quarterly Statistics Report (QSR);
- Billing Determinants by Product; and
- Product Demand Elasticity with supporting documentation.

Reports that provide continuing financial and operating analysis, including:

- Quarterly Revenue, Pieces, and Weight Reports;
- Quarterly 10-Q filings;
- Annual 10-K filings; and
- Monthly National Consolidated Trial Balance and Revenue/Expense.

Summary reports, including:

- National Payroll Hours Summary Report;
- Postal Service Active Employee Statistical Summary; and
- Annual Integrated Financial Plan.

The proposed rules were filed August 22, 2008. Initial comments were due October 16, 2008. Reply comments were due November 14, 2008 with final rules to be published thereafter.

RM2008-5: Accounting and Periodic Reporting Rules

Section 2011 of the PAEA required the Secretary of the Treasury to develop recommendations regarding accounting principles and tax rules applicable to

competitive products. The Commission was directed upon receipt of those recommendations to provide interested persons an opportunity to comment on the recommendations, and then issue rules for the establishment and application of accounting principles and tax rules for the Postal Service with respect to competitive products.

On December 19, 2007, the Secretary of the Treasury submitted a report to the Commission containing recommendations concerning accounting principles and practices that should be followed by the Postal Service for identifying and valuing assets and liabilities associated with providing competitive products, and the substantive and procedural rules for determining an assumed Federal income tax on competitive products income. The Treasury Report discussed specific PAEA accounting and Competitive Products Enterprise income tax requirements, ultimately recommending an accounting approach believed would best meet these requirements. The Commission sought public comments on the Treasury report which were incorporated into the Commission's proposed rules.

On September 11, 2008, the Commission issued Order No. 106 - Order Proposing Accounting Practices and Tax Rules for Competitive Products. These proposed rules focus on establishing accounting practices for competitive products including the costing methodology to be used by the Postal Service; methods for valuing assets and liabilities; the financial reporting requirements for the competitive products enterprise; and rules related to calculating and transferring an assumed Federal income tax.

The proposed rules are intended to promote the goals of transparency and accountability without imposing undue burdens on the Postal Service. They are based on a theoretical, "on paper only" enterprise, do not require new accounting or data collection systems, maintain the Commission's existing definition of attributable cost, and provide the Postal Service optional means for calculating an assumed Federal income tax on competitive products income.

Order No. 106 provided the public 30 days to file initial comments and an additional 15 days to file reply comments. By statute, final rules must be issued by December 19, 2008, unless the Commission and the Postal Service agree on an extension.

RM2008-3: COMPLAINTS AND SERVICE INQUIRIES

The Commission has proposed new rules to address two types of administrative filings authorized under the new postal law: (1) complaints; and (2) rate and service inquiries. The proposed rules set forth procedures governing the disposition of complaints filed with the Commission.

The rules are designed to have the Commission hear and resolve complaints in a streamlined and efficient manner while providing appropriate due process for all

participants. The Commission solicited and received comments on the proposed rules and is in the process of finalizing these rules.

The proposed rules distinguish between the nature of complaints that may be filed with the Commission and recognize the primary mission of the Commission to foster public policy as set forth in the PAEA by focusing on issues and decisions with substantial ramifications. In order to be reviewed as a complaint, the substance of the complaint must deal with problems, needs, or concerns of more than only a limited number of persons or else unfair competition. In most cases, written communications that do not meet the form and manner of a complaint will be treated as rate or service inquiries. The Commission recognizes that in these instances the Postal Service may be the best avenue for resolution of these matters. The proposed rules allow the mailing public to bring their concerns directly to appropriate Postal Service personnel.

Complaints in the first category must satisfy certain "form and manner" requirements. The Commission must be able to ascertain and make an informed judgment about whether or not the complaint raises a material issue of fact or law under Section 3662(b)(1)(1)(A). Consistent with past practice of the Commission the rules explicitly encourage settlement of disputes and add the option of alternative dispute resolution procedures. A determination must be made within 90 days if the Commission will begin proceedings on a complaint.

Most local issues related to problems with individual mailers do not rise to the level of a public postal policy or regulatory concern. Generally, they raise issues which are isolated incidents or those affecting only a few mail users. These are best resolved by the Postal Service at the local level. The Commission will monitor these matters to determine if further Commission action is warranted.

The proposed rules establish a formal approach to the complaint process and due process rights for the filer of the complaint and the Postal Service. For rate and service inquiries the procedures are less formal and encourage the Postal Service to achieve informal resolution of the issues.

RM2008-1: CONFIDENTIAL BUSINESS INFORMATION, POSTAL SERVICE

Proposed rules were filed on August 26, 2008, in conformity with the statutory standards for according confidentiality to Postal Service materials. Statutory standards of confidentiality for Postal Service documents are provided in 39 U.S.C. 504(g) which states that the Postal Service may determine "that any document or other matter it provides to the Postal Regulatory Commission" is exempt from public disclosure under the law. The law also provides that the Postal Service must give reasons, in writing, for its claim. The Postal Service may claim as exempt from disclosure the name and address information of postal customers; certain commercial information, for example trade secrets; certain information related to the negotiation of collective bargaining agreements; information prepared for proceedings before the Commission or the federal

courts concerning postal rates, classes and services; reports and memoranda prepared by outside sources unless disclosure would have been required if the Postal Service had prepared the memoranda itself; and investigatory files compiled for law enforcement purposes, unless legally available to parties other than the Postal Service. The Commission interprets the PAEA as requiring the same kind of balancing of interests under the standards as the Federal Rules of Civil Procedure. Therefore, the Commission proposes rules that could lead to public disclosure of information that the Postal Service initially claimed as non-public. However, the Commission takes seriously its responsibility to achieve a fair balance between the commercial interests of the Postal Service and the public interest in disclosure of information concerning a public entity that operates in commercial markets.

Under the proposed rules, the Postal Service would notify the Commission at the time it files information that it considers specifically identified portions of its report to be non-public and to qualify for a degree of protection from public disclosure. The Postal Service must also include its reasoning for concluding the information is non-public.

In order to meet the often tight deadlines of the Commission, it is important that procedures developed in the rules prevent unnecessary delay in determining whether granting a person access to non-public materials is appropriate. Therefore, the rules propose a streamlined procedure for persons who agree to abide by the Commission's standard protective conditions. The person can attach an executed copy of the Commission's standard protective conditions to its motion; answers to that motion are due within three days after the motion is filed. If the standard motion is not attached, answers are due within seven days after the motion is filed.

The proposed rules also contain a "sunset provision" requiring that protective conditions afforded to any non-public materials filed by the Postal Service shall expire 10 years after such filing, unless the Commission or its authorized representative enters an order providing for an extension of the protective conditions. The Commission or its authorized representative can enter such order in its own discretion or upon the motion of the Postal Service.

The Commission believes that administrative convenience and sound records management practices will be served by this provision and the 10 year period for the sunset provision is adequate to protect the commercial interest of the Postal Service. Comments on the rules and on whether any specific category of non-public materials should be exempted from the sunset provision have been requested.

CLASSIFICATION CASES REVIEWED BY THE COMMISSION

MC2007-1: Bank of America

On October 3, 2007, the Postal Regulatory Commission recommended approval of the proposed baseline Negotiated Service Agreement between the Postal Service and the Bank of America Corporation (BAC). The Postal Service estimated total savings of $23.8 million from the agreement and anticipated a $5.5 million gain in contribution. In addition, the agreement was to have operational benefits to the Postal Service in the form of improved BAC mail addressing quality and adoption of new barcode and bulk mail facility acceptance technologies.

The savings were to be realized through improvements in six separate measures of mail addressing quality: a) increased read/accept rates for First Class mail; b) increased read/accept rates for Standard mail; c) reductions in return rates for First Class operational mail; d) reductions in return rates for First Class advertising mail; e) reductions in First Class mail forwarding rates; and f) reductions in undelivered as addressed (UAA) rates for Standard mail. As part of the agreement, BAC was offered per piece discounts, according to specific schedules applying to these six measures. Based on the Postal Service's estimated improvements in address quality according to the indicated measures and application of the discount schedules, BAC would garner $18.3 million in discounts.

The Commission agreed in concept with the Postal Service's use of this NSA to perform integrated pilot testing of new address quality technologies with a large mailer such as BAC. The Commission accepted the Postal Service's assertions that results from this NSA would prove useful in tailoring future NSAs with other mailers using the same or similar technologies. However, in its Decision, the Commission expressed concerns.

In particular, the Commission was concerned that the Postal Service's estimate of total cost savings from improved read/accept rates for BAC First Class and Standard mail were overly optimistic. The Postal Service did not present any current data specific to BAC with respect to these two mail classes in its proposal. Instead, older system-wide average baseline (existing) read/accept rates were used to measure anticipated improvements in rates. The Commission believed that read/accept rates for BAC First Class and Standard mail may have improved significantly from the baseline figures, and consequently that BAC could be granted discounts without offsetting cost savings to the Postal Service.

The Commission analyzed the Postal Service's financial posture using newer data and found that the Postal Service would lose $45.8 million in contribution through the NSA based on the higher system side a averages for read/accept rates reflected in the new data. The Commission also performed a second more conservative analysis, under the assumption that BAC's read/accept rates would improve further over these averages based on Six Sigma initiatives which the Company was already committed to. However in this case, the Commission still estimated a loss of $25.1 million. Additionally, the

Commission estimated that the Postal Service's total contribution from BAC mail would be about $1.5 billion and therefore regarded any potential loss from the NSA as relatively small. Further, the Commission judged that this NSA would create positive externalities, in the form of modified and better integrated address quality systems, that can be used in future NSAs with other mailers. Consequently, despite its concerns, the Commission approved the NSA but urged the Governors to confirm the operational benefits before proceeding.[2]

MC2007-3: Premium Forwarding Service

The Commission approved the Postal Service's request to change the status of Premium Forwarding Services (PFS) from experimental to permanent. With this service residential delivery customers and many post office box holders can request the Postal Service to reship all mail pieces received at a permanent address to a temporary address once a week through Priority Mail. Forwarding periods can range from two weeks to a year and applicants must pre-pay for the service at the time of enrollment. It is expected that the program will provide a valuable "high end" alternative to existing or ad-hoc piece by piece and class-specific forwarding services provided for First-Class, Periodical and Parcel Post mail.

MC2007-4: Bradford Group

On April 18, 2008, the Commission recommended approval of the NSA between the Postal Service and The Bradford Group (Bradford), a firm marketing collectible items largely through direct mail solicitations. The NSA offered Bradford per piece discounts for above threshold volume levels, negotiated separately for standard letter and flat mail. The discount schedules included incentives for volume expansion through higher per piece discounts per increased volume block. The Postal Service estimated an increase in revenue contribution from the NSA of $5.4 million net of discounts. This estimate was based on after discount volume forecasts provided by Bradford.

The Commission performed its own contribution analysis and concluded that the agreement would generate less new contribution over the three year contract than estimated by the Postal Service but would likely result in a benefit to the Postal Service. The Commission found that positive contributions are expected from the NSA within a range of feasible, after-discount volume levels; and that various risk containment measures included in the contract insulate the Postal Service from contribution losses that would otherwise be realized from volume levels outside these expected ranges. These findings led the Commission to recommend approval of the NSA.

[2]Commissioner Goldway provided a concurring opinion, while Vice Chairman Tisdale dissented.

MC2007-5: Life Line Screening

On May 29, 2008, the Commission recommended approval of the proposed three year baseline NSA between Life Line Screening (Life Line) and the Postal Service. Life Line markets preventive health screenings to consumers on a nationwide basis, in large part because of consumer awareness of the firm's services created through direct mail campaigns. Life Line relies on Standard Letter Mail solicitations as well as other media to generate local interest for direct screening events, its main revenue producer. The Postal Service estimated that the per piece discounts in the agreement would generate an additional 14 million pieces in the first year, and 23 million pieces in the last two years of the NSA. Based on the before and after rate volume increments forecasted by Life Line, the Postal Service estimated a $5.4 million increase in contribution from the NSA.

The Commission performed its own contribution analysis and concluded that the agreement would generate less new contribution than estimated by the Postal Service. However, the Commission's analysis showed that the Postal Service set contract terminating volume levels at amounts where the NSA contribution would be zero. Absent these arrangements, the Postal Service would lose contribution, if volume levels exceed the contract terminating levels due to unexpectedly favorable market circumstances. Similar to The Bradford Group agreement, the NSA also includes caps beyond which volume increments receive no discounts, and minimum volume commitments that Life Line must meet in order to earn discounts above volume threshold levels. The Commission found that all three protective measures, considered collectively, would effectively insulate the Postal Service from any financial harm caused by wide volume swings under the NSA. Therefore the Commission approved the NSA.

MC2008-1: Review of Non-postal Services

In accordance with 39 U.S.C. 404(E)(3) the Commission is to determine which "non-postal services" as defined in Section 404 (e)(1) *(i.e.* a service which is not included in the delivery of letters, printed matter, or mailable packages, including acceptance, collection, sorting, transportation, or other functions ancillary thereto) should continue and which should be terminated. The PAEA amends the Postal Reorganization Act, 39 U.S.C. 101 *et seq.* by among other things, limiting the Postal Service's authority to provide non-postal services to those it offered on January 1, 2006.

Section 404(e)(3) directs the Commission to review each non-postal service offered by the Postal Service on the date of the PAEA's enactment, December 20, 2006, within two years of that date. Any non-postal service the Commission concludes should not continue shall be terminated. Any non-postal service that the Commission authorizes to be continued is to be regulated under the title as a market dominant product, a competitive product or an experimental product.

The review of non-postal services is currently in progress with the Commission and a decision is to be rendered by December 19, 2008.

MC2008-2: Repositionable Notes

The Commission approved a request for a classification change which establishes Repositionable Notes as a permanent part of the mail classification.

MC2008-3: Bound Printed Matter

The request of the Postal Service to require Bound Printed Matter to be paid by permit imprint only was granted by the Commission. The Mail Classification schedule was modified to require that all Bound Printed Matter flats and parcels be paid by permit imprint only. This eliminates single-piece Bound Printed Matter pieces (those entered over the retail counter).

MC2008-4: Premium Forwarding Service

The Commission issued an order transferring Premium Forwarding Service from market dominant within the special services class to the competitive product list.

MC2008-5: Express Mail Contract 1

The Commission granted the Postal Service request to add the Express Mail Contract 1 to the Competitive Product List as a separate product under Negotiated Services Agreements, Domestic as Express Mail Contract 1.

MC2008-6: Inbound Direct Entry Contracts

The Commission authorized the Postal Service to add inbound direct entry contracts with foreign postal administrations to the Competitive Product List.

MC2008-7: Global Plus 2

The Commission approved a request of the Postal Service to add Global Plus 2 Negotiated Service Agreements to the Competitive Product List.

MC2008-8: Priority Mail Contract 1

The Commission approved a request from the Postal Service to have Priority Mail Contract 1 added to the Competitive Product List within the Mail Classification Schedule.

Table 4 – NSA Decisions Through the End of FY 2008

Type of NSA	FILED	APPROVED	DISAPPROVED
Market Dominant PRA	0	3	0
Market Dominant PAEA	0	0	0
Competitive PRA	0	0	0
Competitive PAEA	21	19	0

Note: The 3 Market Dominant NSAs were originally filed in FY 2007.

PUBLIC INFORMATION CASES

Public information cases are initiated as a means for the Commission to solicit comments from interested parties on various aspects of the Commission's work. During FY 2008, four such dockets were opened.

PI2008-1: Service Performance Measurement Systems for Market Dominant Products

The PAEA directs the Commission to consult with the Postal Service concerning the establishment of service standards for market dominant products. The service standards must be measured by an objective external performance measurement system, unless the Commission approves the use of an internal measurement system. Given its obligations under the PAEA and the Postal Service's measurement proposal, which characterized the various measurement approaches as either external or internal, the Commission initiated Docket No. PI2008-1 to solicit public comment on the Postal Service's proposed service performance measurement systems. The Commission issued Order No. 140 on November 25, 2008 approving the Postal Service's request for approval of its proposal measurement system.

PI2008-2: Review of Treasury Report

The PAEA required the Secretary of the Treasury, in consultation with the Postal Service and an independent certified public accounting firm, to develop recommendations for accounting practices and principles that will govern the operation of the Competitive Products Fund and the determination of an assumed Federal income tax to be imposed on competitive products income. Treasury submitted its report and recommendations to the Commission on December 19, 2007.

The PAEA also required that interested persons be given an opportunity to comment on the Report's recommendations in such manner as the Commission considers

appropriate. To fulfill that obligation, the Commission initiated Docket No. PI2008-2 soliciting comments on both Treasury's recommendations, and specific questions posed by the Commission in response to the Report.

After review of the comments, the Commission commenced a rulemaking proceeding to develop regulations to establish the accounting practices and principles to govern the operation of the competitive products and rules for determining the assumed Federal income tax on competitive products income. Interested persons were given an opportunity to comment on the proposed regulations, which will be finalized by the end of Calendar 2008.

PI2008-3: Report on Universal Postal Service and the Postal Monopoly

The PAEA requires the Commission to submit a report to the President and Congress on "universal postal service and the postal monopoly in the United States ... including the monopoly on the delivery of mail and on access to mailboxes." In preparing its report, the PRC is required to consult with the Postal Service and other Federal agencies, users of the mails, enterprises in the private sector engaged in the delivery of the mail, and the general public and address in its report any written comments that it receives. As part of its effort to fulfill these obligations, the Commission initiated Docket No. PI2008-3 to solicit comments on universal postal service and the postal monopoly.

PI2008-4: Inquiry into Cooperative Mail Rule Exception

The PAEA directs the Commission to examine the Cooperative Mail Rule Exception to determine whether it contains adequate safeguards to protect against abuses of rates for nonprofit mail and deception of consumers. The Commission is to report the results of this examination to the Postal Service, along with any recommendations it deems appropriate. During fiscal year 2008, the Commission initiated a docket to obtain public views on this topic and began work on its report.

COMPLAINT CASES REVIEWED BY THE COMMISSION

The Commission has administered three Complaint cases since the passage of the PAEA. The cases have been reviewed for both the applicability of the standards for complaints as established in the PAEA as well as the material issues which form the substance of the complaint.

C2008-1

Filed 12-4-07
Commission Decision Dismissed Complaint 2-1-08
Complaint of Michael Hammond

Michael Hammond filed a Complaint with the Commission which alleged his mail carrier halted delivery service to him at his home on December 18, 2006, because he failed to

relocate his mail receptacle to a specific site on his property after being notified to do so by the Postal Service. Mr. Hammond claimed he did not move his mail receptacle because of problems with snow removal which impacted the proposed new location. Mr. Hammond claimed that the actions of the Postal Service were in violation 39.U.S.C 3662 the Postal Accountability and Enhancement Act and asked the Commission to review the action and restore his mail service.

The Commission requested that local Postal Service officials resolve the matter with the customer. Local Postal Service officials worked to find a solution and the matter was resolved and the customer's mail service was resumed. Therefore, the Commission found the issues raised in the Complaint were moot and dismissed the case on February 1, 2008.

C2008-2

Filed 1-3-08
Commission Decision Dismissed the Complaint 4-2-08
Complaint on Bound Printed Matter

Douglas F. Carlson filed a Complaint with the Commission which alleged that the Postal Service acted unlawfully by restricting access to Bound Printed Matter (BPM) service at Postal Service retail windows. Mr. Carlson contended that the Postal Service was not in compliance with the Domestic Mail Classification system and discriminated against individuals and small business mailers in not offering BPM service at retail windows.

The Postal Service's initial response to the Commission provided the policy which had been communicated to retail window service facilities based upon a policy change. The policy required that BPM service be restricted to payment only if the mailer could affix the postage by stamp, postage meter or PC postage without using the window counter. The Commission rejected this policy change and determined the action resulted in a classification change and the Postal Service required a notice of classification change in order to change the requirements for BPM.

The Postal Service provided justification for the change in services and filed a classification change to require payment BPM by mailing permit imprint only. The classification change mooted the issue before the Commission and the Complaint was dismissed without prejudice in Order No. 68 in the event there was a later determination by the Commission that the classification change was inconsistent with the PAEA.

C2008-3

Filed 6-18-08
Complaint of Capital One Services, Inc.
Status: Active

The Capital One Services, Inc., Complaint is based upon allegations that the Postal Service engaged in discriminatory practices in violation of the law and Commission rulings in that:

- The Postal Service established a Negotiated Service Agreement with Bank of America that is "not pay for performance" and in reviewing a proposed Capital One NSA the Postal Service attempted to impose a "pay for performance" standard on Capital One;

- The basis for the Bank of America NSA only required a large volume mailer to implement the full array of specified mail processing systems in exchange for financial incentives tied to established baselines and the Postal Service did not apply this same standard to Capital One;

- By establishing the Bank of America, NSA, the Postal Service gave an undue or unreasonable preference to Bank of America;

- By not allowing Capital One to establish an NSA with the same standards as Bank of America, it was given an unfair competitive advantage over Capital One; and

- The Postal Service has created a "special classification" not available on public and reasonable terms to similarly situated mailers.

This case is still pending before the Commission.

Table 5 - COMPLAINTS UNDER PAEA

Docket No.	Case Name	Complaint Filed	Disposition	Complaint
C2008-1	Complaint of Michael Hammond	12/4/2007	Dismissed by Commission as moot.	Customer Michael Hammond had mail delivery stopped over a dispute with Postal Service on correct location of mailbox.
C2008-2	Complaint of Douglas F.Carlson	1/3/2008	Dismissed by Commission as moot.	Customer Douglas F. Carlson filed complaint on Postal Service policy of restricting certain types of payment for Bound Printed Matter (BPM) at retail windows. Postal Service filed new mail classification for BPM permitting only certain payment types which made the issues before the Commission moot.
C2008-3	Complaint of Capital One Services, Inc.	6/18/2008	Active status	Capital One Services, Inc. alleges that the Postal Service has engaged in discriminatory practices in violation of Commission rules and law by failing to give it a Negotiated Service Agreement (NSA) on the same or similar terms as the NSA currently in effect with Bank of America.

Chapter V – Other Commission Activities

Under the PAEA, the Commission is afforded a much stronger role in monitoring the service performance of the Postal Service. This role includes consulting with the Postal Service on establishing service standards that realistically reflect the Postal Service's current operations, approving any measurement system that is not externally derived, and reporting annually on Postal Service performance. The PAEA also greatly expands the Commission's role regarding International postal issues.

ESTABLISHMENT OF MODERN SERVICE STANDARDS

The Postal Accountability and Enhancement Act requires that the Postal Service, in consultation with the Commission, establish by regulation a set of modern service standards for market dominant products.[3] Through a series of monthly consultations, the Commission was informed by the Postal Service of its progress toward developing such regulations. In addition, the Commission was briefed by the Mailers' Technical Advisory Committee on its service standard recommendations to the Postal Service. The Commission also received comments from individual mailers, postal labor organizations, and other parties through a formal public inquiry concerning modern service standards. The Postal Service's regulations, entitled "Modern Service Standards for Market-Dominant Products," were published December 19, 2007.

The Postal Service's regulations resulted in a number of upgrades as well as downgrades in service standards, based upon the number of days to delivery between 3-Digit-ZIP Code pairs, for most classes of mail. Table 1 presents a summary of the percentage of ZIP Code pairs upgraded and downgraded by mail class (all values are rounded to the nearest integer).

[3]Section 301 for the PAEA is codified at 39 U.S.C. 3691.

Table 6 - 3-Digit Zip-Code Pairs Upgraded or Downgraded

Mail Class	Upgrades (%)	Downgrades (%)
First–Class	0%	3%
Periodicals	3%	67%
Standard Mail	21%	48%
Package Services	10%	68%
Total	34%	18%

Note: Percentages represent share of 3-Digt ZIP-Code pairs, not mail volume.

POSTAL SERVICE MARKET DOMINANT MEASUREMENT SYSTEMS

The PAEA requires the Postal Service to begin measuring and publicly reporting on its service performance for all market dominant products. The law directs that external measurement systems be used unless alternate systems are approved by the Postal Regulatory Commission. The Postal Service developed a proposed measurement system that included both internal and external aspects. In seeking approval of this system the Postal Service met regularly with the Commission.

On November 25, 2008, the Commission approved the Postal Service's request to employ internal service measurements developed from the Service's Intelligent Mail Barcode (IMb) data to track service performance of bulk First-Class and Standard letters and flats. This data would be combined with externally collected information on receipt date of mail pieces to provide the first system measuring the speed and consistency of delivery for most types of mail. The internal delivery confirmation system will be used to measure service for Package Services and an external system will be temporarily used for Periodicals.

In approving the hybrid system, the Commission considered the Postal Service's assessment that reliable external measurement of all products would be extremely expensive and difficult to implement. Comments received from interested parties generally agreed that it is important to utilize reliable existing data sources where possible, and to avoid requiring costly new external measurement systems.

Although the Commission approved the measurement system, it did have some concerns that the measurement system would not be representative of service performance for all mail. Assuming IMb scanning and reporting technology can be successfully implemented, and full service IMb is utilized by a representative cross-

section of mailers, this service measurement program should produce high quality, minimal cost results. Therefore, the Commission approved its use, and urged the Postal Service to proceed quickly to deploy this system.

The Commission will require the Postal Service to provide quarterly public progress reports while full service IMb is being tested and implemented and will carefully monitor IMb implementation and usage to assure that accurate and representative performance measurements are obtained. If necessary, modifications to the service performance measurement plan will be developed.

The Commission also identified problems with the Postal Service's proposal to combine the measurements for its diverse special services into one index. It found that the proposed measures fail to reflect actual performance for several of the more important services, including Delivery Confirmation and Return Receipt. Consequently, it informed the Postal Service that more realistic measures of actual performance need to be developed in these areas.

INTERNATIONAL

The Postal Accountability and Enhancement Act gives the Commission specific responsibility with respect to international postal treaties and conventions, including the Acts of the Universal Postal Union (UPU). The UPU is an international treaty organization headquartered in Bern, Switzerland, whose main mission is to facilitate quality universal mail service at affordable rates. While the U.S. Department of State is responsible for overall formulation of international postal policy and concluding international postal treaties such as the UPU Acts, the Department of State must request the Commission's view on whether any treaty, convention or amendment that establishes a rate or classification is consistent with our modern system of ratemaking for market dominant products. The Department of State must ensure that all U.S. positions in the UPU are consistent with our view unless there is a foreign policy or national security reason. In FY 2008, the Commission worked closely and collaboratively with the Department of State, Postal Service, Department of Commerce, Office of the U.S. Trade Representative, and the private sector on U.S. engagement in the UPU, particularly with respect to the negotiation of rates paid between postal administrations for the delivery of international mail. We played an active role in preparations and finalization of positions on over four hundred proposals considered at the UPU Congress that took place in Geneva this past summer to amend the UPU Acts.

The Commission has also actively promoted greater dialogue with international regulators and postal stakeholders to share the U.S. experience in postal reform. In FY 2008, the Commission hosted regulators from China, France, the European Union and Japan to exchange information on their respective experiences in postal reform. During the UPU Congress in Geneva, Chairman Blair gave a presentation on the U.S. experience in postal reform to an audience of over 1,500 high-level postal stakeholders representing governments, regulators, postal operators, international organizations and

the private sector. In September 2008, the Commissioners participated in the second U.S.-China Symposium on Postal Reform and Express Delivery that the Department of Commerce organized in Washington, DC, and included representatives from China's postal regulator, operator, and private sector. Chairman Blair spoke about the role of the Commission in regulating the Postal Service and the significant accomplishments achieved in implementing the PAEA. The Commission has also been an active, contributing member of the Federal Advisory Committee on International Postal and Delivery Services created under the PAEA and administered by the Department of State.

PERIODICALS COST STUDY

The PAEA directs the Postal Service and the Commission to jointly study the quality of the data used to determine the attributable costs of periodicals and opportunities for improving the efficiency of periodicals. The Commission has met with Postal Service experts, mailers, mailing associations, and Congress to explore these issues. Work in this area is ongoing.

PUBLIC OUTREACH EFFORTS

Overview

The Office of Public Affairs and Government Relations (OPAGR) serves as the public face of the Commission. The Office is the Commission's primary resource in support of public outreach and education, media relations, and liaison with Congress, the Postal Service, and other government agencies. The OPAGR Director advises Commissioners and Commission staff on legislative issues and policies related to the Commission and the Postal Service in addition to coordinating the preparation of both Congressional testimony and Congressional inquiries concerning the Commission policies and activities.

Congressional Testimony

The Chairman, the Commission Secretary, and the Director of the Office of Accountability and Compliance (OAC) appeared before Congressional Committees to report on the program plans and actions of the Commission and respond to questions from Members. Chairman Blair testified before the applicable House Subcommittee on Federal Workforce, Postal Service and the District of Columbia in October 2007, February, April and May of 2008. Chairman Blair also testified before the responsible Senate Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security in March 2008. The Secretary testified before a joint committee in April 2008, and the Director of OAC testified before the House Subcommittee in July 2008. Congressional testimony by Commissioners and staff is available online at the Commission website.

7/24/2008 Testimony of OAC Director John Waller, on the "Postal Service's Network Plan" before the House Subcommittee on Federal Workforce, Postal Service and the District of Columbia

5/8/2008 Testimony of Chairman Dan G. Blair on "Post-PAEA: What's Next?" before the House Subcommittee on Federal Workforce, Postal Service and the District of Columbia

4/24/2008 Testimony of Chairman Dan G. Blair on "Cooperative Mailing" before the House Subcommittee on Federal Workforce, Postal Service and the District of Columbia

4/3/2008 Testimony of Secretary Steve Williams on "Managing Diversity Leadership" before Joint Subcommittees on Federal Workforce, Postal Service & District of Columbia and Federal Financial Management, Government Information, Federal Services & International Security

3/5/2008 Testimony of Chairman Dan G. Blair on "The State of the U.S. Postal Service One Year After Reform" before the Senate Subcommittee on Federal Financial Management, Government Information, Federal Services and International Security

2/28/2008 Testimony of Chairman Dan G. Blair on "Implementing the Postal Accountability and Enhancement Act of 2006" before the House Subcommittee on Federal Workforce, Postal Service and the District of Columbia

2/4/2008 Submission of Performance Budget Plan Fiscal Year 2009

10/30/2007 Testimony of Chairman Dan G. Blair on "Will Increased Rates put Mailers out of Business?" before the House Subcommittee on Federal Workforce, Postal Service and the District of Columbia

Outreach Activity

During the first full year of operation under the new law, the Commission has engaged in a number of public outreach activities as a key part of its statutory responsibilities.

- As noted earlier, field hearings for a study on the Universal Service Obligation and Mailbox Monopoly were held in Flagstaff, Arizona; St. Paul, Minnesota; Portsmouth, New Hampshire; and a hearing in Washington, DC, along with a public workshop in Washington, DC;

- Appearances by Commissioners and staff before stakeholders and other interested groups such as mailer and industry organizations, postal labor unions and management associations, professional organizations, trade press, and international

bodies to discuss the work of the Commission, engage in informal dialogue and respond to questions; and

- Participation in technical conferences such as those administered by Rutgers University Center for Research in Regulated Industries by presenting technical papers and serving as discussants and session chairs.

Soliciting Public Comments

The Commission solicits public comment in rulemakings, complaints, mail classification cases, public inquiries, rate cases and other matters. There is an opportunity for both formal and informal comment, and both initial and reply comments.

Commenters are encouraged to use the electronic filing system to file their comments online. The Dockets Manager frequently provides hands-on assistance as necessary to new participants. Comments filed electronically are published on our website under the appropriate docket number.

The Commission also maintains a public commenter file containing letters, emails and faxes for each docket. The file is accessible to the Commission and is available for public inspection.

Public Representatives

Section 505 of the PAEA requires the Commission to designate an Officer of the Commission to represent the interests of the general public in all public proceedings that come before the Commission. Anyone from outside the Commission may contact and consult with the Public Representative during the course of a case to discuss how the public interest may be affected. The name and contact information for a designated Public Representative for each active docket is posted on the Commission's website. The Public Representative is generally not bound by exparte restrictions imposed on Commissioners and staff involved in decision-making, and may draw upon analytical and legal resources of the Commission as requiried.

In FY 2008, eight individuals, drawn from the Commission's staff, have served as Public Representatives in 45 Commission dockets.

Consumer Relations

A system was established in FY 2008 to coordinate responses to public and consumer inquiries and correspondence through the OPAGR. A new position, Consumer Relations Specialist, was created and filled to respond to customer inquiries, handle complaints which do not rise to the level of formal complaints, and serve as a liaison with the Office of Consumer Advocate of the Postal Service for service issues.

The Commission began development of a process to manage and track public inquiries, correspondence, and informal complaints. Inquiries will be tracked based on source, such as consumer, media, congressional, or local or state government, along with nature of the inquiries as to whether they are questions, comments, or informal complaints. Further in-depth breakdowns relating to specific service categories and sub-categories, such as retail, delivery, rates, claims, international mail, employee behavior, wait time in line, and other factors the Commission deems of interest to the public will also be tracked. This process will aid the Commission in performing general analyses related to quality of service, and will identify concerns, trends, and potential systemic service problems as part of PAEA's requirement to monitor service.

Modernized Website

The Commission's website, located at http://www.prc.gov, is a significant means of public outreach and was redesigned in April 2008. The website enhances communications with stakeholders, incorporates security improvements, and is more readily accessible to individuals with disabilities.

Consumers can contact the Commission and provide comments or questions regarding rates and service through a comment link on email via the website. Submissions are reviewed and responded to in a timely manner, with service issues referred to the Postal Service's Office of Consumer Advocate as necessary. All e-mails received are available for public inspection at the Commission's offices. Messages concerning postal rates and services become part of the commission's record in the Commenter file for any pertinent active cases.

Other features of value to stakeholders include:

- A direct link to a Consumer Price Index-Urban (CPI-U) trend chart used by mailers for budget planning;

- One-click access to the PRC's Daily Listings (added at users' request);

- A personalized document alert email notification system designed to provide instant notification to stakeholders who sign up for notification when documents meeting pre-selected criteria are published on the website; and

- Additional links for postal information, including the Office of the Consumer Advocate of the Postal Service, local District Consumer Affairs Offices, the Post Office locator, USPS frequently asked questions, postal rates and fees, and other links of consumer interest.

Injury Compensation

The Postal Regulatory Commission continues to provide a safe work environment for its employees. The Commission ended FY 2008 accident free with no on-the-job injuries or lost workdays.

Equal Employment Opportunity (EEO)

During FY 2008, the Commission had no informal or formal EEO complaint filings or counseling requests.

Diversity

In 2008, the Commission continued its agency commitment to support initiatives to recruit, develop and retain a skilled, high-achieving, and diverse workforce. The Commission made measurable progress in this area, ending the year with 55 percent of its female employees in executive or professional level positions. Progress was also made with minorities representing 11 percent of the executive and professional workforce and 20 percent of the overall workforce.

Freedom of Information Act (FOIA)

The Commission disseminates its official orders, opinions and *Federal Register* Notices through the Library and Dockets section of its website. Any public document, including its own, which is filed with the Commission, is available the same day on the website's Daily Listing link. Subscribers can receive email notification of new postings. Accessibility of Commission information has limited the number of FOIA requests.

The Commission received 32 FOIA requests in FY 2008, many of which were redirected to the U.S. Postal Service in an average of five days. The Commission uses both written and electronic methods, depending on the initial contact, to respond to the public. The Commission recently certified its online FOIA Reading Room as meeting statutory requirements.

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