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POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

ANNUAL COMPLIANCE REVIEW, 2017 Docket No. ACR2017

UNITED STATES POSTAL SERVICE
FY 2017 ANNUAL COMPLIANCE REPORT

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INTRODUCTION

The United States Postal Service hereby submits its Fiscal Year 2017 Annual Compliance Report (ACR or Report). The Report is provided pursuant to 39 U.S.C. Section 3652, which requires the Postal Service to file with the Postal Regulatory Commission, within 90 days after the end of each fiscal year (FY), a variety of data on costs, revenues, rates, and quality of service, in order to “demonstrate that all products during such year complied with all applicable requirements” of title 39.¹

Overall, the Report demonstrates that the Postal Service maintained steady progress on most metrics, despite an environment of falling mail volumes – a trend that accelerated in the past year – and significant legal constraints. The Postal Service built upon its achievements of the prior year and further improved service performance for a vast majority of its products in FY 2017, and it also improved on all measures of customer experience. The Postal Service’s market dominant and competitive products were broadly in compliance with the requirements of chapter 36 over the course of FY 2017. The Postal Service reduced the number of workshare passthroughs above 100 percent by eleven, and, in many cases, those passthroughs that remained above 100 percent either fit into one of the statutory exceptions or will be corrected when the Docket No. R2018-1 price changes take effect next month. Competitive product volumes and revenues continued to grow, resulting in a total net competitive contribution of more than 23 percent of institutional costs.

¹ Unless specified otherwise, section numbers used herein refer to statutory provisions in title 39, United States Code.
I. OVERVIEW OF REPORT

A. Contents

This Report consists of both the present document and underlying data appended as 74 separate folders. The present document contains only the most salient information from those folders, in order to demonstrate compliance with title 39 and the Commission’s annual reporting rules. Consistent with the structure that has been used in the past, Section I provides an overview of this Report, its contents, and its methodologies. Section II analyzes market dominant pricing compliance. Section III addresses service performance, customer satisfaction, and consumer access. Section IV discusses competitive products compliance. Section V covers market tests and nonpostal services. Finally, Section VI describes the nonpublic annex.

More detailed information than is contained in this document may be found in the appended folders. A list of the appended folders appears at Attachment One. Each folder includes a preface document explaining its purpose, background, structure, and relationship with other materials in the Report. Broadly speaking, there are three types of data in the appended folders: (1) product costing material; (2) intra-product cost analyses; and (3) billing determinants. The focus of the product costing material, in terms of ultimate output, is the Cost and Revenue Analysis report (CRA), at USPS-FY17-1, and the International Cost and Revenue Analysis report (ICRA), at USPS-FY17-NP2. The intra-product cost analyses underpin Section II’s examination of

3 The folders are sequentially numbered and labeled as USPS-FY17-1, USPS-FY17-2, etc. Folders in the nonpublic annex, discussed in Section VI below, are labeled as USPS-FY17-NP1, USPS-FY17-NP2, etc. (with “NP” signifying “nonpublic”).
workshare discounts. The billing determinants set forth the volume and calculated revenue for each rate cell of every mail product.

Certain materials are presented in two versions, one public and the other nonpublic. The public versions are limited to information on individual market dominant products and aggregate information on competitive products. The corresponding nonpublic versions contain either disaggregated information on competitive products or information on both market dominant and competitive products in contexts in which it is not possible to segregate the two.

Section 3652(g) requires the Postal Service to submit, together with this Report, a copy of its most recent Comprehensive Statement. A copy of the Postal Service’s FY 2017 Comprehensive Statement appears within the FY 2017 Annual Report in USPS-FY17-17. Similarly, a copy of the Postal Service’s annual report to the Secretary of the Treasury regarding the Competitive Products Fund, required by section 2012(i), appears as part of USPS-FY17-39, along with the other Competitive Products Fund materials required by Commission Rules 3060.20 through 3060.23.

B. Roadmap

A separate roadmap document is included at USPS-FY17-9. The roadmap is a technical document that consolidates brief descriptions of each of the appended folders and of the flow of inputs and outputs among them. It also discusses any changes between the methodologies used to prepare this Report and the methodologies applied by the Commission in the FY 2016 Annual Compliance Determination (ACD). In addition, it includes the listing of special studies and the discussion of obsolescence required by Commission Rule 3050.12.
C. Methodology

In general, the Postal Service has prepared this Report using the methodologies most recently approved or applied by the Commission. Any methodology changes are identified in USPS-FY17-9, and, where appropriate, in the preface accompanying each of the appended folders.

A noteworthy difference between this Report and previous ACRs relates to the reporting of attributable costs. In the CRAs for years before FY 2016, the attributable costs of a product were the sum of its volume variable and product specific costs. In compliance with Commission Order No. 3506, in this Report’s CRA the attributable costs of a product are the sum of its volume variable and product specific costs, plus the product’s inframarginal costs calculated as part of the estimation of the product’s incremental costs. Thus, computationally, the attributable costs of each individual product reported in the CRA should in theory match the incremental costs of the same product. For market dominant products, those incremental cost estimates are

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5 In practice, exceptions occur, such as in instances (previously acknowledged by the Commission) in which computational complications preclude separate estimation of incremental costs for certain products, most notably international mail products. See Order No. 3641, Order Adopting Final Rules on Changes Concerning Attributable Costing, PRC Docket No. RM2016-3 (Dec. 1, 2016), at 6. For individual international products, the reported attributable costs will continue to be calculated as the volume variable plus product specific costs. But separate group incremental costs are developed this year for the aggregate groups of market dominant international products and competitive international products. Moreover, that same group of competitive international products is now directly included in the calculation of the group incremental costs for all competitive products applied in the cross-subsidy test for section 3633(a)(1), as discussed below. For domestic negotiated service agreements (NSAs), in contrast, incremental cost estimates are developed this year for individual NSA products. These NSA estimates are based on approximations of the relevant cost driver components for individual NSA products. Consequently, in accordance with Order Nos. 3506 and 3641, inframarginal cost estimates have now been developed for domestic mail products, and are included (along with volume variable and product specific costs) in the attributable costs presented in the CRA reports. For more details, see the preface to USPS-FY17-43.
developed in a public folder, USPS-FY17-43 (Market Dominant Incremental Costs). For competitive products, the incremental costs are developed in either nonpublic folder USPS-FY17-NP10 (Competitive Products Incremental Costs) or, for domestic competitive negotiated service agreement (NSA) products, in nonpublic folder USPS-FY17-NP27.

The change in the measurement of attributable costs potentially affects the ACR in several ways. For example, in the application of the cross-subsidy test for competitive products required under subsection 3633(a)(1), there is little change, as the analysis still compares the sum of competitive products’ revenues with the group incremental costs of competitive products as a whole. But to ensure that each individual competitive product recovers its attributable costs as required by subsection 3633(a)(2), the newly expanded measure of attributable costs is employed, creating a higher standard than the previous measure of volume variable plus product specific costs. Similarly, to ensure that competitive products collectively recover an appropriate share of institutional costs as required by subsection 3633(a)(3), the target share is compared with the difference between the sum of competitive products’ revenues and the sum of competitive products’ redefined attributable costs. Consistent with how this exercise has been conducted in the past, institutional costs are defined as the difference between total accrued costs and the sum of the attributable costs of each

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6 Those are calculated in USPS-FY17-NP10 largely as they have been in the past, except that this year, as noted above, the incremental costs for the group of international competitive products as a whole have been estimated, and the group incremental costs have also been estimated for the combined group of all domestic and international competitive mail. This addresses a suggestion by the Commission in the FY 2016 Annual Compliance Determination, and constitutes a clear improvement over past practice in which the volume variable and products specific costs of competitive International mail were used as a proxy for the incremental costs of that subset of competitive mail products. See Annual Compliance Determination Report, Fiscal Year 2016, PRC Docket No. ACR2016 (March 28, 2017), at 65 (FY 2016 ACD).
market dominant and competitive product. The attributable costs of each domestic market dominant and competitive product used in this exercise notably reflect the definitional changes resulting from Order Nos. 3506 and 3641. As a consequence of the addition of each product’s inframarginal cost to what previously had been only the sum of the product’s volume variable and product specific costs, the costs labelled as attributable costs in each row of the FY 2017 CRA are not directly comparable to the costs reported with the same label in the CRAs for all years prior to FY 2016. Comparisons of product costs between FY 2017 and previous years therefore require a measure of caution.

In accordance with Commission Rule 3050.13, USPS-FY17-9 includes a table listing, in chronological order, the Postal Service’s proposals to change analytic principles that either were pending when the FY 2016 ACR was submitted or have been filed since then.
II. **MARKET DOMINANT PRODUCTS**

Below, the Postal Service discusses, for each market dominant mail class, FY 2017 costs, revenues, and volumes by product, as well as intra-product workshare discounts and passthroughs. Comprehensive cost, revenue, and volume data are contained in the CRA, at USPS-FY17-1, and in the ICRA, at USPS-FY17-NP2. Full data regarding workshare discounts and passthroughs are contained in USPS-FY17-3.

In some limited instances, workshare discount passthroughs that were above 100 percent of avoided costs in FY 2017 do not fit within any of the exceptions listed in Section 3622(e)(2). However, as noted below, many of these passthroughs will shift to 100 percent or below once the prices approved in Docket No. R2018-1 go into effect on January 21, 2018. As to the remaining passthroughs, the Postal Service plans to address them in future price cases.

A. **First-Class Mail**

1. **Cost, Revenues, and Volumes**

Costs, revenues, and volumes for First-Class Mail products appear in the table that follows on the next page.
Table 1: First-Class Mail Volume, Revenue, and Cost by Product

<table>
<thead>
<tr>
<th>Product</th>
<th>Volume (million)</th>
<th>Revenue ($million)</th>
<th>Attributable Cost ($million)</th>
<th>Contribution ($million)</th>
<th>Revenue/Piece ($)</th>
<th>Cost/Piece ($)</th>
<th>Unit Contribution ($)</th>
<th>Cost Coverage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single-Piece Letters/Cards</td>
<td>18,503</td>
<td>8,963</td>
<td>5,532</td>
<td>3,431</td>
<td>0.484</td>
<td>0.299</td>
<td>0.185</td>
<td>162.02</td>
</tr>
<tr>
<td>Presorted Letters/Cards</td>
<td>38,795</td>
<td>14,550</td>
<td>4,565</td>
<td>9,985</td>
<td>0.375</td>
<td>0.118</td>
<td>0.257</td>
<td>318.74</td>
</tr>
<tr>
<td>Flats</td>
<td>1,448</td>
<td>1,987</td>
<td>1,533</td>
<td>454</td>
<td>1.372</td>
<td>1.058</td>
<td>0.314</td>
<td>129.63</td>
</tr>
<tr>
<td>Parcels</td>
<td>191</td>
<td>547</td>
<td>479</td>
<td>68</td>
<td>2.863</td>
<td>2.507</td>
<td>0.356</td>
<td>114.20</td>
</tr>
<tr>
<td>First-Class Mail Fees</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total First-Class Domestic Mail (incl. fees)</td>
<td>58,938</td>
<td>26,184</td>
<td>12,108</td>
<td>14,075</td>
<td>0.444</td>
<td>0.205</td>
<td>0.239</td>
<td>216.25</td>
</tr>
<tr>
<td>Outbound Single-Piece First-Class Mail International</td>
<td>152</td>
<td>231</td>
<td>139</td>
<td>92</td>
<td>1.519</td>
<td>0.916</td>
<td>0.604</td>
<td>165.89</td>
</tr>
<tr>
<td>Inbound Letter Post</td>
<td>401</td>
<td>293</td>
<td>463</td>
<td>-170</td>
<td>0.731</td>
<td>1.156</td>
<td>-0.424</td>
<td>63.28</td>
</tr>
<tr>
<td>Total First-Class Mail</td>
<td>59,491</td>
<td>26,708</td>
<td>12,711</td>
<td>13,997</td>
<td>0.449</td>
<td>0.214</td>
<td>0.235</td>
<td>210.12</td>
</tr>
</tbody>
</table>

With the exception of Inbound Letter Post, all First-Class Mail products covered their attributable costs in FY 2017, with most of them contributing significantly to institutional costs. This comports with the historical role of First-Class Mail as providing the highest contribution to institutional costs of all mail classes. Unfortunately, whereas the year-over-year decline in First-Class Mail volume had been slowing in recent years, it accelerated in FY 2017, with the class losing 4.1 percent, or 2.5 billion pieces. In comparison, First-Class Mail’s volume losses over the previous several years were the following: 6.6 percent (5.7 billion pieces) in FY 2010, 6.4 percent (4.8 billion pieces) in FY 2011, 5.6 percent (4.3 billion pieces) in FY 2012, 4.2 percent (2.9 billion pieces) in
FY 2013, 3.3 percent (2.2 billion pieces) in FY 2014, 2.1 percent (1.4 billion pieces) in FY 2015, and 1.9 percent (1.2 billion pieces) in FY 2016.

In its final year as a market dominant product, the cost coverage for First-Class Mail Parcels was 114.20 percent. On September 3, 2017, the product transferred to the competitive product list.\(^7\)

Inbound Letter Post did not cover its attributable costs in FY 2017; however, this stemmed from the product's unique pricing regime. The Postal Service does not independently determine the prices for delivering foreign origin mail. Rather, these prices are set according to a Universal Postal Union (UPU) terminal dues formula established in the Universal Postal Convention. The Postal Service has been collaborating with other federal agencies, including the Department of State, which has lead responsibility for representation of the United States in the UPU, to improve cost coverage on Inbound Letter Post mail. Based on outcomes at the UPU Istanbul Congress, the Postal Service expects significant increases in Inbound Letter Post terminal dues revenues based on the new Convention cycle effective in January 2018. Indeed, in Docket No. R2018-1, the Commission found that the price increase for Inbound Letter Post would be 16.732 percent, effective January 21, 2018.\(^8\) The upcoming increases in terminal dues should substantially improve the cost coverage for this product moving forward.

\(^7\) Order No. 4032, Order Approving Price Adjustment for First-Class Package Service Product, PRC Docket No. CP2017-230 (Aug. 9, 2017). Keys and Identification Devices remained market dominant, and are now classified under First-Class Mail Flats.

\(^8\) Order No. 4215, Order on Price Adjustments for First-Class Mail, USPS Marketing Mail, Periodicals, Package Services, and Special Services Products and Related Mail Classification Changes, PRC Docket No. R2018-1 (Nov. 9, 2017), at 9 (Order No. 4215).
2. Workshare Discounts and Passthroughs

a. Presorted Letters and Cards

Four of the nine First-Class Mail Presorted Letters and Cards workshare discounts exceeded 100 percent of avoided costs: Automation Automated Area Distribution Center (AADC) Letters (117.6 percent), Automation Mixed AADC Cards (142.9 percent), Automation AADC Cards (133.3 percent), and Automation 5-Digit Cards (118.2 percent).

i. Automation AADC Letters

The passthrough for Automation AADC Letters was 117.6 percent (discount of 2 cents compared to the cost avoidance of 1.7 cents). In Docket No. R2018-1, the Postal Service reduced the discount to 1.6 cents, so when the Docket No. R2018-1 prices take effect, the passthrough will be 94.1 percent. Therefore, the Postal Service believes that no further action is necessary with respect to this passthrough.

ii. Automation Mixed AADC Cards

The passthrough for Automation Mixed AADC Cards was 142.9 percent (discount of 1.0 cents and cost avoidance of 0.7 cents). In Docket No. R2018-1, the Postal Service reduced the discount to 0.6 cents, so when the Docket No. R2018-1 prices take effect, the passthrough will be 85.7 percent. Therefore, the Postal Service believes that no further action is necessary with respect to this passthrough.

iii. Automation AADC Cards

The passthrough for Automation AADC Cards was 133.3 percent (discount of 0.8 cents and cost avoidance of 0.6 cents). In Docket No. R2018-1, the Postal Service reduced the discount to 0.6 cents, so when the Docket No. R2018-1 prices take effect,
the passthrough will be 100.0 percent. Therefore, the Postal Service believes that no further action is necessary with respect to this passthrough.

iv. Automation 5-Digit Cards

The passthrough for Automation 5-Digit Cards was 118.2 percent (discount of 1.3 cents and cost avoidance of 1.1 cents). In Docket No. R2018-1, the Postal Service reduced the discount to 1.1 cents, so when the Docket No. R2018-1 prices take effect, the passthrough will be 100.0 percent. Therefore, the Postal Service believes that no further action is necessary with respect to this passthrough.

b. Flats

Of the three Flats workshare discounts, only the Automation 5-Digit Flats discount exceeded 100 percent of avoided costs. Its passthrough was 129.6 percent (discount of 18.4 cents and cost avoidance of 14.2 cents). In Docket No. R2018-1, the Postal Service reduced the discount to 11.9 cents to match the FY 2016 cost avoidance. The FY 2017 cost avoidance increased to 14.2 cents, so when the Docket No. R2018-1 prices take effect, the passthrough will be 83.8 percent. Therefore, the Postal Service believes that no further action is necessary with respect to this passthrough.

3. First-Class Mail Promotions

During FY 2017, the Postal Service offered three First-Class Mail promotions, discussed in turn below.

a. Personalized Color Transpromo Promotion

The Personalized Color Transpromo Promotion (October 1 to December 31, 2016, and July 1 to December 31, 2017) provides participating mailers an upfront two-
percent postage discount on bills and statements mailed as First-Class Mail presort or
automation letters. To qualify, mailpieces are required to feature marketing messages
in dynamic/variable color print. Mailpieces from mailers who participated in the
promotion in previous years must also include personalized messaging. As of
September 30, 2017, the Postal Service had issued $9.4 million in discounts for 1.2
billion First-Class Mail pieces.

b. Emerging and Advanced Technology/Video in Print Promotion

The Emerging and Advanced Technology/Video in Print Promotion (March 1 to
August 31, 2017) provided participating mailers an upfront two-percent postage
discount on First-Class Mail presort or automation letters, cards, and flats, as well as
regular and nonprofit USPS Marketing Mail letters and flats. To qualify, mailpieces were
required to feature advanced technology such as Near Field Communication, enhanced
augmented reality, Video in Print, or Programmatic and Retargeting Direct Mail. Over
the course of the program, the Postal Service issued $3.1 million in discounts for
roughly 407 million First-Class Mail pieces.

c. Earned Value Reply Mail Promotion

The Earned Value Reply Mail Promotion (January 1 to June 30, 2017) provided
participating mailers a five-cent postage credit for each First-Class Mail Business Reply
Mail (BRM) and Courtesy Reply Mail (CRM) piece returned to the mailer during the
promotion period. At the end of the promotion period, the total credit amount earned
was applied to the mailer’s permit account for application to future mailings of First-
Class Mail presort and automation letters, cards, and flats, and USPS Marketing Mail
letters and flats. Over the course of the program, the Postal Service issued
approximately $49.2 million in credits for roughly 1.1 billion BRM and CRM pieces. To date, approximately $38.7 million worth of credits have been used on First-Class Mail.

B. USPS Marketing Mail

1. Cost, Revenues, and Volumes

Costs, revenues, and volumes for USPS Marketing Mail products appear below.

<table>
<thead>
<tr>
<th>Product</th>
<th>Volume (million)</th>
<th>Revenue ($million)</th>
<th>Attributable Cost ($million)</th>
<th>Contribution ($million)</th>
<th>Revenue/Piece ($)</th>
<th>Cost/Piece ($)</th>
<th>Unit Contribution ($)</th>
<th>Cost Coverage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>HD/Sat Letters</td>
<td>7,094</td>
<td>1,089</td>
<td>515</td>
<td>574</td>
<td>0.154</td>
<td>0.073</td>
<td>0.081</td>
<td>211.5</td>
</tr>
<tr>
<td>HD/Sat Flats &amp; Parcels</td>
<td>11,231</td>
<td>1,979</td>
<td>1,260</td>
<td>719</td>
<td>0.176</td>
<td>0.112</td>
<td>0.064</td>
<td>157.1</td>
</tr>
<tr>
<td>Carrier Route</td>
<td>7,133</td>
<td>1,859</td>
<td>1,498</td>
<td>361</td>
<td>0.261</td>
<td>0.210</td>
<td>0.051</td>
<td>124.1</td>
</tr>
<tr>
<td>Letters</td>
<td>46,973</td>
<td>9,574</td>
<td>4,912</td>
<td>4,662</td>
<td>0.204</td>
<td>0.105</td>
<td>0.099</td>
<td>194.9</td>
</tr>
<tr>
<td>Flats</td>
<td>4,944</td>
<td>1,900</td>
<td>2,569</td>
<td>-669</td>
<td>0.384</td>
<td>0.520</td>
<td>-0.135</td>
<td>73.9</td>
</tr>
<tr>
<td>Parcels</td>
<td>41</td>
<td>46</td>
<td>73</td>
<td>-27</td>
<td>1.266</td>
<td>1.793</td>
<td>-0.667</td>
<td>62.8</td>
</tr>
<tr>
<td>Every Door Direct Mail Retail</td>
<td>758</td>
<td>134</td>
<td>50</td>
<td>84</td>
<td>0.177</td>
<td>0.066</td>
<td>0.111</td>
<td>267.9</td>
</tr>
<tr>
<td>Marketing Mail NSAs</td>
<td>195</td>
<td>47</td>
<td>41</td>
<td>6</td>
<td>0.240</td>
<td>0.210</td>
<td>0.030</td>
<td>114.5</td>
</tr>
<tr>
<td>Marketing Mail Fees</td>
<td>44</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Marketing Mail (incl. fees)</td>
<td>78,370</td>
<td>16,672</td>
<td>10,918</td>
<td>5,754</td>
<td>0.213</td>
<td>0.139</td>
<td>0.073</td>
<td>152.7</td>
</tr>
</tbody>
</table>

As shown above, all USPS Marketing Mail products, other than USPS Marketing Mail Parcels and USPS Marketing Mail Flats, covered their attributable costs in FY 2017. As a class, USPS Marketing Mail covered its attributable costs and contributed significantly to institutional costs.

Under section 3626(a)(6), when the Postal Service adjusts USPS Marketing Mail prices, the estimated average revenue per piece for USPS Marketing Mail sent by nonprofit mailers must equal, as nearly as practicable, 60 percent of the estimated
average revenue per piece for USPS Marketing Mail sent by commercial customers. For FY 2017, the ratio was 58.74 percent.⁹

a. USPS Marketing Mail Parcels

USPS Marketing Mail Parcels covered 62.8 percent of its attributable costs in FY 2017, down from 63.8 percent in FY 2016. While cost per piece fell 3.6 percent in FY 2017, going from $1.86 to $1.79, revenue per piece fell more quickly, declining 5.0 percent, from $1.19 to $1.13, in part because of the removal of the exigent surcharges in the third quarter of FY 2016. The fall in revenue was due in part to a reduction in the average per-piece weight of parcels, which went from 6.1 ounces to 5.6 ounces, or around 8 percent.

The Postal Service remains committed to improving Parcels cost coverage through above-average price increases. In Docket No. R2018-1, the Postal Service increased Parcels prices by 2.768 percent, 43 percent higher than the class average increase of 1.936 percent. This was consistent with the trend over the last several years of increasing the product’s prices higher than the class average, as demonstrated below.

<table>
<thead>
<tr>
<th>Docket No.</th>
<th>(A) Parcels Percent Price Increase</th>
<th>(B) Overall USPS MM Price Increase</th>
<th>(A) as Percent of (B)</th>
</tr>
</thead>
<tbody>
<tr>
<td>R2013-10</td>
<td>1.820%</td>
<td>1.607%</td>
<td>113.2%</td>
</tr>
<tr>
<td>R2015-4</td>
<td>9.295%</td>
<td>1.926%</td>
<td>482.6%</td>
</tr>
<tr>
<td>R2017-1</td>
<td>1.583%</td>
<td>0.900%</td>
<td>175.9%</td>
</tr>
<tr>
<td>R2018-1</td>
<td>2.768%</td>
<td>1.936%</td>
<td>143.0%</td>
</tr>
</tbody>
</table>

⁹ In conformance with section 3626(a)(6), the prices the Postal Service proposed in both of its most recent price cases were designed to result in a ratio of 60.0 percent. Order No. 4215, supra note 8, at 44; Order No. 3610, Order on Price Adjustments for First-Class Mail, Standard Mail, Periodicals, and Package Services Products and Related Mail Classification Changes, PRC Docket No. R2017-1 (Nov. 15, 2016), at 42 (Order No. 3610). However, as the Commission has repeatedly acknowledged, changes in the mix of mail after price changes make it difficult to precisely attain the 60 percent relationship required by law. See, e.g., FY 2016 ACD, at 41.
b. USPS Marketing Mail Flats

USPS Marketing Mail Flats covered 73.9 percent of its attributable costs in FY 2017, down 5.8 percentage points from FY 2016. Per-piece revenue rose modestly over the previous year, increasing 2.4 percent, but this was unfortunately offset by a 9.7 percent increase in per-piece cost. The increase in cost was due in part to the migration of Flats Sequencing System (FSS) pieces from Flats to Carrier Route Flats, as a result of the Docket No. R2017-1 price change. The migration caused Flats mail processing costs (Cost Segment 3) to grow, because the migrating pieces (Carrier Route destinating in FSS zones) had lower mail processing costs relative to the presort levels that remained (e.g., Mixed Area Distribution Center (ADC), ADC, and 3-Digit).¹⁰

Importantly, the decline in Flats cost coverage caused by the migration does not reflect a decline in overall Postal Service efficiency. Combined, Flats and Carrier Route costs increased only 1.63 percent. As discussed in more detail in section II.B.3., Commission Flats Directives, the Postal Service remains committed to raising the product’s cost coverage, and plans to recommend to the Governors an increase in Flats prices of at least 1.05 times the class average in the next market dominant rate case.

2. Workshare Discounts and Passthroughs

In FY 2017, 22 USPS Marketing Mail passthroughs exceeded 100 percent, largely because of shrinking cost avoidances for many rate categories.

¹⁰ The migration also caused Carrier Route Flats mail processing costs to rise, because the migrating pieces had higher mail processing costs than the indigenous Carrier Route Flats pieces.
a. Letters


i. DNDC and DSCF Dropship Letters

The FY 2017 passthroughs for DNDC and DSCF dropship letters were 152.9 percent and 161.9 percent, respectively. In Docket Nos. R2017-1 and R2018-1, the Commission accepted the Postal Service’s reliance on 39 U.S.C. § 3622(e)(2)(B) to justify these passthroughs, contingent on the Postal Service’s adherence to a plan to reduce the passthroughs by 10 percentage points in each market dominant rate case.11 The Postal Service continues to justify these passthroughs pursuant to 39 U.S.C. § 3622(e)(2)(B); it plans to recommend to the Governors a reduction of at least 10 percentage points in the next market dominant rate case, subject to adequate pricing flexibility, operational efficiencies, and changes in cost avoidance.

ii. Automation AADC Letters

The FY 2017 passthrough for Automation AADC Letters was 121.4 percent (discount of 1.7 cents and cost avoidance of 1.4 cents). In Docket No. R2018-1, the Postal Service reduced the discount to 1.3 cents, so when the Docket No. R2018-1 prices take effect, the passthrough will drop 28.5 percentage points to 92.9 percent.

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11 Order No. 3610, at 38; Order No. 4215, at 43.
Therefore, the Postal Service believes no further action is necessary with respect to this passthrough.

iii. Automation Mixed AADC Letters

The Automation Mixed AADC Letters passthrough was 1300.0 percent in FY 2017, compared to 800.0 percent in FY 2016. Consistent with past years, the cost avoidance in FY 2017 changed, decreasing to 0.1 cents from 0.2 cents, which caused the passthrough to increase. Because this barcoding discount encourages mailers to apply an Intelligent Mail Barcode (IMb) to their mailpieces, which is valuable to the efficient operation of the Postal Service, the Postal Service justifies this passthrough pursuant to section 3622(e)(2)(D). Going forward, because of the shrinking cost avoidance of basic IMb barcording relative to the value of Full Service Intelligent Mail, the Postal Service may conduct a fundamental reevaluation of its barcoding strategies.

iv. Nonautomation AADC Machinable Letters

The Nonautomation AADC Machinable Letters passthrough was 106.3 percent in FY 2017 (discount of 1.7 cents and cost avoidance of 1.6 cents). In Docket No. R2018-1, the Postal Service reduced the discount to 1.3 cents, so when the Docket No. R2018-1 prices take effect, the passthrough will be 81.3 percent. Therefore, the Postal Service believes no further action is necessary with respect to this passthrough.

v. Nonautomation 3-Digit Nonmachinable Letters

The Nonautomation 3-Digit Nonmachinable Letters passthrough was 113.6 percent in FY 2017. In Docket No. R2018-1, the Postal Service reduced the discount

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from 2.5 cents to 2.3 cents, to match the FY 2016 cost avoidance. However, because the cost avoidance fell in FY 2017 to 2.2 cents, the passthrough will remain above 100 percent, at 104.5 percent, after the Docket No. R2018-1 prices take effect. The Postal Service intends, in the next market dominant rate case, to recommend to the Governors that they realign the discount with the latest cost avoidance, or it will cite an appropriate statutory exception.

vi. Nonautomation 5-Digit Nonmachinable Letters

The Nonautomation 5-Digit Nonmachinable Letters passthrough was 127.9 percent in FY 2017. In Docket No. R2018-1, the Postal Service reduced the discount from 8.7 cents to 7.1 cents, to match the FY 2016 cost avoidance. However, because the cost avoidance fell in FY 2017 to 6.8 cents, the passthrough will remain above 100 percent, at 104.4 percent, after the Docket No. R2018-1 prices take effect. The Postal Service intends, in the next market dominant rate case, to recommend to the Governors that they realign the discount with the latest cost avoidance, or it will cite an appropriate statutory exception.

b. Flats

Out of the seven presorting and prebarcoding passthroughs for USPS Marketing Mail Flats, only the Automation Mixed ADC Flats passthrough exceeded 100 percent in FY 2017. The Postal Service notes that it calculated all dropship Flats and Parcels passthroughs using the Proposal Seven, Alternative 2 methodology approved by the
Commission in Order No. 4227. The two Flats dropship passthroughs did not exceed 100 percent in FY 2017.

The Automation Mixed ADC Flats passthrough was 190.0 percent in FY 2017, down from 241.2 percent in FY 2016 due to an increase in the cost avoidance from 1.7 cents to 2 cents. Of note, the discount will decrease as part of the Docket No. R2018-1 price adjustment, which will lower the passthrough to 180.0 percent. Because this barcoding discount encourages mailers to apply an IMb to their mailpieces, which is valuable to the efficient operation of the Postal Service, the Postal Service justifies this passthrough pursuant to section 3622(e)(2)(D). Going forward, as noted above, the Postal Service may conduct a fundamental reevaluation of its barcoding strategies.

c. Parcels

Three out of eleven USPS Marketing Mail Parcels presorting and prebarcoding passthroughs exceeded 100 percent in FY 2017. The six Parcels dropship passthroughs calculated using the methodology approved by the Commission in Order No. 4227 did not exceed 100 percent in FY 2017.

The passthroughs for prebarcoding Mixed Network Distribution Center (NDC) Machinable Barcoded Parcels, prebarcoding Mixed NDC Irregular Barcoded Parcels passthrough, and prebarcoding NDC Marketing Barcoded Parcels passthrough were 159.0 percent in FY 2017. These discounts encourage mailers to pre-barcode their parcels, thereby increasing operational efficiency. Accordingly, in Docket Nos.

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13 See Order No. 4227, Order on Analytical Principles Used in Periodic Reporting (Proposal Seven), PRC Docket No. RM2017-11 (Nov. 20, 2017), at 8 (Order No. 4227) (approving the Postal Service’s Alternative 2 calculation within Proposal Seven).

ACR2016 and R2018-1, the Commission accepted the Postal Service’s reliance on 39 U.S.C. § 3622(e)(2)(D) to justify these passthroughs, contingent on the Postal Service’s adherence to a plan to reduce the passthroughs by 10 percentage points in each market dominant rate case.\textsuperscript{15}

The Postal Service continues to justify these passthroughs pursuant to 39 U.S.C. § 3622(e)(2)(D); it plans to recommend to the Governors a reduction in the passthroughs of at least 10 percentage points in the next market dominant rate case, subject to adequate pricing flexibility, operational efficiencies, and changes in cost avoidance. In the long term, the Postal Service may rethink its barcoding strategies, as noted above.

d. Carrier Route Letters, Flats, and Parcels

Seven Carrier Route discounts exceeded their cost avoidances in FY 2017: Letters entered at DNDC compared to origin entry; Letters entered at DSCF entry compared to origin entry; Carrier Route Flat pieces on 5-Digit Carrier Route pallets entered at origin, DNDC, DSCF, and Destination Delivery Unit (DDU); and, Commercial and Nonprofit Basic Carrier Route Flats dropshipped at the DDU.

i. Carrier Route Dropship DNDC and DSCF Letters

The passthroughs for Carrier Route DNDC and DSCF dropship letters were 176.5 percent and 181.0 percent, respectively, in FY 2017. In Docket Nos. ACR2016 and R2018-1, the Commission accepted the Postal Service’s reliance on 39 U.S.C. § 3622(e)(2)(B) to justify these passthroughs, contingent on the Postal Service’s

\textsuperscript{15} Order No. 4215, at 43; FY 2016 ACD, at 32.
adherence to a plan to reduce the passthroughs by 10 percentage points in each market dominant rate case.\textsuperscript{16} The Postal Service continues to justify these passthroughs pursuant to 39 U.S.C. § 3622(e)(2)(B); it plans to recommend to the Governors a reduction in the passthroughs of at least 10 percentage points in the next market dominant rate case, subject to adequate pricing flexibility, operational efficiencies, and changes in cost avoidance.

\textbf{ii. Carrier Route Flats on 5-Digit Carrier Route Pallets}

The four 5-Digit Carrier Route pallet passthroughs were 111.1 percent at each entry point in FY 2017 (discounts of 2.1 cents and cost avoidances of 1.8 cents).\textsuperscript{17} In Docket No. R2018-1, these passthroughs were set to 82.6 percent, based on the then current cost avoidances of 2.3 cents and proposed discounts of 1.9 cents. Given the 0.5 cent fall in the cost avoidances in FY 2017, the Docket No. R2018-1 prices will result in passthroughs of 105.6 percent. The Postal Service intends, in the next market dominant rate case, to recommend to the Governors that they realign the discounts with the latest cost avoidances, or it will cite an appropriate statutory exception.

\textbf{iii. Commercial and Nonprofit Basic Carrier Route Flats}

In FY 2017, the Commercial and Nonprofit Basic Carrier Route Flats DDU dropship passthrough was 107.2 percent, calculated using the methodology from Order No. 4227. FY 2017, the Commercial and Nonprofit Basic Carrier Route Flats DDU dropship passthrough was 107.2 percent, calculated using the methodology from Order No. 4227. This new methodology factors not only the pound-rated per-pound discount

\textsuperscript{16} FY 2016 ACD at 34; Order No. 4215 at 43.

\textsuperscript{17} Carrier Route pieces prepared on 5-Digit Carrier Route pallets compared to 5-Digit Merged pallets save the Postal Service bundle handling costs at each entry point, including origin.
versus origin-entered, but also the piece-rated per-piece discount versus origin-entered. The previous methodology only considered the first discount, and would have produced a passthrough of 55.4 percent. The new 107.2 percent calculation recognizes that, in total, the discounts given exceed the costs avoided. Therefore, the Postal Service intends, in the next market dominant rate case, to recommend to the Governors that they adjust the per-pound and per-piece discounts so that the total dollar value of the discounts is aligned with the total cost avoided, or it will cite an appropriate statutory exception.

e. High Density and Saturation Letters, Flats, and Parcels

Two dropship Letter discounts associated with High Density and Saturation Letters exceeded avoided costs in FY 2017: DNDC Letters compared to origin entry, and DSCF Letters compared to origin entry. In addition, two Flats discounts exceeded avoided costs: the Commercial and Nonprofit High Density and Saturation Flats DNDC and DSCF dropship discounts.

i. High Density and Saturation DNDC and DSCF Dropship Letters

The FY 2017 passthroughs for High Density and Saturation DNDC and DSCF dropship letters were 141.2 percent and 147.6 percent, respectively. In Docket Nos. ACR2016 and R2018-1, the Commission accepted the Postal Service’s reliance on 39 U.S.C. § 3622(e)(2)(B) to justify these passthroughs, contingent on the Postal Service’s adherence to a plan to reduce the passthroughs by 10 percentage points in each market dominant rate case. The Postal Service continues to justify these

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18 FY 2016 ACD, at 36; Order No. 4215, at 43.
passthroughs pursuant to 39 U.S.C. § 3622(e)(2)(B); it plans to recommend to the Governors a reduction in the passthroughs of at least 10 percentage points in the next market dominant rate case, subject to adequate pricing flexibility, operational efficiencies, and changes in cost avoidance.

ii. Commercial and Nonprofit High Density and Saturation DNDC and DSCF Flats

In FY 2017, the Commercial and Nonprofit High Density and Saturation Flats DNDC dropship passthrough was 114.0 percent, while the Flats DSCF dropship passthrough was 124.7 percent. As previously indicated, these passthroughs were calculated using the Order No. 4227 methodology, which factors not only the pound-rated per-pound discount versus origin-entered, but also the piece-rated per-piece discount versus origin-entered. The previous methodology only considered the first discount, and would have produced a passthrough of 57.1 percent for DNDC and 69.5 percent for DSCF. The new 114.0 percent and 124.7 percent calculations recognize that in total, the discounts given exceed the costs avoided. Therefore, for both DNDC and DSCF, the Postal Service intends, in the next market dominant rate case, to recommend to the Governors that they adjust the per-pound and per-piece discounts so that the total dollar value of the discounts is aligned with the total cost avoided, or it will cite an appropriate statutory exception.

3. Commission Flats Directives

In the FY 2010 ACD, the Commission articulated a number of directives related to Flats’ cost coverage. The Commission generally directed the Postal Service “to increase the cost coverage of the Standard Mail Flats product through a combination of above-average price adjustments, consistent with the price cap requirements, and cost
reductions until such time that the revenues for this product exceed attributable costs.”

More specifically, the Commission directed the Postal Service to report in future ACRs on its progress in: increasing Flats prices; implementing operational changes aimed at lowering flats costs; effectuating costing methodology improvements; and phasing out the subsidy of Flats. The Postal Services addresses each of these directives in turn below.

**a. Schedule of Above-Average Price Increases**

The Commission’s FY 2010 ACD directed the Postal Service to present a schedule of above-average CPI price increases for Flats in each subsequent ACR and Notice of Market Dominant Price Adjustment. Since then, the Postal Service has presented and adhered to a schedule of above-average price increases for Flats. The schedule was updated most recently in Docket No. R2018-1, as shown below.

<table>
<thead>
<tr>
<th>Year</th>
<th>Planned Flats Price Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>CPI-U * 1.05</td>
</tr>
<tr>
<td>2019</td>
<td>CPI-U * 1.05</td>
</tr>
<tr>
<td>2020</td>
<td>CPI-U * 1.05</td>
</tr>
</tbody>
</table>

Further, as Demonstrated in Table 5 below, the Postal Service has surpassed its commitment to increase Flats by 1.05 times CPI in each price adjustment since Docket No. R2013-10.

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20 Id. at 107.

Table 5: Flats Price Changes Compared to Overall USPS Marketing Mail Authority

<table>
<thead>
<tr>
<th>Docket No.</th>
<th>(A) Flats Percent Price Increase</th>
<th>(B) Overall USPS MM Pricing Authority</th>
<th>(A) as Percent of (B)</th>
</tr>
</thead>
<tbody>
<tr>
<td>R2013-10</td>
<td>1.810%</td>
<td>1.696%</td>
<td>106.7%</td>
</tr>
<tr>
<td>R2015-4</td>
<td>2.549%</td>
<td>1.966%</td>
<td>129.7%</td>
</tr>
<tr>
<td>R2017-1</td>
<td>2.522%</td>
<td>0.927%</td>
<td>272.1%</td>
</tr>
<tr>
<td>R2018-1</td>
<td>2.167%</td>
<td>2.008%</td>
<td>107.9%</td>
</tr>
</tbody>
</table>

b. Information Requests Related to Flats Costs

In the FY 2010 ACD, the Commission directed the Postal Service to provide the following information about USPS Marketing Mail Flats in each subsequent ACR:

1) all operational changes designed to reduce flats costs in the previous fiscal year and an estimation of the financial effects of such changes;

2) all costing methodology improvements made in the previous fiscal year and the estimated financial effects of such changes; and

3) a statement summarizing the historical and current fiscal year subsidy of the flats product; and the estimated timeline for phasing out this subsidy.\(^\text{22}\)

The Postal Service provides the information below in response to the Commission’s directives. The section titled “Operational Changes” responds to directive 1, and the section titled “Costing Methodology Changes and Subsidy of the Flats Product” responds to directives 2 and 3.

i. Operational Changes

Below, the Postal Service describes the new and ongoing steps it took during FY 2017 to make its processing of USPS Marketing Mail Flats and Periodicals mail more efficient. Collectively, these efforts are expected to improve efficiencies and productivities, and contribute to reductions in overall USPS Marketing Mail Flats and Periodicals costs.

\(^\text{22}\) FY 2010 ACD, at 107.
Where possible, the Postal Service has developed key metrics to monitor and
gauge the operational impact of changes, specifically related to flat mail processing.
The metrics described in the following sections are used on a daily basis to identify
operational or maintenance issues that may be impacting the overall efficiency of the
operations monitored. As situations change, these metrics may be modified or
discontinued and other metrics may be added. In many cases, the operational metrics
employed are aggregate in nature, crossing different mail classes and entry make-up.

However, the Postal Service is unable to provide an estimate of the financial
impacts of these operational initiatives at this time. As the Postal Service explained in
its responses to the Commission’s directive in Chapter 6 of its FY 2015 ACD,\(^\text{23}\) and in
last year’s ACR,\(^\text{24}\) the information generated by the Postal Service’s existing data
systems does not support reliable estimates of the impact of operational initiatives on
flats costs. The Postal Service acknowledges that, after the close of FY 2017, the
Commission initiated Docket No. RM2018-1 to explore opportunities to enhance the
Postal Service’s data systems in order to measure the impact of flats costs.\(^\text{25}\)

\(^{23}\) Response of the United States Postal Service to Commission Information request No. 1, PRC Docket
No. ACR2015 (Nov. 28, 2016); Third Response of the United States Postal Service to Commission
Requests for Additional Information in the FY 2015 Annual Compliance Determination, PRC Docket No.
ACR2015 (July 26, 2016).

\(^{24}\) United States Postal Service FY 2016 Annual Compliance Report, Docket No. ACR2016 (Dec. 29,
2016), at 28.

\(^{25}\) Order No. 4142, Advance Notice of Proposed Rulemaking to Develop Data Enhancements and
provided additional details about the capabilities of certain data systems in response to the Commission’s
first Information Request in that docket on December 4, 2017. See Response of the United States Postal
• **Bundle Operation**

The Automated Parcel and Bundle Sorter (APBS), Automated Package Processing System (APPS), Small Package Sorter System (SPSS), and High Throughput Parcel Sorter (HTPS) sorts bundles of flats to bins for either delivery or subsequent processing. At some locations, processing bundles to destination requires two runs on the machine – a primary sortation and a secondary sortation. By making additional bins available for the primary sortation, the need for a secondary sortation is reduced or eliminated. For example, assume that a particular sortation requires 200 separations, but that the machine only has 150 bins. As a result, 50 separations require rehandling. The introduction of additional bins eliminates or reduces this extra handling.

In FY 2017, the Postal Service continued to expand the APBS and APPS fleet, adding an additional 1,488 bins for sortation, 1,344 of which were added to the APBS in order to reduce the number of piece handlings required to finalize mail in downstream. In addition, the Postal Service added 7 new SPSS and 3 APBS in order to expand processing capabilities and improve efficiency.

In FY 2017, the total pieces fed through the Automated Flats Sorting Machine 100 (AFSM 100) operations declined 6.0 percent, while the aggregate productivity value decreased 7.1 percent, when compared to FY 2016. Similar declines were experienced between FY 2015 and FY 2016. It would appear that the loss of economies of scale related to volume declines has had a negative impact on the productivity values for AFSM100 operations. In response to these changes, the Postal Service removed 50 AFSM 100 machines from processing plants in FY 2017. Additional removals may be required in the future as the organization adjusts to declining mail volumes.
• **Service Performance Diagnostics Tool**

In FY 2017, the Postal Service continued to utilize the Service Performance Diagnostics tool (SPD) to track and improve the flow of USPS Marketing Mail and Periodicals being processed through the network. The Work in Process (WIP) cycle time measures the time between a mailpiece’s arrival at the plant and bundle-to-piece distribution. In FY 2017, the Postal Service transitioned reports from the SPD system to the Informed Visibility (IV) system, which leverages data in near real-time to measure and diagnose service, predicts workload, manages inventory, and provides near real-time end-to-end tracking of mail. Over the past year, the Postal Service created or overhauled numerous dashboards in the IV system to provide its personnel with the tools needed to drive performance and improve service efficiencies.

In FY 2017, WIP cycle time for USPS Marketing Mail Flats decreased, bringing the time down to its FY 2015 level.\(^{26}\) The WIP cycle time for Periodicals remained constant compared to FY 2016. The Postal Service continues to monitor WIP cycle time to identify locations and operations where the time between arrival and bundle-to-piece distribution can be improved. The Postal Service is consistently working to optimize its operations and reduce the cycle time between acceptance and processing.

<table>
<thead>
<tr>
<th>Time Period from SPD</th>
<th>Weighted Median (hours)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(FY 16) Week ending 10/01/15 - 09/30/16</td>
<td>54</td>
</tr>
<tr>
<td>(FY 17) Week ending 10/01/16 - 09/30/17</td>
<td>52</td>
</tr>
</tbody>
</table>

\(^{26}\) See Annual Compliance Determination Report, Fiscal Year 2015, PRC Docket No. ACR2015 (March 28, 2016), at 22 (FY 2015 ACD) (reporting a weighted median of 52 hours in FY 2015).
Table 7: Median 5 Day Mail Processing WIP Periodicals Flats

<table>
<thead>
<tr>
<th>Time Period from SPD</th>
<th>Weighted Median (hours)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(FY 16) Week ending 10/01/15 - 09/30/16</td>
<td>24</td>
</tr>
<tr>
<td>(FY 17) Week ending 10/01/16 - 09/30/17</td>
<td>24</td>
</tr>
</tbody>
</table>

- **Lean Mail Processing**

  In FY 2017, the Postal Service completed deploying Lean Mail Processing (LMP) to mail processing facilities across the nation, and then focused on stabilizing the LMP program. The LMP program is a standardized, statistical program utilized for improving mail processing. In an effort to improve flats processing in FY 17, the Postal Service completed 6 Lean Six Sigma projects and 13 initiatives targeted at improving productivity performance on bundle/parcel sorting equipment. Initiatives included improvement of overall efficiencies, expansion of Facility Access and Shipment Tracking appointments to meet customer needs, reduction of late trips departing processing facilities, reduction of letters processed on flats sorting equipment, and implementation of first-in-first-out staging, among others.

  Personnel in each operational area in a plant, including flats and bundles operations, visually track their real-time performance to ensure they are on target and take appropriate actions to ensure operational goals are met. For example, management at a given plant may monitor and take note of productivity on the APBS throughout a tour to determine whether the operation is on pace to meet that tour’s throughput goal, and make appropriate adjustments as needed to achieve that goal.

- **Reduce Bundle Breakage**

  Bundle breakage results in higher processing costs for the Postal Service, as well as potential damage to mailpieces. Bundle breakage performance from FY 2016 to
FY 2017 increased by 9.4 percent. When bundles lose their presort integrity prior to being completely processed, the Postal Service must handle the individual pieces, which increases handling costs. Accordingly, reducing bundle breakage benefits both the Postal Service and the mailing industry.

The Postal Service is committed to working with the mailing industry, through the Mailers Technical Advisory Committee, to study the causes and impacts of bundle breakage. The Postal Service continues to share information with Mail Service Providers (MSPs) and their individual processing plants to identify areas of opportunity to reduce breakage. In FY 2016, the Postal Service began providing information about instances of bundle breakage to the highest volume impact MSPs and several mail owners on a monthly basis; this practice continued in FY 2017.

In addition, in FY 2017, the Postal Service continued using an internal dashboard to give individual Postal Service processing plants quicker access to bundle breakage data, including: the total number of bundles processed on the APPS or APBS by a facility, and the percentage of that total that were identified as broken; the number of bundles processed by a facility as a percentage of total bundles processed nationwide; and the number of bundles identified as broken at a facility as a percentage of total bundles identified as broken nationwide. This information can also be broken down by first facility scan, breakage facility scan, entry discount, machine type, by MSP, or by mail owner. In FY 2017, the Postal Service added attributes such as job number, CRID, and daily data to provide further insight into the origin and creation of broken bundles. The Postal Service and industry stakeholders use these data to gain insight into root causes of bundle breakage, identify overarching impacts of bundle breakage...
on service, and investigate top opportunity facilities, locations, and machines in an effort to develop strategies to address bundle breakage.

Moreover, in FY 2017, the Postal Service developed Bundle Leakage data that tracks bundles that bypass bundle processing. These data provide some insight into improper flows and manual handlings of bundles. In addition, in an effort to detect improper mail flow and bundle breakage, the Postal Service began tracking 5-Digit and Carrier Route bundles with pieces scanned on the AFSM 100 by Last Scan Facility.

ii. Costing Methodology Changes and Subsidy of the Flats Product

USPS Marketing Mail Flats unit costs reported in the CRA increased from 47.1 cents in FY 2016 to 52 cents in FY 2017. Three costing methodology changes affected Marketing Mail Flats over this period. One was from Docket No. RM2016-12 (Proposal Four), and another was from Docket No. RM2017-8 (also termed Proposal Four); both of these acted to reduce attributable costs for Flats. As Table 8 below illustrates, summing the estimated cost declines for USPS Marketing Mail Flats associated with these two methodological changes yields an approximate total decrease for FY 2016 of $45.2 million dollars.

<table>
<thead>
<tr>
<th>Docket No.</th>
<th>Proposal</th>
<th>Topic</th>
<th>FY2016 Estimated Impact ($000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>RM2016-12</td>
<td>Four</td>
<td>Capacity Variability for Purchased Highway Transportation Costs</td>
<td>-$28,462¹</td>
</tr>
<tr>
<td>RM2017-8</td>
<td>Four</td>
<td>Adjust City Carrier Street Time Parcel Proportions</td>
<td>-$16,733</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td>-$45,195</td>
</tr>
</tbody>
</table>

¹Estimated FY 2016 impact of Proposal Four (Highway) is from Order No. 3973 (June 22, 2017) at 39.
Had the $45 million decrease associated with these two changes been reflected in the FY 2016 CRA, the FY 2016 reported unit costs for Flats would have been lower by that amount.

The third relevant methodological change is the inclusion of inframarginal costs. Comparing pages 91 and 92 of the FY 2016 ACD, it is apparent that commensurately incorporating inframarginal costs for Flats in FY 2016 would have increased the FY 2016 baseline by $14 million. The aggregate effect of the two declines and the offsetting increase would be an overall attributable cost decline of $31 million, meaning that a like-for-like comparison (after controlling for costing methodology changes) between FY 2016 unit costs and FY 2017 unit costs for Flats would be an increase from 46.6 cents (rather than the 47.1 cents shown in the FY 2016 CRA) to the 52.0 cents that appears in the FY 2017 CRA.

Further, beyond changes in costing methodology (as well as operational changes), there were other related developments this year that affected costs for USPS Marketing Mail Flats. As described previously in the Preface to USPS-FY15-31, the preparation rules implemented in January 2014 allowed pieces in 5-Digit scheme FSS bundles to claim Standard Mail Carrier Route rates, if they would have been eligible to do so in the absence of the FSS preparation rules. As also explained in the same Preface, marking issues related to this situation warranted costing adjustments that shifted to Carrier Route some costs that would otherwise have been reported as relating to Standard Flats. Those adjustments were in effect for the first three quarters of FY 2015. Because of classification changes made in Docket No. R2015-4, however, beginning May 31, 2015, all pieces in FSS bundles became part of the Standard Mail
Flats product. As a consequence of these circumstances, certain pieces that would have been classified as part of Carrier Route in the first three quarters of FY 2015 would, throughout FY 2016, have instead been classified as Standard Mail Flats. Therefore, when comparing the reported unit costs of Standard Mail Flats (and, for that matter, of Carrier Route) in FY 2016 to the reported unit costs in FY 2015, it was necessary to consider the effects of these classification changes.

When pieces move in or out a mail category, the effect on reported unit costs is primarily a function of whether the subset of pieces that are shifting have higher or lower than average costs, relative to the total set of pieces present before the shift. This is true with respect to both the category from which the pieces shift, as well as the category into which they shift. In terms of evaluating the change in circumstances between 2015 and 2016, more than one billion pieces shifted from Carrier Route (in FY 2015) to Standard Flats (in FY 2016). Those particular pieces would tend to be in the above-average portion of the cost distribution for Carrier Route (since they get distributed as pieces at the FSS operation and whatever operations handle the FSS rejects), but in the below-average portion for Standard Flats (since they have a 5D scheme presort). Moreover, there were a material number of pieces that made this shift, in excess of one billion pieces, as mentioned above. So, in this scenario, it might be expected that shifting these FSS CR flats from Carrier Route flats to Standard Flats could actually reduce unit Mail Processing costs for both products. Looking at the mail processing data for FY 2015 and FY 2016, this indeed seems to have been the case.

Therefore, it is quite plausible that some portion of the observed decline in the unit costs of Standard Flats between FY 2015 and FY 2016 was related to the June 2015 mail classification changes.

It is important to recall the events that unfolded in FY 2015-FY 2016 and their potential effects on reported unit costs because, with the classification changes approved for Docket No. R2017-1, those results were likely reversed going from FY 2016 to FY 2017. The Docket No. R2017-1 changes began in January 2017 to move pieces from Standard Mail (now USPS Marketing Mail) Flats back into Carrier Route. Based on the same logic described above, this migration would be expected to increase the unit costs for both categories to some degree. Reviewing the FY 2016 and FY 2017 Mail Processing unit costs for these two products appears to confirm these circumstances as contributing to the overall observed increase in the unit costs for Flats in FY 2017.

More broadly, the series of events starting in January of 2014 relating to the preparation, marking, and classification of flat-shaped pieces virtually ensured that unit costs trends for the affected products within USPS Marketing Mail would manifest some volatility. That volatility has certainly been manifest in the costs reported for USPS Marketing Mail Flats over this period, further complicating the already difficult task of assessing progress along the dimensions outlined in the FY 2010 ACD regarding cost coverage for this product.

With respect to USPS Marketing Mail Flats’ financial shortfall, the table below summarizes the gap between revenues and costs, as reported in the Commission’s

---

28 Order No. 3610, at 13-17.
ACDs from FY 2008 through FY 2016,\textsuperscript{29} and as reported in the FY 2017 CRA for this fiscal year:

<table>
<thead>
<tr>
<th>Year</th>
<th>Revenue (millions)</th>
<th>Cost (millions)</th>
<th>Shortfall (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>$3,673</td>
<td>$3,891</td>
<td>$218</td>
</tr>
<tr>
<td>2009</td>
<td>$2,882</td>
<td>$3,497</td>
<td>$616</td>
</tr>
<tr>
<td>2010</td>
<td>$2,592</td>
<td>$3,169</td>
<td>$577</td>
</tr>
<tr>
<td>2011</td>
<td>$2,500</td>
<td>$3,143</td>
<td>$643</td>
</tr>
<tr>
<td>2012</td>
<td>$2,234</td>
<td>$2,762</td>
<td>$528</td>
</tr>
<tr>
<td>2013</td>
<td>$2,138</td>
<td>$2,514</td>
<td>$376</td>
</tr>
<tr>
<td>2014</td>
<td>$2,041</td>
<td>$2,452</td>
<td>$411</td>
</tr>
<tr>
<td>2015</td>
<td>$2,113</td>
<td>$2,633</td>
<td>$520</td>
</tr>
<tr>
<td>2016</td>
<td>$2,380</td>
<td>$2,999</td>
<td>$618</td>
</tr>
<tr>
<td>2017</td>
<td>$1,900</td>
<td>$2,569</td>
<td>$669</td>
</tr>
</tbody>
</table>

The Postal Service has been making efforts to improve the finances of Marketing Mail Flats above and beyond the minimum requirements set by the Commission. The Postal Service implemented rate increases in January 2017 for USPS Marketing Mail Flats that were well above the pricing authority for USPS Marketing Mail overall (2.522 percent for Flats, versus 0.927 percent for USPS Marketing Mail overall), and will be increasing prices for USPS Marketing Mail Flats more than 1.05 times the class average in January of 2018.

\textsuperscript{29} Note that in the FY 2016 Financial Analysis Report (March 3, 2017), the Commission on pages 92 and 93 showed alternate versions of the Flats contribution, both with and without inframarginal costs. The $618 million shown in the table below for the FY 2016 shortfall represents the page 93 figure if inframarginal costs are included within attributable costs (making it more comparable to the FY 2017 row), while the figure on page 92 for the FY 2016 shortfall would alternatively have been only $604 million if inframarginal costs were excluded (yielding a figure more comparable to the rows for all previous years).
4. **USPS Marketing Mail Promotions**

During FY 2017, the Postal Service offered five USPS Marketing Mail promotions, discussed in turn below.

a. **Earned Value Reply Mail Promotion**

A description of the Earned Value Reply Mail Promotion (January 1 to June 30, 2017) is provided in section II.A.3 above. Over the course of the program, the Postal Service issued $49.2 million in credits for approximately 1.1 billion BRM and CRM pieces. To date, approximately $8.2 million worth of credits have been redeemed on USPS Marketing Mail pieces.

b. **Tactile, Sensory and Interactive Mailpiece Engagement Promotion**

The Tactile, Sensory and Interactive Mailpiece Engagement Promotion (February 1 to July 31, 2017) provided participating mailers an upfront two-percent postage discount on regular and nonprofit USPS Marketing Mail letters and flats. To qualify, mailpieces were required to feature advanced print innovations such as developments in paper and stock, substrates, finishing techniques, and inks. Over the course of the promotion, the Postal Service issued $5.4 million in discounts for approximately 1.2 billion USPS Marketing Mail pieces.

c. **Emerging and Advanced Technology Promotion**

A description of the Emerging and Advanced Technology Promotion (March 1 to August 31, 2017) is provided in section II.A.3 above. Over the course of the program, the Postal Service issued $22.5 million in discounts for approximately 5.1 billion USPS Marketing Mail pieces.
d. **Direct Mail Starter Promotion**

The Direct Mail Starter Promotion (May 1 to July 31, 2017), a new USPS Marketing Mail promotional offering in FY 2017, provided participating mailers a five percent postage discount on up to 10,000 regular and nonprofit USPS Marketing Mail letter and flat pieces. To qualify, mailpieces were required to contain: 1) a mobile-print technology (such as a QR Code) that, when scanned, led to a mobile-optimized website, and 2) instructions on how to scan the barcode, as well as a printed URL address. Over the course of the program, the Postal Service issued $108 in discounts for approximately 11,000 USPS Marketing Mail pieces.

e. **Mobile Shopping Promotion**

The Mobile Shopping Promotion (October 1 to December 31, 2016, and August 1 to December 31, 2017), provides participating mailers an upfront two-percent postage discount on regular and nonprofit USPS Marketing Mail letters and flats. To qualify, mailpieces are required to feature mobile technology (such as open-sourced barcodes, proprietary barcodes or tags, and digital watermarks) that connects customers to either a mobile-optimized shopping site or a social media webpage with a click-to-shop feature. As of September 30, 2017, the Postal Service issued $30.8 million in discounts for 6.8 billion USPS Marketing Mail pieces.

C. **Periodicals**

1. **Cost, Revenues, and Volumes**

Costs, revenues, and volumes for Periodicals products appear in the table that follows on the next page.
Table 10: Periodicals Volume, Revenue, and Cost by Product

<table>
<thead>
<tr>
<th>Product</th>
<th>Volume (Million)</th>
<th>Revenue ($Million)</th>
<th>Attributable Cost ($Million)</th>
<th>Contribution ($Million)</th>
<th>Revenue/Piece ($)</th>
<th>Cost/Piece ($)</th>
<th>Unit Contribution ($)</th>
<th>Cost Coverage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-County Periodicals</td>
<td>516</td>
<td>56.9</td>
<td>84.7</td>
<td>(27.8)</td>
<td>0.110</td>
<td>0.164</td>
<td>(0.054)</td>
<td>67.16</td>
</tr>
<tr>
<td>Outside County Periodicals</td>
<td>4,784</td>
<td>1,306.1</td>
<td>1,898.1</td>
<td>(502.0)</td>
<td>0.273</td>
<td>0.397</td>
<td>(0.124)</td>
<td>68.81</td>
</tr>
<tr>
<td>Fees</td>
<td>11.8</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total Periodicals (including fees)</td>
<td>5,301</td>
<td>1,374.7</td>
<td>1,982.8</td>
<td>(608.1)</td>
<td>0.259</td>
<td>0.374</td>
<td>(0.115)</td>
<td>69.33</td>
</tr>
</tbody>
</table>

Cost coverage for the Periodicals class overall decreased in FY 2017, from 73.96 percent to 69.33 percent. In-County Periodicals declined in cost coverage from 70.07 percent to 67.16 percent, and Outside County Periodicals declined in cost coverage from 73.73 percent to 68.81 percent.

Revenue per piece for Periodicals as a whole decreased from 27.0 cents in FY 2016 to 25.9 cents in FY 2017, or 4.07 percent. At the same time, cost per piece increased from 36.5 cents to 37.4 cents, or 2.5 percent. The combination of these factors led to the FY 2017 decline in cost coverage.

Certain operational changes made in FY 2017 to address flats processing and efficiency (both for USPS Marketing Mail and Periodicals) are discussed in Section II.B.3.b of this Report.

2. Workshare Discounts and Passthroughs

Two In-County Periodicals workshare discounts exceeded 100 percent of avoided costs: Saturation, and 3-Digit Automation Letters. Nine Outside County Periodicals workshare discounts exceeded 100 percent of avoided costs: High Density, Saturation, Nonmachinable Nonautomation 3-Digit/Sectional Center Facility (SCF)
Flats, Nonmachinable Nonautomation 5-Digit Flats, Nonmachinable Automation 3-Digit/SCF Flats, Nonmachinable Automation 5-Digit Flats, ADC Automation Letters, 3-Digit Automation Letters, and 5-Digit Automation Letters. The Postal Service justifies all of these passthroughs pursuant to section 3622(e)(2)(C), which permits discounts provided in connection with mail matter of educational, cultural, scientific, or informational value to exceed 100 percent of avoided costs.

3. FY 2016 ACD Directives

In the FY 2016 Annual Compliance Determination, the Commission directed the Postal Service to submit an updated report analyzing “how the removal of FSS pricing in Docket No. R2017-1 impacted the cost, contribution, and revenue of periodicals in FY 2017 and whether the removal improved the efficiency of Periodicals pricing in FY 2017.” The Postal Service provides its updated report in USPS-FY17-44.

D. Package Services

1. Cost, Revenues, and Volumes

Costs, revenues, and volumes for Package Services products appear in the table that follows on the next page.

---

30 FY 2016 ACD, at 22.
Table 11: Package Services Volume, Revenue and Cost by Product

<table>
<thead>
<tr>
<th>Product</th>
<th>Volume (Million)</th>
<th>Revenue($Million)</th>
<th>Attributable Costs ($Million)</th>
<th>Contribution ($Million)</th>
<th>Revenue/Piece ($)</th>
<th>Cost/Piece ($)</th>
<th>Unit Contribution ($)</th>
<th>Cost Coverage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bound Printed Matter Flats</td>
<td>264.5</td>
<td>200.3</td>
<td>132.6</td>
<td>67.7</td>
<td>0.757</td>
<td>0.501</td>
<td>0.256</td>
<td>151.1</td>
</tr>
<tr>
<td>Bound Printed Matter Parcels</td>
<td>277.6</td>
<td>297.2</td>
<td>270.3</td>
<td>26.9</td>
<td>1.070</td>
<td>0.974</td>
<td>0.097</td>
<td>110.0</td>
</tr>
<tr>
<td>Media Mail/ Library Mail</td>
<td>76.5</td>
<td>266.8</td>
<td>352.7</td>
<td>(85.9)</td>
<td>3.487</td>
<td>4.611</td>
<td>(1.124)</td>
<td>75.6</td>
</tr>
<tr>
<td>Alaska Bypass</td>
<td>1.3</td>
<td>33.7</td>
<td>17.4</td>
<td>16.3</td>
<td>25.808</td>
<td>13.347</td>
<td>12.461</td>
<td>193.4</td>
</tr>
<tr>
<td>Fees</td>
<td></td>
<td>3.2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Package Services Mail</td>
<td>619.9</td>
<td>801.1</td>
<td>771.1</td>
<td>28.1</td>
<td>1.292</td>
<td>1.247</td>
<td>0.045</td>
<td>103.6</td>
</tr>
</tbody>
</table>

With the exception of Media Mail/Library Mail, all Package Services products covered their attributable costs in FY 2017. Overall, the Package Services class had a cost coverage of 103.64 percent, increasing from 102.29 percent in FY 2016. The cost coverage for Bound Printed Matter (BPM) Parcels increased by 5.68 percentage points to 109.95 percent. The cost coverage for Alaska Bypass increased by 23.32 percentage points to 193.36. While the cost coverage for BPM Flats decreased by 8.66 percentage points to 151.10, from a class perspective this decline was largely offset by the increase in BPM Parcels’ cost coverage.

Media Mail/Library Mail had a cost coverage of 75.63 percent, which amounts to a 0.45 percentage point increase from 75.18 percent in FY 2016. The increase in cost coverage was small because, while cost per piece fell by 12.5 cents, revenue per piece also fell, by 6.5 cents. The Docket No. R2018-1 price increase for the product is 1.993
percent, above average for the class. The Postal Service intends to recommend to the Governors that they continue applying above-average price increases to improve Media Mail/Library Mail cost coverage.

2. Workshare Discounts and Passthroughs

a. Media Mail / Library Mail

All Media Mail/Library Mail passthroughs were under 100 percent.

b. BPM Flats and BPM Parcels

Four BPM Flats and BPM Parcels discounts exceeded avoided costs in FY 2017: the two DNDC dropship discounts, and the two DSCF dropship discounts.

i. BPM Flats and BPM Parcels DNDC Dropship

The passthroughs for the BPM Flats and BPM Parcels DNDC dropship discounts were 132.9 and 131.8 percent, respectively (discounts of 11.3 and 11.2 cents compared to cost avoidances of 8.5 cents). In Docket No. R2018-1, the Postal Service aligned these discounts with the FY 2016 cost avoidances. However, the cost avoidances decreased in FY 2017, so when the Docket No. R2018-1 prices take effect, these passthroughs will be 120.0 percent. The Postal Service intends, in the next market dominant rate case, to recommend to the Governors that they realign the discounts with the latest cost avoidances, or it will cite an appropriate statutory exception.

ii. BPM Flats and BPM Parcels DSCF Dropship

The passthroughs for the BPM Flats and BPM Parcels DSCF dropship discounts were 109.5 and 114.1 percent, respectively (discounts of 59.0 and 61.5 cents compared to cost avoidances of 53.9 cents). In Docket No. R2018-1, the Postal Service aligned the DSCF dropship discounts with the FY 2016 cost avoidances. However, the cost
avoidances decreased in FY 2017, so when the Docket No. R2018-1 prices take effect, these passthroughs will be 101.1 percent. The Postal Service intends, in the next market dominant rate case, to recommend to the Governors that they realign the discounts with the latest cost avoidances, or it will cite an appropriate statutory exception.

iii. BPM Flats and BPM Parcels DDU Dropship

The BPM Flats and BPM Parcels DDU dropship passthroughs were below 100 percent.

E. Special Services

1. Cost, Revenues, and Volumes

Costs, revenues, and volumes for Special Services appear in the table that follows on the next page.
Table 12: Special Services Volume, Revenue and Cost by Service/Product

<table>
<thead>
<tr>
<th>Service/Product</th>
<th>Volume (Million)</th>
<th>Revenue ($Million)</th>
<th>Attributable Cost ($Million)</th>
<th>Contribution ($Million)</th>
<th>Revenue/ Piece ($)</th>
<th>Cost/Piece ($)</th>
<th>Unit Contribution ($)</th>
<th>Unit Coverage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Certified Mail</td>
<td>199.3</td>
<td>666.8</td>
<td>558.7</td>
<td>108.1</td>
<td>3.35</td>
<td>2.80</td>
<td>0.54</td>
<td>119.35</td>
</tr>
<tr>
<td>COD</td>
<td>0.4</td>
<td>4.2</td>
<td>2.6</td>
<td>1.5</td>
<td>10.57</td>
<td>6.64</td>
<td>3.93</td>
<td>159.12</td>
</tr>
<tr>
<td>Insurance</td>
<td>14.8</td>
<td>74.5</td>
<td>46.9</td>
<td>27.5</td>
<td>5.05</td>
<td>3.18</td>
<td>1.87</td>
<td>158.71</td>
</tr>
<tr>
<td>Registered Mail</td>
<td>2.0</td>
<td>30.4</td>
<td>21.9</td>
<td>8.5</td>
<td>15.33</td>
<td>11.03</td>
<td>4.29</td>
<td>138.92</td>
</tr>
<tr>
<td>Stamped Envelopes</td>
<td>N/A</td>
<td>12.2</td>
<td>7.9</td>
<td>4.3</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>153.86</td>
</tr>
<tr>
<td>Stamped Cards</td>
<td>N/A</td>
<td>0.9</td>
<td>0.3</td>
<td>0.6</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>287.62</td>
</tr>
<tr>
<td>Other Ancillary Services</td>
<td>N/A</td>
<td>433.9</td>
<td>218.9</td>
<td>215.0</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>198.24</td>
</tr>
<tr>
<td>Total Ancillary Services</td>
<td>N/A</td>
<td>1222.8</td>
<td>857.2</td>
<td>365.6</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>142.65</td>
</tr>
<tr>
<td>Int’l Ancillary Services</td>
<td>26.0</td>
<td>35.3</td>
<td>40.9</td>
<td>-5.7</td>
<td>1.36</td>
<td>1.57</td>
<td>-0.22</td>
<td>86.19</td>
</tr>
<tr>
<td>Caller Service</td>
<td>N/A</td>
<td>91.0</td>
<td>25.3</td>
<td>65.7</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>360.23</td>
</tr>
<tr>
<td>Address Management Services</td>
<td>N/A</td>
<td>16.3</td>
<td>7.0</td>
<td>9.3</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>232.34</td>
</tr>
<tr>
<td>Credit Card Authentication*</td>
<td>16.9</td>
<td>17.5</td>
<td>1.6</td>
<td>15.8</td>
<td>1.03</td>
<td>0.10</td>
<td>0.93</td>
<td>1068.38</td>
</tr>
<tr>
<td>Customized Postage</td>
<td>0.0</td>
<td>1.0</td>
<td>0.1</td>
<td>0.9</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>1353.08</td>
</tr>
<tr>
<td>Money Orders</td>
<td>86.8</td>
<td>152.0</td>
<td>156.4</td>
<td>-4.4</td>
<td>1.75</td>
<td>1.80</td>
<td>-0.05</td>
<td>97.21</td>
</tr>
<tr>
<td>Post Office Box Service</td>
<td>N/A</td>
<td>278.7</td>
<td>230.8</td>
<td>47.8</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>120.73</td>
</tr>
<tr>
<td>Stamp Fulfillment Services</td>
<td>N/A</td>
<td>3.9</td>
<td>4.0</td>
<td>-0.1</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>97.16</td>
</tr>
<tr>
<td>Total Special Services Mail</td>
<td>N/A</td>
<td>1,818.4</td>
<td>1,323.4</td>
<td>495.07</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>137.41</td>
</tr>
</tbody>
</table>

*See USPS-FY17-4 for Volume, and USPS-FY17-NP26 for revenue adjustments after revenue-sharing with third-party partners.
2. Cost Coverages

Three special services failed to cover their costs in FY 2017: International Ancillary Services, Money Orders, and Stamp Fulfillment Services.

a. International Ancillary Services

International Ancillary Services would have covered its attributable costs in FY 2017 but for a loss in Inbound Registered Mail. The Postal Service notes, however, that the additional payment per item for Inbound Registered Mail will increase from 0.69 special drawing right (SDR) to 1.1 SDR in 2018, which should help to improve cost coverage.\(^{31}\) In addition, the Postal Service participates in the voluntary supplementary remuneration for inbound registered items, and this too should lead to additional revenue for inbound registered items. Also, during 2017, a few more foreign postal operators became parties to the Inbound Market Dominant Registered Service Agreement 1 multilateral agreement, and this creates another separate source of contribution associated with Inbound Registered Mail, from those countries that exchange under that agreement.\(^{32}\)

b. Money Orders

In the FY 2016 ACD, the Commission found that Money Orders failed to cover costs because of a large cost increase resulting from using incremental costs rather than volume-variable costs. The Commission asked the Postal Service to investigate

\(^{31}\) Universal Postal Convention Article 28, effective January 1, 2018.

\(^{32}\) See Order No. 3471, Order Adding Inbound Market Dominant Registered Service Agreement 1 to the Market Dominant Product List and Approving Type 2 Rate Adjustment, PRC Docket Nos. MC2016-168 and R2016-6 (Aug. 17, 2016).
the accuracy of the incremental costing method with respect to mail processing costs attributed to Money Orders. The Postal Service’s review determined that incremental costs had been overstated. As a result, Money Orders would have covered its costs in FY 2017, except for another costing adjustment. Specifically, FY 2017 costs included a substantial allocation of debit card fees to Money Orders. As a result, Money Orders had a cost coverage of 97 percent. The Postal Service plans to evaluate whether the debit card fees allocation to Money Orders is accurate, and whether it should recommend to the Governors that they raise Money Order fees in the next market dominant rate case, in order to bring the cost coverage over 100 percent.

c. Stamp Fulfillment Services

Stamp Fulfillment Services (SFS) had costs of $4.0 million in FY 2017, but listed revenues of only $3.9 million, resulting in a cost coverage of 97 percent. Notably, this is the product’s highest cost coverage ever. In Docket No. R2018-1, the Postal Service chose not to raise SFS prices, in an effort to reduce window wait times by encouraging customers to purchase stamps through SFS. This pricing strategy accords with the Commission’s comments on SFS in the FY 2012 ACD:

The costs and revenues associated with the SFS product do not entirely capture the value that the Services Center adds to the Postal Service, and to other Postal Service products. Although SFS does not cover its attributable costs, by providing a mechanism for the centralized ordering of stamps, it reduces the costs associated with the retail purchases of stamps. Thus, it promotes the objectives of reducing costs and increasing efficiency. See 39 U.S.C. 3622(b)(1) and (c)(12).

33 FY 2016 ACD, at 61.
34 See FY 2015 ACD, at 68 (Table III-14).
3. **ACD Directive**

In the FY 2016 ACD, the Commission directed the Postal Service to report in the FY 2017 ACR on the number of In-Office Cost System (IOCS) tallies for the Collect on Delivery (COD) product, and to include the confidence interval for the cost coverage.\(^{36}\) The Postal Service provides this information in USPS-FY17-37.\(^ {37}\)

**F. Market Dominant Negotiated Service Agreements**

1. **Domestic Negotiated Service Agreements**

There was one domestic market dominant NSA in effect in FY 2017: PHI Acquisitions, Inc. ("PHI"). Full information regarding the PHI NSA appears in USPS-FY17-30. There were no acquisition or divestiture activities by PHI during Agreement Year 3, and therefore no impact on volume thresholds. From a fiscal year perspective, PHI had FY 2017 NSA volume of 195,484,428 pieces, total revenue after rebate of $46.9 million, and costs of $41.0 million, resulting in a cost coverage of 114.5 percent. PHI earned a rebate on eligible USPS Marketing Mail volume of approximately $123,000 during FY 2017.

The Commission reviews NSAs from a contract year perspective, and it focuses on the net benefit of an NSA to the Postal Service. As shown in USPS-FY17-30, using the Commission’s preferred methodology, the net benefit of the PHI NSA for Agreement Year 3 (July 1, 2016 to June 30, 2017) is estimated to be negative $122,591. Because of continuing operational challenges faced by the mailer, which the Postal Service described in its response to Chairman’s Information Request No. 8, Question 8, in

\(^{36}\) FY 2016 ACD, at 62.

\(^{37}\) USPS-FY17-37, Preface, at 13, item 11.
Docket No. ACR2016 (February 6, 2017), annual volume was less than the baseline. Accordingly, over the course of this Agreement Year there were no incremental pieces to generate additional contribution. The relatively small rebate amount paid ($122,591) constitutes the entirety of the net negative financial impact during Agreement Year 3.

Although Agreement Year 3 shows a negative impact to overall contribution, the agreement to date has generated approximately $603,000 in net positive contribution. Further, on December 8, 2017, the Postal Service filed a notice informing the Commission of steps that it took to ensure that the PHI NSA will generate positive net financial contribution for the Postal Service in the future. In particular, the parties agreed to suspend the Postal Service’s obligation to pay rebates for the period of January 1, 2018 through June 30, 2018, or until a revised NSA that results in positive net financial contribution is approved by the Commission. Depending on whether PHI earns a rebate in Quarter 2 of Agreement Year 4, the suspension of the Postal Service’s obligation to pay rebates for the remainder of Agreement Year 4 should ensure that the NSA’s negative net financial contribution is reduced or eliminated. While the Postal Service acknowledges that the NSA did not satisfy 39 U.S.C. § 3622(c)(10)(A) in FY 2017, its positive net financial contribution to date, and the Postal Service’s recent notice of suspension, militate against any additional corrective action at this time.

In FY 2017, the scale of the PHI NSA was sufficiently small to make market disruption unlikely. Thus, the NSA complied with 39 U.S.C. § 3622(c)(10)(B). Further, in compliance with 39 U.S.C. § 3622(c)(10), similar functionally-equivalent NSAs could have been made available to similarly-situated mailers.
2. **International Negotiated Service Agreements**

Although the Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators 1 product as a whole covered its attributable costs, revenue for an NSA with Royal Post NL did not cover attributable costs. However, that agreement expired at the end of the first quarter, on December 31, 2016.

In response to the Commission’s request in the FY 2016 ACD that the Postal Service include in this Report financial documentation demonstrating that noncompensatory bilateral agreements improve the net financial position of the Postal Service over UPU default terminal dues rates, the Postal Service has provided the requested information in USPS-FY17-NP2.

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38 FY 2016 ACD, at 69.
III. SERVICE PERFORMANCE, CUSTOMER SATISFACTION, AND CONSUMER ACCESS

A. Continued Success in Improving Service Performance

Building upon its broad successes last year in enhancing service performance, in FY 2017 the Postal Service again achieved service performance improvements in the vast majority of categories of its market dominant products. During FY 2010, the Commission issued its final rules on periodic reporting of service performance measurement and customer satisfaction, which are codified at 39 C.F.R. Part 3055. Among other things, Commission Rules 3055.20 through 3055.24 require annual reporting of service performance achievements at the national level for all market dominant products. The Postal Service’s report, including information responsive to the criteria listed in Rule 3055.2(b)-(k), is included as USPS-FY17-29.

The Postal Service set for itself aggressive on-time targets for all market dominant products. It has used those high targets to challenge itself to strive for – and

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39 In FY 2017, the Postal Service did not change market dominant product service standards (including applicable business rules) for any class of mail on a nationwide or substantially nationwide basis.


41 Reporting, however, is not required where the Commission has granted a semi-permanent exception or a temporary waiver. Id. at 21-23.

42 The Annual Report on Service Performance within USPS-FY17-29 includes plans for improving the performance of certain products. Besides that report on Service Performance, USPS-FY17-29 also includes a report on Methodologies for service performance measurement, in compliance with PRC Order No. 3490, Order Enhancing Service Performance Reporting Requirements and Closing Docket, Docket No. PI2016-1 (Aug. 26, 2016). USPS-FY17-29 additionally includes certain data on First-Class Mail (requested in the Commission’s FY 2016 ACD, at 133-35), and a special study on offshore service performance that is required every second year under 39 C.F.R. § 3055.7. Facility-specific data concerning Inbound Letter Post service performance (requested in the FY 2016 ACD, at 68) are submitted within nonpublic folder USPS-FY17-NP30. The nonpublic portion of the data on First-Class Mail in response to the FY 2016 ACD (at 133-35) is also submitted within USPS-FY17-NP30.
achieve – continuous improvement and to provide better service to our customers. For some products and in some districts, these targets have already been met or exceeded.

Even where these aggressive targets have not yet been met, the Postal Service has achieved clear, and sometimes dramatic, improvements in its recent service performance. In a full 13 of the 16 reported individual First-Class Mail product categories, the Postal Service’s FY 2017 performance results exceeded its results in FY 2016.43

The achievement of broad improvements during FY 2017 in 13 of the 16 individual reported First-Class Mail product categories is even more impressive when considered in the context of the Postal Service’s achievements during the prior year in FY 2016. In other words, the FY 2017 successes were not the result of correcting service issues from the year before – to the contrary, this year’s successes built upon last year’s successes, because, in FY 2016, the Postal Service had already improved in 15 of the 16 categories. That means that, for most of the First-Class Mail products (12 of 16), improvements were achieved for at least two years in a row. Overall, in all but one of the 16 First-Class Mail categories, the net service performance improved over the two-year period.

Not only were there improvements across the overwhelming majority of First-Class Mail categories, but a number of these leaps were large. The Commission has

43 Of the only 3 out of 16 First-Class Mail products not to show increases, one (Two-Day Single-Piece Letters/Postcards) was virtually unchanged from the year before, decreasing by less than two one-hundredths of a percent (a drop of less than 0.02 percent). The other two categories were really one and the same – Outbound Single-Piece First-Class Mail International (Three-to-Five-Day) and Outbound Single-Piece First-Class Mail International (Combined). That is, given that performance improved for Outbound Single-Piece First-Class Mail International (Two-Day), the drop in the “Combined” category was driven by the same Three-to-Five-Day performance. Though a drop did occur in that one category, the Postal Service is not satisfied with even one setback, and is addressing how to reverse that product’s performance as described in the plans within its Service Performance Report in USPS-FY17-29.
expressed special concern in recent years over the performance of flats. In FY 2015, Three-to-Five-Day First-Class Mail Flats were on time 65.3 percent of the time. But the Postal Service has worked hard to improve this product, and its efforts have paid dividends. Last year, in FY 2016, Three-to-Five-Day First-Class Mail Flats improved more than five percentage points over FY 2015 (to 70.9 percent); the Postal Service built on that success and improved performance for this product another three percentage points in FY 2017 over FY 2016, to 73.9 percent. Thus in just two years, it improved its performance by nearly 9 percentage points. The Postal Service still has more work to do to make this product’s performance reach its aggressive targets, but its methods for improvement are undeniably driving it in the right direction by large leaps.

The same can be said for the Postal Service’s continued success in improving First-Class Mail Parcels. Two-Day First-Class Mail Parcels jumped from 84.2 percent in FY 2015, to 88.7 percent in FY 2016, to 92.4 percent in FY 2017. The leaps in the Three-to-Five-Day product were even larger – moving from 73.7 percent in FY 2015, to 80.3 percent in FY 2016, to 85.8 percent in FY 2017, improving more than 12 percentage points in just two years. These trends are not only upward; they are steep.

Like Flats, the Commission has expressed special concerns in recent years over Inbound International mail. And, like Flats, the Postal Service has taken the Commission’s concerns seriously and redoubled its efforts to improve service for the Inbound International products. In last year’s ACD (at 68), the Commission acknowledged that the Postal Service had improved Inbound Letter Post performance in FY 2016. However, last year the Commission directed the Postal Service to report more granular data on the performance of that product and how it is being addressed
with this year’s ACR. The magnitude of the resulting improvements speak for themselves: from only 75.6 percent in on-time performance for Inbound Single-Piece First-Class Mail International (Combined) in FY 2015, the Postal Service boosted its performance to 81.4 percent last year in FY 2016, and then boosted it again to 85.5 percent in FY 2017, rising nearly 10 percentage points in the two-year span.

The Postal Service’s First-Class Mail improvements likewise shine brightly when evaluated using composite measurements. In FY 2017, the Postal Service compiled a new First-Class Mail Letter and Flat (FCLF) Composite, which represents a weighted average of the performance of Single-Piece First-Class Mail and Presort First-Class Mail across all service standards, weighted by volume. Applying this new FCLF Composite measure to the past several years of performance data, service performance improved from 89.44 percent in FY 2015 to 92.34 percent in FY 2016, and then improved again to 93.29 percent in FY 2017.

Beyond First-Class Mail, the Postal Service has built upon last year’s successes with continued improvement again this year for other classes of mail as well. Following its improvements last year in 8 of the 9 categories of Marketing Mail (formerly known as Standard Mail), the Postal Service largely repeated its broad jumps with improvements in FY 2017 in 7 of the 9 categories since last year. Moreover, the decreases in the only two categories that did not improve were relatively small – one percentage point and one-tenth of a percentage point in those two categories, respectively. Indeed, in the

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44 As directed, that information is included as part of this ACR, within folder USPS-FY17-29 and nonpublic folder USPS-FY17-NP30.

45 Unlike past First-Class Mail composites, the new FCLF Composite excludes First-Class Mail Parcels, because First-Class Mail Parcels began to be classified as competitive products in September 2017.
latter of those two categories (Marketing Mail Parcels), despite the slight drop, the Postal Service achieved on-time performance in FY 2017 of 98.2 percent, which is more than 7 percentage points above its target of 91.0 percent.

Periodicals were another class of mail in which the Postal Service continued its trend of substantial improvements. Two years ago, on-time performance in both the In-County and Outside County categories lagged at under 78 percent. Last year, the Postal Service improved both categories to about 80 percent. This year, in FY 2017, the Postal Service brought performance in both categories up much further, now in excess of 85 percent. These are not yet at their target levels, but their continued rise demonstrates that the Postal Service’s efforts and methods to improve service performance are working.

As with First-Class Mail, the Postal Service improved its composite scores for the second year in a row for the Marketing Mail and Periodicals classes. The Postal Service compiled a new Marketing Mail and Periodicals Composite in FY 2017, which is comprised of all measured Marketing Mail and Periodicals of all entry types. Applying this new composite measure to the past several years of performance data, service performance improved from 86.77 percent in FY 2015 to 90.01 percent in FY 2016, and then improved again to 91.44 percent in FY 2017, in excess of the composite FY 2017 target of 91.00 percent.

In other classes of mail, the Postal Service achieved most of its service targets. In the Package Services class, the Postal Service exceeded its targets in 2 of the 3
categories. Similarly, within the Special Services class, the Postal Service exceeded its targets in 4 of the 5 product categories.

To be sure, even where the Postal Service achieves its targets, it is still seeking to improve its performance in all categories moving forward on a continuous basis. The Postal Service will continue to implement operational, technological, and employee training initiatives to improve the mail delivery process. This will include improved software to generate better daily operational plans and the development and deployment of more precise tools, such as Informed Visibility, to scan and track mail at each step of the delivery process. Other operational changes will include increasing the amount of advanced mail (mail processed ahead of schedule), ensuring that late arrival mail is captured, and improving delivery point sequencing procedures to make delivery more efficient.

Notably, the amount of commercial mail in official measurement increased in FY 2017 over FY 2016 (which, in turn, had represented an increase over FY 2015) and is expected to continue to increase in FY 2018.

B. Customer Satisfaction with Market Dominant Products

Section 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

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46 In the one category in which it did not achieve its target, BPM Flats, the Postal Service has already been working closely with the Commission to find solutions to the challenges unique to that category. Though its performance still needs more work, its on-time results did improve by more than 3 percentage points from FY 2016 to FY 2017, even after improving more than 8 points during the prior year.

47 In the fifth category, P.O. Box Service, the Postal Service missed its target by only 1.1 percent. Nevertheless, as described in its Service Performance Report that accompanies this ACR within folder USPS-FY17-29, the Postal Service is implementing specific plans for improvement, including site-specific review.
products, also known as mailing services. The Postal Service improved on all measures of customer experience in FY 2017.48

1. Overview

The Customer Engagement and Strategic Alignment (CE&SA) group in Consumer and Industry Affairs was responsible for survey measurement of the level of customer satisfaction with market dominant products during FY 2017 for Postal Service customers. Surveys were administered across all four quarters of the year for three customer groupings – Residential, Small/Medium Business, and Large Business customers.

2. Background

The Customer Insights (CI) program, directed by the Consumer and Industry Affairs department, provides a comprehensive view of the customer experience across the most frequently used customer contact channels. CI’s modular components and flexible design allow expansion and inclusion of additional points of contact to meet the quickly changing customer landscape. The Postal Service is dedicated to delivering excellent customer experiences and the CI program supports this effort.

Customer Insights Measurement System — The CI measurement system provides a holistic view of customer satisfaction. The customer experience is measured across five touch points then weighted and aggregated to create the CI composite score.

48 See USPS-FY17-17, pages 16-17.
3. **Methodology**

For the CI system in FY 2017, Residential and Small/Medium business customers were randomly selected, contacted by mail, and offered the opportunity to complete an online or phone survey. Residential and Small/Medium businesses are sampled sufficiently to ensure, at the District level, a minimum precision level of +/- 5 percentage points, at the 90 percent level of confidence per postal quarter. In addition, a Large Business Panel Survey (>250 Employees) was conducted in quarters 2 & 4.

To measure customer experience with market dominant products, residential, small business, and large business survey respondents were asked to rate their product satisfaction using a six-point scale: *Very Satisfied, Mostly Satisfied, Somewhat Satisfied, Somewhat Dissatisfied, Mostly Dissatisfied, and Very Dissatisfied.* Respondents were also given the option of marking “Don’t Use Product” and those that responded in this manner were not included in the calculations for satisfaction with market dominant products. Customers who indicated that they did not use a product or were not familiar with a product were excluded from the calculated satisfaction ratings.

In FY 2017, the Postal Service continued combining only the top two box scores of *Very Satisfied* and *Mostly Satisfied*, in accordance with general industry standards for measuring customer satisfaction. The scores reported for market dominant products in FY 2017 result from combining only these *Very Satisfied* and *Mostly Satisfied* ratings.

4. **Survey Results – FY 2017 Ratings for Market Dominant Products**

As it did in the 2016 ACR, the Postal Service presents information below regarding customer satisfaction with Market Dominant Products. Overall, customer
satisfaction increased from FY 2016 to FY 2017 in all of the categories measured, as reflected in the Customer Insight (CI) Composite Score shown below:

<table>
<thead>
<tr>
<th>National</th>
<th>FY16</th>
<th>FY17</th>
<th>Var</th>
</tr>
</thead>
<tbody>
<tr>
<td>CI Composite</td>
<td>87.62</td>
<td>88.30</td>
<td>0.68</td>
</tr>
<tr>
<td>POS</td>
<td>86.38</td>
<td>88.53</td>
<td>2.15</td>
</tr>
<tr>
<td>Delivery</td>
<td>76.26</td>
<td>83.22</td>
<td>6.96</td>
</tr>
<tr>
<td>BSN</td>
<td>95.13</td>
<td>96.25</td>
<td>1.12</td>
</tr>
<tr>
<td>CCC</td>
<td>85.18</td>
<td>86.80</td>
<td>1.62</td>
</tr>
<tr>
<td>*eCC</td>
<td>-</td>
<td>3.78</td>
<td>-</td>
</tr>
</tbody>
</table>

*eCC was added as a new metric in FY17.*

The Postal Service saw an increase across all touchpoints from FY 2016 to FY 2017. The POS Survey Overall satisfaction score increased 2.15 points from FY 2016 to FY 2017. Several initiatives were implemented to assist with improving the retail customer experience. A focus on high opportunity retail units allowed the Postal Service to identify root causes and develop personalized solutions for overall improvements. Examples of these solutions included defining roles and responsibilities, staffing and scheduling, and customer service focused training. In addition, these retail units promoted the use of retail employees in the lobby to assist customers prior to reaching the full service counter. The Postal Service also updated its Retail Systems Software (RSS) terminals in FY 2017 to clarify product and service offerings to improve the retail customer experience. The Postal Service managed operational training webinars focusing on roles and responsibilities, planning and scheduling, and retail

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*eCC stands for Enterprise Customer Care, and measures the percentage of customer inquiries that are reopened within 90 days. A lower percentage is a better outcome, since reducing the number of times a customer reopens a previously submitted inquiry drives customer satisfaction.
technology usage in lobbies, and conducted Lean Six Sigma (LSS) Kaizens resulting in Standard Work Instructions for retail employees.

The chart immediately below shows a breakdown of the Mailing Services customer satisfaction results for market dominant products (FY 2017 vs. FY 2016), a separate portion of the customer satisfaction survey related to the Delivery component in the chart above. Following the chart, the Postal Service analyzes these figures to show where the Postal Service’s efforts during FY 2017 were successful and to detail steps it will take in FY 2018 to improve customer satisfaction in this area.

Table 14: Customer Satisfaction with Market Dominant Products (Mailing Services) –

<table>
<thead>
<tr>
<th>Market Dominant Products (Mailing Services)</th>
<th>Residential % Rated Very/Mostly Satisfied</th>
<th>Small/Medium Business % Rated Very/Mostly Satisfied</th>
<th>Large Business % Rated Very/Mostly Satisfied</th>
</tr>
</thead>
<tbody>
<tr>
<td>First-Class Mail</td>
<td>89.05 (89.13)</td>
<td>84.38 (83.34)</td>
<td>77.97 (81.49)</td>
</tr>
<tr>
<td>Single-Piece International</td>
<td>85.18 (84.80)</td>
<td>82.69 (81.34)</td>
<td>69.98 (74.37)</td>
</tr>
<tr>
<td>Standard Mail</td>
<td>83.13 (85.49)</td>
<td>80.32 (79.87)</td>
<td>71.69 (76.89)</td>
</tr>
<tr>
<td>Periodicals</td>
<td>85.66 (85.07)</td>
<td>82.32 (81.86)</td>
<td>70.56 (74.26)</td>
</tr>
<tr>
<td>Single-Piece Standard Post</td>
<td>86.82 (86.28)</td>
<td>82.94 (81.13)</td>
<td>70.30 (75.85)</td>
</tr>
<tr>
<td>Media Mail</td>
<td>86.04 (86.59)</td>
<td>85.10 (84.05)</td>
<td>69.15 (74.28)</td>
</tr>
<tr>
<td>Bound Printed Matter</td>
<td>--* (--*)</td>
<td>82.77 (80.11)</td>
<td>67.70 (73.40)</td>
</tr>
<tr>
<td>Library Mail</td>
<td>87.28 (85.54)</td>
<td>85.98 (83.05)</td>
<td>66.41 (70.56)</td>
</tr>
</tbody>
</table>

* Number of responses received did not meet minimum threshold for 90% level of confidence.

The chart shows variable results in FY 2017 for Residential (although results are higher for the majority of products), slight increases across all products for Small/Medium Business, and decreases for Large Business customer satisfaction.
The vast majority of Large Business customers continue to report being very or mostly satisfied with the Postal Service’s mailing services for all market dominant products. However, the Postal Service recognizes that it must take steps to increase these results, and will focus on improving customer service in FY 2018, both for its Large Business customers and all other customers. As a first step, management will continue to conduct analytics of all of the customer satisfaction results to better understand the key drivers for the current scores. By better understanding the reasons for the current scores, the Postal Service will be able to design and implement customer satisfaction improvements as appropriate. Prior to review of such analytics, however, the Postal Service will continue its efforts to improve overall customer satisfaction with mailing services of market dominant products as it did throughout FY 2017. As far as specific steps in the retail environment, in FY 2018 the Postal Service is continuing its efforts to improve overall customer satisfaction by enhancing retail technology to include more self-service options, software upgrades, and line queue management systems. In addition, the Postal Service is modifying its employee training to include a more customer-centric focus. Ultimately, the goal is to create an extremely efficient retail experience that enhances the customer visit and supports enhancing the Postal Service business in the retail lobby and cross-channel experience. The Postal Service’s specific steps to improve mail delivery and carrier performance are addressed in Section III.B.5 below.

5. Addressing Mail Delivery and Carrier Performance Issues

The Postal Service is sensitive to customer concerns about the overall experience that customers receive with their letters and packages and the performance
of delivery carriers. In FY 2017 responses from the Customer Insights Delivery Survey were as follows:

**Table 15: Customer Insights Delivery Survey Responses**

<table>
<thead>
<tr>
<th>Delivery Residential and Small Business</th>
<th>YTD Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>OSAT</td>
<td>74.60%</td>
</tr>
<tr>
<td>Delivered to correct address</td>
<td>80.93%</td>
</tr>
<tr>
<td>Delivered in good condition</td>
<td>89.69%</td>
</tr>
<tr>
<td>Carrier is friendly and courteous</td>
<td>83.35%</td>
</tr>
<tr>
<td>Damaged Items Marked w/ Stamp/Sticker</td>
<td>15.39%</td>
</tr>
<tr>
<td>Carrier OSAT</td>
<td>76.58%</td>
</tr>
<tr>
<td>The PO Box is meeting my needs</td>
<td>86.00%</td>
</tr>
<tr>
<td>Packages are delivered on time based on expected day of delivery</td>
<td>81.42%</td>
</tr>
<tr>
<td>Tracking information for packages is accurate</td>
<td>79.39%</td>
</tr>
<tr>
<td>Instructions for what to do after receiving a missed delivery notice are clear</td>
<td>65.79%</td>
</tr>
</tbody>
</table>

The Postal Service continued with its mitigation efforts in FY 2017 to address several issues most notably in reducing complaints from customers who believed that their packages were late or missing:

- Delivery Operations worked closely with Consumer and Industry Affairs in establishing distinct categories for package inquiries and complaints that fall under the broad category of “Where is My Package” (WIMP). Previously, these complaints were lumped together, which did not allow for granular analysis. In FY 2017, the Postal Service established nine sub-categories for eCC agents to place WIMP complaints, based on key questions to ask of customers. Categories are as follows:
  - Scanned Delivered Not Received - Package was scanned delivered but the customer cannot find the package
  - Attempt event but not attempted - Attempt scan made but no actual delivery attempt was made
- Not Re-Delivered - Customer requested redelivery but carrier did not attempt redelivery
- Misdelivered package - I received someone else’s package or someone else received my package
- Late Delivery Day with AAU - Package was not delivered on expected delivery day. Arrival At Unit (AAU) scan is present
- Late Delivery Day without AAU - Package was not delivered on expected delivery day. AAU scan is not present
- Left in Unsecure Location - Package was left exposed to elements or theft
- Returned Package in Error - Package was returned when the customer does not believe it should have been
- Returned to Post Office not Attempted - Package was scanned Returned to Post Office not Attempted

Due to software changes and training associated with this effort, the Postal Service was unable to implement the above initiative until week 4 of FY 2018. But the Postal Service is already using these data to understand its largest opportunities for improvement and in which specific geographical areas.

The Postal Service has introduced additional measures to improve service in delivery. For example, Delivery Operations has continued its work in updating the Mobile Delivery Device (MDD) to simplify menu items for carriers and expand options to meet the demands of customers. In FY 2017 the Postal Service added an option on the MDD that would explain to customers when there was an unexpected delivery delay with their package, as well as language to explain to customers when a package was
returned to the postal unit due to an addressing issue, but that the Postal Service would attempt to resolve and re-deliver if possible. This approach provided a solution when a package contained a missing suite number, for example, or when a delivery employee was unable to deliver by customer name but returned the package to the office for review by a more experienced employee on the route. Additionally, utilizing feedback from the U.S. Census Bureau on Undeliverable As Addressed (UAA) errors on alternate address mail, the Postal Service produced a “Blue Tube” training video on proper handling procedures for such items.

C. Consumer Access to Postal Services

Information regarding Post Offices, collection boxes, wait time in line, and delivery points is contained in USPS-FY16-33. The Postal Service closed 304 Postal Service operated retail facilities in FY 2016; see additional discussion on suspended retail units below.

At the end of FY 2016, there were 26,410 Post Offices, 4,444 stations and branches, and 523 carrier annexes. At the end of FY 2017 there were 2,712 Contract Postal Units (CPUs), 721 Village Post Offices (VPOs), and 6,879 Approved Shipper active locations. Nationally, there were 146,252 collection boxes available at the end of FY 2017, compared to 152,539 at the beginning of FY 2017. Average wait time in line decreased at the national level from 2 minutes 48 seconds in FY 2016 to 2 minutes 28 seconds in FY 2017.

In the FY 2016 ACD, the Commission directed the Postal Service to make substantial progress on closing or reopening post offices which had been indefinitely suspended. The Postal Service can report that, as of the end of FY 2017, it has made
substantial progress on resolving a large number of these suspended offices. The Postal Service will be working in FY 2018 and FY 2019 to complete the resolution process for this group of suspended offices. As it does every year, the Postal Service has also dealt with newly suspended post offices within FY 2017.

As of the start of FY 2017 there were 655 suspended post offices. An additional 7 offices were entered into the system retroactively, bringing the total to 662 offices suspended as of the beginning of FY 2017:50

<table>
<thead>
<tr>
<th>STATE</th>
<th>AREA</th>
<th>DISTRICT</th>
<th>OFFICE</th>
<th>FACILITY TYPE</th>
</tr>
</thead>
<tbody>
<tr>
<td>IL</td>
<td>GREAT LAKES</td>
<td>GATEWAY PFC</td>
<td>BOLES</td>
<td>Main PO</td>
</tr>
<tr>
<td>IL</td>
<td>GREAT LAKES</td>
<td>GATEWAY PFC</td>
<td>COATSBURG</td>
<td>Main PO</td>
</tr>
<tr>
<td>MD</td>
<td>CAPITAL METRO</td>
<td>CAPITAL PFC</td>
<td>BURTONSVILLE</td>
<td>Main PO</td>
</tr>
<tr>
<td>MO</td>
<td>WESTERN</td>
<td>MID-AMERICA PFC</td>
<td>COMMERCE</td>
<td>Main PO</td>
</tr>
<tr>
<td>TN</td>
<td>EASTERN</td>
<td>TENNESSEE PFC</td>
<td>LUTTS</td>
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<tr>
<td>TX</td>
<td>SOUTHERN</td>
<td>RIO GRANDE PFC</td>
<td>CRANFILLS GAP</td>
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<td>SOUTHERN</td>
<td>RIO GRANDE PFC</td>
<td>SATIN</td>
<td>Main PO</td>
</tr>
</tbody>
</table>

The Postal Service has been working to resolve these suspensions in the 662 affected offices through re-opening or processing through discontinuance where necessary, as further detailed below. During FY 2017, of the 662 offices, the Postal Service discontinued 304 of the offices51 and re-opened 39 offices, leaving 319 of the 662 offices suspended as of the end of FY 2017.

50 See USPS-FY17-33, Consumer Access to Postal Services, included as part of today’s FY 2017 ACR filing.
51 This total closing/discontinuance number of 304 differs from that reported in the first tab of the “Post Offices” excel file in Folder 33; that tab lists 208 as the total closing/discontinuance number for FY 2017. This discrepancy is the result of different reporting criteria used by Delivery Operations and the Address Management System (AMS) office in tracking the disposition of suspended post offices. AMS does not count certain indefinitely suspended post offices in cases where a Final Determination had been issued to discontinue those offices, and the only remaining step is publication of notification in the Postal Bulletin. The 304 figure more accurately reflects offices in suspension, however, since it treats as
Within FY 2017 itself, an additional 86 offices were suspended. Of the 86, 27 were re-opened during FY 2017. The remaining 59 offices, added to the 319 above, brought the total suspended offices as of the end of FY 2017 to 378.

In response to an information request from the Commission during the 2016 ACR proceeding, the Postal Service provided a projected timeline for resolution of the 662 suspended offices (i.e., the 655 offices plus the 7 added offices, all of which were in suspended status as of the beginning of FY 2017). Of that 662 number, the Postal Service proposed to discontinue 260 of the offices that were near completion of the discontinuance process, and resolve the suspensions of an additional 100 offices, by the end of FY 2017, for a total of 360 suspensions resolved.

Through the end of FY 2017, the Postal Service officially discontinued the 260 offices that were near completion of the discontinuance process through publication of final notification in the Postal Bulletin, plus an additional 44 offices, for a total of 304 offices discontinued during FY 2017. In addition, the Postal Service reopened 39 of the 662 offices suspended as of the beginning of the fiscal year, bringing the total number of suspended office resolutions in FY 2017 to 343.

The Postal Service made considerable progress in resolving suspended offices, but of course, the number of suspensions resolved in FY 2017 fell 17 short of the projected number. The projected goal was not achieved due to the significant amount of time and resources required to individually review and process each office, and the

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suspended those offices that have undergone discontinuance, but for which publication in the Postal Bulletin has not occurred, as provided in Handbook PO-101. See Handbook PO-101 section 422.34.

difficulty of obtaining data and information on the offices that have been suspended for more extended time periods. However, the Postal Service will continue to process the remaining suspended offices, either through re-opening, or conducting discontinuance studies where necessary, to resolve these suspensions.

Accordingly, the Postal Service proposes the following revised timeline to resolve the 378 post offices in suspended status as of the beginning of FY 2018:

Table 17

<table>
<thead>
<tr>
<th>Fiscal Yr</th>
<th>Qtr</th>
<th>Projected Resolved</th>
<th>Projected Remaining Suspended</th>
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<tr>
<td>FY18</td>
<td>Q1</td>
<td>16</td>
<td>362</td>
</tr>
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<td>Q3</td>
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<td>FY18</td>
<td>Q4</td>
<td>70</td>
<td>209</td>
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<tr>
<td>FY19</td>
<td>Q1</td>
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<td>FY19</td>
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<td>69</td>
</tr>
<tr>
<td>FY19</td>
<td>Q3</td>
<td>69</td>
<td>0</td>
</tr>
</tbody>
</table>

**378 offices suspended at beginning of FY18**

Note that this revised timeline would resolve the remaining 319 “original” suspended offices from the 662 total as of the beginning of FY 2017; the Postal Service will also use its best efforts to resolve the 59 “new” suspensions that took place within FY 2017 and remain in suspended status.
IV. COMPETITIVE PRODUCTS

A. Product-by-Product Costs, Revenues, and Volumes

For FY 2017, cost, revenues, and volumes for competitive products of general applicability are shown directly in the CRA and ICRA. In the public CRA, competitive products are disaggregated into six groups – Total Priority Mail Express, Total (non-Express) Priority Mail, Total First-Class Package Service, Total Ground, Total International Competitive, and Total Domestic Competitive Services. The constituent products for each of those groups are listed in a table in the attached Application of the United States Postal Service for Nonpublic Treatment of Materials (Attachment Two). Those groups are further disaggregated in the Nonpublic CRA (USPS-FY17-NP11). For competitive products not of general applicability, available data on international customized mailing agreements (ICMs) for FY 2017 are presented in the ICRA materials within USPS-FY17-NP2. For domestic competitive products not of general applicability, information is provided in USPS-FY17-NP27.

B. Section 3633 Standards

This section addresses compliance with the competitive product pricing standards of section 3633, which have been implemented by the Commission at 39 C.F.R. § 3015.7.

1. Subsection 3633(a)(1)

Subsection 3633(a)(1) requires that competitive products not be cross-subsidized by market dominant products. The Commission’s regulations define the most appropriate test for this standard as the incremental cost test for the aggregation of
competitive products. Under this test, if the aggregate revenues from competitive products equal or exceed the aggregate incremental costs of competitive products, then competitive products overall have not been cross-subsidized by market dominant products.

In past ACRs, the Postal Service presented what was termed a “hybrid” estimate of incremental costs, in which an estimate of the aggregate incremental costs of domestic competitive products (including group specific costs) was added to an estimate of the volume variable plus product specific costs of international competitive products. The “hybrid” characterization reflected the blending of an actual estimate of domestic incremental costs with a volume variable plus product specific cost proxy for international incremental costs. The need for the hybrid approach stemmed from the structure of the ICRA, which precluded direct application of the incremental cost model to international products. As demonstrated in Proposal 22, Docket No. RM2010-4, the hybrid estimate was an improvement over the full proxy of volume variable plus product specific costs for both domestic and international competitive products, plus group specific costs, used before FY 2009. The hybrid approach provided stronger protection against cross-subsidy than the previous full proxy approach.

For FY 2017, however, additional improvements have strengthened the protection even further by allowing direct estimation of the group incremental costs for the group of all competitive products (domestic and international). Although the structure of the ICRA and the complexity of the international classification structure still

53 See 39 C.F.R. § 3015.7(a).
54 Proposal 22 was approved in Order No. 399, Order Accepting Analytical Principles Used in Periodic Reporting (Proposals Twenty-Two through Twenty-Five), PRC Docket No. RM2010-4 (Jan. 27, 2010).
preclude estimation of incremental costs for individual international competitive products, in accordance with a suggestion made by the Commission in the FY 2016 ACD, efforts were successful to split international cost information within cost pools between market dominant and competitive products. This allows the incremental cost model to estimate the effects of removing all competitive products simultaneously, and thus provides exactly the information necessary to fully conduct the cross-subsidy test as intended.

The group incremental cost estimate for domestic competitive products, the group incremental cost estimate for international competitive products, and the group incremental cost estimate for the group of all competitive products – fully documented in USPS-FY17-NP10 – are presented below. Note that the estimate for all competitive products is calculated separately from those for domestic and international, and thus is not merely the sum of those two estimates.

<table>
<thead>
<tr>
<th>FY2017 INCREMENTAL COST CALCULATION FOR TOTAL COMPETITIVE PRODUCTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group Specific</td>
</tr>
<tr>
<td>----------------</td>
</tr>
<tr>
<td>Domestic Competitive Mail (Market Tests)</td>
</tr>
<tr>
<td>International Competitive</td>
</tr>
<tr>
<td>Total Competitive</td>
</tr>
</tbody>
</table>

*The Group Inframarginal costs for Total Competitive are estimated separately, and they (and thus Total Competitive Incremental) are not the sums of the two previous rows. Costs are in $1,000s.*

The total competitive group incremental cost of $13.884 billion is well below total competitive products revenue of $20.689 billion (shown on page 3 of USPS-FY17-1). Therefore, based on these estimates, it is clear that competitive products in FY 2017

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55 FY 2016 ACD, at 65.
were not cross-subsidized by market dominant products, and thus were in compliance with subsection 3633(a)(1).

2. **Subsection 3633(a)(2)**

Subsection 3633(a)(2) requires that each competitive product cover its costs (i.e., maintain a cost coverage of at least 100 percent). As discussed above, the CRA Reports for FY 2017 presented in USPS-FY17-1 and USPS-FY17-NP11 now show product-level attributable costs for each domestic product as the sum of volume variable costs, product specific costs, and the inframarginal costs estimated as part of the incremental costs for that product. Similarly, using the methodology explained in the Preface to USPS-FY17-43, corresponding attributable cost estimates for domestic competitive NSA products are presented in USPS-FY17-NP27. For international products, however, attributable costs continue to reflect, as in prior years, the sum of volume variable and product specific costs. As shown in the Nonpublic CRA (USPS-FY17-NP11), USPS-FY17-NP27, and the ICRA (USPS-FY17-NP2), every competitive product maintained a cost coverage of at least 100 percent, with the exception of the following: four domestic NSAs, International Money Transfer Service (IMTS), Outbound International Insurance, one GEPS 6 contract, two GEPS 7 contracts, and three bilateral agreements with foreign postal operators.

a. **Domestic Competitive Products**

As noted above, there were four domestic NSAs that did not cover their costs. Of these, three either expired or were terminated. The remaining one – Priority Mail Contract 123 (Docket No. CP2015-80) – is being monitored pending reevaluation. Its cost coverage fell minimally below 100 percent due to a shift to a lighter customer
profile. The contract involves return packages, which incur lower unit delivery costs due to bulk delivery. The Postal Service is reviewing the underlying cost model because it may not appropriately reflect the actual functions performed on behalf of the customer that are causing costs to be incurred, and the direction of the potential discrepancy would appear to be an overstatement of costs. The Postal Service will monitor contract performance and renegotiate pricing if necessary.

In addition, there were two domestic NSAs – Priority Mail and First-Class Package Service Contract 7 (Docket No. CP2015-114) and Priority Mail Express, Priority Mail and First-Class Package Service Contract 9 (Docket No. CP2016-103) – that had one of their multiple components not cover its costs. However, each of these NSAs as a whole covered its costs.

b. International Competitive Products

The Postal Service offers the following observations on international competitive products for which revenues did not exceed attributable costs. First, both inbound and outbound components of International Money Transfer Service (IMTS) were reported to be below cost in FY 2017. The volume of IMTS continues to be small; consequently, the Postal Service reiterates its observations in its June 30, 2015 response to the FY 2014 ACD, namely, that “[b]ecause the number of IMTS transactions is small, it is difficult to obtain enough IOCS tallies through sampling to reliably estimate attributable cost for IMTS, resulting in relatively volatile unit costs.”56 There were only seven International Money Order IOCS tallies in FY 2017. Prices for IMTS-Outbound

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increased substantially on January 22, 2017, including a 73.7 percent increase in prices for International Money Orders. IMTS – Outbound almost covered its attributable costs in FY 2017. In FY 2018, the higher prices for IMTS – Outbound implemented in January 2017 will be in effect for the entirety of the fiscal year. In addition, prices for IMTS – Outbound will increase again on January 21, 2018, including a 3.6 percent increase for International Money Orders.\(^5\) Thus, the Postal Service considers that it has taken measures to address the cost coverage of IMTS – Outbound.

Second, the Postal Service notes that Outbound International Insurance did not cover attributable costs. One reason for this may be that claims for Priority Mail International (PMI), for which no fee is paid, are assigned to the Outbound International Insurance product, rather than to the PMI product. The Postal Service will continue to explore this issue to determine if a change in reporting of these claims costs is in order. In addition, in January 2017, the Postal Service raised prices for Priority Mail Express International (PMEI) insurance and PMI insurance by 4.7 percent and 4.8 percent, respectively. Also, prices for PMEI insurance and PMI insurance are scheduled to increase by 4.0 percent and 3.9 percent, respectively on January 21, 2018.

Third, although Global Expedited Package Services (GEPS) 6 contracts collectively covered their attributable costs, one of the seven GEPS 6 contracts in effect in FY 2017 did not cover its attributable costs. However, there was very little volume under that contract, and it was not renewed. Also, although GEPS 7 contracts collectively covered their attributable costs, two GEPS 7 contracts did not cover their

attributable costs. There was very little volume under both of those agreements, and one of the agreements expired on November 30, 2017. The Postal Service is considering what actions it should take concerning the one GEPS 7 contract currently in effect, for which the shortfall is quite minimal. There was too little volume under that contract in FY 2017 to draw definitive conclusions, but the Postal Service will continue to monitor that agreement.

Fourth, although the Inbound Competitive Multi-Service Agreements with Foreign Postal Operators 1 product as a whole covered its attributable costs, three agreements within that product did not cover attributable costs, two of which have expired. Revenue under the competitive portion of the NSA with China Post Group that expired at the midpoint of the fiscal year, on March 31, 2017, did not cover attributable costs. Also, revenue for the NSA with Royal Post NL that expired at the end of the first quarter of the fiscal year, on December 31, 2016, did not cover attributable costs, and that agreement was not renewed. In addition, the competitive portion of the current NSA with China Post Group (which is a relatively small portion of the entirety of the flows under that bilateral), which went into effect on April 1, 2017 and is scheduled to expire on June 30, 2018, did not cover attributable costs by a very small percentage. The Postal Service will monitor this situation in developing any new proposal for a successor agreement.

3. Subsection 3633(a)(3)

Subsection 3633(a)(3) states that competitive products must collectively cover what the Commission determines to be an appropriate share of the Postal Service’s institutional costs. In its regulations, the Commission has determined that an
appropriate minimum share is 5.5 percent of total institutional costs.\textsuperscript{58} Page 3 of USPS-FY17-1 shows total institutional costs of $30.872 billion. Applying the 5.5 percent to that figure yields a target contribution of $1.698 billion. Page 3 of USPS-FY17-1 shows total competitive product attributable costs of $13.538 billion (consisting of $13.3187 billion of volume variable costs, $0.1635 billion of product specific costs, and $0.0559 billion of inframarginal costs), and total competitive product revenue of $20.689 billion.

Subtracting the former from the latter results in total competitive product contribution of $7.153 billion. Taking into account the competitive market test net contribution figure of -$0.9 million reported in USPS-FY17-NP27, the overall net competitive contribution amount changes to $7.152 billion, which exceeds 23 percent of institutional costs, well in excess of the 5.5 percent requirement. Thus, the subsection 3633(a)(3) requirement was met in FY 2017.

C. Priority Mail Express International Discount

In response to the Commission’s request in Docket No. CP2017-20 concerning the monitoring of the discount for some Priority Mail Express International items at retail, the Postal Service provides an analysis of the Priority Mail Express International discount’s effect in a separate workpaper included in USPS-FY17-NP9, along with a list of destination countries and weight steps for which the Postal Service offered the Priority Mail Express International discount.\textsuperscript{59}

\textsuperscript{58} See 39 C.F.R. § 3015.7(c). The Commission is presently conducting a new review of the appropriate share in Docket No. RM2017-1.

D. ACD Directive

In its FY 2016 ACD, the Commission directed the Postal Service to “identify each NSA product that had no mailpieces shipped under the contract when it files future ACRs.” In response, the Postal Service has included this information in USPS-FY17-NP27 (for domestic NSAs) and USPS-FY17-NP2 (for international NSAs).

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60 FY 2016 ACD, at 83.
V. MARKET TESTS AND NONPOSTAL SERVICES

A. Market Dominant Market Tests

In FY 2017, there were no market tests of experimental products offered under the provisions of section 3641 that were categorized as market dominant.

B. Competitive Market Tests

Customized Delivery and GEM Merchant Solution were the only competitive market tests of experimental products authorized under the provisions of section 3641 in FY 2017. Information for these market tests is provided under seal in USPS-FY17-NP27. The Postal Service does not have a method for estimating the quality of service of its competitive experimental products. The Postal Service does not believe that the offering of these competitive experimental products created an inappropriate competitive advantage for the Postal Service or any mailer.

C. Nonpostal Services

FY 2017 revenue, cost, and volume data for the two market dominant nonpostal service products are provided below.
### Market Dominant

#### FY2017

<table>
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<tr>
<th>1</th>
<th>Alliances with the Private Sector to Defray Costs [includes MoverSource nonpostal service]</th>
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<td>Revenue</td>
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<tr>
<td>Expense</td>
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<td>Net Income (Loss)</td>
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<tr>
<td>Volume</td>
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<table>
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<tr>
<th>2</th>
<th>Philatelic Sales</th>
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<tr>
<td>Expense</td>
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<tr>
<td>Net Income (Loss)</td>
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<tr>
<td>Volume</td>
<td>2,671,547</td>
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Revenue and expense are for fulfillment only

Comparable data for the seven competitive nonpostal services in effect and active in FY 2017 are provided in USPS-FY17-NP27.
VI. NONPUBLIC ANNEX

Section 3652(f)(1) contemplates the use of a nonpublic annex for documents or other materials that the Postal Service considers exempt from public disclosure, pursuant to 39 U.S.C. § 410(c) and 5 U.S.C. § 552(b). In particular, section 410(c)(2) exempts from mandatory disclosure “information of a commercial nature…which under good business practice would not be publicly disclosed.” Accordingly, such information is contained in this Report’s nonpublic annex.

A complete listing of the contents of the nonpublic annex appears at Attachment One. In general, the nonpublic annex contains the same types of materials that were included in the nonpublic annex in Docket No. ACR2016. Thus, its primary contents are:

(1) versions of the CRA and Cost Segments and Components reports that provide disaggregated information for competitive products, and supporting materials underlying the CRA (such as the CRA “B” workpapers, the CRA model, and files relating to the various costing data systems);

(2) the ICRA, supporting materials underlying the ICRA, and data for international customized agreements with customers;

(3) billing determinants for domestic and international competitive products; and

(4) information on individual domestic competitive product NSAs.

An Application for Nonpublic Treatment of Materials regarding the nonpublic annex appears at Attachment Two.
CONCLUSION

The Postal Service respectfully submits the forgoing Report for FY 2017.
# LIST OF APPENDED MATERIALS

## PUBLIC FOLDERS

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<td>USPS-FY17-1</td>
<td>FY 2017 Public Cost and Revenue Analysis (PCRA) Report</td>
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<tr>
<td>USPS-FY17-2</td>
<td>FY 2017 Public Cost Segments and Components Report</td>
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<td>USPS-FY17-3</td>
<td>FY 2017 Discounts and Passthroughs of Workshare Items</td>
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<td>USPS-FY17-4</td>
<td>FY 2017 Market Dominant Billing Determinants</td>
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<td>USPS-FY17-5</td>
<td>Cost Segment and Components Reconciliation to Financial Statements and Account Reallocations (Reallocated Trial Balances)</td>
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<td>USPS-FY17-6</td>
<td>General Classification of Accounts (Formerly Handbook F-8)</td>
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<td>USPS-FY17-7</td>
<td>Cost Segment 3 Cost Pools &amp; Other Related Information (Public Portion)</td>
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<td>Equipment and Facility Related Costs</td>
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<td>(First and Marketing Mail) &amp; Periodicals Cost Model</td>
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<td>FY 2017 Delivery Costs By Shape</td>
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<td>FY 2017 Window Service Cost by Shape</td>
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<td>Business Reply Mail Cost Model</td>
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<td>FY 2017 Bound Printed Matter Mail Processing Costs</td>
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<td>USPS-FY17-23</td>
<td>MODS Productivity Data</td>
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<td>USPS-FY17-24</td>
<td>FY 2017 Non-Operation Specific Piggyback Factors (Public Portion)</td>
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<td>FY 2017 Mail Processing Piggyback Factors (Operation Specific)</td>
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<td>USPS-FY17-26</td>
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<td>FY 2017 Nonprofit Mail Cost Approximations</td>
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<td>Annual Report on Service Performance for Market Dominant Products</td>
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<td>FY 2017 Market Dominant NSA Materials</td>
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<td>USPS-FY17-34</td>
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<td>Rural Carrier Cost System (RCCS) Documentation (Public Version)</td>
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USPS-FY17-36 Transportation Cost Systems (TRACS) Documentation (Public Version)

USPS-FY17-37 In-Office Cost System (IOCS) Documentation (Public Version)

USPS-FY17-38 USPS Market Dominant Product Customer Satisfaction Measurement Survey Instruments

USPS-FY17-39 FY 2017 Competitive Products Fund Reporting Materials

USPS-FY17-40 2017 Rural Mail Count

USPS-FY17-41 International Market Dominant Billing Determinants

USPS-FY17-42 FY 2017 Revenue, Pieces, and Weight Report (Public Version)

USPS-FY17-43 FY 2017 Market Dominant Product Incremental Costs

USPS-FY17-44 Update to Periodicals Pricing Report

NONPUBLIC FOLDERS:

USPS-FY17-NP1 FY 2017 Domestic Competitive Product Billing Determinants

USPS-FY17-NP2 FY 2017 International Cost and Revenue Analysis (ICRA) Report

USPS-FY17-NP3 FY 2017 International Cost Segments and Components Report

USPS-FY17-NP4 FY 2017 ICRA Domestic Processing Model (Cost Matrices, Reports, Control File, & Changes)

USPS-FY17-NP5 FY 2017 ICRA Overview/Technical Description

USPS-FY17-NP6 FY 2017 International Cost Segment Spreadsheets

USPS-FY17-NP7 Cost Segment 3 International Product Costs by Cost Pools (Volume Variable Cost Pools)
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<td>FY 2017 Competitive Product Incremental and Group Specific Costs</td>
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<td>FY 2017 Nonpublic Cost and Revenue Analysis (NPCRA) Report</td>
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<td>Cost Segment 3 Cost Pools &amp; Other Related Information (Nonpublic Portion)</td>
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<tr>
<td>USPS-FY17-NP19</td>
<td>FY 2017 Non-Operation Specific Piggyback Factors (Nonpublic Portion)</td>
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<td>USPS-FY17-NP20</td>
<td>FY 2017 Mail Processing Costs by Shape (Nonpublic Portion)</td>
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<tr>
<td>USPS-FY17-NP21</td>
<td>In-Office Cost System (IOCS) Documentation (Nonpublic Version)</td>
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<tr>
<td>USPS-FY17-NP22</td>
<td>City Carrier Cost System (CCCS) Documentation (Nonpublic Version)</td>
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<td>USPS-FY17-NP23</td>
<td>Rural Carrier Cost System (RCCS) Documentation (Nonpublic Version)</td>
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<td>USPS-FY17-NP24</td>
<td>Transportation Cost Systems (TRACS) Documentation (Nonpublic Version)</td>
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<tr>
<td>USPS-FY17-NP25</td>
<td>Mail Characteristics Study (Nonpublic Portion)</td>
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<tr>
<td>USPS-FY17-NP26</td>
<td>FY 2017 Special Cost Studies Workpapers – Special Services (Nonpublic Portion)</td>
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<td>USPS-FY17-NP27</td>
<td>FY 2017 Domestic Competitive NSA &amp; Nonpostals Materials</td>
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<tr>
<td>USPS-FY17-NP28</td>
<td>FY 2017 Revenue, Pieces, and Weight Report (Nonpublic Version)</td>
</tr>
<tr>
<td>USPS-FY17-NP29</td>
<td>Cost Segment and Components Reconciliation to Financial Statements and Account Reallocations (Reallocated Trial Balances) (Nonpublic Version)</td>
</tr>
<tr>
<td>USPS-FY17-NP30</td>
<td>Annual Report on Service Performance for Market Dominant Products (Nonpublic Portion)</td>
</tr>
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</table>
APPLICATION OF THE UNITED STATES POSTAL SERVICE
FOR NONPUBLIC TREATMENT OF MATERIALS

In accordance with 39 C.F.R. § 3007.21 and Order No. 225,¹ the United States Postal Service (Postal Service) hereby applies for nonpublic treatment of the thirty appended folders identified as nonpublic in Attachment One of the FY 2017 Annual Compliance Report (collectively, the “Nonpublic Annex”). As is apparent from the Attachment One list, the majority of the folders in the Nonpublic Annex have a corresponding public folder.

In many instances, a set of material has been divided into one portion that relates to Market Dominant products and another portion that relates to Competitive products. In those instances, the public folder includes the portion of material relating to Market Dominant products, and the nonpublic folder includes the portion of materials relating to Competitive products. In many other instances, two versions of materials are prepared, one that is public and contains aggregated information regarding Competitive products or large groups of Competitive products, and another that is nonpublic and contains information regarding Competitive products that is disaggregated to the product level. In general, except for the six groups of Competitive products for which cost data are shown in the Cost and Revenue Analysis (CRA), all disaggregated cost information relating to Competitive products, and all background data used to develop disaggregated cost information on Competitive products, are filed under seal in the Nonpublic Annex.

(1) The rationale for claiming that the materials are nonpublic, including the specific statutory basis for the claim, and a statement justifying application of the provision(s);

The materials designated as nonpublic consist of commercial information concerning postal operations and finances that under good business practice would not be disclosed publicly. Based on its longstanding and deep familiarity with the postal and communications businesses and markets generally, and its knowledge of many firms, including competitors, mailers, and suppliers, the Postal Service does not believe that any commercial enterprise would voluntarily publish information pertaining to the costs, volumes, revenues, and markets for its competitive products, as well as inbound market dominant products for which rates are negotiated with other postal operators. In the Postal Service’s view, this information would be exempt from mandatory disclosure pursuant to 39 U.S.C. § 410(c)(2) and 5 U.S.C. § 552(b)(3) and (4).²

(2) Identification, including name, phone number, and email address for any third-party who is known to have a proprietary interest in the materials, or if such an identification is sensitive, contact information for a Postal Service employee who shall provide notice to that third party;

The Postal Service believes that the only third parties that have a proprietary interest in the materials submitted in connection with the FY 2017 Annual Compliance Report are identified in Appendix 1 to this Application. The Postal Service also hereby provides notice that it has already informed each third party, in compliance with 39

² In appropriate circumstances, the Commission may determine the appropriate level of confidentiality to be afforded to such information after weighing the nature and extent of the likely commercial injury to the Postal Service against the public interest in maintaining the financial transparency of a government establishment competing in commercial markets. 39 U.S.C. § 504(g)(3)(A). The Commission has indicated that “likely commercial injury” should be construed broadly to encompass other types of injury, such as harms to privacy, deliberative process, or law enforcement interests. Order No. 194, Second Notice of Proposed Rulemaking to Establish a Procedure for According Appropriate Confidentiality, Docket No. RM2008-1 (Mar. 20, 2009), at 11.
C.F.R. § 3007.20(b), of the nature and scope of this filing and its right to address its confidentiality concerns directly with the Commission.\(^3\) In addition, because the Postal Service maintains that (i) some competitive negotiated service agreement (NSA) customers’ identities are commercially sensitive and should not be publicly disclosed, and (ii) language and cultural barriers may make it difficult for those seeking access to nonpublic information to provide proper notice to the applicable third parties, Postal Service employees who will be responsible for providing notice to these specific third parties are also identified in Appendix 1.

The Postal Service further provides, as identified in Appendix 2 to this Application, a list of those third parties that have a proprietary interest in the materials by nonpublic folder.

(3) A description of the materials claimed to be nonpublic in a manner that, without revealing the materials at issue, would allow a person to thoroughly evaluate the basis for the claim that they are nonpublic;

The materials in the Nonpublic Annex fall into several categories. The first category is the Nonpublic CRA, and all of the background materials feeding into the Nonpublic CRA. These materials, in general, show cost information at the product level, including disaggregated information for Competitive products. These materials are found in folders USPS-FY17-NP10, USPS-FY17-NP11 - USPS-FY17-NP14, USPS-FY17-NP18 - USPS-FY17-NP25, and USPS-FY17-NP27. Descriptions of the contents of these folders can be found in the roadmap document, filed at USPS-FY17-9. The

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\(^3\) The Postal Service, in conjunction with the United States State Department, has requested that the Universal Postal Union International Bureau (IB) issue a Circular notice to all countries and designated operators informing each of its rights under 39 C.F.R. § 3007.20(c). This notification was published by the IB on December 18, 2017.
roadmap indicates the corresponding public folder which contains information similar to that in each nonpublic folder, except that, in the public folder, the cost information for Competitive products is generally aggregated into one Competitive products row. Therefore, examination of the corresponding public folder should allow a person to understand the nature of the contents of the nonpublic folder, and evaluate accordingly.

A second category consists of Special Cost Studies materials that provide cost information below the product level for Competitive products. These materials are found in folders USPS-FY17-NP15 - USPS-FY17-NP17, and USPS-FY17-NP26. Again, descriptions of the contents of these folders can be found in the roadmap document, filed at USPS-FY17-9. The roadmap indicates the corresponding public folder which contains information similar to that in the nonpublic folder, except that, in the public folder, the cost information below the product level relates to Market Dominant, rather than Competitive, products. Therefore, examination of the corresponding public folder should allow a person to understand the nature of the contents of the nonpublic folder, and evaluate accordingly.

A third category consists of the International CRA (ICRA) and the supporting documentation. These materials are found in folders USPS-FY17-NP2 - USPS-FY17-NP7 and USPS-FY17-NP9. Collectively, they present the inputs and the analyses used to attribute and distribute costs to International products. In general, the ICRA follows the same basic methodologies used in the CRA – dividing accounting data into cost segments and components, distributing the attributable costs within segments to products, and summing the total attributable costs of a product across segments.
Descriptions of the contents of the individual ICRA-related folders can be found in the roadmap document, USPS-FY17-9. There are no corresponding public folders.

A fourth category is the Competitive product billing determinants. These are found in USPS-FY17-NP1 for domestic Competitive products, and USPS-FY17-NP8 for International products. They are comparable in format to the Market Dominant billing determinants presented in USPS-FY17-4, but include the corresponding information for Competitive products. Again, examination of the corresponding public folder should allow a person to understand the nature of the contents of the nonpublic folder, and evaluate accordingly.

In general, the premise of this application is that, for Competitive products and certain market dominant International products, disaggregated cost data (and detailed volume and revenue data, such as that provided in billing determinants) constitute commercially-sensitive information and should not be publicly disclosed. The Postal Service is therefore placing all such information in the Nonpublic Annex, and filing it under seal. One exception to this approach appears in the CRA. The CRA (USPS-FY17-1) presents some disaggregated data for Competitive products, but those data are not disaggregated down to the product level, as they are in the Nonpublic CRA (USPS-FY17-NP11). Instead, in the CRA, the Postal Service has aggregated data for Competitive products into six product groups. Those groups are Total Priority Mail Express, Total First-Class Package Service, Total (non-Express) Priority, Total Ground, Total Competitive International, and Total Domestic Competitive Services. (The product rows in the Nonpublic CRA that are rolled up into each of the six Competitive product group rows in the CRA are shown in the table below.) At this level of disaggregation,
the Postal Service has been unable to identify any of its major competitors that are
publicly disclosing a potentially greater amount of disaggregated competitive cost data.
The Postal Service maintains that the further disaggregation shown in the Nonpublic
CRA should thus appropriately remain confidential. The Postal Service believes that
the approach jointly embodied in its CRA and Nonpublic CRA prudently maximizes the
amount of information available to the public, keeping such information as detailed as
possible without prompting the competitive concerns outlined in the following section.

**FY2017 Public-Nonpublic Crosswalk Table**

<table>
<thead>
<tr>
<th>Category in Public Version CRA</th>
<th>Categories Rolled in from Nonpublic Version CRA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Priority Mail Express</td>
<td>Domestic Priority Mail Express</td>
</tr>
<tr>
<td></td>
<td>Domestic Priority Mail Express NSAs</td>
</tr>
<tr>
<td>Total First-Class Package Service</td>
<td>First-Class Package Service</td>
</tr>
<tr>
<td></td>
<td>First-Class Package Service NSAs</td>
</tr>
<tr>
<td>Total Priority Mail</td>
<td>Domestic Priority Mail</td>
</tr>
<tr>
<td></td>
<td>Domestic Priority Mail NSAs</td>
</tr>
<tr>
<td></td>
<td>Priority Mail Fees</td>
</tr>
<tr>
<td>Total Ground</td>
<td>Parcel Select Mail</td>
</tr>
<tr>
<td></td>
<td>Parcel Select NSAs</td>
</tr>
<tr>
<td></td>
<td>Parcel Return Service Mail</td>
</tr>
<tr>
<td></td>
<td>Parcel Return Service NSAs</td>
</tr>
<tr>
<td></td>
<td>Standard Post</td>
</tr>
<tr>
<td>Total Competitive International</td>
<td>Outbound International Expedited Services</td>
</tr>
<tr>
<td></td>
<td>Inbound EMS</td>
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<tr>
<td></td>
<td>Outbound Priority Mail International</td>
</tr>
<tr>
<td></td>
<td>Inbound Parcel Post (at UPU Rates)</td>
</tr>
<tr>
<td></td>
<td>First-Class Package International Service</td>
</tr>
<tr>
<td></td>
<td>International Priority Airmail (IPA)</td>
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<tr>
<td></td>
<td>International Surface Airlift (ISAL)</td>
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<tr>
<td></td>
<td>International Direct Sacks M-Bags</td>
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<tr>
<td></td>
<td>Outbound International NSA Mail</td>
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<tr>
<td></td>
<td>Inbound International NSA Mail</td>
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<td></td>
<td>International Mail Fees</td>
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<td></td>
<td>International Mail Fees</td>
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<tr>
<td></td>
<td>International Money Transfer Service</td>
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<tr>
<td></td>
<td>International Ancillary Services</td>
</tr>
<tr>
<td>Category in Public Version CRA</td>
<td>Categories Rolled in from Nonpublic Version CRA</td>
</tr>
<tr>
<td>-------------------------------</td>
<td>-----------------------------------------------</td>
</tr>
<tr>
<td>Total Domestic Competitive Services</td>
<td>Premium Forwarding Service</td>
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<td></td>
<td>Address Enhancement Services</td>
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<tr>
<td></td>
<td>Greeting Cards</td>
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<tr>
<td></td>
<td>Shipping and Mailing Supplies</td>
</tr>
<tr>
<td></td>
<td>Post Office Box Service</td>
</tr>
<tr>
<td></td>
<td>Other Ancillary Services</td>
</tr>
</tbody>
</table>

(4) Particular identification of the nature and extent of commercial harm alleged and the likelihood of such harm;

If the information the Postal Service determined to be protected from disclosure due to its commercially sensitive nature were to be disclosed publicly, the Postal Service considers it quite likely that it would suffer commercial harm. This information is commercially sensitive, and the Postal Service does not believe that it would be disclosed under good business practices. In this regard, the Postal Service is not aware of any business with which it competes (or in any other commercial enterprise), either within industries engaged in the carriage and delivery of materials and hard copy messages, or those engaged in communications generally, that would disclose publicly information and data of comparable nature and detail.

The protected materials consist of comprehensive analytical tools and reports employed by the Postal Service for several purposes in its operations and finances. Most prominently, in the context of the ACR, they enable the Postal Service to address the issues mandated in 39 U.S.C. § 3652(a) having to do with the costs, revenues, rates, and quality of service of competitive postal products. Furthermore, many of the materials outlined in section (3) above consist of sub-reports, workpapers, and other documentation used to create the basic reports in the CRA and ICRA. These materials
share the protected status and confidential nature of the basic reports, since they provide the building blocks that permit compilation of the data and statistics and would permit competitors to gain the same types of knowledge, understanding, and insights at finer levels of detail. The Postal Service believes that this information would lead to competitive harm, if publicly disclosed.

As explained below, the data and information considered to be nonpublic can be classified in several general groupings: product cost information; general product volume and revenue information; product billing determinants; and information pertaining to service and pricing agreements with particular mailers or suppliers (NSAs). The following describes generally the expected harms from each of these classes of information. The explanations also include a separate discussion of international mail products, and their relatively distinct characteristics that arise from the structure of international business, including the involvement of foreign postal operators and international organizations.

**Cost Information**

Information relating to the costs of producing products is generally considered to be among the most sensitive commercial information. The CRA and ICRA present data and statistics for products that would provide competitors with valuable information, enabling them to better understand the Postal Service’s cost structures, operational capabilities, and pricing and marketing strategies. This confidential information includes per-piece costs in several analytical categories (attributable costs, volume variable costs, and product-specific costs), as well as cost contribution and cost coverage
(margin) by product. Such information would be extremely valuable to competitors in assessing the strengths and weaknesses of various postal products. Armed with detailed product cost information, competitors would be able to better identify and understand areas where they could adapt their own operations to be more competitive with postal products and better assess how to price and market their own products in such a way as to target the Postal Service’s weaknesses and compensate for its strengths in producing and marketing various products. Furthermore, information contained in the various sub-reports, workpapers, and other documentation that feed the reports would provide an even more refined knowledge of the Postal Service’s costs, cost structures, and capabilities. In this regard, the structure of the Postal Service’s analytical tools and reports is well known among the postal community from years of exposure in general rate cases under the former regulatory regime. Postal costs are recorded in elaborate systems of general ledger accounts. These are grouped into various functional and other categories (cost segments and components) for further analysis and ultimate allocation and distribution to individual products. The level of detail contained in the sub-reports and workpapers is highly refined and would enable competitors, and existing and potential customers with whom the Postal Service might negotiate particular contract rates, to gain competitive or negotiating advantages that could lead to suppressing potential financial gains from the sale of postal products or the diversion of business away from the Postal Service to competitors. Either of these results would constitute serious commercial harm.
**Volume and Revenue Information**

Competitors could use the product-specific revenue, pieces, and weight information to analyze the Postal Service’s possible market strengths and weaknesses and to focus sales and marketing efforts on those areas, to the detriment of the Postal Service. Disclosure of this information would also undermine the Postal Service’s position in negotiating favorable terms with potential customers, who would be able to ascertain critical information about relevant product trends (e.g., average revenue per piece, average weight per piece). Finally, as explained in greater detail below, disclosure would expose certain foreign postal operators and other customers to the same competitive harms, to the extent that a category is associated with a single customer or a small group of customers. The Postal Service considers these to be highly probable outcomes that would result from public disclosure of the material filed nonpublicly.

**Billing Determinants**

Billing determinants present a special category of volume and revenue information that would enable highly refined understanding of individual products aligned specifically to their individual price structures. In this regard, billing determinants present a picture of each product’s experience, analyzed according to the different mail characteristics that comprise the elements of the product’s price structure. Detailed billing determinants, especially combined with specific product cost information, would enable competitors to better analyze the strengths and weaknesses of individual products, including specific elements of the markets for them, such as
advantages in certain weight categories and distance zones. This information would provide insights into how competitors might adapt their operations and product offerings, alter their pricing, and target their marketing to take business away from the Postal Service.

Armed with this type of information, competitors would likely focus their marketing and price cutting efforts on the Postal Service’s most profitable products. This would lead to erosion of contribution for these products through lost sales and/or the need to lower prices to remain competitive. Postal product cost and contribution information would provide suppliers of postal transportation and other services with information they could use to seek higher rates for services they provide. This would lead to higher postal costs and loss of contribution. Although the extent of the commercial harm is difficult to quantify, even small changes in market share, prices, or costs could lead to millions of dollars in lost revenue, higher costs, and lower margins. It is highly likely that if this information were made public, the Postal Service’s competitors and suppliers would take advantage of it almost immediately.

**Negotiated Service Agreements**

The utility of the sensitive information in billing determinants and other materials would be particularly enhanced with regard to NSA product information relating to particular customers. First, revealing any customer identifying information would enable competitors to focus marketing efforts on current postal customers that have been cultivated through the Postal Service’s efforts and resources. The Postal Service considers it highly probable that, if this information were made public, the Postal
Service’s competitors would take immediate advantage of it. Many NSAs include a provision allowing the mailer to terminate the contract without cause by providing at least 30 calendar days’ notice. Therefore, there is a substantial likelihood of losing the customers to a competitor that targets them with lower pricing.

Other NSA-related information consists of mailing profiles. This information, if disclosed from any source within the CRA or ICRA, would offer competitors invaluable insight into the types of customers to whom the Postal Service is offering each type of competitive NSA. Even without identifying individual mailers, competitors would be able to direct their sales and marketing efforts at the customer segment that the Postal Service has had the most success at attracting. This would undermine both existing customer relationships and the potential for other new NSA customers.

A similar rationale applies to information showing product revenue, volume according to weight, pricing, and insured value levels, as well as adjustment factor calculations based on product revenues. This information is commercially sensitive, and the Postal Service does not believe that it would be disclosed under good business practices. Competitors could use the information to analyze the Postal Service’s possible market strengths and weaknesses and to focus sales and marketing efforts on those areas, to the detriment of the Postal Service. The Postal Service considers these to be highly probable outcomes that would result from public disclosure of the material filed nonpublicly.

Commercially sensitive information related to NSAs is included in the agreements and their annexes, and in related financial work papers. Typically, these materials are filed under seal or redacted when the agreements are established as
products. Since the Commission’s rules governing confidentiality have taken effect, the Postal Service has filed applications for nonpublic status with each agreement. The reasoning expressed in those applications supports and is consistent with the discussion here.

Information derived from these documents is included in some of the materials filed in the Nonpublic Annex here. This information may include prices, product cost, contribution, or cost coverage. It also may concern customer mailing profiles, product volume, weight and revenue distribution, and product insured-value distribution. Competitors for the services covered by these agreements consist of domestic and international transportation and delivery firms and even foreign postal operators, which could use the information to their advantage in negotiating the terms of their own agreements with the Postal Service. Competitors could also use the information to assess offers made by the Postal Service to customers for any possible comparative vulnerabilities and to focus sales and marketing efforts on those areas, to the detriment of the Postal Service. Customers could use the information to their advantage in negotiating the terms of their own agreements with the Postal Service. The Postal Service considers these to be highly probable outcomes that would result from public disclosure of the redacted material.

Potential customers, including foreign postal operators, could deduce from the rates provided in individual pricing agreements, in work papers, or in a Governors’ Decision, whether additional margin for net profit exists. From this information, each customer or foreign postal operator could attempt to negotiate ever-decreasing prices or
incentives, such that the Postal Service’s ability to negotiate competitive yet financially sound rates would be compromised.

Information derived from financial work papers supporting NSAs can include costs, assumptions used in pricing formulas and decisions, formulas and negotiated prices, mailer profile information, projections of variables, and cost coverage and contingency rates that have been included to account for market fluctuations and exchange risks. All of this information is highly confidential in the business world. If this information were made public, the Postal Service’s competitors would have the advantage of being able to assess the Postal Service’s costs and pricing and determine the absolute floor for Postal Service pricing, in light of statutory, regulatory, or policy constraints. Competitors would be able to take advantage of the information to offer lower pricing to postal customers, while subsidizing any losses with profits from other customers. Such competitors could include foreign posts, which in some instances are not required to use the Postal Service for delivery of parcels destined to the United States. Additionally, foreign postal operators or other potential customers could use costing information to their advantage in negotiating the terms of their own agreements with the Postal Service. Eventually, this could freeze the Postal Service out of the relevant markets.

**International Product Information**

The Postal Service believes that the same vulnerabilities and harms discussed above that would result from the disclosure of the cost, volume, and billing determinant information would also generally apply to international product information designated
as nonpublic. In particular, the harms resulting from disclosure of competitive information in the CRA would also result from disclosure of similar information, workpapers, and supporting documentation related to the ICRA. International mail products and business, however, exhibit operational and pricing distinctions not always shared by domestic counterparts. In particular, international products may be either inbound or outbound and, in some instances, are affected by bilateral and multilateral agreements among foreign postal operators. In some cases, particular lines within the ICRA reflect agreements with a single foreign postal operator. The public disclosure of this information would likely lead to limitations on the negotiating positions of both the Postal Service and the other foreign postal operator in similar agreements they might wish to negotiate with other foreign postal operators. The same is true where the partner is a private entity rather than a foreign postal operator: for example, disclosure of statistical, billing, and cost information about GXG could limit the ability of FedEx Express, a supplier to the Postal Service, to negotiate effectively, and could allow competitors to analyze the traffic for competitive advantage against FedEx Express. Further, the outbound letter monopoly has been largely suspended by virtue of 39 C.F.R. § 320.8, thereby contributing to the intensity of competition in this market. The more disaggregated nature of the product information in the international context and the relatively smaller numbers associated with them make the international data particularly vulnerable to analysis and use by competitors.
Facility-Specific Performance Information

Competitors could use the facility-specific performance information to analyze the Postal Service’s possible market strengths and weaknesses and to focus sales and marketing efforts on those areas, to the detriment of the Postal Service. If the facility-specific performance data were available publicly, then competitors could target locations with relatively weaker performance and could focus sales and marketing efforts in those locations to the Postal Service’s detriment. The Postal Service considers these to be highly probable outcomes that would result from public disclosure of the material filed nonpublicly.

(5) At least one specific hypothetical, illustrative example of each alleged harm;

The following restates the harms discussed above and presents at least one hypothetical situation illustrating the consequences of disclosure.

Harm: Competitors, mailers, and suppliers could use cost, revenue, and volume summary data and statistics in the CRA and the ICRA, disaggregated by individual product and by NSA category, to gain knowledge and insights about the relative strengths and weaknesses of the Postal Service’s competitive product lines. That refined understanding would, in turn, give competitors advantages in seeking to divert business from the Postal Service and to gain new business for which the Postal Service might compete. Mailers and suppliers would be able to negotiate favorable deals with the Postal Service more effectively. As a result, the Postal Service would experience losses of existing and new business, or erosion of contributions and margins.

Hypothetical: The CRA and ICRA provide data by product that indicate total revenues, attributable costs, volume variable costs, product specific costs, and per-piece attributable costs, contribution, and cost coverage (margin). These data are broken out by individual product and separated between products purchased through public schedules and those purchased through contract rates (NSAs). Hypothetically, this information is made public. Competitors use it to gain a refined understanding of the
relative strengths and weaknesses of the Postal Service’s product lines (domestic and international), the individual strengths and weaknesses of particular products, and the degree to which products are sold through public schedules, compared to contract pricing arrangements. Financial analysts for the competitors relay their assessments to colleagues in the competitors’ marketing and investment divisions. This information provides a better foundation to enable competing firms to make decisions regarding investments and product design in their own product lines. Based on such assessments, for example, firms that have individual products for domestic express service (overnight), international express service, or package service comparable to Priority Mail determine that they have potential for competitive gain against the Postal Service in these areas and, accordingly, decide to allocate investments in improved operations, supplier arrangements, and technologies to improve their competitive positions. To the extent that these decisions actually make the firms more competitive, the Postal Service loses existing or new business.

**Hypothetical:** Cost, contribution, and/or cost coverage information is released to the public and becomes available to a competitor. The competitor, which could be a foreign postal operator operating in the United States, assesses the profitability of certain services based on the data released. The competitor then targets its advertising and sales efforts at actual or potential customers in market segments where the Postal Service has substantial contribution, thereby hindering the Postal Service’s ability to keep these customers’ business.

**Hypothetical:** Cost, contribution, and/or cost coverage information is released to the public and becomes available to a supplier of materials, transportation, or other
services. Suppliers are made aware of expected contribution margins by product and are better able to assess the relative strengths and weaknesses of the Postal Service’s product lines. With this information, suppliers, including foreign postal operators in the case of international products, decide to increase the rates they charge the Postal Service to provide transportation and/or other services or become more resistant to negotiating favorable prices for their goods and services.

**Hypothetical:** Cost information is disclosed to the public. Mailers who seek to negotiate individual contract rates with the Postal Service gain a better understanding of the average or unit costs of particular products, as well as the relative and absolute strengths and weaknesses of particular product lines. This information enables the mailers to negotiate contract rates with the Postal Service more effectively than in the absence of such information. Similar disclosures result in advantages for foreign postal operators or other competitive entities in international mail.

**Harm:** The various companion reports, sub-reports, workpapers, special cost and other studies, and documentation contained in the Nonpublic Annex would provide detailed and refined knowledge and understanding of the individual costs, cost structures, contributions, and cost coverages (margins) of individual postal products and contract pricing agreements. These materials, which produce and support the summary data and statistics contained in the CRA and ICRA, would provide highly detailed information regarding operational procedures used to produce the products, the costs and relative efficiencies of operations and sub-operations, and the amount and character of overhead, including the relative proportions of volume variable and overhead costs. Companion reports and sub-reports provide detailed functional analyses of Postal Service costs within a framework that is well-understood, or easily learned, from information in the Public Annex, or from familiarity with or research into past postal rate cases. Public disclosure would therefore be tantamount to publishing virtually every detail regarding the relative costs and efficiencies of providing postal competitive products. This information would provide blueprints for competitors, suppliers, and mailers who might seek to negotiate favorable contract rates. The information would better enable them to make favorable operational, investment, pricing, and marketing decisions in relationships with the Postal Service. The results would be loss of existing or
future business for the Postal Service, or the erosion of total revenues, contributions, margins, and overall financial stability.

Hypothetical: The Cost Segments and Components reports of the CRA and ICRA are disclosed to the public. These reports group costs recorded in postal accounts according to various functional categories. The costs are distributed by postal product. The hypothetical disclosure provides competitors with a detailed understanding of the cost structures of each competitive postal product, the relative strengths and weaknesses of each product from cost perspectives, and the flexibilities available to the Postal Service within the legal framework applicable to postal prices. The refined understanding resulting from disclosure enables competitors to make decisions that would compensate for Postal Service strengths and capitalize on its weaknesses. These decisions might involve design of competing firms’ own products, alternative price structures, operational procedures, and marketing strategies. They could also involve formulation of negotiating approaches and strategies by existing and potential suppliers of goods and services used in producing postal products, and the formulation of more informed negotiating positions by mailers seeking to enter into favorable contract rate arrangements with the Postal Service. Such competitive advantages lead to diversion of business away from the Postal Service or reduction of potential contribution from individual contracts.

Hypothetical: Cost distribution models, cost estimation models, and several sub-reports feeding into the CRA and ICRA are disclosed to the public. These materials provide highly refined information that would improve understanding of product cost structures and the behavior of postal costs. Certain cost reports, such as those outlining in detail the application of specific cost pools by mail processing operation in
estimating product costs, provide detailed knowledge of operational procedures employed by the Postal Service in offering products and services. This information enhances competitors’ abilities to make informed decisions about investment in capital and technologies used to produce their own competing products. For example, knowledge of inflexibilities in processing Priority Mail, or in transportation used to convey Parcel Return Service, leads competitors to explore more efficient processing of competing products or to negotiate more competitive transportation contracts used for competing products. Over time, annual disclosures of such information enable competitors (or suppliers and mailers) to identify and understand trends in cost behavior that better inform their decision-making. Such developments lead to an erosion of the Postal Service’s competitive position and a loss of business or contribution.

**Hypothetical:** Information in certain reports and documentation of special cost and other studies (e.g., Parcel Return Service cost models) is disclosed publicly. Such information provides a better understanding of the Postal Service’s customer base for particular products. For instance, data from mail characteristics studies enables competitors to formulate a profile of the Postal Service’s customer base for certain products. This information better enables competitors to devise marketing and sales strategies that target the most vulnerable markets for particular postal products. More effective marketing by competitors leads to reduced sales by the Postal Service and an erosion of contributions and margins.

**Hypothetical:** Cost models and sub-reports feeding the CRA and ICRA reports are disclosed to the public. Detailed knowledge of the Postal Service’s cost estimation, cost distribution, and special study models and procedures provides competitors, as well as
mailers who seek favorable contract rates, with tools that enhance their abilities to analyze postal costs and operations. Large, sophisticated firms who have competed with the Postal Service for long periods of time have been exposed to them before and likely have developed their own sophisticated analytical tools and therefore might not benefit as much from these models; however, the hypothetical availability of this information decreases barriers to entry in certain competitive markets and creates new competitors that erode the Postal Service’s customer base.

**Harm:** Competitors could use disaggregated product volume, weight, and revenue distribution information to assess vulnerabilities and focus sales and marketing efforts to the Postal Service’s detriment.

**Hypothetical:** Disaggregated revenue, volume, and weights contained in the Nonpublic Annex are disclosed to the public. Another delivery service’s employee monitors the filing of this information and passes it along to the firm’s sales and marketing functions. The competitor assesses the profitability of certain services on a per-piece or per-pound basis or the Postal Service’s relative concentration in certain service offerings. The competitor then targets its advertising and sales efforts at actual or potential customers in market segments where the Postal Service appears to have made headway, hindering the Postal Service’s ability to reach out effectively to these customers.

This example applies even more strongly for information split between NSA mail and other mail in the same category, because the competitor can assess the profitability and market strengths of the Postal Service’s offerings to a small subset of NSA customers, thereby gaining somewhat more particularized insight into the
characteristics of customers that the Postal Service specifically targets with its own contractual sales efforts.

**Harm: Customers, including foreign postal operators, and suppliers could use disaggregated product volume, weight, and revenue distribution information to undermine the Postal Service’s leverage in negotiations.**

**Hypothetical:** Disaggregated revenue, volume, and weight information in the Nonpublic Annex is released to the public. A foreign postal operator’s employee monitors the filing of this information and passes the information along to its international postal relations functions. The foreign postal operator assesses the Postal Service’s average per-item or per-pound revenue for categories about which it is negotiating with the Postal Service, with particular focus on categories known to be included in bilaterals with other foreign postal operators (*e.g.*, letter post, air and surface parcels, and EMS). Accurately or not, the foreign postal operator uses the average revenue information as a justification for pricing demands in negotiations, refusing to accept a higher price without steeper concessions than the Postal Service might otherwise have been able to foreclose. The Postal Service's ability to negotiate the best value from the bargain suffers as a result. This hypothetical applies with equal force for customers other than foreign postal operators, for NSA mail and non-NSA mail that can be made subject to an NSA (*e.g.*, International Priority Airmail, which can be included in Global Plus 1 NSAs), and for partnerships with suppliers such as FedEx Express with respect to GXG.

**Harm: Public disclosure of information in the report would be used by competitors of the NSA customers to their detriment.**

**Hypothetical:** A competitor of a Postal Service NSA customer obtains unredacted versions of the billing determinants for domestic and international products, including
NSAs and ICMs. It analyzes the work papers to assess the customer’s underlying costs and uses that information to identify lower cost alternatives to compete against the Postal Service customer. Likewise, suppliers of goods and services to the NSA customer can use the detailed information to their advantage in negotiations with the NSA customer.

**Harm:** Public disclosure of information contained in the Nonpublic Annex associated with international delivery services provided in partnership with specific third parties would be used by those parties’ competitors to their detriment.

**Hypothetical:** A competitor of Canada Post Corporation, such as a competing international delivery service, obtains information contained in the Nonpublic Annex. The competitor analyzes the information to assess the average per-piece and per-pound revenue for Inbound International Letter-Post NSA Mail, Expedited Parcels and EMS which correspond to Canada Post’s average per-piece and per-pound cost for U.S. delivery of its pertinent products. The competitor uses that information to assess the market potential and, as a baseline, to negotiate with U.S. customs brokers and freight companies to develop lower-cost alternatives and undermine Canada Post’s market offerings. The same scenario could apply with respect to comparable information, such as settlement charges due or payable, for other foreign postal operators or for FedEx Express concerning Global Express Guaranteed (GXG).

**Harm:** Competitors could use customer mailing profiles, product volume, weight, and revenue distributions, and product insured-value distribution information to assess vulnerabilities and focus sales and marketing efforts to the Postal Service’s detriment.

**Hypothetical:** Customer mailing profile information in the Nonpublic Annex is released to the public. Another delivery service’s employee monitors the filing of this information
and passes the information along to its sales and marketing functions. The competitor assesses the typical size, mailing volume, and content characteristics of Postal Service NSA customers. The competitor then targets its advertising and sales efforts at actual or potential customers with similar profiles, hindering the Postal Service’s ability to reach out effectively to these customers.

This hypothetical would apply even for more generic product-level data, from which one could calculate the distribution of the Postal Service’s overall customer base in terms of item weight, revenue, or value (in the case of international insurance). For these reasons, release of any of the nonpublic information would pose actual commercial harm to the Postal Service, regardless of the information’s present favorability.

**Harm:** Revealing customer identifying information associated with competitive domestic and international NSAs would enable competitors to target the customers for sales and marketing purposes.

**Hypothetical:** The identities of customers with which prices are established in NSAs are revealed to the public. Another expedited delivery service passes along the information to its sales function. The competitor’s sales representatives quickly contact the Postal Service’s customers and offer them lower rates or other incentives to terminate their contracts with the Postal Service in favor of using the competitor’s services. Lost sales undermine the Postal Service’s revenues.

**Harm:** In billing determinants and supporting documentation pertaining to domestic and international competitive NSAs, disclosure of information that would reveal prices associated with particular pricing agreements would provide competing domestic and foreign postal operators, or other potential customers, extraordinary negotiating power to extract lower rates from the Postal Service.
**Hypothetical:** Customer A’s negotiated rates are disclosed publicly. Customer B sees the rates and determines that there may be some additional profit margin between the rates provided to Customer A and the statutory cost coverage that the Postal Service must produce in order for the agreement to be added to the competitive products list. Customer B, which was offered rates identical to those published in Customer A’s agreement, then uses the publicly available rate information to insist that it must receive lower rates than those the Postal Service has offered it, or it will not use the Postal Service for its expedited package service delivery needs.

Alternatively, Customer B attempts to extract lower rates only for those destinations for which it believes the Postal Service is the low-cost provider among all service providers. The Postal Service may agree to this demand in order to keep the customer’s business overall, which it believes will still satisfy total cost coverage for the agreement. Then, the Customer would use other providers for destinations other than those for which it extracted lower rates. This would affect the Postal Service’s overall projected cost coverage for the agreement, so that it no longer would meet its cost coverage requirement. Although the Postal Service could terminate the contract when it first recognized that the mailer’s practice and projected profile were at variance, the costs associated with establishing the contract, including filing it with the Postal Regulatory Commission, would be sunk costs that would have a negative impact on the product overall.

**Harm:** In billing determinants and supporting documentation pertaining to domestic and international competitive NSAs, public disclosure of information contained in underlying financial analyses would be used by competitors and customers to the detriment of the Postal Service.
Hypothetical: A competing package delivery service obtains a copy of information contained in unredacted versions of financial work papers associated with particular agreements. It analyzes information contained in the work papers to determine what the Postal Service would have to charge its customers in order to comply with business or legal considerations, including meeting its minimum statutory obligations regarding cost coverage and contribution to institutional costs. It then sets its own rates for products similar to those that the Postal Service offers its customers below that threshold and markets its purported ability to beat the Postal Service on price for domestic or international delivery services. By sustaining this below-market strategy for a relatively short period of time, the competitor, or a group of the Postal Service’s competitors acting in a similar fashion, freeze the Postal Service out of one or more relevant delivery markets. Even if the competing providers do not manage wholly to freeze out the Postal Service, they significantly cut into the revenue streams upon which the Postal Service relies to finance provision of universal service.

Harm: In billing determinants and supporting documentation pertaining to domestic and international competitive NSAs, public disclosure of product volume, weight, revenue distribution, and product insured-value distribution would enable competitors to assess vulnerabilities and focus sales and marketing efforts to the Postal Service’s detriment.

Hypothetical: For Inbound Air Parcel Post, a competing package delivery service determines what the Postal Service would need to charge its customers (which may include foreign postal operators) to meet its minimum statutory obligations for cost coverage and contribution to institutional costs. The competing package delivery service then sets its own rates for products similar to those the Postal Service offers other postal operators under that threshold and markets its ability to beat the Postal
Service’s price for inbound air parcels. By sustaining this below-market strategy for a relatively short period of time, the competitor, or a group of the Postal Service’s competitors acting in a likewise fashion, freezes the Postal Service out of the inbound air parcel delivery market.

**Hypothetical:** For EMS and Canada Post Bilateral for Inbound Competitive Services, another postal operator sees the price and concludes that there may be some additional profit margin between the rates provided to Canada Post and the statutory cost coverage that the Postal Service must produce in order for the agreement to be added to the competitive products list. That postal operator then negotiates lower prices with the Postal Service on its own behalf or uses its knowledge to offer postal customers lower prices than they currently receive. Either or both ways, the Postal Service loses market share and contribution.

**Harm:** Competitors could use facility-specific performance information to gain knowledge and insights about the relative strengths and weaknesses of the Postal Service’s service performance. That refined understanding would, in turn, give competitors advantages in seeking to divert business from the Postal Service and to gain new business for which the Postal Service might compete. As a result, the Postal Service would experience losses of existing and new business, or erosion of contributions and margins.

**Hypothetical:** Facility-specific performance information is released to the public and becomes available to a competitor. The competitor assesses opportunities to provide certain services in new markets based on the data released. The competitor then targets its advertising and sales efforts at actual or potential customers in market segments where the Postal Service has relatively weaker performance, thereby hindering the Postal Service’s ability to keep these customers’ business.
(6) The extent of protection from public disclosure deemed to be necessary;

The Postal Service maintains that the portions of the materials filed nonpublicly and relating to competitive products should be withheld from persons involved in competitive decision-making in the relevant markets for competitive delivery products (including private sector integrators and foreign postal operators), as well as their consultants and attorneys. Additionally, the Postal Service believes that actual or potential customers of the Postal Service for these or similar products should not be provided access to the nonpublic materials.

(7) The length of time deemed necessary for the nonpublic materials to be protected from public disclosure with justification thereof; and

The Commission’s regulations provide that nonpublic materials shall lose nonpublic status ten years after the date of filing with the Commission, unless the Commission or its authorized representative enters an order extending the duration of that status. 39 C.F.R. § 3007.30.

(8) Any other factors or reasons relevant to support the application.

None.

Conclusion

For the reasons discussed, the Postal Service asks that the Commission grant its application for nonpublic treatment of the Nonpublic Annex of the FY 2017 ACR.
## Appendix 1 to Application for Nonpublic Treatment

### List of Impacted Third Parties and Contact Information

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<thead>
<tr>
<th>Impacted Third Party Number</th>
<th>Contact Information</th>
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| 1                          | New Zealand Post Limited  
Rachael Manson  
Global Business Director  
+64 21 988 866  
Rachael.Manson@nzpost.co.nz |
| 2                          | Hongkong Post  
Mr. Steve Lau, Senior Manager, International Business, External Affairs Division  
+852 2921 2120  
steve_lau@hkpo.gov.hk |
| 3                          | Deutsche Post AG  
Birgit Bünningmann, Head of Direct Entry  
+49 228 182 21513,  
birgit.buennigmann@deutschepost.de  
AND  
Ivo Wisser, Product Manager Direct Entry  
+49 228 182 24105,  
i.wisser@deutschepost.de |
| 4                          | Royal Mail  
Guy Fischer,  
Director, Overseas Contracts & Policy  
+44 7703104937  
guy.fischer@parcelforce.co.uk |
| 5                          | China Post Group  
Ms. Wu Yan,  
Deputy Director of International Postal Affairs  
International Cooperation Department  
China Post Group  
+86 13 621 256 616  
wuyan@ems.com.cn |
| 6                          | BBVA Bancomer USA, Inc.  
Aurora Garza Hagan, CEO  
281-765-1525  
aurora.garza@bbvabancomerusa.com |
|   | Korea Post  
|   | Mr. Dong hee YOO  
|   | Assistant Director of International Business  
|   | +8244 200 8298  
|   | ydhwo@korea.kr  
|   | Australian Postal Corporation  
|   | Michael Cope, Head of Global Development, International Postal  
|   | +61 (0)2 93198750  
|   | michael.cope@auspost.com  
|   | PostNL  
|   | Wim van de Sande, Senior Terminal Dues Manager  
|   | +31 (0)6 83 64 57 90  
|   | wim.van.de.Sande@postnl.nl  
|   | Jan Sertons  
|   | PostNL Director International Relations  
|   | +31 6 226 99 828  
|   | Jan.sertons@postnl.nl  
|   | Domestic Competitive NSA Customers  
|   | Elizabeth A. Reed, Attorney, Pricing and Product Support  
|   | 202-268-3179  
|   | elizabeth.a.reed@usps.gov  
|   | International Competitive NSA Customers  
|   | Christopher C. Meyerson, Attorney, Global Business  
|   | 202-268-7820  
|   | christopher.c.meyerson@usps.gov  
|   | Kyle Coppin, Attorney, Global Business  
|   | 202-268-2368  
|   | Kyle.R.Coppin@usps.gov  
|   | FedEx Express  
|   | James H. Ferguson, Corporate Vice President  
|   | 901-434-8600  
|   | jhferguson1@fedex.com  
|   | Canada Post Corporation  
|   | Ewa Kowalski, Director International Mail Settlement and USPS Relations  
|   | 1 (613) 734-6201  
|   | ewa.kowalski@canadapost.ca  
|   | Yves Samson  
|   | Manager International Mail Settlement/International Relations  
|   | (613) 734-3000 ext. 55616  
|   | yves.samson@canadapost.ca
| 14 | Correos de México  
Jimmy Ortiz, Manager, International Postal Relations  
202-268-6356  
jimmy.ortiz@usps.gov |
|----|--------------------------------------------------|
| 15 | KPG  
Vincent Mougey, Manager, New International Opportunities  
202-268-3437  
Vincent.J.Mougey@usps.gov  
Allie Schneider Laakso  
Business Solutions Specialist  
202-268-2262  
Allison.S.Laakso@usps.gov |
| 16 | UPU Designated Operators  
Contact information for all UPU Designated Operators is available at:  
http://pls.upu.int/pls/ap/addr_public.display_addr?p_language=AN |
| 17 | EMS Operators  
List of EMS Operators is available at:  
http://www.ems.post/members-ems-cooperative  
Contact information for EMS Operators is available at:  
http://pls.upu.int/pls/ap/addr_public.display_addr?p_language=AN |
### Appendix 2 to Application for Nonpublic Treatment
#### List of Impacted Parties by Non-Public Folder

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